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**The Irish social partnership and the
“celtic tiger” phenomenon**

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International Institute for Labour Studies Geneva

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Introduction*

Ireland is the miracle economy of the 1990s. In 15 years, it transformed itself from one of the poorest countries in Europe into one of the richest. Ireland's record compares favorably not just with other, much touted examples of economic success in the last few years, like the Netherlands and the US, but also with Asian "tigers," even before the latter's economic setbacks of the late 1990s. Understanding the sources of Ireland's economic success is therefore relevant for a much wider audience than just the people of the Emerald Isle.

The country's economic transformation began in 1987 and overlapped in time with the institutionalization of social partnership, that is, the centralized determination of wage increases through three-year collective agreements. Much of the economic literature discounts this overlap as sheer coincidence.¹ Other factors, particularly massive FDI inflows but also clairvoyant educational policies that increased the supply of skilled labor at a time in which demand was also increasing, are held responsible for the country's remarkable performance. Social partnership is, according to these views, at best epiphenomenal, at worst counterproductive. However, if one reads other literatures (e.g. NESC, various years; O'Donnell and O'Reardon, 1997; 2000; Mac Sharry and White, 2000; Auer, 2000) or talks with the policy-makers, one hears the opposite view, namely that social partnership played a fundamental role in the making of Ireland's economic miracle. This more positive assessment seems to be shared by the Irish population as a whole. In 1999, 78 percent of poll respondents agreed that social partnership was important for Ireland's economic success (Fitzgerald and Girvin, 2000: 283).

In this paper, we seek to understand in what ways, if any, social partnership contributed to the "Celtic Tiger" phenomenon as well as the political process through which centralized wage determination was initiated and sustained over time. Our analysis centers on the notion of competitiveness gains, which we define as reductions in unit wage costs. We argue that social partnership introduced important changes in the process of wage formation in this country. Thanks to social partnership, wage increases in the "dynamic" multinational sector (characterized by high productivity growth) came to be tightly linked with wage and productivity increases in the much more sluggish domestic portion of the manufacturing sector. This represented an important departure from the recent past, when wage settlements struck in the high productivity sector had unduly influenced the process of wage formation in the economy as a whole and thus led to labor shedding in the low productivity sectors (Baker, 1988; Barry and Hannan, 1995; Barry, 1996).

Both the economics and the politics of social partnership in Ireland are significantly different from the traditional Scandinavian model of centralized wage bargaining in a small open economy. The Scandinavian model is based on a key distinction between exposed and protected sectors (Aukrust, 1977; Edgren et al., 1973; Flanagan et al., 1983). The Irish economy is, however, more appropriately conceptualized as a three-sector economy, with a non-exposed sector, a high-tech/high productivity, "modern" manufacturing sector (mostly foreign-owned), and a low productivity, "traditional" manufacturing sector (mostly domestic).

Linked with the particular features of the Irish economy, the Irish social partnership defies much received wisdom about the politics of centralized wage restraint. It is often argued that wage centralization is only advisable in countries where strong unions in the exposed sectors shape the wage policy of the

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¹ These skeptical views on the effectiveness of incomes policies are not just limited to Ireland. For similar considerations concerning other countries, see Locarno and Rossi, 1995; Dornbusch, 1991.

labor movement as a whole, and that the benefits of centralization are lost in countries where public sector unions wield enough power to decisively influence the choices of union confederations (Garrett and Way, 1999; Crouch, 1988; Franzese, 2001).

Yet this line of reasoning does not apply to Ireland. In this country, public sector unions were not only much stronger than private sector ones, they also played, in partnership with general unions, a key role in initiating and sustaining the Irish social partnership. Private sector unions (that is, the craft unions) opposed, often vociferously, centralized wage regulation. Given the huge profitability of the private sector, these unions thought they could get higher wage increases by negotiating alone than through central bargains.

Support from the public sector unions did not come without costs. The Irish social partnership has not been a model of public sector wage restraint. Public sector wages grew faster than private sector ones, and faster than in other countries (see OECD, 2001). However, because private sector wages were linked to the productivity gains of the less dynamic manufacturing sectors, it was possible for the public sector to exercise a role of wage leadership without seriously undermining the competitiveness of the Irish more dynamic sectors and linked to this, of the Irish economy as a whole.

The remainder of the paper is organized as follows. Section 1 reconstructs the trajectory of social partnership over time. Section 2 summarizes a number of explanations for Ireland's economic performance. Section 3 analyzes wage and productivity trends in different industries. Section 4 examines the configuration of pro-partnership coalitions as well as the determinants of compliance with centralized provisions. Section 5 concludes.

1. The development of the Irish social partnership

In 1987, when the Programme for National Recovery (PNR) – the first of five successive partnership agreements – was negotiated, Ireland was faced with a serious economic crisis. Government debt and deficit were skyrocketing,² investments were stagnant, and, undeterred by emigration, unemployment was on the rise (Government of Ireland, 1987).

With the PNR, the Irish Congress of Trade Unions (ICTU) agreed to limit wage increases to 3 percent for the first £120 of weekly pay and 2 percent for the part exceeding £120 for each of the three years covered by the agreement. The minimum increase was £4 per week. Also, the ICTU committed itself not to take industrial action that would result in additional cost increases for the employers.³ This latter clause signaled an important departure from the practice of two-tier bargaining that had characterized previous centralized agreements in the 1970s (Hardiman, 1988; Roche, 1997; Mooney, 1978). In exchange, government agreed to reform the tax system so that take-home pay would be increased. Government also agreed to keep the value of social welfare allowances unaltered.

Negotiation of the PNR was preceded by a wide-ranging strategy report prepared by the National Economic and Social Council (NESC), a tripartite consultative body (NESC, 1986). While falling short of explicitly advocating incomes policies, this report laid out the conceptual architecture for the PNR as well as the other social partnership agreements that followed. It underlined the importance of a stable macroeconomic framework, to be achieved by reducing public expenditures and public debt and through a stable exchange rate policy. It emphasized the need to enhance competitiveness of the traded sectors by keeping average cost increases below the weighted average of Ireland's major trading partners. Finally, it underscored the need to simultaneously reduce personal tax rates and expand the tax base.

The PNR was a consensual document, produced and signed by all the social partners, including the unions. It signaled that at least at the peak level, all major socioeconomic actors had come to share the same analysis of the Irish economy (O'Donnell and O'Reardon, 1996). This was different from the past.

² According to NESC (1993: 155), debt servicing consumed one third of tax revenues per year.

³ The only ground for decentralized bargaining contemplated in the agreement was for the constitution of pension or sick leave schemes where they did not already exist.

In fact, previous centralized wage negotiations in the 1970s had been marred by lack of consensus on the main determinants of economic crisis. The employers and (to a lesser extent) the government linked unemployment to excessive wage demands that diminished the competitiveness of Irish tradable sectors in international markets. The unions entertained a different view, namely that unemployment was the result of insufficient domestic demand and was to be combated through public job creation (Roche, 1997: 189-90).

During the three years covered by the PNR (1988-90), the Irish economy performed extremely well. GNP grew strongly (3.6 percent per year) and led to improvements in virtually all other macroeconomic indicators. Interestingly enough, the combination of small nominal wage increases, low inflation, and tax reductions led to higher real disposable wages between 1988 and 1990. In the previous period of free-for-all collective bargaining between 1980 and 1987, real take-home pay had, instead, declined (NESC, 1993: 46).

After this encouraging beginning, social partnership became the backbone of Irish economic policy. Each three years, a new agreement was approved. These agreements contained both wage guidelines (see Table 1) and a number of social and economic measures. Also, each new agreement was preceded by a NESC Strategy Report, which provided the analytical underpinnings for discussion on specific issues. In 1991, the Programme for Economic and Social Progress (Government of Ireland, 1991) reintroduced the notion of two-tier bargaining, which had been a characteristic feature of centralized agreements in the 1970s (Hardiman, 1988; Roche, 1997). In fact, it established that "exceptionally," wage increases up to three percent could be negotiated at decentralized level in addition to increases distributed centrally. Not surprisingly, a sizeable proportion of local agreements implemented the 3 percent clause. However, the employers sought to link payments to workplace restructuring and productivity increases (Roche, 1997: 208).

With the PESp, the social partnership approach was extended to the local level as well through the so-called "Area-Based Response to Long-Term Unemployment" (ABR) (Government of Ireland, 1991). Local companies composed of representatives of the traditional social partners, public officers, and – interesting innovation – members of other voluntary organizations, especially associations of the unemployed, were constituted in particular areas. They were charged with the task of designing and implementing appropriate employment policies in their areas of jurisdiction (Sabel, 1996; Walsh et al., 1998).

The early 1990s were difficult years for Ireland as growth subsided and unemployment began to grow again. Social partnership, however, managed to overcome this cyclical contraction. The 1994 Programme for Competitiveness and Work (PCW) focused on employment creation. There were no major changes in strategy compared with previous years. Monetary policy continued to aim for steady exchange rates within the European Exchange Rate Mechanism (ERM). Fiscal policy continued to be restrictive. The key to sustained growth and employment creation continued to be the notion of competitiveness. This implied a continued policy of wage moderation, further reductions in the tax wedge (difference between gross income and take-home pay), controls over public sector expenditures, and measures to increase the efficiency of the non-traded sectors of the economy (NESC, 1993). A clause in the PCW allowed for additional bargaining over wages at the decentralized level only in case percentage increases were lower than 3.5 pounds per week in the private sector and 2.8 pounds per week in the public sector (Government of Ireland, 1994).

The 1996 Partnership 2000 (P2000) agreement centered on two distinct themes: the need to extend social partnership to the enterprise level and the need to reduce social disparities and exclusion (NESC; 1996; Government of Ireland, 1996). The focus on enterprise-level partnership was based on the belief that as at the national level, at the workplace level, too, cooperative relationships between labor and management could be instrumental to increase competitiveness and reap mutual gains. The agreement was exhortatory rather than prescriptive in this regard, however. Perhaps for this reason, partnership at the enterprise level does not seem to have diffused widely in Ireland (Roche and Geary, 2000; Gunnigle et al.,

1999).⁴

The theme of social exclusion was linked to a major innovation in the institutional structure of social partnership at the national level, namely the inclusion of voluntary and community organizations in the bargaining process (O'Donnell and O'Reardon, 2000; O'Donnell, 2001). This "social" pillar, mainly composed of religious, women, youth, and unemployed organizations, had been lobbying for accession to the bargaining table since the early 1990s. It was finally admitted in 1996. P2000 contained policy initiatives aimed at social exclusion, involving additional expenditures of £525 million.⁵ According to Gunnigle et al. (1999: 217), these social measures sought to satisfy the concerns of the social pillar. Wage negotiations remained the province of the traditional tripartite partners, however. P2000 maintained the ban on decentralized wage negotiations except in cases where nationally distributed increases were lower than certain minima. These minima were, however, set at even lower levels than in the previous agreement (£3.5 per week, £2.4 per week, and £1.6 per week in the second, third and fourth phases of the agreement, respectively).

With the 2000 Programme for Prosperity and Fairness (PPF), social partnership shifted its emphasis from macroeconomic policy to more supply side-oriented policies. Unemployment was no longer the most pressing problem; labor and skill shortages were (Government of Ireland, 2000; NES, 1999). The agreement contained a series of recommendations on issues like skill development, infrastructural investments (e.g. roads and public transportation), the provision of more affordable housing, and the development of childcare facilities. Social policies were also devoted a significant amount of attention. In particular, the parties agreed on the need to develop a series of indicators to monitor progress in this field.

The wage portion of the agreement was similar to the past. This time, however, minimum increases were much higher than in previous agreements. The parties also agreed to engage in a thorough revision of pay determination in the public sector aimed at introducing clearer links between pay and performance and comparability with private sector jobs requiring similar skills. In December 2000, the resurgence of inflation in Ireland led to an additional round of pay negotiations. These provided for additional wage increases at the national level. They also introduced the possibility for decentralized bargaining for amounts up to 2 percent of basic pay (plus a one-off lump sum increase of 1 percent).

As the above overview has shown, the basic structure of the Irish social partnership agreements remained more or less the same over time. Against the background of fiscal conservatism and monetary orthodoxy, these agreements exchanged wage restraint for tax cuts.⁶ At the same time, social partnership sought to target the worst kinds of social inequalities and exclusion, first by keeping constant the real value of transfers, and then, when the public coffers had been replenished through several years of sustained growth, through more substantive measures.

So far, the Irish social partnership has proven remarkably resilient, even though it is unclear how it will respond to the wage pressures that have recently begun to emerge. Introduced to deal with a major economic crisis and two-digit unemployment rates, social partnership was later adapted to the new era of full employment and labor market shortages. In the process, it absorbed and processed a variety of new, supply-side issues. Social partnership also managed to navigate safely through major changes in the political environment. During the 1990s, all main political parties in Ireland (Fianna Fail, Fine Gael, Labour, and Progressive Democrats) were involved in government at some point and as such, all had direct involvement with social partnership. While social partnership has been a permanent feature of the Irish political economy in the last 15 years, there is still much debate as to whether it really made a contribution to the Irish economic miracle and if so, of what kind. The next section reviews this debate.

⁴ For different views on this theme, see O'Donnell and Teague (2000).

⁵ Additional £900 million were devoted to cuts in personal taxes.

⁶ In this regard, the PPF contains the following, important statement: "The social partners support the policy of establishing a single standard rate income tax band for all individual tax payers" (Government of Ireland, 2000: 11).

2. Does social partnership matter?

Between 1988 and 2000, the performance of the Irish economy was impressive. Real GDP grew 132 percent, compared with 45 percent in the US and the Netherlands, 32 percent in the EU as a whole, and 29 percent in the UK. In the same years, unemployment fell from 16.2 percent to 4.2, practically the same figure as the US and well below the EU average of 8.2 percent (see Figure 1). As argued by the OECD (1999), the sources of Ireland's outstanding economic record are to be found in a combination of different variables, not in a single variable. Virtually all sources underscore the importance of multinational investments in explaining the remarkable performance of the Irish economy (see, for example, Barry, 1999; Barry et al., 1999; Murphy, 2000). Others emphasize the clairvoyance of educational policies that increased the supply of skills at a time in which their demand was also increasing and hence, contributed to keep the price of skilled labor low (Fitz Gerald, 2000). Quite surprisingly, social partnership is rarely included in the package.

In fact, economists have often expressed skeptical views as to whether social partnership really played an important role in the Irish success story. Early on, Bradley et al. (1991: 9-10) set the tone of the debate by arguing that according to their model of the Irish economy,⁷ wage disinflation was not the product of the PNR social partnership agreement. In fact, the same variables that had proved adequate in explaining wage formation in the 1960s and 1970s – namely, 1) output price variation (assumed to be exogenous and equal to world levels for the industrial sector); 2) the tax wedge (difference between gross product wage and net take-home consumption wage); 3) unemployment; and 4) labor productivity growth – also proved appropriate in the late 1980s. In other words, there was no evidence of a break in wage behavior, which could be traced back to the partnership agreement. In the authors' opinion, the benefits of centralized bargaining were more in bringing about industrial peace than in lowering wage increases. This assessment was echoed by other, sometimes much harsher views expressed later in the decade.

Durkan, for example, (1992: 358) argued that the PNR agreement had had a negative impact on the Irish economy. The wage rates negotiated centrally were higher, the author argued, than the economy could afford and they would have been lower had decentralized bargaining continued. The reason why the agreement was negotiated had to do, according to the author, solely with industrial relations purposes, and particularly with the need to reduce industrial conflict at the workplace level. Even for this purpose, however, a centralized agreement was unnecessary. High unemployment alone would have sufficed to tame the unions, as demonstrated by the experience of 1981, when centralized bargaining broke down but no increase in industrial disputes was registered. Tansey (1992: 368) brought Durkan's views to their logical conclusions and proposed to discontinue the experience of centralized bargaining and return to decentralized bargaining at the expiration of the PESP.

These skeptical assessments are not just a feature of the past, namely of a period in which the Irish economy was still in the doldrums and it was unclear what impact, if any, social partnership was having on it. More recently, and in completely different economic circumstances, Fitz Gerald (1999: 160) has argued that the effects of the partnership approach have been largely overestimated. This author acknowledges social partnership's role in reducing the levels of conflict in the country. In this regard only, social partnership has had beneficial consequences for the performance of the Irish economy. Social partnership, however, has had no independent effect on wage moderation. It has just "validate[d] the results which market forces had made inevitable." (Fitz Gerald, 1999: 162). Among these market forces, this author emphasizes the role of Ireland's unusually elastic labor supply curve (particularly due to migration, as well as increasing female participation) in keeping wages under control.

Along similar lines, Walsh, too, (1999: 223) explains wage moderation through the combination of "the initial slack labor market conditions and the very elastic supply of labor." This author's analysis of the Irish economic success is the following:

"A combination of low inflation, rapid gains in productivity, and a stable effective nominal exchange

⁷ This was the Economic and Social Research Institute (ESRI) Medium-Term model (see Bradley and Fitz Gerald, 1991).

rate resulted in pronounced gains in competitiveness to industry since the middle-1980s. This operated like a successful devaluation, stimulating demands for Irish exports ... Combined with the high initial level of unemployment and the rapid growth of the working-age population, it facilitated rapid growth of employment combined with low wage inflation.” (Walsh, 1999: 220).

Like other economists, Walsh, too, (1999) is unwilling to attribute low wage inflation to an institutional factor, namely social partnership, and prefers to explain it with a combination of various supply-side factors like initial slack labor, ease of migration, rising working age population, and rising female participation (in turn, correlated with educational achievement and hence, with the supply of skills). Incidentally, the importance attributed to slack labor is in conflict with the author’s assertion that “the role of the unemployment rate in the Irish wage formation process is weak.” (Walsh, 1999: 205).

Another line of argument is more generous towards social partnership arrangements and considers them to be one element in a broader policy mix leading to “expansionary fiscal contractions.” The core argument in this literature is that a particular type of fiscal adjustment package – one in which cuts in public expenditures (as opposed to tax increases) play a pivotal role – contributes to boost a country’s competitiveness (Alesina and Perotti, 1997). Nominal exchange rate devaluations and incomes policy arrangements constitute additional accessory elements in this policy mix. In the late 1980s, Ireland experienced drastic fiscal correction, with public debt falling by 14 percent of GDP between 1990-91 (the period after fiscal contraction) and 1985-86 (the period before), and primary adjusted public deficit declining by almost 8 percent of GDP in the same period (see Alesina and Ardagna, 1998: 535).⁸ This fiscal correction attracted a lot of international attention, because it was associated with economic expansion rather than the traditional recessionary effects one would expect based on standard Keynesian theory.

One explanation for expansionary fiscal contraction emphasizes the role of expectations (Giavazzi and Pagano, 1990) in increasing private consumption. Adjustments based on public spending cuts signal (when credible) that future taxes will be lower than in the past and thus, increase present consumption (see also Alogoskoufis, 1992; Geary, 1992: 60). Empirically, expansion depends on whether the effect on expectations dominates the reduction in public consumption. The macroeconomic evidence, however, does not seem to support this explanation based on the role of private consumption. This remained stable in Ireland (as percentage of GDP) in the period before and after fiscal consolidation. The two drivers of growth seem to have been private investments and foreign trade (Alesina and Ardagna, 1998: 536).

An account of the Irish story, which is consistent with these data has been provided by Alesina and co-authors in various articles focusing on fiscal adjustment in OECD countries (see, for example, Alesina and Perotti, 1997b; Alesina and Ardagna, 1998). This literature starts from the basic insight that the internal composition of adjustment packages matters and that while adjustments based on tax increases are deflationary (through the traditional Keynesian mechanisms), adjustments based on expenditure cuts are expansionary, especially when they are based on reductions in the government wage bill and/or on cuts in social transfers. The mechanisms through which expenditure-based adjustment packages translate into economic recovery have little to do, however, with the role of expectations and more with traditional supply-side factors linked with competitiveness, that is, reductions in unit labor costs relative to trade competitors (Alesina and Perotti, 1997). In this regard, this literature also features a role for social partnership-like agreements with trade unions.

The supply-side mechanisms are most clearly spelled out in Alesina et al. (2002). The increase in competitiveness materializes through labor market channels. Cuts in public sector employment lower private sector wages by increasing labor supply and reducing the private sector workers’ reservation wage. Similarly, cuts in income taxes reduce wage demands by the unions (Alesina et al., 2002: 573). Both channels reduce labor costs and increase profits. Higher profits, in turn, translate into greater investments.

⁸ Primary adjusted public deficit is adjusted for the effects of economic cycle by estimating what the government budget would have been had unemployment remained the same as in the previous year. See Alesina and Ardagna (1998: 544) for details.

These competitiveness gains are especially pronounced when (as in the Irish case) fiscal adjustment is preceded by an exchange rate devaluation and an incomes policy negotiated with the unions (Alesina and Ardagna, 1998). The Irish pound was devaluated by 8 percent vis-à-vis other currencies in the European Monetary System in August 1986. Also, the PNR agreement contributed to transform the nominal depreciation into a real one by keeping wage costs low. An agreement with the unions seems to be an important element of expansionary fiscal contraction packages for political reasons as well. In fact, cuts in public wages and employment may be very difficult to implement without union consent.

While more favorably inclined towards social partnership than the other arguments examined above, this line of argument shares with the former a style of analysis based on aggregate, economy-wide data.⁹ This approach may be ill suited to the Irish case, given the dualistic structure of the Irish economy. This is divided into foreign and domestic components, each characterized by completely different conditions of efficiency and profitability. The next section moves from the national level to industry-level analysis. Our focus is on the manufacturing sector because this sector has been an engine of growth for the Irish economy as a whole, according to virtually all commentators. We seek to understand how an internally diverse industrial structure interacts with wage setting rules to produce different conditions of competitiveness.

3. Multinationals, social partnership, and the "Irish disease"

One element that virtually all commentators single out as crucial for Ireland's economic success is the role of multinational companies (MNCs), particularly American. According to a widely-shared view (well exemplified by Murphy (2000)), US MNCs were on the lookout for a European base in preparation for the 1992 completion of the single market. Ireland was their nation of choice for various reasons, including very low corporate tax rates and a staunch commitment to European integration (unlike in the UK), but also the availability of an English-speaking as well as relatively well educated labor force. Based on these considerations, Murphy (2000: 14) argues that: "a considerable part of the economic growth witnessed in Ireland is US growth that was waiting to happen somewhere in Europe."

a) The role of multinationals

There is no doubt that multinational companies are of fundamental importance for the Irish economy. Already in 1985, the first year for which data are available,¹⁰ foreign firms accounted for 50 percent of gross output (32 percent for US firms) and 41 percent of manufacturing employment (20 percent for US-owned firms), even though they represented only 16 percent of the total number of Irish manufacturing establishments (6 percent for US firms). These figures indicate that the scale of foreign establishments was and still is much greater than that of domestic ones (see Table 2).

In 1998, the last year for which data are available, the weight of MNCs had further increased. They accounted for 72 percent of gross output (54 percent for US-owned firms), 47 percent of manufacturing employment (27 percent for US firms), and 15 percent of the number of establishments (6 percent for US

⁹ Honohan (1999) has cast doubt on the applicability of the arguments advanced by Alesina and co-authors to Ireland. It is unclear whether the Irish adjustment really qualifies as expenditure-based as opposed to tax-based (see Honohan, 1992). Cuts in taxes are only perceptible if they are expressed as percentage of GDP. In real terms, taxes increased by 11 percent between 1987 and 1990. Real public sector wages declined between 1987 and 1988 and then between 1988 and 1989, but returned to their previous levels in 1990, and even slightly exceeded the initial levels. Similarly, real cuts in transfers were minimal between 1987 and 1990 (-1.7 percent) (Honohan, 1992: 301; see also Callan and Nolan, 1992; O'Reardon, 1999). These small magnitudes make one question the validity of an argument that attributes primary responsibility for Ireland's boost in competitiveness to the particular features of the fiscal adjustment program.

¹⁰ These data are based on the yearly Census of Industrial Production.

firms).¹¹ Between 1985 and 1998, MNCs performed much better than their domestic counterparts. The domestic establishments increased employment by 15 percent and gross output by 87 percent. The foreign sector increased employment by 51 percent (80 percent for US firms) and gross output by 383 percent (469 percent for US firms). By looking at these numbers, there is no doubt that MNCs have been the propulsive force behind Ireland's recent economic success.

Interestingly enough, MNCs are concentrated in sectors (like the data processing, electronic, or pharmaceutical sectors) in which Ireland does not have a comparative advantage (Barry et al., 1999). Nonetheless, data on backward linkages show that foreign companies are not only well-embedded in the local economy, but also that their local linkages are increasing over time. In 1991, for every 100 jobs in foreign manufacturing, there were additional 46 service jobs (40 in 1983) and 16 manufacturing jobs (12 in 1983) in input-producing sectors. The numbers for domestic manufacturing were similar but slightly lower: 34 service (36 in 1983) and 17 manufacturing jobs (19 in 1983) (see Barry et al, 1999: Table 3.8, based on O'Malley, 1995).¹²

The major problem with an explanation solely based on the role of the MNCs is timing. MNCs are not new to the Irish scene. In 1985, the number of foreign manufacturing establishments was higher than in 1998. Also, there were almost as many US establishments as in 1998 (see Table 2). Beginning with the abolition of the Control of Manufactures Act in the late 1950s – an Act which prohibited foreign ownership of Irish assets – foreign investment has been systematically pursued by the Irish policy-making authorities (particularly in high-tech sectors) through location grants and a zero corporate tax regime, later substituted with a 10 percent tax on all manufacturing (Barry et al., 1999: 45). It needs to be explained why the performance of MNCs increased dramatically between the late 1980s and the 1990s.

b) The moral economy of wages and the "Irish disease"

Until few years ago, MNCs were held responsible for a peculiarly "Irish" disease. Because they had greater capacity to pay than domestic companies, MNCs set wage increases at higher levels than their domestic counterparts could afford. Due to comparability claims, however, high wage settlements in the high productivity MNC sector had a tendency to spread to the other, less dynamic sectors as well, and therefore caused cost problems in the domestic sector (Barry 1996; Barry and Hannan; 1995).

These conclusions were based on an inter-industry analysis of wage and productivity trends by the Economic and Social Research Institute (Baker, 1988; see also Baker, 1985). This analysis divided the Irish manufacturing sector into 'modern' and 'traditional' portions and then calculated wage and productivity trends for both. The modern sector included some of the most dynamic and technology intensive industries, mostly foreign-owned, i.e., pharmaceuticals, office and data-processing (ODP) machinery, electrical engineering, and the more capital-intensive portion of the food industry, particularly production of cola concentrates. The traditional sector included all other industries.

¹¹ Gross output figures are generally inflated by the transfer pricing practices of MNCs. Given the favorable tax regime, these have an interest in attributing to their Irish subsidiaries as great a proportion of global profits as possible. Changes in gross output should be less affected by these transfer-pricing practices, albeit not entirely exempt. To have an idea of how transfer-pricing practices may affect change data as well, it is helpful to confront GDP data (which include MNCs' repatriated profits) with GNP data (which exclude them). If in 1987 Irish GNP was 10 percent lower than GDP, in 1998 the gap had risen to 12.17 percent.

¹² Between 1988 and 1997, FDI flows increased from 91 to 1676 million US\$. In this period, the proportion of FDI originating from NAFTA countries grew from 53 to 86 percent (OECD, 2000). Between 1989 and 1999, FDI flows as percentage of GDP increased faster in Ireland than in most other countries (OECD, 2001b). However, Ireland started from very low levels in 1989. In 1999, Irish FDI inflows as percentage of GDP were still lower than in Sweden and Holland – economies that did not experience the same rate of spectacular growth as Ireland. It looks as though Ireland caught up with other countries in terms of FDI inflows rather than outperform them.

The results of this analysis, summarized in Figure 2, showed that between 1980 and 1987, a period in which Irish collective bargaining was decentralized, average weekly earnings increased at more or less the same pace in the modern and traditional sectors. Productivity, however, grew much faster in the former than in the latter. In other words, wage settlements in the modern sectors of the economy (which could afford them) seemed to trickle down to the more traditional sectors as well, even though there were marked differences in productivity trends. The consequence was that while the modern sector reduced unit wage costs and gained competitiveness (even when unit wage costs were adjusted for changes in exchange rates) (Baker, 1988), the traditional sector experienced cost problems and shrank.

The employment performance of the two sectors varied accordingly. While employment increased by 21.9 percent in the modern sector, it declined by 26.9 percent in the traditional sector. In other words, employment creation in the more dynamic industries was unable to compensate for labor shedding in the other industries. In fact, between 1980 and 1987, the Irish manufacturing sector as a whole lost 19.6 percent of its workforce (Baker, 1988: Table A2, p. 35).

These data dovetail with more qualitative accounts of industrial relations practices in Ireland, which emphasize the importance of wage norms and in general, of the "moral economy" (Swenson, 1989) in explaining wage determination. Between the 1970s and the 1990s, the Irish industrial relations system oscillated between centralized and decentralized bargaining. Even when wage bargaining was decentralized, wage increases seemed to be more responsive to particular wage norms, like the notion of a "going" wage increase, than to differences in productivity gains across sectors and companies. These institutional influences on wage setting were linked to a long-standing feature of Irish wage negotiations, the notion of "pay" or "wage" rounds (Roche, 1997).

From 1946 until 1970, Irish industrial relations were dominated by pay rounds, namely by decentralized negotiations taking place more or less synchronically. These started when the war ban on wage negotiations was lifted and all bargaining groups found themselves negotiating at the same time. With pay rounds, trade union officials became accustomed to the idea of a going rate of increase (Roche, 1997: 168). Comparisons among bargaining groups, much more than economic conditions, played a key role determining wage outcomes in these rounds.

McCarthy et al. (1975) conducted an in-depth analysis of the six pay rounds between 1959 and 1970. They found that "wage rounds tend[ed] to set a rate of increase below which it [wa]s difficult for employers to settle for any length of time, regardless of the state of their firm or industry." (McCarthy et al, 1975: 40). These authors' survey results indicated that 56 percent of trade union leaders perceived pay rounds to be "a short period in which every worker gets a similar (but not necessarily identical) wage increase." A sizeable minority of trade unions leaders (17.8 percent) even perceived them to be a "short period in which every worker g[ot] the same (cash) wage increase." (McCarthy et al., 1975: 29) Finally, McCarthy et al. (1975) also identified a number of key wage bargains involving skilled workers (e.g., electrical and maintenance craftsmen as well as construction workers), which acted as wage leaders, namely "appear[ed] to induce other groups, which [we]re not directly involved, to seek similar increases" (p. 55).

In the 1970s, concerns with the inflationary consequences of decentralized negotiations led to bargaining centralization (Roche, 1997: 177; Gunnigle et al., 1999: 193). Centralized wage agreements set basic wage increases for all sectors as a whole but also included provisions for so-called "above-the-norm" (or "below-the norm") increases to be negotiated at the local level. Just as in the previous period, issues of comparability played an important role. A built-in element in national pay bargaining was compression of wage differentials through a variety of mechanisms including lump-sum increases, minimum and maximum cash increases, and tapered percentage increases favoring the low-paid (Roche, 1997: 180; Gunnigle et al., 1999: 196). Decentralized negotiations compensated for the leveling effects of centralized bargaining, however, and re-established (or even widened) existing wage relativities.

Peter J. Money (1978: Table 4, p. 246) provided estimates of the distributional consequences of so-called "National Agreements" in the 1970s. Between 1970 and 1977 (a period covered by six National Agreements, the effect of central wage increases would have been to improve the relative position of the lower-paid. In fact, average hourly earnings should have increased by 163 percent (men) and 263 percent

(women) in low-paying industries; 152 percent (men) and 249 percent (women) in middle-paying industries; and 142 percent (men) and 222 percent (women) in high paying industries, if only National Agreement provisions were taken into account. However, the leveling effects of centralized bargaining disappeared when total wage increases (that is, including those resulting from decentralized bargaining activities as well) were factored in. Total wage increases were 212 percent (men) and 268 percent (women) in low-paying industries; 210 percent (men) and 258 percent (women) in middle-paying industries; and 216 percent (men) and 252 percent (women) for high-paying industries. Clearly, high-wage workers were able to restore wage differentials vis-à-vis low-wage workers through company level bargaining (Mooney, 1978: 248).

It looks as though wage compression through national wage agreements, just as in other countries like Sweden and the UK (see Martin, 1984; Flanagan et al, 1983: 418-36; Iversen, 1999), spurred compensatory wage demands at the company level and, in so doing, compromised one of centralized bargaining's key functions, that of ensuring wage restraint (Roche, 1997: 186). As a result, the employers became increasingly disenchanted with centralized negotiations. In fact, as in other countries (Pontusson and Swenson, 1996; Swenson and Pontusson, 2001), they were key in bringing about the return to a decentralized bargaining structure (Gunnigle et al., 1999: 200).

The years between 1981 and 1987 were characterized by "free-for-all" collective bargaining. According to some commentators, this was a period in which the notion of "wage round" lost much of its previous significance in the sense that agreements became less concentrated in time and wage increases more reflective of market conditions than had previously been the case (Roche, 1997: 195; Gunnigle et al., 1999: 202). However, as the wage data presented above clearly show (Figure 2), wage norms continued to shape the process of wage formation. MNCs acted as wage leaders in this phase. The wage deals concluded by foreign MNCs, particularly those struck early on in the course of rounds, became a reference point for other bargaining groups (Roche and Geary, 1997: 288). As a result, unit wage costs grew in the Irish manufacturing sector as a whole (Baker, 1988: 39).

The evidence provided so far corroborates the arguments made by institutional economists about the fundamental role that wage norms (rather than strictly economic factors) play in shaping Irish labor market outcomes.¹³ It is in this respect, in our opinion, that the contribution of social partnership agreements has to be regarded as fundamental. Beginning with the PNR of 1987, these agreements seem to have introduced a new wage norm in the Irish economy – one that closely linked wage increases with the ability to pay of the least dynamic portions of the Irish manufacturing section. In so doing, social partnership agreements dramatically boosted the cost competitiveness of the most dynamic sectors and firms. The "Irish disease" turned into "Irish blessing."

c) The effects of social partnership

We replicated Baker's (1988) analysis (Baker, 1988) for the period between 1985 and 1998.¹⁴ We divided the Irish manufacturing sector into modern and traditional components, each one corresponding to Baker's

¹³ See O'Donnell and O'Reardon (1996: 90) critique of liberal economists' arguments against social partnership: "Liberal economists struggle to explain Ireland's dismal economic performance from 1980 to 1987, including the doubling of unemployment, during a period without centralised and politicised bargaining. In arguing that social partnership arrangements are maintaining a high level of unemployment, these economists ignore the fact that *without national agreements, income determination will remain a non-competitive, highly collectivised, process, with tendencies to monopoly power on both sides of industry. Ireland is simply not going to move to the atomistic bargaining which underpins the analytical argument of liberal economists.*" (emphasis ours) These words echo those pronounced by McCarthy et al. several years before (1975: 57): "Although many product prices may continue to be largely determined by supply and demand, wage determination is almost invariably affected by other factors, for example, custom, convention, notions of equity and orbits of coercive comparisons."

¹⁴ The data we use are published in Central Statistical Office, Statistical Bulletin, various issues. The series are: "Monthly and Quarterly Volume of Production Indices for Industrial Sectors – Unadjusted"; "Total Number of Persons Engaged Classified by Industrial Sector"; "Gross Earnings and Hours Worked for All Industrial Workers (Adult and Non-Adult Rates of Pay) by Sector." Due do problems of data comparability, we were unable to construct a single series covering the whole period between 1980 and

original grouping. The results of the analysis are summarized in Figure 3. As in the past, there were tremendous differences in productivity growth across the two sub-sectors: 203 vs. 40 percent. However, the behavior of wages had completely changed vis-à-vis the period of decentralized bargaining. In fact, the (real) hourly wage index increased by 41 percent in the modern sector and by 45 percent in the traditional sector. It was no longer the case that wages chased the high productivity growth of the modern sector. The reverse was true. Productivity increases in the traditional sector provided a yardstick for wage increases in the economy as a whole. Differences in employment trends were quite striking. While the five industries composing the modern sector jointly more than doubled (116 percent) their employment, the rest of manufacturing, constituting the traditional sector, only increased employment by 8 percent over the 1985-1998 period (overall employment growth in the manufacturing sector was 33 percent).

These results also held by adopting different bases of classification. Baker (1988) assigned industries to the "modern" and "traditional" groupings based on a mix of two criteria, ownership of assets and/or productivity growth. Industries that were dominated by foreign MNCs and/or that grew fast were classified as modern; the others were placed in a residual category. We created two groups, "dynamic" and "lagging," purely based on productivity growth in the period 1985-1998. If this was greater than (lower than) the mean plus (minus) $\frac{1}{2}$ s.d., the industry in question was classified as "dynamic" ("lagging").¹⁵ Productivity increases were 231 percent in the dynamic sector and 13 percent in the lagging one. Yet wage increases were higher in the lagging sector than in the dynamic sector: 43.6 percent vs. 40.9 percent.

We also created an alternative grouping, "foreign" and "domestic," based on the following rule: if more than 75 (less than 25) percent of employment in 1985 (or the first year for which data are available) was in foreign-owned units, the industry in question was classified as "foreign" ("domestic").¹⁶ Just as the former, this classification, too, turned out to be quite similar to the one adopted by Baker (1988). In fact, the "foreign" sector was composed of pharmaceuticals, the remainder of chemicals (excluding basic industrial chemicals), ODP machinery, electrical engineering, and instrument engineering (but not other foods as in Baker (1988)). The results of this comparison are summarized in Figure 4. Wage increases in the foreign sector closely matched those in the domestic sector, which in turn proceeded in parallel with productivity increases in the domestic sector.

It looks as though firms in the foreign sector merely mimicked wage trends in the domestic sector, regardless of differences in productivity growth rates.¹⁷ As a result of these developments, the foreign portion of the Irish manufacturing sector benefited from a tremendous increase in competitiveness in this period. Unit wage costs declined by 54 percent in the foreign sector while they remained flat (and even slightly increased between 1997 and 1998) in the domestic sector.¹⁸ Also, visual inspection of Figure 4 reveals that between 1985 and 1987, wages in both the foreign and domestic sub-sectors continued to grow faster than productivity increases in the domestic sector, even though the growth rate of wages slowed down between 1986 and 1987. This is consistent with Baker's results (1988). After 1987, that is after social partnership began, wages closely aligned themselves to the productivity increases of the domestic sector.

1998.

¹⁵ Pharmaceuticals, electrical engineering, ODP machinery, other food, and the knitting industry were included in the "dynamic" sector. Compared with Baker (1988)'s classification, the productivity criterion excludes instrument engineering and includes knitting. Clothing, paper and paper products, production and preliminary processing of metals, manufacture of metal articles, mechanical engineering, manufacture and assembly of motor vehicles (including parts), manufacture of other means of transport, slaughtering and preserving of meat, manufacture of dairy products, other textiles, leather and footwear, and miscellaneous industries composed the "lagging" sector. This was less encompassing than Baker (1988)'s "traditional" sector.

¹⁶ Data on employment by nationality of ownership are from CSO's Annual Census of Industrial Production.

¹⁷ Obviously, they could do so only to the extent that they did not have to compete for labor with domestic firms due to excess supply. This condition may be disappearing now that the labor market is at full employment.

¹⁸ Adjusted for variations in the exchange rate, unit wage costs showed similar trends. They declined dramatically in the foreign sector – between 63 (D-mark) and 39 percent (US \$). In the domestic sector, however, there were reductions in unit wage costs only vis-à-vis the D-Mark (-17 percent), not other currencies. In the domestic sector, unit wage costs increased by 38 percent when expressed in US\$.

Similar results were obtained by using nominal data on wage and salaries per person employed and nominal net output per person employed.¹⁹ These data permitted comparisons across firms of different national origin, across all industries (see Figure 5). Once again, the data showed that nominal wage increases in foreign multinationals, and particularly American multinationals, matched the wage increases of domestic companies, despite dramatic differences in net output per person. These increases were, in turn, only slightly above those resulting from provisions in centralized wage agreements.

Not surprisingly, the correlation between wage and productivity increases was almost never significantly different from zero at standard levels of confidence, independently of the period chosen (see table 3). In light of these findings, the views about social partnership that were summarized above, namely that social partnership had no independent effect on wages and simply validated a set of results that would have been brought about by market forces anyway, or worse that social partnership generated higher wage increases than would have emerged under decentralized bargaining, appear unsubstantiated.²⁰ First, decentralized bargaining between 1980 and 1987 (in a period of high and growing unemployment) increased unit wage costs in all but the most advanced and dynamic industries. Second, it is hard to imagine what kind of market processes could have produced zero correlation between wage and productivity gains and the kind of inter-sectoral patterns described above.

Our interpretation of the data is that wage increases were determined by social partnership agreements. Social partnership introduced a new kind of wage norm in the Irish labor market, one that set wage increases in all sectors slightly above the provisions of centralized agreements, that is, more or less equal to the productivity growth (and hence ability to pay) of Irish firms. In so doing, social partnership allowed foreign MNCs, particularly American, to pay the same wage increases as domestic companies despite astronomical differences in productivity gains and therefore, considerably increase their cost competitiveness. This interpretation emphasizes the key role that pay norms and comparability have historically played in the Irish labor market.

The Irish labor market is divided into union and non-union sectors. As is typically the case with Anglo-Saxon economies, union contracts are not binding for non-union companies. We do not know whether the firms in the “dynamic” and “foreign” sectors described above were predominantly union or non-union. In fact, data on unionization rates by sector or nationality of ownership are not available.²¹ We know, however, that 85 percent of US MNCs established in Ireland since the mid-1980s do not recognize unions (Roche, 2001: 44; see also Gunnigle et al., 1999: 133-4). This is the result of the Irish Industrial Development Agency (IDA)’s decision to stop requesting union recognition as a precondition for its attractive location packages (Gunnigle, Morley, and Turner, 1997; Roche and Geary, 1997: 283). Indeed, an industrial relations regime that allows union non-recognition seems to be an important factor in the location decisions of US high-tech MNCs (Gunnigle and McGuire, 2001: 59).

If it were true that the firms where productivity growth skyrocketed between the late 1980s and the 1990s were predominantly non-union, the Irish social partnership would stand out as an interesting and almost paradoxical example of reversed incomes policy – one in which institutionalized wage restraint is beneficial not because of its direct effects on the unionized sector, but rather for its indirect influence on wage setting in non-union companies.²²

4. The politics of wage restraint in Ireland

Having argued that social partnership did affect wages (despite claims to the contrary), it remains to be

¹⁹ These data are from CSO’s Census of Industrial Production.

²⁰ For a recent rehearsal of the debate on the usefulness of social partnership and related skepticism, see “Personnel conference debates partnership.” *The Irish Times*, May 25, 2002: p. 19.

²¹ This is based on an e-mail exchange with Bill Roche (May 13, 2002).

²² It needs to be emphasized, however, that large non-unionized MNCs are bound by the centralized agreements by virtue of their membership in IBEC, the employer association (interview with Brendan Butler, Director of Enterprise, IBEC (Dublin: Sept. 3, 2001).

understood how social partnership came about, that is, what kind of coalitions supported and reproduced it over time, and why it "stuck," that is, why centrally negotiated wage increases were not undone by wage drift (i.e., additional wage increases negotiated at the company level) as it has frequently been the case in other countries, as well as in Ireland in the past. On both counts, Ireland stands out as an exception to prevailing views.

a) Pro-partnership coalitions

Social partnership did stick. Average wage drift was slightly above 1 percent per year in manufacturing as a whole. This is very moderate in comparative perspective. In fact, wage drift in the order of 3.5 – 4.5 percent per year was more or less expected in Sweden only a few years ago (Edgren et al., 1973: 25). Figure 6 displays wage trends in various sectors in the period covered by four social partnership agreements (1987-1999). It clearly shows that civil service played a role of wage leader. In fact, wage drift was considerably higher in the public sector (with the possible exception of education) than in the manufacturing sector as a whole. In addition to wage increases distributed centrally, the public sector could also count on "special pay awards," intended to restore comparability with other categories. The public sector's higher wage increases than industry are despite much lower productivity growth in the service sector as a whole (including the public sector) (Duffy et al., 1999: 9). Figure 6 also shows that the gap between centrally negotiated and de facto wage increases appears to be growing over time – a worrisome sign for the future of social partnership.

The public sector's wage leadership is consistent with its dominant role in the Irish labor movement. Based on union reports, Roche and Ashmore (2001:18) estimate that 55 percent of union membership in the Irish Congress of Trade Unions (ICTU), the Irish union confederation, was in the public sector and 45 percent in the private sector in 1995. Unionization rates by sector are also much higher in the public than in other sectors. In 1992 (1998), unionization was 73.4 (74.1) percent in public administration and defense and 54.3 (46.9) percent in production industries.²³

The Irish trade union movement is not based on industry unions as in most continental European countries. Rather, as in the UK, it is organized in general unions, representing semi-skilled workers across all sectors, craft and other grade-specific (e.g. white collar workers) unions, and public sector unions. Some unions (totaling 11.5 percent of membership in 1995) are Irish branches of British-based organizations. Figure 7 provides a breakdown of union membership in the ICTU. It clearly shows that general and public service unions have the largest shares.

These two types of unions played a fundamental role in the establishment first, and then reproduction over time, of social partnership agreements. Social partnership emerged as a pact between the state and the union confederation ICTU. Organized employers did not play a very important role in the formative stages. They believed decentralized bargaining would be more effective in ensuring wage moderation. They also disagreed with specific union demands, like the one-hour reduction in working time to 39 hours per week and the request for minimum increases of £4 per week. Government had to work hard to persuade them to stay at the bargaining table and as a result, some of the union's demands, like the proposed reduction in working time and the minimum payment, were, only in the private sector, subordinated to the results of plant-level negotiations (*Irish Times*, Oct. 8, 1987; see also Gunnigle et al, 1999: 206; Roche, 1997: 200). It was only after social partnership became a clear success that the employers became clear supporters. For them, centralized negotiations were less costly than decentralized bargaining.²⁴

The different unions affiliated to the ICTU had mixed feelings about the desirability of social partnership and this is clearly reflected in the way they voted in the various union conventions (see Baccaro, 2002). The 1987 PNR was approved because both the two major general unions at the time, the ITGWU (140,000 members) and the FWUI (60,000 members), and all of the major public sector unions

²³ These data are from Roche and Ashmore, 2001: 17, and are based on labor force surveys.

²⁴ Interview with Brendan Butler, IBEC, cit.

voted in favor of the deal.²⁵ This was enough to produce a majority. However, most ICTU-affiliated unions voted against the PNR.

Later agreements were less controversial than the first and majorities larger. However, unions whose primary constituencies were in the private sector, like the craft unions, opposed the agreements. Given the huge boost in profitability in this sector, these unions hoped to gain more by negotiating alone (see Teague, 1995: 262). Public sector unions supported them. In light of wage trends presented above, which show that wage increases were higher in the public than in the private sector, this support is not surprising. The major general union SIPTU (the result of a 1990 merger between ITGWU and FWUI) was unflinchingly pro social partnership. Because this is an *encompassing* union in the sense of Olson (1982), namely, a union that organizes across all sectors simultaneously, it probably internalizes the systemic consequences of wage policy for the economy as a whole. This may explain SIPTU's support for social partnership.²⁶

Theory suggests that wage centralization should not be advisable in a country where unions in sectors not exposed to international competition (e.g. public sector unions) have a greater chance to influence wage policy than organizations in exposed sectors (Crouch, 1988; Garrett and Way, 1999; Franzese, 2001). In fact, unions in exposed sector are more likely to be responsive to the threat to their employment prospects resulting from militant wage behavior than unions in non-exposed sectors. In other words, because they are likely to lose their jobs if costs in their sectors are too high vis-à-vis competitors, unions in exposed sectors are likely to spontaneously moderate wage demands, unlike unions in sectors sheltered from international competition (where prices are set as mark-up on costs) or unions sheltered from competition *tout court*.

Bargaining centralization/coordination is, therefore, most effective, both per se and in its interaction with monetary policy (Franzese, 2001), the more traded-sector actors dominate bargain and public sector actors follow. If centralized bargaining is dominated by public sector unions it may even be counterproductive, as excessive wage settlements may be unduly generalized to the rest of the economy. In this case, centralized bargaining would neither produce nominal benefits, that is, a lower rate of wage inflation, nor real benefits, namely greater employment. Regression results confirm these basic insights (Garrett and Way, 1999; Franzese, 2001).

In Ireland, public sector unions did have greater influence than their private sector counterparts in shaping wage policy. In 1988, Colin Crouch (1988: 72) produced an indicator of exposed sector dominance, based on percentage of union membership in exposed sector unions. Ireland came at the bottom of a list of 14 European countries. As it is shown by the evidence presented above, the situation does not seem to have changed in later years. Yet, the Irish social partnership had extremely beneficial effects. Why?

The reason, we argue, relies in the particular structure of the Irish economy. The theory laid out above relies on the traditional two-sector model of a small open economy (see Aukrust, 1977; Edgren et al., 1973). The economy was divided in two sectors, distinguishing between sheltered and exposed industries. The former were conceptualized as price-takers; namely, their prices were determined on international markets. The latter fixed their prices as mark-up on costs. In other words, sheltered sectors, unlike exposed sectors, could pass on their cost increases to consumers and keep profits unaltered without fear of losing market share to foreign competitors (or having to reduce profits). For technological reasons, productivity growth was much faster in the exposed than in the sheltered sectors. It was assumed that whatever wage level prevailed in either of the two sectors, it would trickle down to the other as well, through competition for scarce labor (in a full employment scenario) and/or comparability mechanisms.

²⁵ The vote was very close within ITGWU, see Baccaro (2002: 17).

²⁶ In this regard, the position of the ATGWU, the other (much smaller) general union, is interesting. This union has been among the staunchest opponents of social partnership over the years. Traditionally, the ATGWU's position is explained by reference to its ideological/cultural background. Because this is a British-based union, its attitude towards bargaining is typically adversarial (see Roche, 1997: 179; Hardiman, 1992: 342-3). However, most of this union's membership is in the private sector (Roche, 2000: 355). Therefore, the ATGWU's response to social partnership appears overdetermined by both its ideology and sectoral interests.

These conditions identified a “main course” of wages. Wage increases should stay in the corridor represented by changes in world prices (adjusted for exchange rate changes) plus productivity increases in the exposed sector. If wage increases exceeded the main course – as it might happen when the non-exposed sector acted as wage leader – companies in exposed sectors would either lose competitiveness (and market share) or reduce their profits. Both things would have negative consequences for the economy.

Yet the Irish economy is more appropriately conceptualized as a three-sector economy. In fact, there is a clear distinction within the exposed sector, i.e., the manufacturing sector, between the modern sub-sector, characterized by high productivity growth, and the traditional one, with much lower productivity growth. Hence, there are de facto two “main courses” for wages in Ireland, one much ampler, which is appropriate for the modern sub-sector, and a narrower one for the traditional sub-sector. Wage pushfulness in the non-exposed sector may exceed the limits of admissible cost increases for the traditional sector (and thus cause unit labor cost growth in that sector) and, provided it stays within the second wage corridor, still allow competitiveness gains in the modern sector.²⁷ *Ceteris paribus*, this should produce a transfer of resources from the (shrinking) traditional to the (expanding) modern sector. At a time in which the economy is in full employment, this may even contribute to ease emerging labor market tensions.

In brief, a three-sector economy like the Irish appears able to tolerate a certain amount of wage pushfulness in the non-exposed sector. Much more worrisome for such an economy is the situation referred above as “Irish disease,” which seems to have characterized the years between 1980 and 1987, namely wage pushfulness in the modern sector, which spreads to the other sectors of the economy as well.

b) The problem of compliance

Why did unions go along with centralized wage policies even when they disagreed with them? Why did the peripheral structure of unions abide by the terms negotiated at the center? In other words, how do we understand *compliance* (along both horizontal and vertical lines) with social partnership provisions?

Corporatist theory provides distinct answers to these questions. In a nutshell, this theory argues that particular organizational features of interest groups minimize internal conflict and maximize capacity for compliance (for more on the theory, see Baccaro, 2002b). These features are *concentration* (Golden, 1993; Iversen, 1999) and *hierarchical control* (or *centralization*) (Schmitter, 1979; Streeck, 1982). Concentration refers to the number of actors involved in bargaining on each side. The higher this number (the lower the concentration), the higher the likelihood of that disagreement may emerge and with that, also *leapfrogging* or wage spirals. Hierarchical control refers to institutional/organizational mechanisms for peak-level control over action by peripheral structures. If, for example, strike funds are directly controlled by the center (or, *a fortiori*, if unauthorized strikes are illegal); if plant leaders are appointed from above and therefore, are accountable to the upper echelons rather than their workplace constituencies; if approval from higher structures is required for collective agreements to be valid, decentralized structures find it more difficult to pursue their own wage policies and compliance is greater.²⁸

The problem with corporatist theory is that it does not reflect the recent Irish experience, nor the experience of other European countries (e.g. Italy). Ireland does not have a corporatist interest representation structure nor did it develop it in the last 15 years (Baccaro, 2002). In fact, the lack of such corporatist structure, and especially of a strong and cohesive labor movement with a high degree of

²⁷ However, this does not seem to have happened in Ireland (at least in the period examined). As argued above, manufacturing wage increases were lower than public sector ones and appeared to stay in line with productivity increases in the domestic/traditional sector.

²⁸ Corporatist theory sometimes emphasizes one organizational dimension (e.g., recently, concentration) over the other. To properly resolve the problem of compliance, however, this theory requires both dimensions. In fact, without mechanisms of vertical control, even a highly concentrated interest group – for example, a single union confederation – may be unable to ensure compliance from its members. It may very well be the case that concentration overlaps empirically with hierarchy. There is no reason, however, to conflate the two dimensions analytically.

“authoritative centralization,” was considered responsible for the failure of centralized bargaining in the late 1970s (Hardiman, 1988).

The organizational structures of Irish interest groups did not change much between the late 1980s and the 1990s. The degree of internal concentration increased over time, thanks to union mergers (Roche and Ashmore, 2001), but with 52 unions affiliated to the confederation ICTU in 1995, and several more in 1987, when social partnership began, the Irish labor movement is still more fragmented than others. Workers can choose among multiple unions, if they want to. Workplace representation structures are quite strong and based on elected representatives accountable to their members. The peak confederal levels do not have formal coercive power over their affiliate unions, except threat of expulsion. Authoritative control is limited by the decentralized structure of collective bargaining. In other words, wage guidelines negotiated at the national level every three years have to be incorporated into collective agreements at lower levels (at the company level in the manufacturing sector) to become effective (Gunnigle et al., 1999: 188). The ICTU has no formal way to ensure that these contracts comply with the general guidelines.

We have argued in previous work (Baccaro, 2002) that the Irish labor movement relied heavily on democratic mechanisms of decision-making to generate coordination within its own ranks and legitimize its centralized policies. Unions which disagreed with the policies of the central confederation went along with them because they corresponded to the will of the majority.²⁹ Also, union refrained from violating the majority principle within the union confederation because they realized that if they did so, they would encourage similar behavior from their own internal opposition.³⁰

Here we add another element to the explanation for why social partnership agreements held. Different from the centralized agreements of the 1970s (which through a variety of mechanisms, like tapered percentage wage increases and minimum cash increases, had a tendency to bring about wage compression), the social partnership agreements of the 1980s and 1990s were distributionally neutral, that is, they did not seek to compress inter-industry wage differentials.

This last statement is based on the following exercise, summarized in Table 4. We applied the pay terms of the various social partnership agreements to the December 1987 distribution of average weekly earnings in different manufacturing industries. We found that social partnership left inter-industry wage differentials unaltered. Only during the terms of the PNR was there a modest tendency for wage compression, due to tapered percentage increases. The minimum cash increase provisions of social partnership agreements only affected average wages in two sectors, knitting and clothing, and brought about no appreciable compression. During the PCW and P-2000 agreements, minimum increases were too low to impact the average weekly wage of any industry at all.³¹ If one also considers that centralized agreements involved tax modifications targeting the middle class as a *quid pro quo* for wage restraint, it becomes clear the Irish social partnership is not of the egalitarian variety often encountered in the Scandinavian countries (Teague, 1995; Iversen, 1999).³²

²⁹ Ben Kearney, Republic of Ireland Secretary of the ATGWU (a union that voted against all of the Irish social partnership agreements): “We’re very loyal Congress members, I’m afraid. We believe in the whole concept of Congress. We feel that whatever has to be done has to be done from within.” (Bundoran: July 3, 2001).

³⁰ Interview with Patricia O’Donovan, former Deputy Secretary General of the ICTU. Geneva: April 9, 2001.

³¹ When one considers the distribution not of average weekly wages, but of average weekly wage costs, that is average wage in the industry (determined solely by centralized agreements) multiplied by employment in that particular industry, both the latter half and the upper half of the distribution become more disperse over time. This increased dispersion in the distribution would be entirely due to changes in the inter-sectoral distribution of employment, since centralized agreements are found to be distributionally neutral.

³² In this regard, Fitzgerald (2001: 179) reports the following, interesting anecdote. During negotiations for the 1994 PCW, the union negotiators were presented with alternative tax packages with different distributional consequences. They chose a package benefiting their more highly skilled members – a category whose support in the internal decision-making process was deemed important. “Thus the final package agreed involved somewhat higher increases in the tax bands, and slightly lower increases in personal allowances, than other options under consideration.”

This lack of explicit redistributive intent may have made compliance with centralized agreements easier. We know from the experience of other countries that egalitarian wage policies, namely policies aimed at bringing about inter-sectoral and inter-skill compression, are deeply divisive (Baccaro and Locke, 1998). It seems that wage egalitarianism conflicts with deeply held norms of social justice (Sen, 1992), for example that remuneration should be proportional to ability and effort. Inevitably, attempts at reducing wage differentials from above unleash opposite reactions from below. Workers mobilize to restore pay comparability with other categories and in the process, lodge additional wage claims. More often than not, these dynamics wind up undermining centralized institutions. It is probably not a coincidence that Austria is the only traditionally corporatist country in which centralized wage negotiations did not experience major disruptions between the 1980s and early 1990s and that in Austria, unlike other countries, compression of wage differentials was never an explicit goal of centralized wage regulation (Wallerstein et al. 1997; Iversen, 1996; 1999).

A comparison between the National Agreements and National Understanding of the 1970s, which eventually collapsed because they proved unable to ensure wage restraint, and the Social Partnership Agreements of the late 1980s and 1990s, which were extremely successful in limiting wage drift, reveals that organizational structures do not matter much in explaining compliance (or lack thereof) with centralized agreements. In fact, the organizational characteristics of the Irish labor movement and more generally, interest group system did not change much between the two phases. Organizational policies appeared to be much more important than organizational structures. In the first phase, the Irish union movement was committed to bringing about a compression of wage differentials through centralized agreements; in the second, it was not.

Distributionally neutral wage policies eliminated a major source of intra-organizational conflict. In these conditions, "soft" resources – e.g. decision making procedures that could be perceived as procedurally fair – sufficed to generate internal coordination. Democratic procedures helped the Irish labor movement to hold to its side of the bargain. However, a few rifts have recently begun to emerge. Prior to the PPF negotiations in 1999, ASTI, one of the three teacher unions, seceded from the ICTU because it was unwilling to be bound by the confederation's wage policy. After secession, ASTI lodged a 30 percent pay increase demand. Interestingly enough, it was one of the public sector, not private sector unions the first to break the rule of majority decisions within Congress.³³ Only time will tell whether this is an isolated episode or a worrisome sign of incipient fragmentation. If it were the latter, the future of social partnership in Ireland would be at risk.

5. Concluding remarks

Based on an analysis of wage and productivity trends, this paper has argued that social partnership altered the process of wage formation in Ireland. In particular, it linked wage increases in the economy as a whole to the productivity gains (and ability to pay) of the most traditional, labor intensive, and (presumably) more highly unionized domestic portions of the manufacturing sector. In so doing, it injected robust doses of cost competitiveness in the industries dominated by foreign MNCs, where productivity skyrocketed while wage increases grew (barely) in line with the rest of the economy. These trends were a significant departure from the recent past, when high wage settlements in the MNC sector had shown a tendency to spill over to the other sectors, where they generated cost problems.

The Irish social partnership differs from existing national models in important respects. It is often argued that centralized wage regulation is advisable in countries where the interests of workers and firms exposed to the discipline of international competition dominate non-exposed sectors and shape the agenda of encompassing interest groups. Yet public sector unions, a prototypically non-exposed group, played a fundamental role (in partnership with the major general union SIPTU and the state) in initiating first, and

³³ There is also evidence, however, to suggest that wage increases in the educational sector had been lower than in the rest of the public sector.

sustaining later, the various social partnership agreements in Ireland. As a result, wage increases were higher in the public sector than in the manufacturing sector. Yet, the competitiveness of the exposed sector was not affected.

Due to the particular structure of the Irish manufacturing sector, the Irish economy appears much less vulnerable to public sector wage pushfulness than other economies, at least as long as there is a gap between productivity growth in the modern and traditional sectors and as long as public and (non-exposed) service sector wage settlements stay well within that gap. By promoting the transfer of labor force from declining to expanding sectors, wage increases set slightly above the average ability to pay of the domestic sector may even contribute to assuage some of the tensions that have recently emerged in the Irish labor market. Much more serious for the Irish economy seems to be the state of affairs referred to above as “Irish disease,” namely a situation in which the high-productivity growth sector acts as wage leader and dictates the terms of wage settlements for the economy as a whole.

In contrast to much corporatist theory, the Irish social partnership survived and even prospered in the absence of appropriate institutional preconditions, namely monopolistic and highly centralized interest groups. In this regard, the Irish case suggests that these institutional preconditions matter less than it was previously thought. In fact, the organizational features of the Irish interest representation system did not change much between the early phase of centralized bargaining in the 1970s and the more mature social partnership agreements of the 1980s-1990s. Yet the outcomes of the two phases were considerably different.

The distributional profile of wage policies seems to be more important than organizational structures in explaining compliance with centralized provisions. In fact, wage policies aimed at bringing about compression in inter-sectoral (and inter-skill) wage differentials appear to have an in-built tendency to generate wage rivalries and in so doing, destabilize centralized wage institutions. The fact that centralized wage policies were distributionally neutral during the phase of social partnership, unlike the previous phase of national agreements, contributed to eliminate a source of potential instability in Ireland.

This last element leads us to consider the issue of social outcomes. The Irish social partnership does not exhibit the trademark redistributive features of Northern European social corporatist models (Teague, 1995). Research has uncovered a marked increase in earning dispersion, particularly between 1987 and 1994, and especially at the top of the distribution (Barrett, Fitz Gerald, and Nolan, 2000; Barrett, Callan, and Nolan, 1999).³⁴

Despite a considerable widening of earning inequality, incomes did not change much. This was due to both the redistributive effects of the tax and social welfare system (especially in the 1987-1994 period) and to favorable developments in labor market participation. In fact, of the many women that took up jobs in this period, the majority had spouses in the lower, rather than upper half of the income distribution (Nolan and Maître, 2000). Poverty decreased in real terms thanks to the marked increase in real incomes. However, poverty defined as percentage of mean household income increased. (Layte, Nolan, and Whelan 2000). One has to conclude that the Irish social partnership has (so far) proven unable to counter growing inequality even though it managed to avoid that the bottom of the distribution fell too much below the median.

One of the key assumptions of the classic model of small open economy was that powerful socioeconomic forces ensured the invariance of the profit and wage shares (see Aukrust, 1977: 113). Yet this assumption is bluntly violated in the Irish case. At an aggregate level, the wage share declined from 71 to 56.9 percent of GDP between 1987 and 2000 (European Commission, 2000: Table 32). As argued above, the Irish model is one in which wages grow systematically less than productivity while workers are compensated for their wage restraint through reductions in income taxes (which are generally regressive).

Even abstracting from the traditional problem of enforcing wage restraint in a labor market

³⁴ Our data show that average industry wages did not change much and that all of the increase in wage dispersion was due to changes in the inter-industry composition of employment. In other words, employment grew faster in high-paying than low-paying manufacturing industries. This finding is, however, compatible with an increase in within-industry wage dispersion.

characterized by full employment, there are some reasons to doubt that this model is sustainable over the long run. First, success of this model depends on other countries not following the same route. If this were to happen, a giant and socially disruptive race to the bottom would ensue. Second, tax cuts translate sooner or later into cuts in the quantity or quality of public services (including market-correcting redistribution), unless the economy grows at the stellar rates of the past few years.

The Irish social partnership needs to change to remain viable. In particular, it needs to ensure competitiveness based on know-how, skills, and capacity to innovate, not just lower wage costs and taxes than the most proximate competitors. Also, it needs to strengthen the effectiveness of the public sector while avoiding financial imbalances. The social partners seem well aware of the problems that lay ahead. They have been through tougher times in the past. It remains to be seen whether they will find the capacity (and political will) to come up with creative solutions to the new challenges they are now faced with.

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Table 1. Pay terms of the Irish social partnership agreements (private sector)

	PNR			PESP			PCW		
	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96
Wage Increase	3% on first £120 of weekly pay; 2% on the rest	3% on first £120 of weekly pay; 2% on the rest	3% on first £120 of weekly pay; 2% on the rest	4%	3%	3.75%	2%	2.5%	2.5% for first 6 months; 1% for extra 6 months
Minimum Increase (per week)	£4	£4	£4	£5	£4.25	£5.75		£3.5	£3.5
Local Increase				3%					

	P-2000 (lasts 3 yrs and 3 months)			PPF (lasts 2 yrs and 9 months)		
	1996-97	1997-98	1998-99	1999-00	2001-00	2002-01
Wage Increase	2.5%	2.25%	1.5% for the first 9 months; 1% for the next 6 months	5.5%	5.5% (additional 2% + 1% lump sum after renegotiation in Dec. 2000)	4%
Minimum Increase (per week)		£3.5	£2.4 (£1.4 for the 4 th phase)	£12	£11	£9
Local Increase		2%				

Table 2. The Irish manufacturing sector by nationality of ownership

1985							
	No of establishments	Total persons engaged	Gross Output (£000)	Wages and Salaries (£000)	Wages and Salaries per Person	Net Output per Person (£000)	Persons engaged per establishment
Irish	3908	111010	7186991	1022963	9215.05	18.9	28
EEC countries	369	28692	1806443	296636	10338.63	26.9	78
I. UK	169	14343	1025368	161343	11248.90	30.3	85
Germany	107	8821	443634	79218	8980.61	22.3	82
Non EEC countries	390	47597	5441499	510888	10733.62	57.7	122
II. US	291	36591	4608663	399634	10921.65	67.3	126
Japan	10	1332	106002	12509	9391.14	22	133
Switzerland	14	1168	37136	9900	8476.03	27.3	83
Total Foreign	756	76289	7247942	807525	10585.08	46.1	101
Total	4667	187299	14434934	1830488	9773.08	30	40
1998							
	No of establishments	Total persons engaged	Gross Output (£000)	Wages and Salaries (£000)	Wages and Salaries per Person	Net Output per Person (£000)	Persons engaged per establishment
Irish	3977	127529	13403778	1969681	15444.97	37.6	32
EEC countries	345	36668	5510553	700357	19099.95	80.7	106
UK	122	11824	2228187	245551	20767.17	113.5	97
Germany	100	10400	1005161	179835	17291.83	4304	104
Non EEC countries	380	78575	29512954	1581690	20129.69	237.5	207
US	295	66018	26208052	1304397	19758.20	258.4	224
Japan	23	3574	683837	73876	20670.40	74.1	155
Switzerland	24	3505	1132538	77953	22240.51	267.4	146
Total Foreign	725	115243	35023507	2282047	19802.04	288.4	159
Total	4702	242772	48427285	4251728	17513.26	109.2	52

Source: CSO, Census of Industrial Production

Table 3: Correlations between wage and productivity increases in Ireland (29 manufacturing sectors)

Period	Correlation coefficient
1998-1985	-0.04
1998-1987	0.12
1987-1985	0.1
1990-1987	-0.13
1993-1990	0.34*
1996-1993	0.04
1998-1996	-0.21
1986-1985	0.01
1987-1986	0.18
1988-1987	-0.2
1989-1988	0.25
1990-1989	0.01
1991-1990	0.49***
1992-1991	-0.3
1993-1992	0.14
1994-1993	0.22
1995-1994	-0.2
1996-1995	0.03
1997-1996	-0.08
1998-1997	-0.01

* p-value < 0.1 *** p-value < 0.01

Table 4: Distributional consequences of the social partnership's pay terms (manufacturing sector)

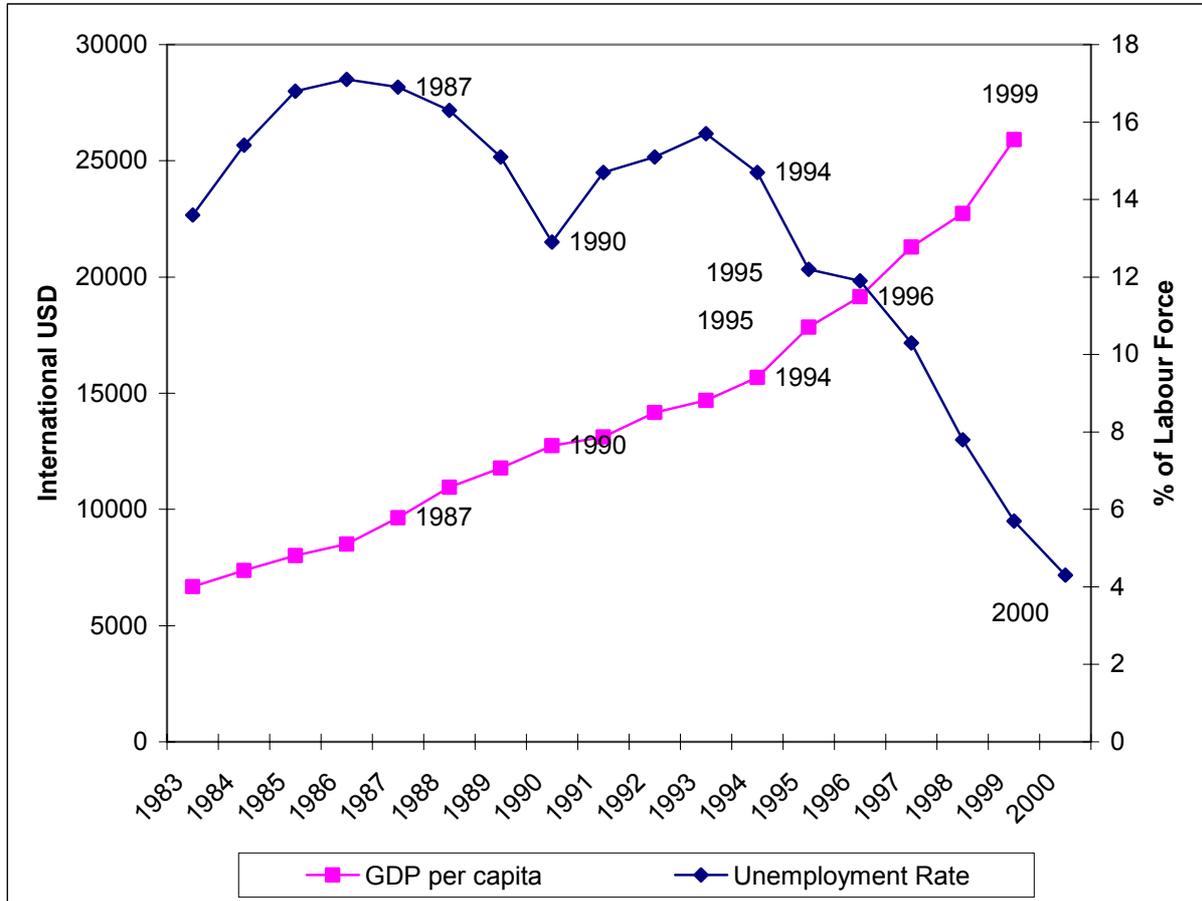
	PNR			PESP			PCW		
	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96
Industries whose average wage was affected by the minimum cash increase provisions	Knitting, Clothing	Knitting, Clothing	Knitting, Clothing		Knitting, Clothing	Knitting, Clothing			
10 th /50 th Percentile	0.747	0.748	0.750	0.750	0.750	0.750	0.750	0.750	0.750
90 th /10 th Percentile	1.735	1.730	1.724	1.724	1.724	1.724	1.724	1.724	1.724

	P-2000			PPF		
	1996-97	1997-98	1998-99	1999-00	2001-00	2002-01
Industries whose average wage was affected by the minimum cash increase provisions				Knitting, Leather and Footwear, Clothing	Knitting, Clothing	Knitting, Clothing
10 th /50 th Percentile	0.750	0.750	0.750	0.750	0.750	0.750
90 th /10 th Percentile	1.724	1.724	1.724	1.724	1.724	1.724

The pay rules of the various social partnership agreements are applied to the distribution of average weekly wages across 29 manufacturing sectors in December 1987 (based on CSO, [Statistical Bulletin](#), Table 4: "Average weekly earnings of industrial workers," December 1988).

The following simplifying assumptions are introduced in calculating wage increases: that the 3% local wage increase made available by the PESP was paid in the course of 1991; that the local increase contained in the P-2000 agreement was paid in the course of 1997; that the duration of the 4th phase of P-2000 was of six months rather than nine (in other words, that P-2000 lasted three years rather than 3 years and 3 months); and that the duration of the 3rd phase of the PPF was of 12 months rather than nine (in other words, that the PPF lasted 3 years rather than 2 years and 9 months).

Figure 1. Growth and employment in Ireland, 1983-2000



Source: ILO, Key Labour Market Indicators, Geneva 2002

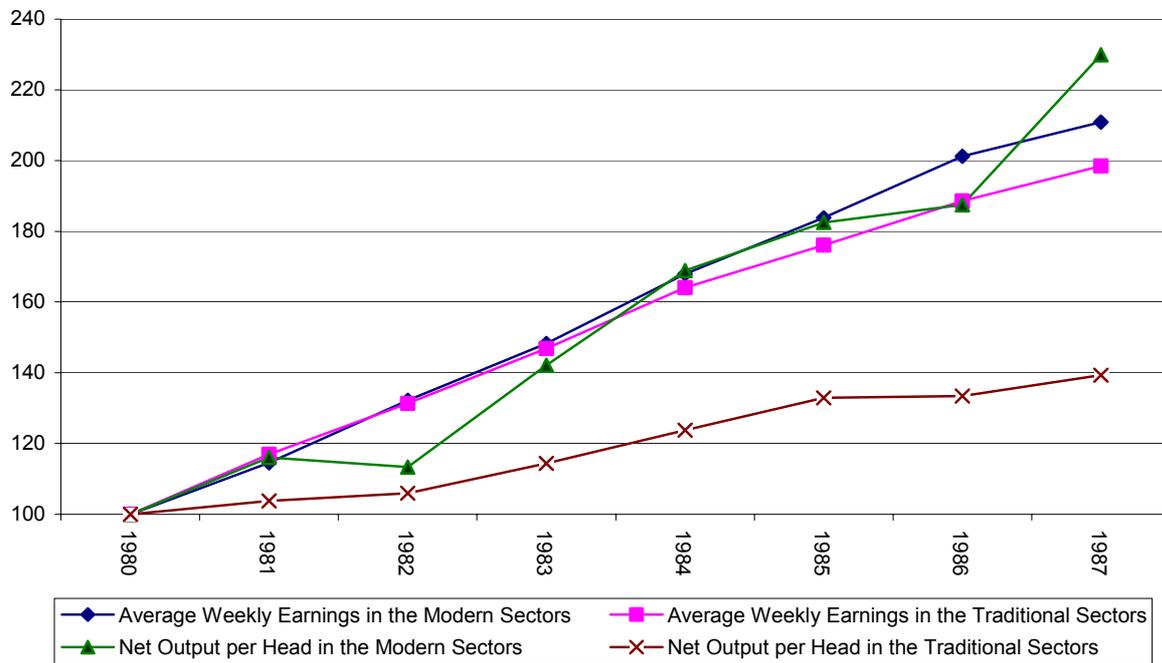
Figure 2: Productivity and wage trends in "modern" and "traditional" manufacturing industries (1980-1987)

Modern industries

I. Nace 70 Code	
257	Pharmaceuticals
33	Office and data processing
34	Electrical engineering
37	Instrument engineering
411,414,415,418, 423	'Other foods'

Traditional industries

Nace 70 Code	
24	Non-metallic mineral products
251,255, 256, 258-260	Basic industrial chemicals (251) and other chemicals
22,31,32,35,36	Rest of metals and engineering
412,413,416,419,420-422	Rest of food
424-429	Drink and tobacco
43	Textiles
44,45	Clothing, footwear, leather
46	Timber, wood, furniture
47	Paper and printing
14,48-49	Miscellaneous industries



Source: Baker (1988)

Figure 3. Productivity and wage trends in “modern” and “traditional” manufacturing industries (1985-1998)

Modern and traditional industries

Same as in Figure 2

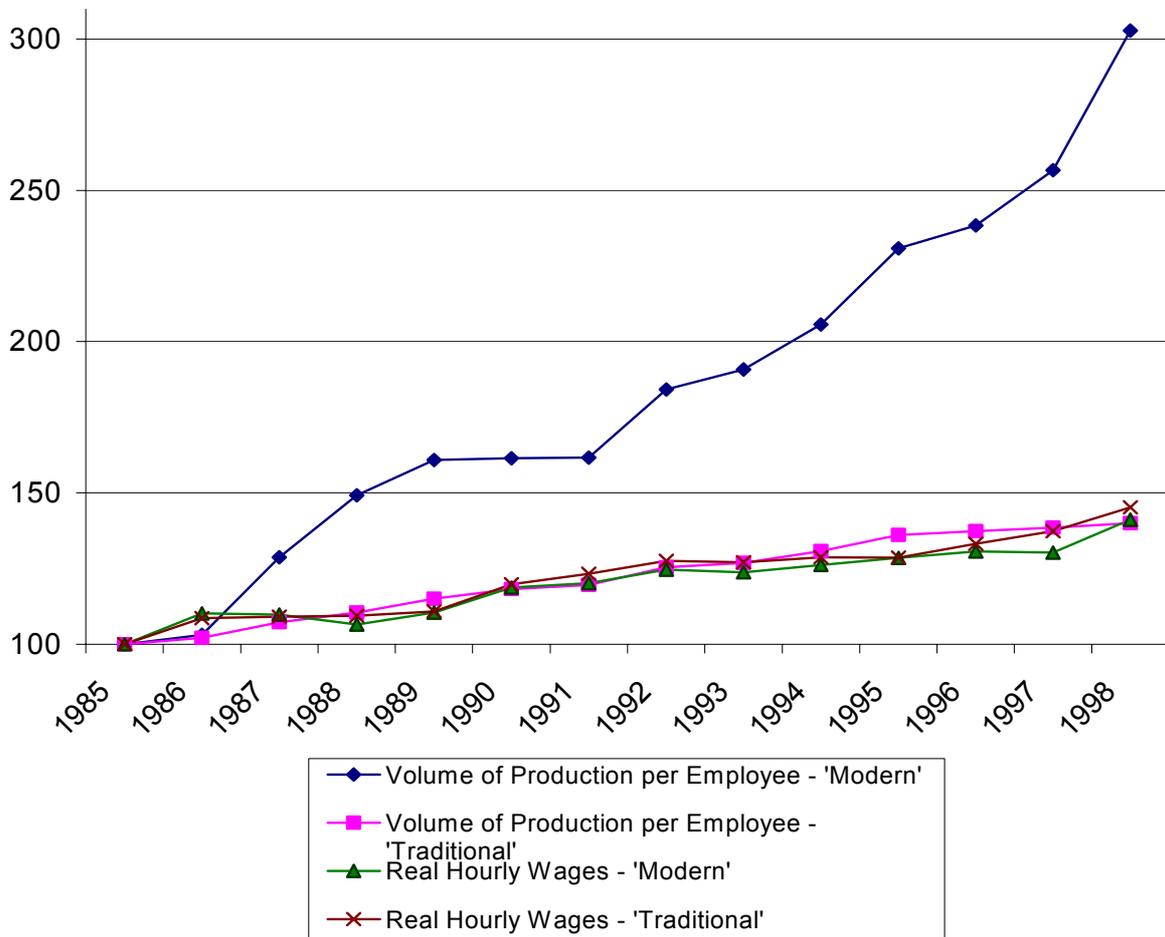


Figure 4. Productivity and wage trends in "foreign" and "domestic" manufacturing industries (1985-1998)

Foreign industries

Nace 70 Code	
257	Pharmaceuticals
255,256, 258-260	Other chemicals
33	Office and data processing
34	Electrical engineering
37	Instrument engineering

Domestic industries

Nace 70 Code	
24	Non-metallic mineral products
22	Production and preliminary processing of metals
31	Manufacture of metal articles
412	Slaughtering and preserving of meat
413	Manufacture of dairy products
46	Timber and wooden furniture
473-474	Printing and publishing
35	Manufacture and assembly of motor vehicles, including parts
36	Manufacture of other means of transport
416,422	Grain milling and manufacture of animal and poultry food
419	Bread, biscuit and four confectionery

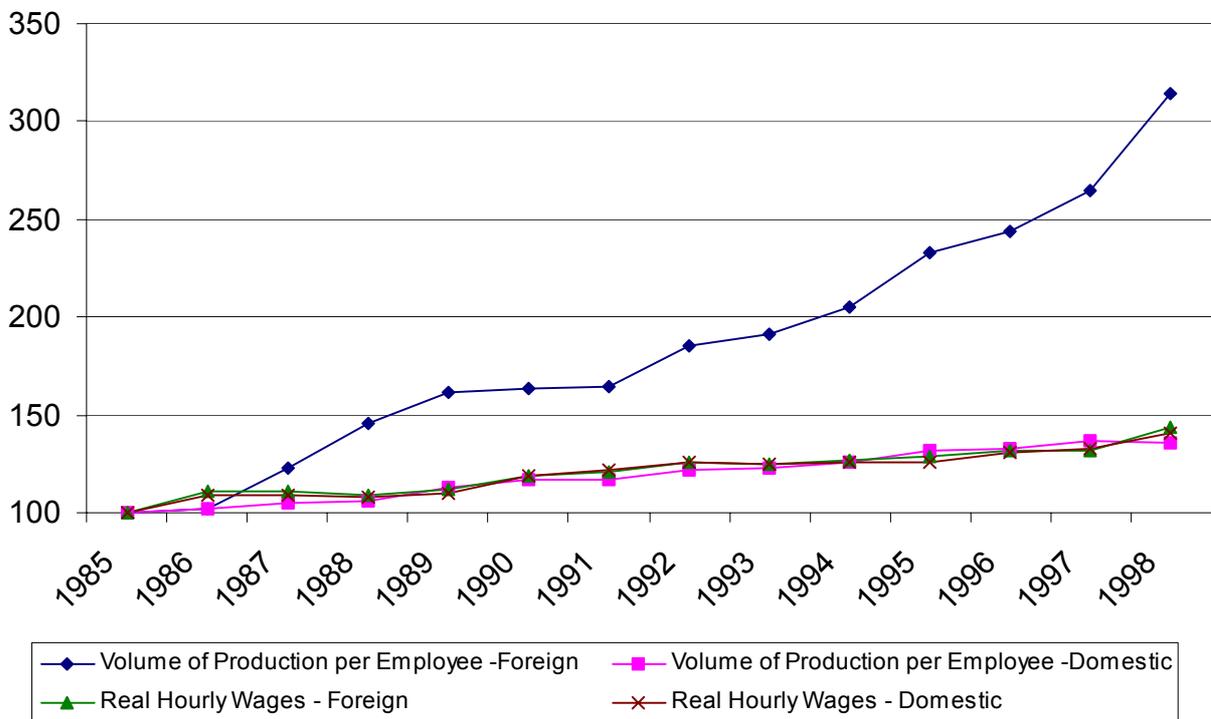
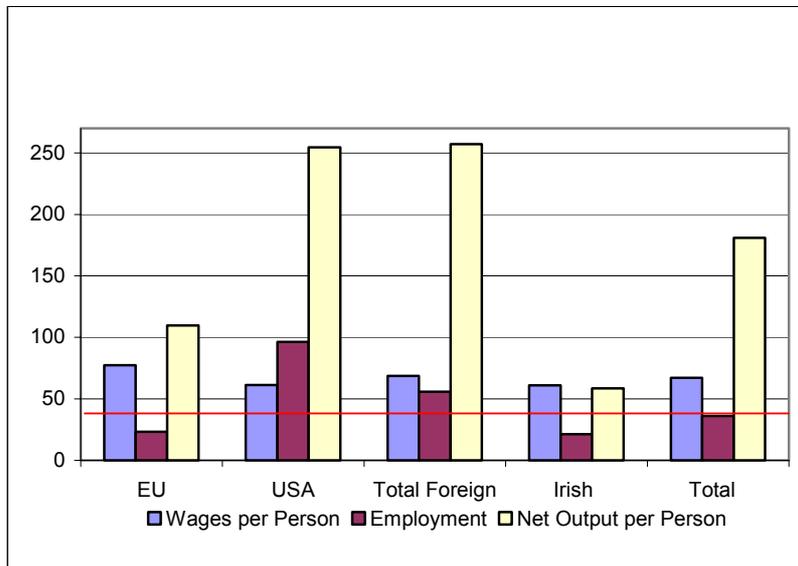


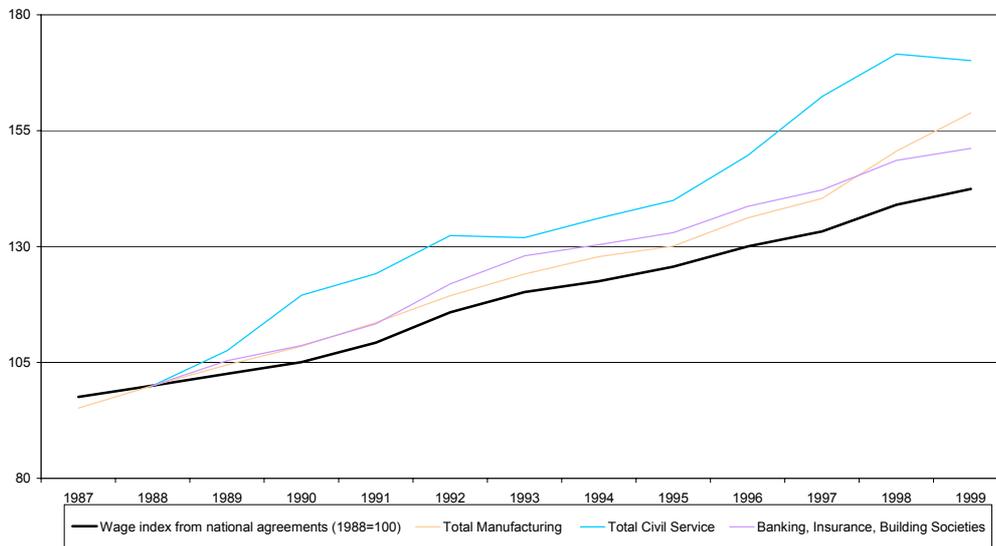
Figure 5. Nominal wage and productivity increases by nationality of establishments (1987-98)



The red solid line represents wage increases resulting from provisions in the social partnership agreements.

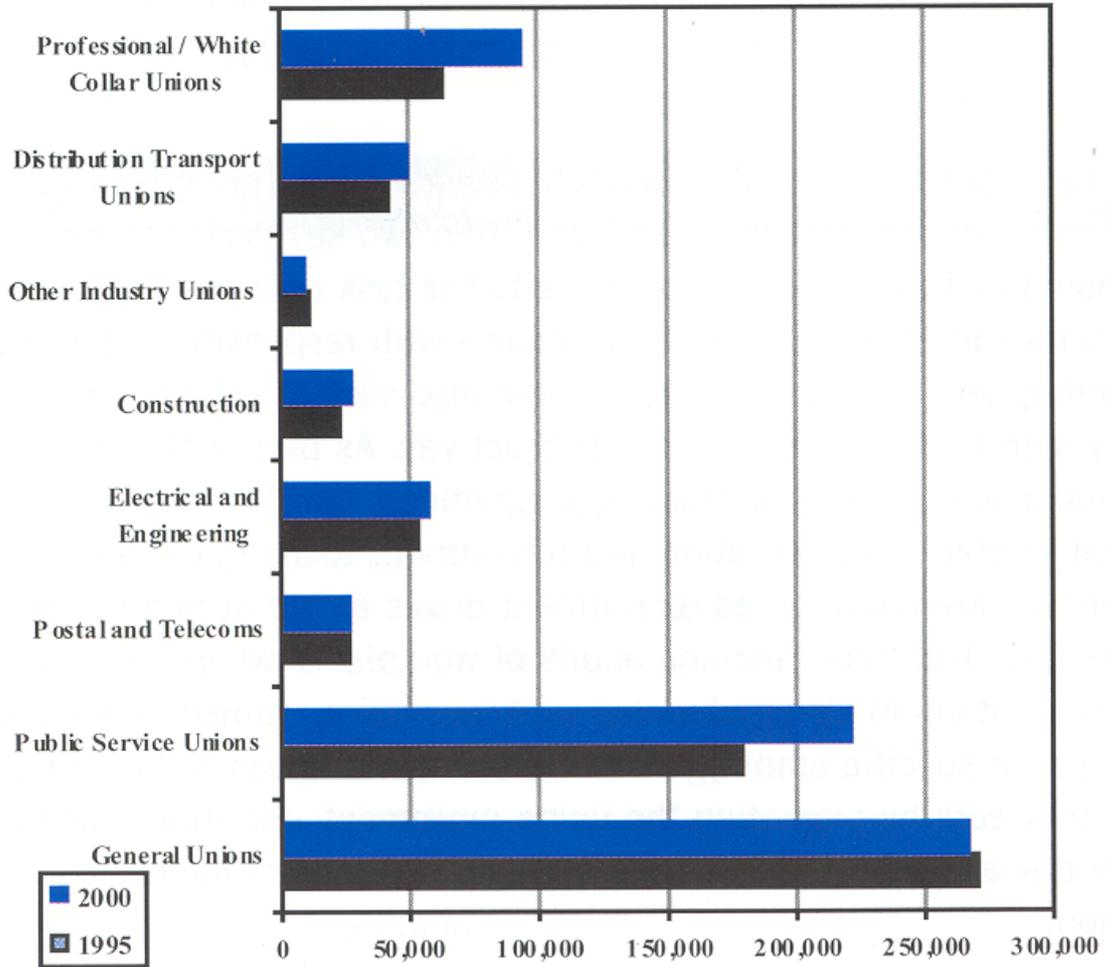
Source: Census of Industrial Production, 1987 and 1998.

Figure 6: Wage trends in Ireland (1988=100)



Source: own calculations on CSO data

Figure 7: Distribution of union membership in the ICTU



Source: ICTU (2001: 65)