

PSYCHOLOGY AND THE ECONOMY OF IRELAND

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The preceding essay in this journal established that economics needs to develop closer links with psychology in order to move the scope and understanding of the discipline forward. Andrew Allen now enhances the economic theory explaining the Celtic Tiger with a psychological perspective on this phenomenon. He asserts that in our efforts to maintain such economic growth we need to complement sound economic policies with psychological insights.

Introduction

An underlying assumption in a vast number of economic models and theories is that of rationality. Individuals are thought of as economic actors who maximise their utility subject to a budget constraint and companies set marginal revenue equal to marginal cost in order to maximise profit. There is certainly some merit to this approach, particularly in the aggregate, but in reality the actions of individuals and companies alike can not always be thought of as rational.

The Celtic Tiger economy of the 1990s is a success story that has received much attention from both political and economic commentators worldwide. The majority of studies and writings on the reasons for Ireland's economic success, contain recommendations on which course of action should be taken in order to maintain growth, using economic theories which assume rationality. However further insight into the economy's performance can be gained by using principles of behaviour in general, rather than just assuming all human behaviour to be rational. Sub disciplines such as social, developmental, evolutionary and, of course, organisational psychology can complement the study of the Irish economy. When analysing the factors that influenced rapid growth in the 1990s and determining to what extent rapid growth should be considered tantamount to an increase in the happiness of Irish citizens, it is helpful to examine the relevant issues using the theories of psychology in conjunction with those of economics. This essay will do just that.

The first section looks at the limitations of using economic growth as a measure of the quality of life or happiness of a nation. The second section examines the issues affecting Ireland's competitiveness and looks at ways of maintaining competitiveness in future years. The third section looks at taxation and efficiency while the fourth examines factors that influenced the Celtic tiger. The fifth section deals with employment and the sixth section concludes the paper.

The Limitations of Economic Growth

In the last decade, and especially in the late nineties, Ireland has experienced strong economic growth. Obviously, from an economic perspective, this is viewed as beneficial. However, economic growth is a means through which the *utility* of people is increased and the term 'utility' is essentially interchangeable with 'happiness'. In "The Psychology of Happiness", Argyle (2001) points out that psychological research at large has not found material income to be the most successful determinant of happiness. Rather, happiness is correlated to a greater extent with social factors, such as family and friends. At a more basic level, it is linked to neurotransmitters such as dopamine and serotonin, which are activated through goal-related activity such as sport or indeed work (Argyle, 2001).

Bank of Ireland recently predicted that economic growth in 2006 will be driven by increased incomes, rather than increased credit. However, the increase in credit in the Irish economy of the last few years is simply too large to ignore. Research by Brown et al. indicated that non-residential mortgage credit in particular is linked with increased levels of stress (and with it, decreased utility). Although long-term increases in credit are arising from residential mortgage loans, credit in the last few months has been driven upwards by non-mortgage credit (Brown et al, 2005). Increased levels of stress within the population will moderate the benefits of any economic growth that this credit brings to the economy.

If we assume technology is driving Ireland's economic growth, as the Solow model proposes, then modern Irish lifestyles are becoming more divorced from their evolutionary heritage. An example of this is the increasing incidence of obesity in Ireland. Obesity among Irish children is growing at a rate of 1% per year. This will almost certainly place an increased burden on the health system in years to come. Evolutionary psychology argues that early humans developed a predilection for foods high in fat and sugar, as these foods were in short supply. With fast food and

'junk' food (as a result of advances in technology) increasingly available to the Irish population, obesity is the result (Lazar, 2005).

Competitiveness

As wages are continually rising in Ireland, one method of maintaining competitiveness is through workers giving better 'value for money'. Obviously, education is one method of doing this. Another is reducing the amount of stress within the workforce in order to increase productivity. It is estimated that tens of millions of workdays are lost every day in the E.U. due to stress-related illness. Organisational psychology research has indicated that a good social support system within the work place and employee training in stress management significantly reduces stress. In fact, U.S. research has shown that every dollar spent on stress management yields over five dollars worth of improved job performance (Statt, 2004). Ireland will be less able to compete if it has a stressed-out work force.

A competitive economy should have strong innovation. Extensive psychological research has been conducted on this topic. One method of innovation frequently used by firms is that of "brainstorming", where workers meet and suggest as many ideas as possible before deciding which ideas are the most effective. However, research by Diehl & Stroebe has shown that brainstorming is actually less effective than workers thinking up ideas by themselves and then coming together (as cited in Hewstone et al., 1997). However, brainstorming is still a popular practice. Irish firms should be made aware of the limitations of brainstorming.

Ekvall devised a Creative Climate Questionnaire, which he contended measured aspects of working environments that are correlated with innovation. (It should be noted that innovation is not just the creation of new products, but also of better ways of doing things within a company). These include humour, trust and emotional involvement with the performance of the workplace. These factors also tend to be linked with overall job satisfaction (Ekvall, 1996). A survey by the Irish Independent recently indicated that the most common reason for workers leaving firms is a failure to get on with their co-workers. It is quite likely that a lack of humour or trust is evident in these situations.

Guilford argued that creative/innovative thought is driven by the ability to think divergently (i.e. thought which does not slip into the trap of being habitual). By exercising one's ability to think divergently, one can become more innovative. Guilford tested this by using tests such as asking people to think of as many different uses for a brick as possible. The

divergent thinker should be able to think of many different uses and also many different kinds of uses (Guilford, 1984). That Edward DeBono can charge over €500 for a course in this kind of thinking is indicative of the value workers and firms are beginning to place on divergent or 'lateral' thinking.

Taxation

One of the canons of taxation is efficiency, and an efficient tax should have little scope for evasion. However, Wenzel (2005) has pointed out that compliance with taxes is closely linked with the mores of one's social group. If there is a 'subculture' of not paying taxes within a certain group (e.g. some politicians in earlier decades if not today) then measures such as tax havens may not prove as effective as hoped. Although such havens may promise confidentiality (to prevent fear of disgrace etc.) they ignore the psychological support tax evaders gain from their shared participation in the crime.

Another canon of taxation is equity. Unfortunately for policymakers, the idea of 'equity' is almost purely subjective. Lewis asked people whether or not they agreed with the statements 'I find tax to be an imposition' and 'Tax helps to pay for essential services that aid to the greater good'. While around half of people agreed with the first statement, 80% agreed with the second! (Lewis, 1982). This demonstrates the psychological construct known as cognitive priming. If a particular idea is mentioned to us, our subsequent thoughts will be coloured by that thought. One could well imagine a discussion on 'Questions & Answers' about income tax. If the most articulate speaker on the programme argues that income tax is unfair, then the viewers will in future be more likely to perceive the injustices of income tax. If the most articulate speaker champions income tax on the grounds that it is progressive, then viewers will develop a more positive attitude towards income tax.

The Celtic Tiger

The strong increase in economic growth during the nineties was linked to entrepreneurial spirit (among other things). Entrepreneurial spirit is more evident in people who have what psychologists call 'an internal locus of control'. What this means is that the person in question believes that he has control over his own life. Hofstede has found in a major cross-cultural study

that internal locus of control is to be found more frequently in individualistic societies. It would not be erroneous to suggest that Irish society has become more individualistic, particularly following the demise of the Catholic Church's extra-secular influence.

Foreign direct investment from the USA continues to be a large factor in strong economic growth. It has been suggested that US investment in Ireland is determined by cultural factors as well as incentives such as low tax, access to E.U. markets and an English-speaking work force. This is illustrative of the ingroup/outgroup effect described by social psychologists Turner & Tajfel in their social identity theory (1979, as cited in Hogg & Vaughan, 2005). We consider ourselves to be part of an 'in-group'. Those who do not belong do the in-group form the out-group. We are more attentive to the positive traits and less attentive to the negative traits of fellow members of our in-group. The inverse is true for the out-group. So it goes with US investors. As Ireland is culturally similar to the US, not to mention a huge number of Irish descendents currently live in the US, US investors will notice positive aspects of Ireland more swiftly than they will notice positive investment opportunities in culturally diverse countries.

Employment

In the last ten years Ireland has seen increasing immigration of workers from foreign countries. An ESRI report has shown that although many immigrants have good qualifications, they tend to end up working in lower-skilled employment. Economic theory would suggest that indigenous lower-skilled workers should feel threatened by competition for work by such immigrants. However, research by Dustmann (2004) indicates that feelings of animosity towards immigrants (where they exist) are at least as determined by old-school xenophobic prejudice as rational, economic thought processes. This would suggest that a policy of anti-prejudice education and advertisements (as can be seen in the kNOw RACISM campaign) would be effective in combating anti-immigration sentiment.

Long-term unemployment has not been a serious problem for Ireland in recent years. However, research by Ek et al indicates that long-term unemployment is, in some ways, determined years before it occurs. Among the long-term unemployed, incidence of adolescent bullying is three times higher than it is in the general population. Low social status as an adolescent is also associated with long-term unemployment in adulthood, particularly among males (Ek, 2005). This indicates that truly effective active labour market policies should target those adolescents who are at risk of being long-

term unemployed in the future, and not just those who have already suffered the effects of hysteresis.

As technology continues to progress, constant re-skilling of the work force is becoming a necessity. Developmental psychologists have pointed to the risks of a generation gap in continued up-skilling. As workers grow older, they become less likely to engage in voluntary training programs in work and tend to prioritise security and leisure over education and advancement (Berk, 2001). With a gradually ageing workforce, Ireland should not allow older workers' skills decay due to a lack of ongoing training.

Conclusion

The Irish experience is one which many countries, particularly the ten new EU accession states, will seek to emulate. There are many lessons to be learned from Ireland's economic success in the last fifteen years, however governments would do well to note that economic processes are always and everywhere coloured by the intricacies of our psychology.

We examine the past so that we may look to the future. The last ten years have been kind to the Irish economy, but complacency is a great threat to its next ten years. In continuing to strive for greatness, policymakers and firms should take account of how psychological processes affect the outcomes of their decisions and how their decisions in turn affect people's psychological well-being. Above all, the fatal assumption of humans as rational economic agents should be left to textbooks.

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