

'Stimulating Recovery'

By Sinéad Pentony

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I am going to speak for a few minutes about the current economic context. And in doing so, I will draw on work completed by TASC in recent months, which informs our analysis of the current context. I am also going to focus particularly on the jobs crisis and the need for investment

TASC's principle objective

TASC's principle objective is to bring about greater economic equality in Ireland. When we talk about economic equality, we are talking about the need for a fairer distribution of society's resources, as part of a well-regulated social market economy. Economic equality informs our analysis of what is happening in the economy. The conservative economic narrative is completely devoid of any reference to equality, and this was one of the key factors that informed our decision to host this event. We will not achieve a job-rich and inclusive recovery if we fail to address inequalities within the economy.

Today's event is also timely given that preparations for Budget 2011 are well underway at this stage, while information on key economic indicators released last week has generated debate on our economic performance, which is clearly demonstrating the impact of Government economic policy.

All policy options now need to be put on the table and debated publicly. Today's seminar is intended as a contribution to that process.

Turning the corner

In recent months, talk about the economy has been dominated by the rhetoric of 'turning the corner' and a 'return to economic growth'. But let's consider what many commentators mean by 'turning the corner'. They primarily mean that Ireland will **technically** exit recession by experiencing positive 'economic growth' for two quarters, consecutively. I emphasise the word '**technical**' because most people won't notice the difference – and the international evidence regarding historical collapses of this scale indicates we are likely to experience 'jobless growth' for some time to come. Many people will continue struggling with unemployment, or with the fear of unemployment – and many will continue struggling to keep their homes. Businesses will struggle to remain viable, and public services will continue to be stretched, trying to deliver more with less.

Key questions

While there is a possibility that we may **technically** exit recession at some point during 2011, there are a number of key questions that need to be answered:

- What is **driving** this recovery?
- What **type of recovery** are we going to have? And
- **Who is going to benefit** from this recovery...and **who will be left behind?**

Mixed news on the economy

To shed some light on these issues we must examine what is happening in the economy. Firstly, with increased competitiveness and a weaker euro, net exports are up. Ireland is currently running a record trade surplus, although this is primarily a function of reduced demand leading to a 28% drop in imports. This is the main factor driving us towards a '**technical**' recovery. Consumer confidence appears to have bottomed out, and the May tax figures show a slowdown in the rate of decline in retail purchases. Nonetheless, the May tax figures still remain 10% below last year's levels. In the context of the latest unemployment figures, this is hardly surprising.

Let's not forget: tax flows from economic activity, not from cutting the economy further

Who will benefit?

So at best, the signs are telling us that we are heading for a 'weak' technical recovery driven by export growth. It is unlikely that an improvement in the net export figures will be sufficient for a sustained recovery - certainly, it cannot by itself come close to delivering the hundreds of thousands of jobs that we now need. Ernst & Young in their most recent economic forecast identify the danger of a two-tier economy, with the export sector driving growth, while the domestic economy lags behind. The sectors of the economy most devastated are construction and retail. These sectors will not share in this export led growth. Preventing these (often unskilled) workers from falling into long term unemployment will require targeted strategies involving job creation, and retraining and upskilling.

Also, as many other countries go down the road of imposing austerity measures, the level of aggregate demand internationally will decline. Needless to say, this will have a negative knock-on effect on any prospects for an already 'weak' recovery that is largely dependent on export growth. This recession has highlighted our vulnerability as a small open economy to the ups and downs of the global economy, and clearly demonstrates the need for a more diversified economy, with a

stronger indigenous sector and a lesser dependency on the financial sector. Yet without access to credit, the domestic economy will continue to lag behind.

The worsening situation

The latest CSO figures released just last week indicate that the unemployment crisis is continuing to worsen – the unemployment rate now stands at 13.7%. This gives us the second highest unemployment rate in the Eurozone, and the third highest in the OECD. I alluded to last week's exchequer figures earlier. Tax revenues continue to fall, reflecting the impact of the Government's deflationary economic policy. A strategy focussed single-mindedly on addressing the deficit at the expense of everything else – such as a coherent jobs strategy – risks strangling any nascent recovery.

Cutting public spending during a severe recession can have a perverse impact on the public finances, because much of what the Government saves by spending less; it loses, as a weaker economy depresses tax receipts. Both Michael and Ray will talk about this in more detail. Larry Summers, the Director of President Obama's National Economic Council, recently stated that *'it is impossible to sensibly address either unemployment or long-run fiscal challenges in isolation'*. This statement highlights the inter-relationship between unemployment and the deficit – and the fact that the deficit cannot be addressed in the absence of dealing with the unemployment crisis.

So what can we do?

Back in March, TASC co-ordinated an Open Letter from 28 economists and social scientists to the Government. The initial purpose of this Letter was to generate debate. It was argued that the Government's economic strategy is failing, and it warned that the current strategy of combining public spending cuts with tax increases on low and average income earners would lead to stagnation or at best a jobless recovery. Three months on from the publication of this Letter, and our warnings are being borne out.

We need a sea change in current policy because we are in a hole and we need to stop digging. Specifically, there needs to be a targeted investment strategy focussed on generating employment in the short term, and addressing the serious economic and social deficits that are harming the economy's productive capacity in the medium and long term. Investment coupled with a restructuring of taxation and expenditure in a progressive and expansionary manner to ensure a job-rich recovery – this, and not the current deflationary strategy, is the road to recovery and inclusive growth.

If we valued jobs as much as economic growth, we would measure the success of our economic policy by the employment rate (and of course the quality of those jobs), rather than crudely measuring national success as a function of increasing 'economic growth'. Full employment and quality of life should be the central goals of economic policy – not side-effects. There needs to be a realisation that resolving the jobs crisis will have to be a central element of any successful strategy to address Ireland's financial problems.

Investment

Investment in physical infrastructure and human capital is an investment in the future - and it creates jobs. A recent report from Davy Stockbrokers catalogues “pitiful” levels of investment by the private sector, and states that as a result of a “glut of investment in the wrong places”, Ireland’s technological capacity has “not advanced much over the last decade”. The Report also found that most of the increase in “core” productive capital stock was related to the State or semi-State sectors. Our infrastructure – think broadband - puts us at a distinct disadvantage when it comes to exploiting future economic opportunities.

The current environment is characterised by tight credit and by fragile confidence. This has implications for future levels of private investment. Consequently, the only realistic source of large scale investment in the economy is the state itself. A feasible short term solution to the jobs crisis would be a temporary increase in capital expenditure. Obviously, such an increase in investment must be carefully targeted at projects that are job-intensive and that will provide long-term economic and social benefits. All approved projects should, of course, pass a cost benefit analysis and such projects must have long term positive impacts on the country’s productive capacity. Examples of these types of project include (but are not limited to):

- Improving the **physical infrastructure in the areas of public transport, education and health;**
- Developing a world class **high-speed broadband network;**
- Developing our **green energy infrastructure** – especially in areas such as wind and wave energy where Ireland has a competitive advantage;
- **Regenerating deprived areas** e.g., in Limerick or in parts of Dublin – in many cases, such regeneration projects had reached an advanced planning stage before being shelved, and, of course, they are highly labour intensive.

We must invest in our capacity to recover and to re-invent ourselves. Otherwise we will be left behind. Recently, Craig Barrett from Intel specifically rejected the notion that Ireland could strengthen its competitiveness on the basis of cutting costs, emphasising instead the need to expand investment in the development of high-tech activities and in enhancing educational provision in science and maths. To quote him directly “...*to be competitive, we need to be smart and innovative, not cheap*”. So, if we are going to have a job-rich and sustainable recovery, we need to look at the bigger picture.

The bigger issues

The big picture requires us to consider the question of what direction Ireland should take in order to secure a job-rich sustainable economic future. What’s missing is a new vision for the economy that is:

- characterised by knowledge and by life-long learning;

- resource-efficient and environmentally sustainable; and
- inclusive in the sense of fostering a high-employment;
- focused on the re-distribution of income and wealth generated by economic activity.

Policies to sustain demand and foster job creation should be a key priority of economic policy. Structural reforms of supply-side policies are essential to move towards smart, green and inclusive growth. There needs to be a holistic review of taxation policy – can we continue to afford to forego billions of lost revenue through tax breaks? The focus should move to sources of sustainable tax revenue – this means taxing wealth as well as taxing income. Moving towards a more diversified economy will also reduce Ireland’s exposure to sectoral shocks.

Funding recovery

Calls for investment are met with well worn responses of “the money isn’t there” or “we can’t afford to borrow”. In the TASC Open Letter, we outlined a number of options that could be pursued. Examples included utilising the borrowing capacity of our public enterprises to invest in our infrastructure; using our cash balances and introducing solidarity and municipal bonds. The main point being that **we have options** and the current situation requires us to be as creative in finding the resources to invest in our capacity to recover as we have been in finding the resources to bail out financial institutions.

Conclusion – what needs to be done and how it can be done

To conclude, I would like to re-iterate a number of points:

The rhetoric of ‘turning the corner’ will at best materialise into a weak ‘technical’ recovery that will be characterised by jobless growth. The benefits of this recovery will be felt mainly by the export sector, such as the large multinationals. The domestic economy (in particular SMEs) will continue to struggle. High levels of unemployment will be a key feature of the economy, the cost of which will place extreme pressure on the public finances. Few will benefit from this type of recovery and many will be left behind.

We need to change the direction we are going in because we are in a hole and we need to stop digging. There needs to be a realisation that resolving the jobs crisis will have to be a central element of any successful strategy to address our financial problems. There needs to be a targeted investment strategy focused on generating employment in the short term, and addressing the serious economic and social deficits that are harming the economy’s productive capacity in the medium and long term. We need investment coupled with a restructuring of taxation and expenditure in a progressive and expansionary manner to ensure a job-rich recovery. And we need to be creative about how we finance investment.

Finally – I said it earlier, but it bears repeating: revenue flows from economic activity, not from cutting the economy further

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