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IRELAND'S REFERENDUM ON THE FISCAL COMPACT

A LIFELINE AFTER THE RISE AND FALL OF THE CELTIC TIGER?

Dieter W. Benecke

In the referendum held on 31 May 2012, 60 per cent of the Irish people voted in favour of accepting the European Fiscal Compact, thus agreeing that Ireland should in future be legally bound by its rules. For Ireland and the other countries in the European Union, the "Treaty on Stability, Coordination and Governance in the Economic and Monetary Union", agreed by 25 of the 27 heads of state and government on 9 December 2011, is vital if we are to preserve the EU and the euro.

THE NECESSITY OF AND PREPARATIONS FOR A REFERENDUM ON THE FISCAL COMPACT

The new government in Ireland that was formed in March 2011 had agreed to the fiscal compact in Brussels and announced that it wanted to apply the rules of the pact, even if they were not explicitly prescribed by law, because of the urgent need for budget discipline and debt reduction combined with initiatives for growth.

Article 3, Section 2 of the treaty refers to "preferably constitutional" provisions of binding force on those governments that are parties to the treaty. The fiscal compact rules are to "take effect in the national law." Opponents of the fiscal compact in Ireland could certainly have used these rules as an excuse to claim that the treaty was unconstitutional.[1] In order to avoid this, the government

1 | While opponents of the fiscal compact accept the result of the referendum, they are still trying to stop the pact becoming law and have initiated legal proceedings to determine ▸

accepted the suggestion of the country's president and public prosecutor that the constitution might be affected by the country's obligations under the pact, and decided to call a referendum. It was also necessary to act quickly, as the treaty was due to come into force on 1 January 2013, and it seemed unlikely that the country's constitutional court would make a decision on the issue in such a short space of time.

According to Article 47 of Ireland's 1937 constitution, any proposed change to the law that affects the constitution must be put to the people in a referendum. So far, 29 referendums have been held, including a vote on the Treaty of Lisbon, which was initially rejected by 53.4 per cent of the population in a referendum held in 2008.[2] The treaty was finally accepted by a clear majority of people in a second referendum in 2009, with 67.1 per cent voting in favour.[3]

The fiscal compact returns to the rules set out in the Stability and Growth Pact (Maastricht Treaty) which stipulate that eurozone countries should cap their budget deficits at 3 per cent and their government debt at a maximum of 60 per cent of GDP. The Maastricht rules, introduced in 1992 as eligibility criteria for adopting the euro, are to be tightened in light of the current financial crisis, so that countries that do not observe the Maastricht rules can be called before the European Court of Justice and forced to pay a fine. However, unlike before, where the

whether the European financial stability instruments, the ESM and the ESFS, are in fact constitutional.

2 | The government at the time assumed that the result was a foregone conclusion and failed to inform the people sufficiently about the content of the treaty. One former minister even went so far as to admit that he hadn't even read it, let alone understood it.

3 | Ratifying the Treaty of Nice also required two referendums. In the first referendum in 2001, the treaty was rejected by 53.9 per cent of the people then accepted by 62.9 per cent in the second referendum. Earlier EU treaties such as that on the single market (1987), the Maastricht Treaty (1992) and the Treaty of Amsterdam which built on this (1998) had been ratified at the first attempt. Other examples of important political referendums include those on renouncing a claim to sovereignty over Northern Ireland that had previously been enshrined in the constitution (1998) and the abolition of the death penalty (2001). Referendums have also been held on social issues, such as the 1995 referendum on divorce, which resulted in a remarkably close vote of 51 per cent in favour of allowing divorce.

governments of the member states had to agree, now in the event of a refusal to pay a fine, they must exercise a psychologically much more difficult veto. Another measure to increase budgetary discipline is the capping of future new borrowing (the structural deficit) to 0.5 per cent of GDP per annum.

Opponents of the Treaty of Lisbon were of course especially vocal during the parliamentary and media debates that became increasingly heated from mid-April onwards. These opponents had already succeeded in persuading voters to reject the Treaty of Lisbon in the first referendum held in 2008. The fear that spread among the Irish people that they might not be allowed to remain in the European Union, membership of which had made their past prosperity possible, prompted the government of the time to call a second referendum, and this time 67.1 per cent of the "frightened" Irish voted in favour of the Treaty of Lisbon. The main argument of the opponents of the Treaty of Lisbon was the country's potential loss of sovereignty – still today a particularly sensitive subject in Ireland, a country that had declared independence in 1919 after numerous uprisings and a guerrilla war against the British occupying forces, but it was not until 6 December 1921 that the signing of the Anglo-Irish Treaty officially sealed its independence from Britain.

In 2008 the main argument of the opponents of the Treaty of Lisbon was the country's potential loss of sovereignty – still today a particularly sensitive subject in Ireland.

This issue of sovereignty was also a powerful argument used by those opposed to the fiscal compact. Added to this was the argument that the pact is in fact not an incentive for stability and growth, but actively encourages austerity measures, and so would lead to a decline in public services and a rise in unemployment. The main advocates of a No vote in the referendum were some, but not all, unions and three of the political parties, the nationalist Sinn Féin (14 of 166 seats in parliament),[4] the extreme left-wing Socialist

4 | People in many countries take Sinn Féin's nationalism to mean that they are "right-wing" or conservative. This is not the case. Over the years, the party has become more and more involved in social problems. "Nationalist" here means that the party was linked to the military and guerrilla activities of the Irish Republican Army (IRA) in Northern Ireland and Great Britain. They are still identified with a now more peaceful IRA and continue to strive for the re-unification of all Ireland. Sinn Féin continues to attract a growing number ▸

Party (two seats) and the left-wing Alliance People before Profit (two seats).

The Socialist Party as well as the nationalist party Sinn Féin, was unsuccessful in advocating the refusal of the fiscal compact. | Source: William Murphy (CC BY-SA).

The government learned from the experiences of its predecessors with the referendum on the Treaty of Lisbon, and prepared more information to give to voters in order to avoid the possibility of a second referendum. Supporters of the fiscal compact included the ruling parties Fine Gael (77 seats) and Labour (38 seats), plus the former ruling party and now opposition Fianna Fáil (20 seats). Some unions

of voters, as was seen in the recent 2011 parliamentary elections, and was further strengthened by a strong, but ▸ ultimately unsuccessful showing by its candidate in the presidential elections (Deputy Prime Minister of Northern Ireland Martin McGuiness). Their No campaign in the lead-up to the referendum also increased the party's popularity. Voters from poorer backgrounds felt they were better represented by Sinn Féin than by the Labour Party, which they would normally support, but which was in favour of the fiscal compact. In a poll carried out shortly before the referendum, Sinn Féin achieved a 24 per cent approval rating for the first time (previously its support had fluctuated between 10 and 12 per cent). Support for Fine Gael had fallen from 38 to 34 per cent, while Labour had dropped from 33 to 19 per cent. Cf. *The Irish Times*, 28 May 2012. Sinn Féin's attempts to have the referendum postponed by a decision of the courts failed when it became clear that 60 per cent of the people were likely to vote in favour of the pact.

decided to recommend a Yes vote to their members, partly because they recognised the realities of the situation, and partly because they felt they had a gun to their heads. Trade associations also argued in favour of the treaty, especially the International Financial Services Centre, run by former Prime Minister John Bruton (Fine Gael), and the Farmers' Association.

The arguments in favour of the fiscal compact can be summarised as follows:

- Budget discipline is essential and will be enforced by the fiscal compact.
- Debt reduction is the only way to put to more constructive use capital that is freed up from servicing the country's debt.
- Debt reduction is the only way to achieve long-term growth and create more jobs.
- Stepping away from the fiscal compact could lead foreign investors to believe the Irish are unreliable and to consider Ireland as no longer being a bridge with the single European market.
- The bailout that Ireland agreed with the EU and the IMF in 2010 requires the country to exercise budget discipline; otherwise the remaining payments may be put at risk.
- Any rejection of the fiscal compact would undermine access to the solidarity of the other EU partners, and particularly to the European Stability Mechanism (ESM), as funds from the ESM can only be granted to countries that have ratified the fiscal compact. Many top Irish economists have pointed out in numerous newspaper articles how this would turn out to be very expensive for their country.

The government's launch of new initiatives on employment and investment have made it clear that it is not just focusing on austerity but also very much on growth. It has described the fiscal compact as being a stability and growth pact, while its opponents have tried to discredit it by claiming it is just an austerity pact. In saying this, the opponents of the treaty – just like Alexis Tsipras, the leader of the Greek leftist party Syriza – were under the illusion that the Irish government could renegotiate the fiscal compact and that the country would still have access to the ESM even if the treaty were not ratified because the EU partners would not abandon a eurozone country, as had been shown in Greece.

The opponents of the pact hoped to gain added momentum for their campaign from the government crisis in the Netherlands, the election of François Hollande in France and the Greek elections held on 6 May, in which almost two-thirds of the population voted for parties that were hostile to austerity policies. In Ireland too, at least by more minor players, Germany was portrayed as the enemy of flexible debt management. The fiscal compact opponents hoped to be able to build an EU-wide front to fight the tide of budgetary discipline, saying that only higher spending (so in the Irish case, more borrowing) could revive the economy and reduce unemployment (which in Ireland currently stands at 14 per cent). This deliberately ignored the fact that it is precisely the countries in Europe with the highest levels of debt that also have the highest rates of unemployment.

Experience had shown that in referendums extraneous issues often influence the vote.

Debates held in public and in the media became extremely heated. Experience had shown that in referendums extraneous issues often influence the vote. As a result, it was not clear what would be the impact on the vote of the austerity measures and tax increases that the government had already implemented[5] and to what extent the parties of the left would be able to influence those sectors of the Irish population that had been particularly affected by the financial crisis. Two weeks before the referendum, the No camp was snapping at the heels of the Yes supporters.

According to the Irish constitution, the government has to remain neutral when referendums are called. It has to leave all campaigning to the parties and private groups, but it must ensure that its citizens are informed about the issue.

5 | According to a survey carried out by *The Irish Times* on 28 May 2012, these two measures caused public satisfaction with the government’s work to shrink to 27 per cent, while 67 per cent of the population claimed to be dissatisfied with the government’s work. These results were published three days before the referendum and once again caused uncertainty in the predictions of success for the pro-fiscal compact campaign.

The Irish government fulfilled its obligations by sending every household a handy information brochure on the fiscal compact that contained the text of the treaty but no commentary. Government supporter and former President of the European Parliament, Pat Cox, launched a private Yes initiative. The ruling parties and the opposition party that was in favour of the fiscal compact, Fianna Fáil, along with the business federations, also significantly ramped up their activities to support the treaty in the two weeks before the vote. Their main arguments revolved around "lack of investor confidence" and "no access to the ESM". These efforts helped the Yes camp to gain support during the final days leading up to the referendum. Polls predicted that around 60 per cent of voters were likely to vote in favour of the fiscal compact, which motivated the Yes camp to redouble their efforts in order to keep potential Yes voters from staying away because they thought the result was a foregone conclusion.

To neutral observers it may seem a little strange that the fiscal compact could stir up so much controversy. After all, in 2010 Ireland had been given a bailout by the European Union (together with Portugal). And some "gratitude" – a rare phenomenon in politics – might also have been expected for the fact that Ireland had benefited so much from joining the EU in 1973 and from the many years of EU subsidies. But despite the bailout from the EU and the IMF, Ireland remained in a critical situation in terms of its economy, employment and finances, and this overshadowed the referendum for large swathes of the population. The supporters of the pact did not specifically address the fear that the country would be cut off from receiving further necessary aid from European institutions such as the EU and European Central Bank (ECB) or from the possibility of extending its repayment period if it rejected the treaty. But of course their opponents implied that the government had tacitly stirred up this fear by pointing to the provision of the treaty stating that the ESM could only be used by countries that ratified the fiscal compact.[6]

Despite the bailout from the EU and the IMF, Ireland remained in a critical situation in terms of its economy, employment and finances, and this overshadowed the referendum.

6 | Cf. "Coalition played on fears of electorate, Adams (President of the Sinn Féin party, author's note) claims", *The Irish Times*, 2 Jun 2012.

RESULTS OF THE REFERENDUM

A No to the fiscal compact would not only have brought with it the financial disadvantages spelled out within the treaty. Without exaggeration, it would have been a disaster for the government, as anti-government feeling has grown markedly amongst large sections of the population due to the spending cuts and tax increases.[7] However, thanks to the intensive but neutral information provided by the government and the active pro-pact campaign run by the parties and institutions that supported the treaty, most voters gained an understanding of the pact and began to look on it more favourably. This helped to reduce the very high percentage of undecided voters (at times more than 50 per cent) in the last week before the referendum. This is even more remarkable when we realise that at the beginning of the year polls showed that over 60 per cent of the population were opposed to the fiscal compact.

According to the official results, 60.3 per cent of the population voted in favour of the fiscal compact and its legal ramifications, with 39.7 per cent voting against. The number of invalid votes was less than 1 per cent. This is a very clear result and shows that the majority of people of Ireland are not only in favour of budgetary discipline as stipulated in the fiscal compact, but also of their country moving closer to Europe. Only half the population took part in the referendum.[8] It can be assumed that there was a range of different reasons why people did not vote. It may be that voters were not sufficiently informed, despite the good communication efforts on the part of the government and the intense debate in the media, or that they simply felt irritated by the abrasive for and against arguments aired on television. Laziness, apathy or fatalism ("what difference am I going to make?") may have been other reasons. And then three days before the referendum, polls showed that the Yes vote was likely to be around 60 per cent, meaning many voters felt they did not have to vote as "it was all over". It may also have been that this

The majority of people of Ireland are not only in favour of budgetary discipline as stipulated in the fiscal compact, but also of their country moving closer to Europe.

7 | It should not be forgotten that the first rejection of the Lisbon Treaty sounded the death knell for the previous government.

8 | In the second referendum on the Lisbon Treaty the turnout was 59 per cent and, as previously mentioned, the vote in favour was 67.1 per cent.

referendum was considered too important to simply use it as a means of expressing dissatisfaction with the government – as had been the case in previous referendums – but at the same time there was a feeling of wanting to avoid strengthening the government's position by handing it an overly-positive result.

The majority of people in 38 of the 43 constituencies voted in favour of the fiscal compact. Although there was little difference in the way people voted in urban areas (Dublin, Cork, Limerick, Galway) compared to rural constituencies, there was a clear difference between the more prosperous and less well-off sections of the population.

Analysts have suggested that the main motivation for voting in favour of the fiscal compact was the fact that the country's financial situation, and particularly that of the banks, means that it will remain vital to have access to European bailout funds. Many observers believed the "fear factor" – the concern of being left in dire financial straits – provided a major motivation to vote for the treaty. It is true that the present budgetary situation complies with the requirements set by the "Troika",[9] but this does not mean that Ireland will be able to survive without more financial aid if faced with challenges such as a further downturn in the global economy. So we should not underestimate the constructive element in this result: voters felt Ireland should play an active role in the EU.

It is not necessarily given that Ireland will be able to survive without more financial aid if faced with challenges such as a further downturn in the global economy.

A second, more psychological element that motivated the voters to vote Yes is the situation in Greece. Ireland is in a much better position than Greece because its economic, social and, above all, political structures are generally in reasonably good order despite the crisis and have little in common with the political, structural and budgetary problems besetting the Greeks. The majority opinion is that budget discipline is essential if the country is not to fall into a Greece-like position of total dependency on its European partners, something that is also a question of national pride

9 | The financial experts of the ECB, EU and IMF monitor Ireland's financial situation every three months and so far have come to the conclusion that Ireland has actually "more than satisfied" the terms of its bailout programme.

for the Irish. The feeling is that this budget control was lacking in the previous government after the collapse of Lehman Brothers' Bank.

Table 1

Selected referendum results (in per cent)

Region	**Turnout**	**For Fiscal Compact**	**Against Fiscal Compact**
Dublin	52.4	56.3	43.7
Dublin South	57.1	75.8	24.2
Dublin South East	48.8	72.3	27.7
Dublin North West	51.9	46.8	53.2
Cork	50.9	61.0	39.0
Limmerick	48.1	66.0	34.0
Galway	47.5	60.5	39.5
Mayo*	47.8	67.2	32.8
Claire**	49.8	65.7	34.3
Sligo North**	48.0	60.3	39.7
Cavan/Monaghan**	48.8	57.6	42.4
Kerry***	47.5	62.5	37.5
Donegal****	42.2	44.3	55.7
Dun Laoghaire*****	57.2	74.2	25.8
Total	50.5	60.3	39.7

* Prime Minister's mainly rural constituency
** Rural regions
*** Constituency with mixed economy, tourist region
**** Neighbouring province to Northern Ireland, strong Sinn Féin influence
***** Well-off suburb of Dublin

Source: Official final results.

It seems probable that a look in their own wallets also gave voters an impetus to vote Yes, as least as far as the middle classes were concerned. They were reluctant to lose everything they had worked for over the last 15 years. From a personal point of view, and of course from the government's viewpoint, a Yes vote was bound up with the hope of relaxing the EU's bailout conditions, but also above all with the hope of getting the ECB's permission to resolve the banking crisis more quickly. This view was particularly strong amongst voters who had their own industrial, service or agricultural businesses, as the EU remains the mainstay of the Irish economy. This is particularly true of the agricultural sector, whose production is vital for both the domestic and export markets.

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The majority of the population in rural areas – where there is generally a more stable, if more modest, standard of living – voted in favour of the fiscal compact, apart from County Donegal, where Sinn Féin has a great deal of influence. Predominantly middle-class urban constituencies also returned a clear Yes vote. The only urban constituencies that voted No were Dublin North West and Dublin South Central, but the result was very close (51 to 53 per cent). The left-wing parties' core supporters tend to live in these working-class, low-earning constituencies.

In contrast, voters in the more well-off constituencies voiced a loud Yes to the fiscal compact. Attitudes towards this treaty are of course not just influenced by prosperity, but also by levels of education. A better understanding of the significance of the fiscal compact, and a political pro-government and pro-EU vote tipped the balance to produce a Yes vote of over 65 per cent, rising to 70 per cent in some areas. This should not lead to the impression that it is only the better-off sections of the population who are in favour of the EU and its rules. The vast majority of the more left-leaning population are also in favour of Ireland being members of the EU, and support for the euro is at a similar level. However, there is a widespread sense of disappointment about the fact that the EU has bent over backwards to help Greece while Ireland's bailout conditions have not been eased, despite the country's "good management".

The extreme left Socialist Party has seized on the critical or negative attitudes towards the fiscal compact held by the working class and low-earners as evidence of a "class divide" in Irish society, because "the working-class people have been the biggest victims of austerity".[10] There is no doubt that the financial crisis caused by the previous government had hit low-earners and the unemployed particularly hard, although the Irish social security system has provided a cushion against most of the worst effects. But talk of a "class divide in Irish society" can be happily consigned to the realms of political propaganda. Rejection of the fiscal compact in the five constituencies that voted No was "only" between 51 and 55 per cent.

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What is more interesting, and in fact more significant for the future, is the realisation that there were more No voters among young people than among older sections of the population.[11] This may have been partly because of the fact that a very one-sided campaign was waged against the fiscal compact on Facebook.

THE RISE AND FALL OF IRELAND

The particular significance of the referendum and its outcome is apparent from Ireland's political, financial and social situation. The political "sensibility" of the Irish and their relations with the EU and particularly with Britain have their roots in the country's eventful history.

A Brief Look at Ireland's History

In the 17th century, three kingdoms were fighting for ascendancy in Ireland, triggering intervention on the part of England. Oliver Cromwell conquered Ireland for the English throne, destroying churches and monasteries and forcing Catholicism and Irish national culture to go underground.

10 | Cf. Carl O'Brien, "Far stronger No vote in poorer areas suggests shift to class politics for some", *The Irish Times*, 2 Jun 2012. The article quotes representatives of left-wing parties who believe there is evidence that in some sub-constituencies 80 per cent of voters rejected the fiscal compact.

11 | Cf. *The Irish Times*, 1 Jun 2012. The influence of Sinn Féin may also have had an impact. The party is gaining increasing support among younger people, a fact that is causing widespread concern.

England increased its power in the north of Ireland after massive waves of immigration from Scotland. As a result, the country's economy was largely dominated by the English aristocracy, leading to the widespread impoverishment of the Irish people, culminating in failed harvests and terrible famines in the mid-19th century. This, combined with large-scale emigration to the USA, England, Canada, Australia, New Zealand and Argentina, reduced the native population by almost one-third. It took until 1921 for the Irish to gain independence from the British after a long-drawn-out guerrilla war – sacrificing six of the northern counties. Until the 1990s, this resulted in bloody uprisings and terror attacks by the Irish and equally brutal reprisals by the British.

Until the 1970s, Ireland was dominated by its pre-independence history and by Catholicism. In the 1980s this was overlaid with a growing USA-oriented desire, to achieve massive economic growth. On the political stage, ideology played second fiddle to pragmatism. The two traditional parties, Fine Gael (meaning "family or tribe of the Irish") and Fianna Fáil ("soldiers of destiny"), emerged from the battle against the British, and their political manifestos are very similar. Ireland has never had a strong social democratic movement such as that seen in Scandinavia or Germany because the Irish parties mainly evolved out of resistance movements, and until the 1970s industry was very much secondary to agriculture. Therefore, the Labour Party has always stood in the shadows of the two main parties, but it has helped to shape the country's political landscape as a coalition partner, and it has gained more influence since the last elections in 2011.

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The Boom Years

When Ireland joined the European Economic Community (EEC) in 1973, the country was the poorest in the Community in terms of per capita income. It was largely thanks to EEC subsidies (structural funds, social funds, development funds, agricultural subsidies) that Ireland managed to close the gap with other EEC member states. This would not have happened without the efforts of the country's well-educated population; the way the EEC funds were invested

American companies were motivated by the lack of language difficulties and the relatively low rate of tax to use Ireland as a kind of "investment bridgehead" between the USA and the eurozone.

in a sensible and largely corruption-free way; and the decision by U.S. and European firms to open offices in Ireland, attracted by the possibility of skilled workers and – until the 1980s – low wages. American companies were also motivated by the lack of language difficulties and the relatively low rate of tax to use Ireland as a kind of "investment bridgehead" between the USA and the European single market and the eurozone.[12] In spite of a slump in the early 1990s, by 2007 Ireland had the second-highest per capita income in the EU after Luxembourg. Unemployment fell from as high as 20 per cent in the 1970s to 4 per cent in 2005. Between 1995 and 1999 the Irish economy showed average growth rates of 8.6 per cent, and between 2000 and 2007 the Irish economy did after all see an increase of 4.3 per cent per annum.[13] In 2007 there was another budget surplus. The country became known as the "Celtic Tiger", and its economic model seemed to have little in common with other countries that experienced crashes during the oil crisis or the economic crises that beset Asia and Russia.

This growth was fuelled by Ireland's traditionally strong agricultural economy, particularly in terms of processed agricultural products; a flourishing pharmaceutical industry with an equal focus on both the domestic and export markets; a successful IT and financial services sector; and particularly by the construction industry. Between 1993 and 2001, around 300 new, mainly high-tech businesses moved their operations to Ireland.[14] By 2007, 250,000

12 | The tax advantage played a major role in U.S. companies' investment decisions. The corporate tax rate in the USA stood at 35 per cent, while in Ireland it was just 12.5 per cent (to the detriment of Germany and France). If the United States introduces taxation on profits earned by U.S. firms abroad, a measure that has been announced by President Obama, then Ireland will become less attractive for U.S. direct investment.

13 | Economic and Social Research Institute (a government-funded think tank), annual reports. See also the optimistic analysis by Garret Fitzgerald (former Fine Gael prime minister), "Short-term pain should not blind us to bright future", *The Irish Times*, 17 May 2008. Similar arguments were made by Alan McQuaid (Chief Economist at Bloxham Stockbrokers) in 2007 in his article "'Celtic Tiger' could roar again soon", *The Irish Times*, 21 Sep 2007.

14 | Cf. Garret Fitzgerald, "What caused the Celtic Tiger phenomenon?", *The Irish Times*, 21 Jul 2007.

skilled workers had relocated to Ireland, many of them returning Irish emigrants or people of Irish descent.

However, the boom was somewhat curbed by rising prices, particularly in the construction industry (up to 70 per cent in some areas between 2000 and 2007), but this was largely balanced by sharp wage increases in both the private and public sectors. The minimum wage was increased to 8.65 euros, so in 2007 it was the second-highest nominal and sixth-highest inflation-adjusted minimum wage in the EU. Between 1995 and 2007, average wages and income increased by around 50 per cent.[15] During these boom years, it was easy for the government, employers and trade unions to see eye-to-eye. The country saw the emergence of what seemed to be a strong middle class with a great deal of purchasing power. Before 2008 there were still plenty of voices being raised – if somewhat tentatively – to warn that the dominance of the banking and construction sectors would lead to an unhealthy economic structure. After 2007, the Central Bank voiced concerns that the economy could overheat, but this failed to set off alarm signals in the government of the time under the recently re-elected Fianna Fáil party.

The Collapse of the Banks and Economic Decline

In September 2008, immediately after the collapse of Lehman Brothers, it became clear to even the most dyed-in-the-wool optimists that Ireland's newfound prosperity was mainly built on sand.

The Fianna Fáil government that ruled for 15 years (until 2011) felt "closer to Boston than Berlin" (in the words of one of its ministers), not only because of the massive direct investment made by major U.S. firms (such as Dell, Microsoft, Pfizer) and because of Irish companies' particular interest in the U.S. export market, but also because of the government's neo-liberal orientation.[16] In September 2008, immediately after the collapse of Lehman Brothers' Bank, it became clear to even the most dyed-in-the-wool optimists that Ireland's newfound prosperity was mainly built on sand, i.e. on credit. In order to avoid a similar Lehmanesque catastrophe, the government of the

15 | Central Statistics Office. A summary is also given in *The Irish Times*, 2 Feb 2012.

16 | The USA is also home to many influential Irish associations made up of Americans of Irish descent who are always keen to express their "nostalgic patriotism", not just at St. Patrick's Day parades.

time guaranteed "overnight" all the Irish banks' assets and liabilities, leading to a chain reaction in other European countries. The banking crisis and Ireland's subsequent sovereign debt and economic crises led to the incumbent government being voted out of power and had several causes:

- Following the example of the USA, interest rates on loans were set so low and the banks were so "generous" in giving loans that a great many people fell into debt, not just for investment purposes such as buying a house, but for buying "nouveau riche" luxury goods like holidays, expensive cars, Mediterranean holiday homes, etc. And it was not just well-off people who were tempted by the favourable U.S. dollar to fly to New York to do their Christmas shopping.[17]

- The banks were basically unregulated. It was common knowledge that the government did not want the supervisory authorities to regulate the banks too strictly.[18] As a result many excessively high loans were granted with very little security, leading to high levels of public debt after the government came to the aid of the banks in 2008. The lack of regulation meant that not enough was known about the true situation of the banks and their lending. The banks held no solidarity funds or crisis funds.

- A tax regulation allowed investments in land and in home building to be written off. As building costs increased on average by 60 to 70 per cent between 2000 and 2007, it seemed to make sense to invest profits from other economic sectors into the construction sector in order to reduce tax on earnings and income and achieve higher returns in future in the construction sector. Today there are countless houses and flats standing empty all across Ireland.

17 | Factually correct, but of course politically dubious, was Prime Minister Enda Kenny's statement at the Davos forum in January this year that one of the reasons for the crisis was that "…people simply went mad borrowing…".

18 | So it was possible for a manager at Bank A to let his bank borrow several million euros and then in November transfer it to Bank B (a bank run by a "friend") so that the borrowing would not appear on Bank A's balance sheet. Then the following January the manager at Bank A would take the borrowing back into "his" bank. The head of the Irish Financial Services Regulatory Authority resigned in January 2009.

- Because the Irish banks were having so much success granting loans in Ireland, they also began financing property in the USA and Britain. As a result, the fall-out from the Lehmans crisis hit the Irish banks twice as hard.

- There was a tight circle of "insiders" who carried out cosy transactions between its members. This "Golden Circle"[19] made up of bankers, construction magnates and financial speculators maintained close relations with the Fianna Fáil government. Corruption or objectionable and large-scale nepotism is hardly a rarity in politics. Bankers and construction magnates transferred huge amounts of assets to their wives, children, nephews, etc. before the crash, and it seems unlikely that the government of the time was unaware of what they were doing. This made it very difficult for the new Fine Gael/Labour coalition government that was elected in 2011 and the judiciary to retrieve these assets in order to cover the debts.

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- Fiscal policy also had an indirect impact. Although income tax rates are relatively high (with a top rate of 42 per cent being imposed on mid-level earnings), the rate of corporate tax at just 12.5 per cent is so low that medium-to-long-term investors were certainly attracted, but also financial speculators.[20]

Thus, along with healthy developments in the manufacturing and service industries, the modernisation of the agricultural sector, growth in exports and increased domestic demand, the boom years were to a large extent determined by speculation and by the hope that the economy would keep

19 | In 2010, the Think Tank for Action on Social Change (TASC) published a "map" of economic and social relationships among the upper echelons of Ireland's business leaders ("Mapping the Golden Circle", Dublin 2010). This showed very clearly how company directors worked together. This of course goes without saying in a small country like Ireland, but this fact should have made the regulators all the more vigilant.

20 | This is likely to have been one of the main reasons why the German Hypo Real Estate Holding AG set up the Dublin branch of the German DEPFA Bank, which was a major contributor to the losses suffered by Hypo Real Estate.

on growing.[21] For many people, the deeply-rooted Catholic principles of ethics that once had such a hold on Irish society had been crowded out by the economic boom. This was also aided and abetted by the Catholic Church's loss of credibility after the constant revelations of sexual abuse by priests and the cover-ups carried out by the Church authorities.

BUDGETARY AND FISCAL POLICY

The "marketisation of politics", an issue that was also part of the referendum on the fiscal compact, can also be expressed in concrete figures. The sudden boom makes it less interesting to look back at the figures before 2007. Until then, there was a lack of any sense that it is a good idea to build savings when times are good in order to have a cushion when times take a turn for the worse. Between 2000 and 2007 the level of debt was only 25 per cent of GDP, placing it well below the Maastricht criterion of 60 per cent.

Until 2007 there was a lack of any sense that it is a good idea to make savings when times are good in order to have a cushion when times take a turn for the worse.

This changed drastically in 2008, when the Fianna Fáil government took fright after the collapse of Lehmans and guaranteed the deposits and loans of six Irish banks, provided the banks with bailouts and nationalised the particularly ailing Anglo-Irish Bank (AIB). By the end of 2011, national debt had risen to 107 per cent of GDP (148 billion euros);[22] the 0.2 per cent budget surplus in 2007 (3 per cent in 2006) had turned into a deficit of 7.1 per cent of GDP by 2008 and by 2011 had risen to 10.1 per cent of

21 | Some sections of the middle classes also took part in this speculation, as they believed the property boom would continue. They sank their savings into property, but also took out mortgages that are now almost impossible to repay because property prices have dropped by 60 per cent since 2007 and many properties can no longer be rented. Young executives also often bought houses that were too large and too expensive because they assumed they would carry on climbing the career ladder and earning what at times were excessively high salaries. Those executives who lost their jobs are now deeply in debt and caught in the negative equity trap.

22 | According to figures from the IMF quoted in *The Irish Times* on 8 Aug 2011, Ireland's total debt (including private debt) stood at 196 billion euros or 43,838 euros per person (Germany: 32,499 euros). This is only 2 per cent of Europe's total debt (e.g. Italy: 23 per cent), so it should be dealt with within the EU.

GDP. In May 2010 the European Central Bank (ECB) began to buy Irish (and Portuguese) government bonds at an interest rate of around 5 per cent. By July 2011 this rate had increased to 14 per cent on the global money markets.

The public began to have the impression that the government would not be able to deal with the crisis, especially as the initial figures announced by the banks had been seriously sugar-coated. The worsening banking and financial crisis during 2008-2009 created increasing feelings of distrust among the Irish public. This fact, along with pressure applied by the media and the opposition, forced the government to request an EU bailout in November 2010. Just like Portugal, Ireland found itself obliged to allow the Troika to inspect its finances and hand out advice. Unmoved by the grumblings of the opposition and some members of the media about Ireland's loss of sovereignty, in November 2010 the government decided to seek shelter under the umbrella of the EU's rescue fund, receiving a bailout of 85 billion euros at an interest rate of 5.8 per cent.[23] The UK – themselves recipients of an IMF bailout in 1976 – offered an additional bilateral loan of 7 billion pounds.[24] Sweden – which like the UK is not a member of the eurozone – offered a further 500 million euros.[25]

Unmoved by the grumblings of the opposition about Ireland's loss of sovereignty, the government decided to seek shelter under the umbrella of the EU's rescue fund.

In this way, the Irish government was initially able to cover the majority of its bank debts and the capital needed to recapitalise its banks, and it did not have to make drastic cuts to social services in the areas of pensions, healthcare or education. The government also set up NAMA, the National Asset Management Agency, which "bought"

23 | This interest rate is relatively high by today's standards, though it is still much lower than the rate on the international money markets. It is currently under review by the Irish government and the EU. Ireland is hoping for a reduction, while the EU (particularly Germany and France) want a lessening of Ireland's tax advantages in return.

24 | This may also be due to the fact that Northern Ireland (as part of the United Kingdom) exports around two-fifths of its goods to the Republic of Ireland. A worsening of the economic crisis in Ireland would certainly have affected Northern Irish exports and caused employment problems.

25 | In the early 1990s Sweden was in financial difficulties, so the Swedish government bought bank debt and later offloaded it at a profit. Iceland and Latvia have also received assistance from Sweden.

receivables from the banks in the sum of 77 billion euros at discounts of between 30 and 50 per cent. This followed the Swedish model of the early 1990s. The projects that formed the subject of the loans – construction projects, land purchases, company expansions – are to be sold in the course of the next ten years so that the money can be returned to the taxpayer. The Anglo-Irish Bank, which was the most hard-hit because of poor management and reckless lending, became 100 per cent nationalised. Salary caps were imposed on those banks that were now partly state-owned, as happened in many other European countries. Public sector employees saw their salaries reduced by 20 per cent and were offered incentives to take early retirement. However, the ECB opposed the government's plan of imposing a Greek-style "haircut" on private and government bondholders.

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Between 2008 and 2011, these austerity measures and restrictions on lending led to many small businesses having to close their doors and to widespread lay-offs, causing the unemployment rate to jump to 14.7 per cent.[26] After the demonstrations in Greece, Italy and Spain, some European journalists wonder why the austerity measures have triggered relatively little protest in Ireland. This has nothing to do with lethargy or "fatalism" of the Irish, but has more to do with the following:

- The people were aware of the fact that they had elected the government (four times!) that led them into the crisis.
- The standard of living during the boom years was considered disproportionately high compared to other countries in Europe.
- People still had vivid memories of how much worse things had been in the past.
- The social support network (welfare payments, unemployment benefits, family solidarity) is still intact.

26 | From 2000 to 2004, the unemployment rate dropped to 4.3 per cent and shared with Luxembourg the lowest rate in the EU. In 2007 the unemployment rate increased to 5.5 per cent due to the slowdown in the global economy. The collapse of the service and tourism sectors, business closures and the crisis in the USA led to unemployment rocketing to 14.7 per cent in 2008/2009; since then it has only dropped slightly to 14.3 per cent.

- People wanted to give the new government a chance.[27]

It is of course possible that massive protests may have ensued, had the previous government not stepped down. Perhaps we can also say – with a grain of salt – that the behaviour of the Irish people is an expression of their national culture, and perhaps it is even a little "Catholic": we are all sinners and now we have to atone for our sins.

After signing the bailout agreement with the EU, the Fianna Fáil government threw in the towel and called early elections, which turned out to be a disaster for Fianna Fáil and the Greens[28] and which handed a clear majority to Fine Gael and the Labour Party.[29]

The new government entered office in March 2011 and began following the course that had been set out for them by the Troika. Along with public sector cuts and budget consolidation, its main priority is to create conditions for growth. Small and medium-sized enterprises, which suffered particularly badly when the banks cut their lending, are now to be supported with special loans. There is a sense of cautious optimism that the crisis can be brought under control in the foreseeable future. This is based on the fact that exports are continuing to flourish, and have enjoyed an increase of 5.5 per cent in 2011; that the economy is still competitive despite the closure of countless small businesses; and that domestic demand has only shrunk slightly. The new government's plan to create 100,000 new jobs certainly sounds somewhat over-optimistic, but at least they have made the commitment to increase their focus on the labour market[30] and create incentives for more investment on the part of both domestic and international companies.[31]

27 | This goodwill that was initially very strong seems to have now been exhausted, something that was particularly obvious during the public debate on the fiscal compact referendum.
28 | Fianna Fáil lost 57 of its 77 seats, the Green Party lost all its seats in parliament.
29 | Fine Gael won 77 and the Labour Party 38 of 166 seats.
30 | The unemployed are obliged to undertake further training or face cuts to their benefits.
31 | The government has been exercising intensive "economic diplomacy" in the EU countries, the USA, India and China. Particular significance was attributed to the recent visit of Chinese Vice-President Xi Jinping, who made Ireland his only stop in Europe after visiting the USA.

Unemployment is certainly the worst legacy left behind by the previous government. This problem is being artificially eased by the fact that young, well-educated Irish nationals are emigrating,[32] a "safety valve" that was traditionally used in Ireland between the 1860s and the 1960s.[33] This brain drain will of course also make it more difficult for Ireland's economy to get back on the path of recovery.[34]

The problem of unemployment is being artificially eased by the fact that young, well-educated Irish nationals are emigrating.

The consequences of the national debt that totalled 148 billion euros in November 2011 have been cushioned by the EU rescue package. The present government is abiding by the rules set out by the Troika, and this has led to increased confidence in the financial markets.[35]

The present government is planning to take the following actions to deal with the crisis:

- A budget adjustment of 3.8 billion euros.
- Spending cuts in the amount of 2.2 billion euros, with a view to reducing current spending by 1.5 billion and capital costs by 0.7 billion euros. The budget deficit has already dropped to 10.1 per cent of GDP (the Troika's upper limit was set at 10.6 per cent). According to the finance ministry, the deficit for 2012 will be 18.9 billion

32 | It is estimated that some 40,000 Irish nationals emigrated each year between 2009 and 2011. A survey of the emigrants showed that they were not unemployed; they were mostly young people who had jobs in Ireland, but who believed their prospects would be brighter in countries such as Canada, Australia and New Zealand. Cf. Fiachra Ó Cionnaith, "40,000 Irish-born people emigrated last year", *Irish Examiner*, 28 Jun 2012, http://irishexaminer.com/ireland/40000-irish-born-people-emigrated-last-year-198914.html (accessed 17 Jul 2012).

33 | In 1861 population levels of 4.5 million were only reached in 2011 thanks to a relatively high birth rate by European standards and to immigration from Central and Eastern Europe and Nigeria during the boom years.

34 | In order to justify the government's commitment to the banks, reference has often been made to the crisis in Argentina in 2000/2001. But this overlooks the fact that Argentina, like Sweden and later Iceland, had more flexibility due to the possibility of devaluing their national currency.

35 | This is expressed by falling interest rates for new or renewed government bonds. According to *The Irish Times* of 30 January 2012, on 26 January 2012 two-year bonds were swapped for three-year bonds, which entailed paying interest at 5.2 per cent. It is the aim of the government to only pay 4 per cent on two-year bonds and 5 per cent on five-year bonds.

euros (2011: 21.4 billion euros) and by 2015 it should have fallen to 7 billion euros, to 2.9 per cent of GDP, which would be within the 3 per cent target set by the Maastricht-Lisbon Treaty and the Fiscal Compact.

- Create additional revenue of 1.6 billion euros through additional taxes; since 1 January 2012, VAT has increased from 21 to 23 per cent and a property tax of 100 euros has been introduced; capital gains tax, energy tax and tax on cigarettes have all increased; and a land ownership tax is to be levied from 2013.
- Build approximately 400 million euros in public sector savings by downsizing 6,000 staff to 294,000.
- Improve the labour market by providing loans for small and medium-sized enterprises, 17 billion euros for capitalisation measures and 550 million euros for investment in research and development.
- Expanding trade with countries outside of Europe.

The new government has inherited a very difficult situation. It deserves to be supported by Europe as it works on resolving its financial problems, if necessary in the form of improved bailout conditions.

Table 2

Economic trends 2011 to 2015 (percentage change)

	2011	2012	2013	2014	2015
GDP growth	1.0	1.3	2.4	3.0	3.0
Domestic demand	-2.5	-1.3	0.0	1.0	1.2
Government spending	-3.0	-2.2	-2.2	-2.3	-2.1
Investment	-11.0	-1.0	3.2	4.6	4.8
Export	4.6	3.6	4.5	4.8	4.8
Import	1.6	1.6	2.8	3.4	3.8
Inflation	1.2	1.9	1.4	1.5	1.9
Employment	-1.9	0.2	0.8	1.2	1.6
Unemployment	14.3	14.1	13.5	12.9	11.6

Source: Department of Finance, Dublin forecast, Dec 2011.

In 2011, a positive growth figure was achieved for the first time since 2007, (one per cent, see Table 2). Based on the structure of the Irish economy and the work behaviour of the Irish people, it seems that the growth rates targeted for the next few years are not just pie-in-the-sky. Of course it should not be forgotten that the gap between high-earners and low-earners that widened still further during the boom years cannot be significantly closed by such relatively modest growth, particularly if exports continue to be more dynamic than domestic demand. As a result, social policy has to be made a top priority.

Whether the negative investment trend can be halted so quickly will depend to a great extent on the actions of the government and whether it can create a climate of confidence for foreign investors. At present it looks as if this could succeed, a fact that certainly contributed to the positive overall vote in the referendum on the fiscal compact. It is likely that any rapid reduction in unemployment figures, which are still forecast to be high in 2015, will depend primarily on the success of vocational training initiatives.[36] General education also needs to undergo a modernisation programme if Ireland's open economy is to remain competitive. If the forecast growth is achieved, then the projection shown below relating to financial governance is also realistic (Table 3).

Table 3
Financial governance, projection 2011-2015

	bn euros	**per cent of GDP**					
	2010	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Income	53.9	34.6	34.9	34.5	34.7	34.8	34.6
Expenditure	102.8	65.9	44.9	43.1	42.2	39.8	37.5
Borrowing	48.8	31.3	10.1	8.6	7.5	5.0	2.9
Interest payments	4.9	3.1	3.3	4.2	5.6	5.8	5.7

Source: Department of Finance, Dublin, Dec 2011.

36 | After previous scandals, new vocational training systems are now being established, but the results cannot yet be quantified.

The government is serious about cutting public spending, which also demonstrates its clear commitment to the fiscal compact. A restructuring of the public sector offers possibilities of making more savings without cutting welfare benefits. But of course whether these targets are achieved is not only dependent on the government and the Irish people. A less optimistic view of global economic trends would mean Ireland failing to meet the Maastricht criteria by 2015. It would have a better chance of hitting its targets if loan repayments were extended and the interest rate on the bailout were reduced.

Along with the debt problem, top priority is also being given to reducing unemployment. A new initiative entitled "Pathways to Work" offers assistance to people who are starting up new companies and advice for the unemployed at job centres. The government subsidises new appointments for 18 months and obliges unemployed persons to engage in further training and to accept jobs that are lower-paid than their previous work. The programme is particularly aimed at helping the long-term unemployed (more than 21 months) to re-integrate themselves into working life. A new initiative, Change Nation, plans to invite 50 leading social innovators and social entrepreneurs from all over the world to attend a conference in Dublin to further stimulate innovation, and existing competitions for young inventors will be intensified.

The government obliges unemployed people to engage in further training and to accept jobs that are lower-paid than their previous work.

It is not yet possible to assess the success of these initiatives, but one thing is certain: without them it would be even more difficult for Ireland to pull itself out of its current plight. To put it simply, it is a case of "roll up your sleeves, tighten your belts and create some initiatives". For observers who are interested in the stability of the EU and the euro, this attitude seems very positive compared to the "protest culture" that is prevalent in other debt-ridden EU countries.

Of course these policies have their nay-sayers. Criticism is particularly strong in socially-committed circles who rightly demand greater distributive justice; something they feel is so far missing in the government's programme. Despite the debt crisis, the country is still prosperous, but 20 to 25 per cent of the population are living on the poverty line. Along with unemployment and poverty, the most important social problem is the healthcare system, which has for years been unable to meet the needs of a modern, generally prosperous but aging society. The government's education cuts can also be viewed in a less-than-positive light. The political structure also needs to be modernised: there have long been calls to abolish the Senate, which is mainly made up of members of councils and committees and is increasingly seen as a relic of the past. There is also a need to reduce the size of parliament and modernise the ministries by increasing their specialist knowledge.[37]

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THE RAMIFICATIONS OF THE REFERENDUM

The result of the referendum on the fiscal compact clearly demonstrates that the Irish are well aware of the problems they face and realise that these problems have not only been caused by their governments and certain business sectors, primarily the banks, but that they themselves as voters and consumers also have to take their share of the blame. The present government is led by a prime minister who is working hard to find solutions to these problems, and he seems to have the support of a very effective cabinet. The finance minister and social protection minister in particular have a prominent role to play in facing the current challenges. The coalition seems to be working well. If we can believe public opinion – the Irish media is generally extremely critical – then we can expect the government to continue to produce positive results.

The private sector is also taking some positive steps, though it is still not doing enough. Many investors have increased their commitment to Ireland. According to the Swiss-based *World Competitiveness Yearbook*, Ireland has climbed to 20th in the world rankings. It still has major weaknesses in the area of lending but is at the top when it comes to

37 | Traditionally, ministers rely on the assistance of advisers. The new government has cut the formerly exorbitantly high salaries of these advisers, but are still spending around 3.2 million euros a year on them. *The Irish Times*, 28 Jan 2012.

qualifications, workforce flexibility, investment incentives and openness to the global market.[38]

In terms of financial and economic policy, the government is on the right track, as was further attested by the latest Troika assessment in April. Some voters may have been swayed by the fact that Ireland still needs more assistance from the EU, but the result of the referendum also shows that the Irish people want to support the direction the government is taking – that of cutting costs and stimulating growth. But the referendum has also given the government a warning that it needs to pay even more attention to its social policies. Economic recovery will only happen as planned by 2020 if the gap between the richer and poorer elements of society is reduced and if general and vocational education is improved.

This referendum will certainly not be the last referendum on Europe if efforts continue to create closer financial, economic and social ties with Europe and if the Eurozone does not fall apart. So it is likely that the Irish people will have many more opportunities in mid-term to express their opinions on issues relating to Europe and the government's direction. The inevitable loss of sovereignty that will accompany closer European integration will, in turn, certainly cause some political irritations, particularly on the part of Sinn Féin. This argument can best be countered by reducing the country's dependency on EU and ECB funds – so through fiscal consolidation. In this way, Ireland can be better helped by easing the EU bailout conditions set in 2010 than by providing more funding. Perhaps the next EU fiscal compact should not only allow for the imposition of penalties, but also for the granting of rewards to countries that maintain sensible financial policies.

38 | Cf. *The Irish Times*, 1 Jun 2012.