THE ROLE OF MONEY IN KEYNESIAN ECONOMICS

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It is unquestionable that macroeconomics has been suffering a major 'identity crisis' for some time now. Apart from reasons of simplicity there seems to be no reason why one should reason from a macro rather than a micro perspective - why should macrovariables matter more than their component parts? There is also a strong overlap between macroeconomics and monetary economics, which suggests that the implicit assumption of much macro reasoning is that it is money that makes the difference between a full General Equilibrium (GE) model and a standard IS/LM macro model. In this essay I will argue that there has been a consistent failure since the time of Keynes to explain precisely why money should matter. My conclusion will be that the GE framework provides both some neat answers to certain monetary controversies, but equally that it suggests whole range of unanswered questions of its own.

Keynes was in no doubt that the revolutionary nature of his theory sprung from its monetary nature:

"Money enters into the economic scheme in an essential and peculiar manner" (1936, p. xxii).

Money mattered because of its influence on the interest rate (r) which was perhaps the key variable in his system. Keynes proposed what he thought was a revolutionary theory of interest rate determination, namely the 'liquidity preference' (LP) theory in opposition to the 'classical' orthodoxy of 'loanable funds' (LF). A major problem with the General Theory (GT) is that any precise statement Keynes makes when explored further does not sit well with the general thrust of his book, and so it is with his LP theory. One of the few discernable proposition in the book is that saving and investment determine the aggregate volume of employment, and not the rate of interest, which is determined by the money supply and money demand. Keynes is unambiguously clear on this point and attached great importance to it. This proposition was immediately attacked when the book was published, and in my opinion rightly so. There are two senses in which Keynes was wrong Firstly, he saw the LP V^s LF as representing the crux of his departure from Classical economics. Secondly, he saw it as legitimate to separate saving and investment decisions from money demand decisions, a procedure which undermines both his own theory, and later 'reinterpretations' of it.

On the first point, LP V^s LF is not a useful way of seeing the Keynes V^s Classics controversy. Suppose we are analysing the effects of an increased propensity to save. A stylized classical economist who believes that saving affects r (LF) would say that this would cause a fall in r. A Keynesian economist, who believes that saving influences the level of income, would say that it will cause a fall in the level of economic activity. Keynes was quite emphatic that these were distinct theories. In 1937 he wrote in a letter to Ohlin

"If there is no change in the liquidity position, the public can save ex-ante and ex-post and ex anything else until they are blue in the face without alleviating the problem (r too high) in the least - unless, indeed, the result of their efforts is to lower the scale of activity". Thus saving only affects r indirectly by causing a fall in the transactions demand for money after income has fallen. But income only falls in the first place because wages are less than perfectly flexible. And if the classical economist follows his analysis through then he should observe that the fall in r will cause a fall in the velocity of money (increased hoarding) which unless wages are perfectly flexible will cause a fall in income. So the real issue is not what determines what, but rather how prices and quantities adjust. Once one takes a GE perspective and carries out an analysis through to its logical conclusion, the Keynes versus the Classics controversy becomes purely a matter of procedure. This is essentially the answer to the LP V^s LF controversy which followed the publication of GT, and is related to Keynes separation of factors determining the interest rate from those determining employment.

There are a number of ways of seeing Keynes' dichotomy. It can be seen frm the 'neo Walrasian' view point of Hicks, who even as Keynes was writing GT was developing his own GE framework in 'Value and Capital' (1939). From this view point it is nonsense to pursue an argument about whether r is determined by saving and investment or by money supply and money demand because in GE everything affects everything else, and no one price is determined in any one market - this is seen as a legacy of Marshallian partial equilibrium theorizing. Hicks and Hansen formalized this observation by pointing out that the quantity of money and liquidity preference determine not r, but an LM curve. In this repect, it is interesting to note that the framework Hicks developed to illustrate the differences between "Mr. Keynes and the Classics' ended up showing their essential similarity. It was claimed that this was becuase Hicks had been unfair to Keynes, however it would seem that the 'classical economist' who makes an appearance in IS/LM is not a fair representative of the opponents of Keynes at the time.

The most forthright of these critics was D.H. Robertson. He tackled another aspect of Keynes' monetary theory - that ther existed a 'dual decision hypothesis' in decisions involving wealth: firstly how much income to hold in the form of wealth and secondly in what form. Keynes believed that r was only influenced by the second of these decisions:
"[the interest rate] was usually regarded as the reward of not spending, whereas in fact it was the reward of not hoarding" (1936, p.174) i.e. that r is influenced by decision to hold cash rather than by decisions to save. There then ensued a controversy about which of these views was correct; Robertson however showed that this debate was easily reconciled. There are three ways an agent can dispose of his income - he can spend it, lend it or hoard it. These three categories are mutually exclusive. The caricatured classical claim was that r is the reward for not-spending i.e. for lending and hoarding, whereas Keynes' claim that r is the reward for not hoarding i.e. for spending and lending. The common factor in both arguments is lending, thus the debate is easily resolved by stating what r is rather than what it is not. It is as if someone put an apple on the table and A claims it is not an orange and B claims it is not a banana, and then A and B start arguing about whether the apple is more 'not an orange' than it is 'not a banana'. Keynes refused to see this however, and used his forceful personality to ensure that no-one else did either, and this confusion has persisted right up to this day.

Robertson was not just a critic of Keynes however, he had a monetary theory of his own which is a far better representation of the direction in which classical theory was moving in the 1930s than anything Keynes said. He had r determined by a whole range of factors ranging from the genuinely classical productivity and thrift to the Keynesian motives of liquidity preference etc. While Keynes seems to have been well versed in some of the technical characteristics of money (cf Chap. 17) he seems to have overlooked some rather simpler ones - namely that in a monetary economy whether you spend or save or invest or hoard, you need cash. A decision to save or invest involves a demand for money to execute the transaction, and thus will affect r directly and not through income or any of the battery of 'effects' that have sprung up
since 1936. Keynes was certainly right to point out the inconsistency of 'classical theory' (by which he can only mean writers such as Thornton and Ricardo) which claimed that r was determined purely by productivity and thrift while allowing it to be affected by an increase in money supply without explaining how a change in the quantity of money affects investment or saving propensities. It is quite acceptable for him to start his theory at the money demand function stage, but it is a false dichotomy to assume that saving and investment decisions can be somehow exercised without cash, and will only affect r after they have caused a fall in income, an effect which seems to occur in a 'goods sector' which is entirely independent of the money market until income has already fallen. Pursuing the logic further, if a decision to save can have an effect without having to be executed with cash, then since consumption is the counterpart of saving, in Keynes' system a decision to consume must be able to be effective even without a monetary transaction taking place. This makes nonsense of the notional/effective demand distinction which some see as crucial to understanding GT. If there is such a distinction then it is certainly not money that gives rise to it. This in turn casts doubt on the dual decision hypothesis as an interpretation of the General Theory since it extracts from the book something that in logic couldn't be in there. Clower was clearly reading offf the page into someone else's book; however I am reluctant to carry one of his assertions to its logical conclusion
"Keynes either had a dual decision hypothesis at the back of his mind, or most of the General Theory is theoretical nonsense". (Clower, 1965, p.120).

Robertson was also aware that 'the general theory of interest' didn't in fact determine the rate of interest at all, but was a 'bootstrap' theory, determining movements around some elusive rate. His criticisms centred around the speculative demand for money. The speculator in Keynes's system doesn't seem to speculate on anything except other speculators - again the forces of productivity and thrift are denied a role in interest rate determination. However, one gets the clear imp[ression from GT that Keynes is talking about movements around some interest rate, which he is reluctant to give a name to and/or define. In his 'pursuit of sharp distinctions' Keynes disposed of a concept, the natural rate of interest, that would have been of great use to him. Leijonhufvud argues that such a concept could be used in an attack on the 'natural rate hypothesis' by showing that an economy won't achieve its natural rate of unemployment unless it achieves its natural rate of interest. Perhaps one reason why Keynes avoided such a concept was because he feared it would have involved him in a largely inconclusive debate about Capital Theory that was in progress in the 1930s. The main reason for the fruitlessness of this debate was that capital theory then was in a 'pre paradigm state' - the participants couldn't even agree what the issues were. GT had the beneficial effect of short-circuiting these controversies by switching attention from stocks such as 'capital' to flows such as Investment, Consumption and Saving. In the hydraulic Keynesian model, all problems about volume and value are forgotten. The debate about the nature of capital resurfaced in the 1950s and 1960s as the 'Cambridge Controversy', which reached two major conclusions :

(1) There are serious problems with defining and measuring aggregate capital - consequently beware of aggregate production functions

(2) Full GE is immune from these criticisms. However it is arguable that the internal consistency of GE theory results from its high level of abstraction. It seems hard to say anything about anything in these models. The interest rate is of no special significance - it is just another price. It is irrelevant to claim that the interest rate is determined in the money market or that the real wage is determined in the labour market, since each price is affected by every market. However this confuses GE as a framework with GE as a theory. Wile the theory has had little to say so far about the co-ordination problems in actual economies where there are missing markets etc. it can be developed in this direction within the GE framework of constrained choice by individual actors. However one of my central points is that the Keynesian view that money is at the root of the trouble has led to a number of false trails all concerned with the role of money in GE models. This began with Patinkin's work (1956) which as far as some economists were concerned settled for all time the role of money in a modern capitalist economy. It is believed for instance that his book conclusively proved the neutrality of money. What it did prove was that excess demand functions were homogenous of degree in all prices meaning that only relative prices matter. It in no way follows from this that if you double the money supply, you double the price level - such an analysis must assume stability results that have never been proved. Today we have the 'microfoundations of money' literature which applies complex mathematical analysis to the question of what conditions must we impose on an idealised economy to bring an asset such as money into being. Hahn has noted the incongruity of asking such a question in a framework purely concerned with Walrasian equilibrium which ignores "the powerful influence exerted by the future and past on the present ......[and the problems] if the requisite future markets are missing" (Arrow and Hahn, 1971,p369).

Another attempt to recussitate the role of money was that of Clower (1965) which has already been mentioned. The central aspect of this was the so called 'Clower constraint', that "money buys goods and goods buy money but that goods do not buy goods". The problem is that an involuntarily unemployed worker can't communicate to a prospective employer that he would buy his goods if he was employed by him because such a demand would not be 'effective' since he has no money. We have already questioned the claim that this is how GT should be interpreted, but how valid is it in its own right? In my view the problem is not the existence of money; rather if the worker was employed he would consume at best a very small proportion of what his employer produces - the problem could equally arise in a multi good barter economy. This in turn assumes that the worker could actually dispose of whatever 'own-product' he happens to be paid in. Hahn poses the example of someone who works for a company manufacturing sulphuric acid in such an economy. This worker may have considerable difficulty in disposing of the acid to obtain precisely that bundle of goods that he wants - there could still be a problem of deficient demand; it has merely been transferred from employer to worker. Yet fans of Clower tend to the view that no co-cordination problems can cause in a barter economy because there, the Clower constraint doesn't apply - goods buy goods which buy goods, so no problems of deficient demand can arise. This is not true however - goods are only liquid in equilibrium - in disequilibrium a barter economy would face chronic liquidity failures. It doesn't make sense, given all the alleged advantages of money over barter that money should be less efficient than barter in certain sense. The real problem is not the role of money, but rather that of establishing an equilibrium, maintaining it and traversing from one equilibrium growth path to another when required. Incidentally, the notional/effective demand distinction was also made crucial to Clower's interpretation of Keynes' attack on Say's Law. Again money is not essential to this. If an increase in saving manifests itself as a move into Renaissance paintings the same employment problems arise. Any nonreproducible asset will suffice to invalidate Say's Law.

There seems to be no shortage of views abouth where we should go next. Clower and Hahn and others seem to agree than an extension must involve some exploration of price setting behaviour. Clower has suggested a research program involving the explcration of conditions that will facilitate the emergence of middle men, and factors that will govern their price (and quantity) setting behaviour. Hahn says:
"We look casually around, and General Motors doesn't look very small and trade unions don't look very small......... and when ther are large agents around, then the Walrasian model isn't so helpful" (Hahn, 1980, p.164).

He suggests a game theoretic approach, wher individually rational actions may lead to equilibria that can be improved by government policy - 'bootstrap equilibria' as he calls them. Such problems could arise in any economy, monetary or otherwise. What does matter however, is liquidity and Keynes was correct in pointing out that when there is uncertainty, liquidity becomes very important. There will be a desire for liquidity based on a desire to keep one's options open, and except in the certainty based Walrasian world, such a desire is bound to have some role in the functioning of the economic system. However, alternative equilibrium notions are required to discuss these questions and one bias that must be overcome is the view that anything that is not a Walrasian equilibrium is a disequilibrium.

My conclusion therefore is that we need to clear the ground of models that always work (GE) and models that never work (Keynes inspired models). If economies work quite well a lot of the time and collapse very occasionally but in a truly catastrophic fashion then so should our models.
"But as yet no one has the recipe for modelling systems that function very well most of the time, but sometimes work very badly to co-ordinate economic activities" (Leijonhufvud, 1976, p.103).

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THE CAUSES OF CRIME IN IRELAND

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Crime is an issue which is of constant importance in our society. In the last few months we have had the issue of the 'general', debates about cross-border co-operation, and headlines about possible changes in the administrative structures of the Gardai, and these are but the current topics in the area. It is not surprising that crime is considered important in our society. The aim of a society is to help the citizens to maximise the fulfillment of their lives, and if crime is widespread, or even if crime exists, then this is a strong indication that this is not happening. The people committing the crime aren't fulfilled, the victims certainly aren't pushed towards fulfillment, and fear of crime can affect everybody. If crime is particularily high in a certain type of society, we must ask if the benefits of the society outweigh the high crime, or are these benefits worth it at all ? Would perhaps a different approach to crime yield lower crime rates (and more fulfilled lives for people) without having to alter the fabric of society ? Either way, the criminal justice system now accounts for 2% of GNP, and so crime is certainly a subject which merits serious study. This paper looks at crime in the Republic of Ireland, and how the level of crime has increased dramatically in the last 25 years. It tries to discover what has caused this huge and unprecedented increase, and identifies six specific factors. The need for this sort of study is compounded by the fact that very little research seems to have been done in the area - two ESRI and one NESC report (all involving David Rottman who has now emigrated), and a handful of academic papers. Because of Rottman's preeminence, I shall refer to him several times.

To begin with, it is, I suppose, best to attempt a definition of 'crime'.Rottman outlines two approaches: The first, 'legalistic', approach defines crime as " an act punishable by law, as being forbidden by statute or injurious to public welfare ."[1] However, this is really too broad a definition for our purpose, since it includes hundreds of thousands of offences each year of regulations designed to get people to do things in a specific way, regulations which have come increasingly to rely on criminal law, eg. traffic infractions (getting a parking ticket etc.), throwing litter on the ground and so on. It is really only the more serious offences against the law that we are concerned with. Again, the approach to defining 'serious' is legalistic - in Ireland, this is done through the Indictable\Non-Indictable distinction. Since

'serious' is approxomated by 'indictable' , it is this measure I will use as the true measure of crime in Ireland . The annual statistics are published in the Garda Commissioner's ' Report on Crime ' to the Minister for Justice. The second approach tries to find the 'natural properties' of crime , and defines a crime as an action having these properties , regardless of legal definitions .
Therefore , a crime might be any action injurious to social welfare , and a criminal any person who commits an action which injures social welfare . There are two problems with this - firstly , who decides what is best or injurious for society ? Obviously , sociologists will not be neutral about the type of society they want , and will judge accordingly . Secondly , these crime measures would be very difficult to quantify , and this is of course the main advantage of using 'Indictable Offences' ; these are recorded through the criminal justice system .
Before continuing (using the legalistic definition) , I should point out the problems associated with using this 'Indictable Offences' measure.
(1) The ' natural properties ' approach has a point in arguing that the Indictable Offences measure is crude and rigid . Especially in a changing society , it is quite likely that the social good changes constantly , and cannot be legislated for . As an example , ten years ago , somebody selling contraceptives was a criminal , and could be jailed . Now , the Government are urging people to wear them ! Similarily , workers who 'sit-in' in factories are also 'criminals' , going by the present law . The law is usually only changed when there is already a need in society to do so , and it is inevitable that a time-lag will exist during which acts not injurious to society will be classified as being so
(2) The Indictable\Non-Indictable distinction has not been kept up to date . Technically , the difference between them is that any person charged with an Indictable offence has the right to be tried by judge and jury in the Circuit court , whereas Non-Indictable charges are heard in the District court , and then by judge only . When offences were classified as one or the other , they may have been 'serious' and 'unserious' , but now , stealing a box of matches (Indictable) should hardly be considered more serious than drunken-driving (Non-Indictable) .Of course , for the most part , the measures are still fairly accurate .
(3) Crimes can only be recorded in the official statistics if they are reported and recorded . Many people choose not to report a crime to the Gardai , and they in turn sometimes ignore minor offences . As the NESC points out ; " What is actually recorded as a crime is largely determined by the interaction between the Gardai and the wider society ."[2]Victim surveys,where people are asked what crimes they were the victim of in the previous year

and if they reported them show an underestimation of true crime levels by up to 50%.[3] However,there are also doubts about victim studies,and besides,unless the public's confidence in the Gardai alters dramatically,the trend figures are still valid for any particular period.I don't think for example that anyone would argue that crime has not increased in Ireland sice 1961,and that more is simply being reported.

The number of indictable crimes,as measured,has increased in the Republic of Ireland as shown in Table 1.

Table 1

Indictable offences in the Republic of Ireland(selected years).

1961	14818	
1971	37781	
1981	89400	
1983	102387	(peak)
1986	86574	

(source:Annual Report on Crime)

In the 5 years 1957-1961,the average number of indictable offences committed was 15792;beetween 1982 and 1986 the average was 95,520.This means that crime in the latter period was 6.05 times that in the former.Moreover,this increase occurs in all categories of crime-offences against the person rose threefold,offences against property using violence rose elevenfold,and offences against property without violence rose elevenfold.Rottman ,in a detailed analysis,found that every single offence has increased in frequency over the period,except for "larcency of pedal cycles"[4].The effects of this huge increase in crime are very real:

-£350m a year is now spent in the criminal justice system

-in real terms,expenditure on the courts doubled between 1961 and 1981,that in the Garda Siochana trebled,and that on the prisons thirteenfold.

-crime is now a major current affairs and general election issue

-the number of houses with private security firms has hugely increased

-marches and vigils have been held against crime on Dublin's streets with an associated rise in vigilante activity.

It will be noted from the figures that crime has actually fallen since 1983,but the indications are that the decrease bottomed out in 1987 and there is no reason to believe that the overall trend is still not upward.The decrease seems to have been due to the decrease in drug related offences,since the country got to grips with the drugs problem which peaked in 1983.It also coincides with high emigration among young working class people,who,as we shall see,are those most likely to commit crime.It would

certainly be wrong to assume that crime will not increase in the coming decades-all the evidence is to the contrary.
Why crime has increased as it has in Ireland is an extraordinarily difficult question to answer.There are almost as many theories about crime as there are criminologists,and there always seem to be special factors at work anyhow-the random variable u is the only one that can be included with any certainty in an analysis of crime.My approach to the question is based on the following opportunities available to commit crime,and the propensity on the population to actually take advantage of these opportunities i.e. crime=opportunities x propensity.
This might seem obvious,but just stating it would simplify a lot of criminology.Rottman ,for example,divides criminology into two competing theories-the "Structural Perspective" and the "Social Disorganisation Perspective".The former basically corresponds to my "opportunities"-"Explanation.........is sought exclusively in terms of changes in circumstances;the questions of why particular individuals or which individuals will respond to these circumstances is not considered"[5].Social disorganisation " emphasises the disruption and dislocation that inevitably accompanies change"......."it refers to the absence of clear and agrees rules-a breach in the constitutive order of human activity"[6].Since Rottman only works with these two perspectives,and chooses the first as the most relevant to Ireland,he neglects entirely to examining "propensity" in explaining why crime has increased.I agree that Social Disorganisation (certainly so described)is not particularly relevant to Ireland,but in asking which one of these two theories explains crime,he,in my opinion asks the wrong question.
I think looking at crime ,as many criminologists do,purely in terms of a change in external circumstances,is a very blinkered view The NESC made some brief comments on the matter,which I would agree with,but nobody seems to have followed through in an Irish context-"....An individual makes decisions,including those to do with breaking the law,within a societal framework which structures the range and type of options open to that individual"[7].The propensity to commit crime is very important,I think,and must be examined in asking why crime has increased.Therefore I shall examine first the changes in opportunities to commit crime,and second the changes in reasons why people would people would take advantage of them.
Since 1961,the opportunities to commit crime have increased greatly.This is for three reasons,first,the amount of property in Ireland has increased.This sounds almost too straightforward,but it is a factor nonetheless.Property crime accounts for(and always has) over 90% of all crime and the increases in property crime

can be seen in the following table,along with increases in the GNP,a proxy for the amount of private property in the country.

Table 2

Increases in GNP and in property crime(selected years)

	GNP(weighted)	Property crime(weighted)
1961	100	100
1971	145	258
1981	196	627
1986	203	611

(Source:National Income and Expenditure Accounts.)

The idea behind this is simple enough-the amount of targets has increased. The following quote from a *MAGILL* article on crime gives the flavour of this argument "prior to 1965,there were the good old days.There was little crime.One reason there was little crime was because there was little of anything........there were fewer buglaries because there was less to steal inside most houses.Today,there is a wealth of portable valuables in a much greater number of houses.There was nothing as valuable as a video worth stealing from a house back in the good old days,and so the height of a delinquents ambition in the 1950s and the early 1960s was stealing apples from orchards."[8].Videos are an obvious example;cars would be another.The amount of cars has increased fourfold in the last 25 years-so car thieves have four times as many targets.

Rottman's detailed analysis suggests a most interesting relationship between the amount of property crime rate;

"about 1964,a basic transformation occurred in the seriousness of loss sustained through property crime.Before 1964,there is no evidence that property crime was increasing systematically in response to the opportunities available.This is reversed in the years after 1964,where the annual increases are so large as to more than merely compensate for the growing oppoptunities."[9].

Obviously,it is impossible to establish for definite a causal link between the amount of property in Ireland and the amount of property crime,but the following figures from Rottman show the trend he was talking about.He uses personal expenditure as opposed to GNP,and his figures aren't deflated by the GDP deflator.

Table 3

Value of property stolen and Personal Expenditure(selected years)

	Personal Expenditure	Property stolen
1951	100	100
1956	124	77
1961	153	91
1965	207	206

1966	219	259
1971	370	1036
1975(last year)	704	3333

(Source:ESRI paper no 102,p.76)

Up until the early 1960s,even though property increased,property crime fell in real terms.Between 1961 and 1965,the level of property crime caught up to the 1951 proportion of property,and since 1965,property crime has increased so much that by 1975,the last year of Rottman's survey the value of property stolen has increased 33 fold since 1951,whereas property value had only increased 7 fold.

This leads one to the belief that the increase in property was a necessary but not sufficient condition for the increase in crime and that after 1965 there are other factors at work.Whether one regards the relationship however as a simple causal one or as a more complex one the increase in property was undoubtedly one factor in increasing crime since 1961.

(2)The population has increased.

Again this is fairly straightforward.The increase in population increases firstly the number of potential criminals and secondly the number of potential victims.Since over 80% of crime is consistently committed by those under the age of 29[10],and these are also most likely to be the victims of crime[11],the following figures give some indication of the relevant increase in population.

Table 4.

Population aged 10-29,selected years.

	Population	Weighed
1961	826,017	100
1971	954,528	116
1981	1,189,847	144
1986	1,225,936	148

(Source:Census of Population,Various years,1986 Summary population report)

While it is impossible to say how much of the crime increase was due to this population increase,as Table 5 shows,the overwhelming proportion of crime is committed by a relatively small proportion of the population.

Table 5.

<u>Age</u> distribution of <u>national population</u> and of <u>persons apprehended.</u>

0-9	20.6%	1.9%
10-14	10.0%	17.5%
15-16	4.0%	19.3%

17-20	7.1%	23.6%
21-29	13.3%	22.3%
30+	45.0%	15.4%

(For the year 1979 for indictable crimes)
(Source NESC no.77,p115)

The increase in the 10-29 age group would therefore be expected to have caused a much larger proportional increase in crime.I think it is fair enough to assume that this is the case,but as with the property/property crime relationship,it is difficult to judge how straightforward the relationship is.The 10-29 population had fluctuated previously without drastic changes in the crime figures.Emigration in the 1950s,for example ,mainly affected this age group,but crime was fairly constant.It is hard to know if the post 1961 increase in this age group was enough in itself to cause greater crime,and I shall examine other contributory factors later.

The other relevant change in population is the number of households,again representing opportunities to commit crime.This increased as follows.

Table 6.

Number of households in the Republic of Ireland.

1961	455,394
1971	726,000
1981	898,000
1986	976,304

(Source:Various Census of Population Reports)

(3) Urbanization.

It may seem strange to include urbanization here as increasing the opportunities for crime but I think that while urbanization is certainly responsible for increasing people's propensity to commit crime,it also increases the opportunities.First of all,to look at the trend in urbanization:

Table 7

Population of towns and cities,selected years.

1961	1,330,000
1971	1,556,000
1981	1,915,000

(Source:Various Census of Population Reports.)

This increased opportunities in the following way.As we have seen,over 60% of crimes are committed by those under 20.These are not professional criminals,and they are not particularly mobile.Therefore,much of this crime is simply these young people availing of opportunities which come their way.If the population

was rurally based there would be fewer houses,fewer shops,and fewer targets in general presenting themselves.
In other words , if property and population increase (as they did) , crime would be expected to increase everywhere (as it did) , but the increase could be expected to be larger in urban areas (as it was) because of the increase in targets within range of the people committing offences . This is shown in Table 8 , which gives crimes committed per 1000 people in the Dublin Metropolitan Area and the Rest of the Country (figures are not kept on an Urban\Rural basis , and even the present figures were not kept before 1974) . Table 8 clearly shows a link between urban areas and the level of crime.

Table 8

Crime per '000 people , DMA , Rest of Country (specific years)

	D.M.A.	Rest
1974	27.2	8.2
1981	51.9	15.1
1986	47.9	14.7

(Source ; Reports on Crime , various years)

Rottman urges caution however - " Though the contribution made by urban areas , and particularily in Dublin , to the national crime level trends was clearly greater than that made by the non-urban areas , the differential is not dramatic . "12 Only for housebreaking and larceny of vehicles is there a definite link between urbanization and crime , he concludes .

Having examined how the opportunities for crime have increased , I shall now examine how (I believe) the propensity to commit crime has also increased . Much of this increased propensity is based on the modernisation of our society , but I must make clear that I am not saying either that modernisation is bad , or that modernisation must inevitably lead to crime increases . What I am saying is that the speed with which the process occured in Ireland , combined with our traditional inability to plan for the long term , made crime increases inevitable . Japan and Switzerland are two countries where modernisation has not increased crime ; in fact Japan has seen a substantial decrease in crime .
Modernisation can be defined as the process of change a country undergoes in evolving from a pre-industrial to an industrial society . Its primary characteristic therefore is industrialisation , and this is accompanied by urbanisation (less dependance on agriculture , more economies of scale for business) , smaller family size (more mobility needed , bigger emphasis on

17-20	7.1%	23.6%
21-29	13.3%	22.3%
30+	45.0%	15.4%

(For the year 1979 for indictable crimes)
(Source NESC no.77,p115)

The increase in the 10-29 age group would therefore be expected to have caused a much larger proportional increase in crime.I think it is fair enough to assume that this is the case,but as with the property/property crime relationship,it is difficult to judge how straightforward the relationship is.The 10-29 population had fluctuated previously without drastic changes in the crime figures.Emigration in the 1950s,for example ,mainly affected this age group,but crime was fairly constant.It is hard to know if the post 1961 increase in this age group was enough in itself to cause greater crime,and I shall examine other contributory factors later.
The other relevant change in population is the number of households,again representing opportunities to commit crime.This increased as follows.

Table 6.
Number of households in the Republic of Ireland.

1961	455,394
1971	726,000
1981	898,000
1986	976,304

(Source:Various Census of Population Reports)

(3) Urbanization.
It may seem strange to include urbanization here as increasing the opportunities for crime but I think that while urbanization is certainly responsible for increasing people's propensity to commit crime,it also increases the opportunities.First of all,to look at the trend in urbanization:

Table 7
Population of towns and cities,selected years.

1961	1,330,000
1971	1,556,000
1981	1,915,000

(Source:Various Census of Population Reports.)

This increased opportunities in the following way.As we have seen,over 60% of crimes are committed by those under 20.These are not professional criminals,and they are not particularly mobile.Therefore,much of this crime is simply these young people availing of opportunities which come their way.If the population

was rurally based there would be fewer houses,fewer shops,and fewer targets in general presenting themselves.
In other words , if property and population increase (as they did) , crime would be expected to increase everywhere (as it did) , but the increase could be expected to be larger in urban areas (as it was) because of the increase in targets within range of the people committing offences . This is shown in Table 8 , which gives crimes committed per 1000 people in the Dublin Metropolitan Area and the Rest of the Country (figures are not kept on an Urban\Rural basis , and even the present figures were not kept before 1974) . Table 8 clearly shows a link between urban areas and the level of crime.

Table 8

Crime per '000 people , DMA , Rest of Country (specific years)

	D.M.A.	Rest
1974	27.2	8.2
1981	51.9	15.1
1986	47.9	14.7

(Source ; Reports on Crime , various years.)

Rottman urges caution however - " Though the contribution made by urban areas , and particularily in Dublin , to the national crime level trends was clearly greater than that made by the non-urban areas , the differential is not dramatic . "12 Only for housebreaking and larceny of vehicles is there a definite link between urbanization and crime , he concludes .

Having examined how the opportunities for crime have increased , I shall now examine how (I believe) the propensity to commit crime has also increased . Much of this increased propensity is based on the modernisation of our society , but I must make clear that I am not saying either that modernisation is bad , or that modernisation must inevitably lead to crime increases . What I am saying is that the speed with which the process occured in Ireland , combined with our traditional inability to plan for the long term , made crime increases inevitable . Japan and Switzerland are two countries where modernisation has not increased crime ; in fact Japan has seen a substantial decrease in crime .
Modernisation can be defined as the process of change a country undergoes in evolving from a pre-industrial to an industrial society . Its primary characteristic therefore is industrialisation , and this is accompanied by urbanisation (less dependance on agriculture , more economies of scale for business) , smaller family size (more mobility needed , bigger emphasis on

materialism) , growing individualism (less need for communities , high level of international culture) . In looking at how these trends have increased the propensity to commit crime however , I will first look at the effect of another supposed characteristic of modernisation - the changing of a society into a meritocracy . In all , there are three reasons the propensity has increased .

(1) People are more dissatisfied with their lives

It seems obvious that a primary determinant of the level of crime in a society is going to be peoples' happiness or otherwise with their lives . If everybody is perfectly contented , then there will be no motive for anyone to engage in criminal activities . While it is very hard to guage the level of peoples' satisfaction with their lives , it is an almost universal assumption that contentment is a function of material possessions , and if people are materially better off , they will be more satisfied and less likely to commit crimes . But at a time when the traditional values of progress and social justice are seemingly being fulfilled to a degree never before experienced , crime has been increasing at an alarming rate in many Western countries ; in Ireland , just when long standing problems of development and employment had apparently been resolved , crime came to be regarded as a major social problem. It is , in fact , my impression that the last 25 years , despite the increased material wealth , have not brought greater contentment for many people . Why this may be the case is an extraordinarily difficult question to answer . What I think may have happened is that people changed their expectation of what they 'deserved' from life by quite a lot , and the reality changed by a lot less . I will try to explain this .

Fifty years ago in Ireland,there was almost no class mobility whatsoever.If a young person was growing up as the son of a small farmer,he got the farm or he emigrated.Similarly,the daughter married or emigrated.The cities were no different-the working class stayed working class and the richer classes stayed richer.Since the divisions were so institutionalised(and there is no doubt that huge divisions existed) most people accepted the social order as given.This attitude was reinforced by the high level of religous devotion in Ireland,with the willingness to accept as God's wish the valley of tears as a short run sacrifice for the next.

With modernisation however,the old system was recognised as bad for society as a whole and the post modernisation Ireland is supposedly founded on the principle of meritocracy.The shift to industry from agriculture has caused far more jobs to be gained by interview and the extension of free secondary schooling to all students is intended to allow the best people to do best.Religon

has declined in importance so there is no spiritual basis for not doing well.The new system is,in summary,intended to evaluate each person on their merits,no matter what their background.
Despite the ideal,in reality social mobility is barely better than it ever was.The poorer areas get the worst housing,which causes large problems raising and educating children.The Irish educational system is itself severely biased towards the middle class and exam results and backgrounds of university students are biased accordingly.Even if someone manages to overcome these barriers,allegations are often made that job discrimination exists on the basis of home residence.
There does not exist therefore any sort of meritocracy but instead a largely self perpetuating class system which does not rely on inherited wealth any longer but on more complex,but no less effective methods.The richer sections and poorer sections of the population have even clustered in seperate areas to an extent never before seen,and boundaries in cities are almost declined by social class differences.
These are not my opinions but the findings of almost all studies on Irish society.Clancy found "a close relationship between social class and educational achievement"[13] and accused the government of " a distinct lack of commitment to meritocratic principles".Hannan,who studied the area for the ESRI found ".....the basic trend for the universities is for a more efficient use by the middle class...to recreate itself"[14].The Institute of Public Administration found that "....the incidence of unemployment,underemployment and low paid employment are clearly related to social class and occupational structures and they therefore compound other class based deprivations"[15].
My point is that hundreds of thousands of people in Ireland are living on material standards lower than those they were led to expect they would get and lower than those which they deserve to get if the system worked properly.When one considers how much success and its trappings are emphasised in modern Ireland,I feel there is good reason for many of these people,in the lower socio-economic groups,to have a right to feel aggrieved.This happens to coincide with the confirmed fact that the overwhelming majority of crime is committed by people from lower socio-economic groups.Rottman's report for NESC covered the socio-economic characteristics of Dublin residents apprehended in connection with crime.He discovered "...a pattern of early school leaving and marginal employment-as unskilled or semi-skilled labourers-or unemployment is present.Only 37% of those aged less than 17 were still in school,while 54% of that age group were listed as unemployed....8 out of 10 males aged 17 or over brought into the criminal justice system are listed as unemployed...Overall,the

educational and labour force disadvantages of persons entering the criminal justice system are very substantial"[16].

Given these shocking statistics,I don't think there is any doubt but that a link exists between socio-economic circumstances and the crime level.Absolute poverty cannot be blamed,since absolute standards of living are higher than ever before.My proposed link,as I've outlined is on the basis of the unfairness of the system,which makes people frustrated and dissatisfied with their lives.

This could lead to crime in three ways-(i)the frustration itself could cause people to react in a criminal manner(ii)Crime could be looked upon as a way to beat the unfair system-allowing an individual to reach the material standard which he deserves,albeit by resorting to unfair means himself.Crime could be looked upon as an expression of social protest,which might have taken the form of a direct protest in the last century when the constraints on working class life chances were more obvious but now takes the form of crime ,against the more subtle constraints of the post modernisation era.

Whatever the specific causal relationship I believe this link must be explained and could well be responsible,for example for the property crime trend examined earlier(Table 3).Remember that property crime accounts for over 90% of total crime so it is of central importance to explain the property crime increase.We saw that from 1951 to 1965 the real level of property crime did not increase at all,but remained at or below the same proportion of total property it had been in 1951.After 1965,however property crime increased at a far more rapid pace,increasing 16 fold in value in 10 years whereas total property value rose only 3.5 fold.Before 1965 this can be explained as simply the reaction to increased opportunities,but after 1965 the relationship obviously changes.In my view,the alienation,frustration and discontent caused by modernisation have to have played some part in this increase.

I must reemphasise that I am in no way arguing against modernisation,or against post modernisation capitalist industrial democracies.Quite the contrary-I am saying that the failure to make the new system work as it is meant to is responsible for increasing crime-the problem is not the new system,but the way it was introduced.

(2).Constraints on people have lessened.

There are two sides to this argument-on the one hand,there is more individualism,and on the other,morality and community are less important as opinion formers.Individualism is ,of course,another by-product of modernisation.Greater education encourages people to think for themselves,as does greater access

to the media.People are far more likely now to make up their own minds about whether or not to commit a crime,and far more likely to follow it through.
This is especially true of the 15-21 age group who account for over 50% of national crime and who according to NESC "are at a crucial stage in the life cycle,when occasional adolescent rebellion,unless dealt with carefully,can develop into adult criminal roles"[17].Individualism means that if people in this age group feel like committing crime,they are buttocks far more likely to go ahead and do so than they once would have been.According to Röttman,"In Ireland,as in other countries,the ordinary process of transition from adolescence to adulthood brings a growing attachment to conventional institutions and responsibilities,particularly work and marriage"[18].In other words,before people make attachments with society,they commit most crime.
This is where several of the causes of crime tie together.The 17-21 population has increased,as can be seen from Table 4.Their dissatisfaction and alienation has also increased,especially in the lower socioeconomic groups.Finally,they are far more willing to express themselves.The three factors have come together to cause the explosion of crime committed by young working class people,as shown in the available statistics.The only wonder is that the "attachment to conventional institutions and responsibilities" is so strong that it reduces crime by so much as people get older.
The flip side of this new individualism is that people feel less inclined not to commit crime now because the church or community says they shouldn't do so.The close knit communities of old did not allow for much crime,since everybody knew everybody else,and strangers stuck out.Since modernisation,a far greater proportion of people travel to work everyday,so people don't know their neighbours as well,and strangers in an area are not noticed.This is compounded by many people not caring anyway whether their neighbours are victims of crime;"community spirit" not being what it was.Rottman eloquently describes the process-"consensus and homogeneity which forged social solidarity within the communal village become displaced by the functional interdependence that characterises the complex and segmented division of labour in modern society"[19].
(3)Greater chance of success.
The final reason I believe the propensity to commit crime has increased is because an offender in 1988 has a lot lower liklihood of getting caught than an offender in 1961 had.This means,I feel,that the criminal justice system now acts as a smaller deterrent than before.The number of people convicted and

punished has increased.The number imprisoned has increased.The number of Gardai has increased.The resources devoted to combatting crime have increased.However,I believe that what affects a potential offender is not the absolute numbers,but the chances of him getting clean away,or caught,if he commits an offence.The following table shows how his chances of escaping detection have improved.

Table 9.

% chance that a crime is not detected.

1961	33.6%
1971	53.6%
1981	63.4%
1986	68.4%

(Source:based on detection rates in "Report on Crime"-various years)

It is difficult to know what effect this had on the crime rate,but it had certainly had some effect.It is important to note that the actual numbers of criminals caught increased,but there was such an explosion of crime that the percentage caught dropped.Therefore,while the level of absolute deterrents increased the real deterrent fell.No country could afford keep security levels in proportion with crime,this would now mean over 40,000 Gardai in Ireland for example.

Therefore,if the other causes of crime were to be alleviated in the future,and crime fell,then the real deterrent would rise and push crime down further.Concentrating purely on this cause of crime,as the "law and order brigade" do ,is shortsighted.International research has shown this doesn't work and in Britain the crime rate has risen by more than 50% since Mrs.Thatcher came into power,on a policy of increased law and order 8 years ago.

To summarise then,I have tried to analyse what the factors are that caused such a massive increase in crime in Ireland in the last 25 years.I decided that the increase in crime was due both to an increase in the opportunities for crime and an increased propensity of people to commit crime.The former was examined by looking at the increase in property,the population growth and urbanisation.All three seemed to have caused an increase in crime.The propensity was examined by looking at the increased level of frustration of many people in Irish society with both their own lives and the way society has dealt with them,the breakdown of constraints on people,and the increased chances of a crime not being detected.I believe I have given strong intuitive reasons for crime to be dependent on each and all of these variables.

This paper then,simply looked at the causes of crime in our country.It is a lot easier to examine the causes than propose solutions,and I won't attempt to do that here.However I must say that the first step towards any solution is always a clear identification of the problem,and I feel that the amount of time and resources we devote to this in Ireland is far too small.Much of what has gone above represents my striking into unknown territory,because nobody else seems to have done reaserch in these areas.Compared to the amounts spent on security and law and order,the amount spent analysing where and how money should be spent is minimal.Ireland is no different from many other countries in this respect but this is hardly an excuse.There is (as ever) some cause for hope-the recent promotions in the Gardai have brought several analytical minds into senior positions.It is to be hoped that they will encourage more thoughtful approaches to combatting crime than those who have gone before.

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THE CHANGING PATTERN OF INDUSTRIAL RELATIONS IN THE 1980'S

Majella Fahy.

During the 1980s,against a background of rapid political,economic and legal change the nature of industrial relations between employers and unions and management and employees bagan a period of readjustment which has continued to the present time.The new patterns of industrial relations which have emerged have been epitomised by more assertive management,"union realism" and a general belief (promoted by government) that the efficient functioning of the economic market place is all important.Also union power has been greatly weakened and unions have been effectively excluded fron influencing government policy.This is in sharp contrast to the '60s and '70s when attention was focussed on the establishment of industrial relations procedures and institutions and this was underpinned by aggressive,reactive and powerful trade unions which were periodically incorporated into government policy making.

The new pattern of industrial relations that are emerging and the changes that they bring can only be accounted for when they are related to the wider socioeconomic environment as well as the political and legal systems.All of these factors have acted together to impinge on the sources of power available to trade unions and in this way have changed the face of industrial relations.

Objective and subjective power are the two main sources of power which enable employee groups to resist industrial closure and indeed any other management decision which they oppose.If recent industrial disputes are examined it will be seen that their sources of power have been under constant attack both through political and legal systems and the economic envirinment.

The most significant forms of objective power are the strength of union organisation and the strategic importance of the workers covered.As the recession has deeepened and consequently unemployment has increased,union membership has decreased robbing unions of an important source of power.Deskilling has reduced the strategic importance of workers;making them easily replaceable.It is a vicious circle;workers are unable to successfully resist deskilling procedures because they know that there are four million unemployed in the U.K. and a quarter of a million in Ireland and so can be easily replaced,particularly if their jobs require little "skill".Power also depends on how

workers view their own situation.Taking into account that four million people are unemployed and that an increasing proportion of those in employment have experienced unemployment (fewer than 1/3 of registered unemployed have been continuously registered as such for more than one year) it is easy to se why people's commitment to resistance has diminished as unions weakened and job losses become inevitable.
It couls be argued that stoppage in "hi-tech" industries involves high costs and so strengthens a trade union's power depsite deskilling procedures as management would be eager to avoid such stoppages.That may be so in an environment where alternative sources of labour are hard to find but the 1980s is not such an environment.It is also a fact that the hi-tech sector has strongly resisted trade unionism in its plants.For proof,one only need look at the activities of management during the Greenwick or Wapping disputes.During the Greenwick photo processing labs dispute in which APEX sought recognition,Ward ,the owner of the factory employed other people to replace the strikers.During the News International dispute at Wapping Rupert Murdoch demanded that unions agree to end the closed shop system,that all papers should be produced with new technology,that a positive and binding commitment not to strike should be made and that demarcation lines should cease to exist.The talks broke down and union members ballotted for strike action.On the 24th January 1986 the strike began and in the same day News INternational issued all printers and nonjournalists with notice of dismissal and announnced that they were moving all their titles to Wapping.Within two days all the titles were being produced at Wapping by newly recruited employees.
The balance of power has most definitely shifted,the legitimacy of closure and other management tactics have been redefined and market criteria have prevailed.The miners' strike represented another staging of the battle to redefine legitimacy:whether closure is acceptable on the basis of market criteria alone or whether social considerations should be taken into account.The facts of the NUM strike are well known and the conclusion was that the government via the British Coal Board won,asserting the primacy of market forces and weakening the trade union movement.If the miners had won the legitimacy of closure on economic grounds would once again have been questionable.
The Ranks dispute in Ireland had a simlar effect.The dispute arose in 1982 when RHM foods announced the rationalisation of their Irish operation with seventy redundancies to be divided between their Dublin and Limerick plants.The problem arose when Ranks pleaded inability to pay the redundancy settlements which had been set out in an agreement in 1978.The matter was referred to

the Labour Court and it side with the workers.The company ignored their recommendations and used its ultimate weapon-the threat of withdrawal of all operations from Ireland if the workers did not return to work.The workers gave in and within three weeks the company announced that it was closing down its Irish operations.Workers occupied the Dublin plant and were subsequently sent to prison for refusing to obey a court order.In May 1983 as a result of legal proceedings a liquidator was appointed,the remaining workers were removed and twenty-six workers received no redundancy payment.The dispute highlighted the weakness of unions in the face of closure and the outcome resulted in a strengthening of management power.It was farcical for RHM to say that they were unable to amke the redundancy payments when at the same time they were investing £20m in their British operations,yet they got away with it and our legal system helped them to do so.Unions are powerless in the face of "runaway" plants and that is something that will never change as long as our economy is run along capitalist lines;however through legislation we could back union strength in order to help even out the balance of power,but instead we throw all our legal weight behind employers.It was held to be illegal for workers to occupy the Ranks plant in Dublin,but it was not illegal for the company to pull out of Ireland without giving twenty-six workers even their statutory entitlements.A company has always been able to close down its operation,what has changed are the acceptable grounds for doing so.

Further proof that there has been a shift in the balance of power can be seen in the decline in strike action in recent years despite or perhaps because of the increase in job losses.The proportion of U.K. vehicle manufacturers reporting strike action fell from 67% in 1980 to 23% in 1984.Kenneth Walsh conducted a study of twenty five companies from various industries between 1982 and 1984.The figures show that nine out of the fifteen companies in the manufacturing sector reported a decrease in disputes,this compares to three out of ten in the services sector.In the same period the manufacturing sector witnessed the most job losses.

This shift in the balance of power has been strenghtened by legislation.The major thrust of the Tory lesislation of the 1980s is towards extensive restriction on the immunities which trade unions previosly enjoyed and essentially it means that the collective strength of the workers is to be limited by the boundaries of the employment unit.For example ,the 1980 Employment Act removed protection in trade disputes against common law civil liability in secondary action which means that workers who take action in a dispute which their own employer is not a primary party can be held liable.

According to the 1980 act dismissal for nonmembership of a trade union is illegal and it also states that where a closed shop agreement is in operation an employee can object on grounds of conscience to joining a trade union.This makes a closed shop almost impossible to administer and as a result closed shops have been on the decline in Britain,weakening trade unions even further.
The scope of a trade dispute under which employees can be protected has been narrowed by the 1982 employment Act.Before this act a dispute needed to be "connected" with employment matters,now it has to relate wholly or mainly to them.This implies that industrial action launched to protect jobs as part of a wider campaign against government policies of privatistion(say) may now lose the immunity it could have had under the 1906 act.
The 1980 act removed the limited obligation that ACAS could replace on employers to recognise trade unions.This legislation came about as a result of the loophole discovered in the Greenwick case ,which made it impossible for ACAS to enforce its procedures.However if the government had been interested in the in strengthening trade unions it could have found a way to blockk the loophole;instead they removed the obligation placed on employeers to recognise unions!
However,despie all this legislative intervention employeers have been slow to use it.For example in 1983 Shell was involved in a dispute about a pay increase.As the dispute escalated workers from the Stanlow plant (where an all out strike was called after a worker wsa disciplined) picketed the Haydock distribution terminal in Merseyside,twenty six miles away and eventually secondary picketing rose to include about one third if Shell's distribution terminals .In October 1983 Shell obtained an interlocutary injunction from the High Court(under s.16 of the Employment 1980 it is unlawful to picket except at your place of work).The TGWU ignored the injunction and in fact picketing spread.Shell however did not inititate contempt of court proceedings;it concentrated istead on negotiating a new wage settlement.Shell is a long established MNC and it was involved in a straightforward dispute.It had established industrial relations practices within a voluntaristic tradition and in this case the economic stakes were not high enough to make management willing to shatter all of that by pursuing legal action.However,the point is that when a company does consider the economic stakes to be high enough it can resort to this form of legal backup and this gives added strength to management.Collective power is the only power that trade unions have and together with increasing

unemployment and transnational employers,this legislation strips workers of their power.

Having looked at the major causes of the changing pattern of industrial relations it is necessary to examine the effects of these changes.The question is whether or not increased risk of job loss,weak trade unions and a hostile government have made employees more defensive and restrictive in their working practices or on the contrary more "realistic" and "flexible"?

After Labour's defeat in the 1983 general election in the U.K. the idea of "realism" began to emerge at the TUC conference and Eric Hammond and the EEPTU were the main exponents of the "new realism".This new mood is something that suited Mrs. Thatcher and her government.Therefore it is ironic and indeed an indication of the "union bashing" mentality of Thatcher/Tebbit that it was they who dealt this new idealism its first severe blow.

In January 1984,Sir Geoffrey Howe announced that the Unfair Dismissal and other provisions of the 1970s Employment Protection Acts were being would no longer to apply to staff at Government Communications Headquarters(GCHQ).New conditions of service were to be introduced under which staff would be permitted in future to belong only to a departmental staff association approved by their director.Staff were informed that if they remained in their traditional trade unions they would be transferred to other posts of the civil service and if they refused to complete the option forms or to transfer,then their employment would be terminated.

In light of the new mood of realism the unions were shocked but believed that if they reasoned with Mrs. Thatcher that she would see the error of her ways,however she stood firm.Comments made by Larry Smith,the TGWU's executive officer would probably reflect most trade unionists' feelings on this matter :

"New realism was dead and buried before last Christmas when Maggie Thatcher took secret decisions to ban unions at GCHQ ,persevere with anti trade union laws and to take on the miners."The EEPTU have continued to pursue the ideal on "New Realism";they sign no-strike agreements and seek to co-operate with employers.Other unions have been forced through risk of job loss and a hostile government to back down on issues such as recognition(at GCGQ) and redundancy(miners'strike) but they have not done so willingly.

Have employers made use of the change in the balance of power?The decrease in the level of demand ,the increase in product market competitiveness and changes in the nature of consumer demand all provide a strong incentive for managers to increase their control over profitability.This means reducing

costs and increasing flexibility of labou. terms of time,numbers and production.
Both an IMS survey and the Labour research department found that flexibility was on the increase in Britain,but that flexible working practices were motivated by cost cutting rather than an interest in changing the employment culture at the core.It has been argued that management decisions owed more to concerns with product quality and standardisation than to labour management issues.It is pointed out that deskilling does not necessarily lead to enhanced control(we are told that workers can sabotage machinery-but this would still cost them their job) and that the crises in Britain have not provoked a decisive move in management policy towards unqualified anti-unionism.It appears that a substantial decrease in the scope of collective bargaining and of management dependence on union mediation in dealing with employees is a more widespread objective and is often connected with more general production strategies.
The answer to this arguement is quite simple.It doesn't really matter what the motivation for management decisions is ,the net effect is the same.Labour flexibility agreements are now being negotiated even in industries that are traditionally associated with strong trade union opposition to this issue e.g.miners are negotiating a five year multi skilling program and a six day week.Management have used the economic situation to coerce employees into agreeing to such arrangements.The shift towards unitary policies based more on coercion than cooperation has gone largely unchallenged.Unions lack the power and members the will to conduct major campaigns against policies which are porttrayed as common sense and the "economic facts of life".While not being specifically anti-unionist management have used this weakness to further their own ends.
In view of what has happened in the first half of the 1980s what role will management play in future industrial relations practices?Management realise that simple compliance by employees is not enough if a company is to compete successfully.So an effort is made to "involve" employees on an individual and collective basis in "key" decisions that affect them.Mechanisms have been put into place which obscure the dividing line between management and employee interests.Employee shareholding schemes and sophisticated communications networks have been set up e.g. team briefing systems and corporate videos in which the managing director talks directly to employees.The interesting thing is that a WIRS survey shows that while the level of consultation is low but increasing there is a decrease in negotiation on non pay issues.In

other words,the employees level of control over their working environment is actually decreasing.
If management had the choice they would probably use sophisticated paternalism as their method of controlling industrial realtions.This means that they would refuse to recognise trade unions and that they would make working conditions so good that employees would have no choice/need for a trade union.However,this is expensive to operate and only the large MNCs such as Digital can afford to operate it.
Most British and Irish companies(and particularly older ones which recognise trade unions) would probably be content to use a consultation approach.However this is probably the most dangerous of techniques as far as employees are concerned.Consultation promotes the idea of problem solving and stresses the importance of communications.Confrontation and the division between employer and employee interests are obscured.What management is seeking is a situation akin to sophisticated paternalism without the perks.
The recession has meant an acceleration of structural change in the economy.Employment is growing in small scale industry,an area where employer attitudes to trade unions have traditionally been hostile and the level of part-time/casual labour is high.This implies that trade unions face severe organisational problems.The production industry's share of the work force decreased from 30% in 1979 to 26.7% in1984,while the service sector's share increased from 20.3% in 1979 to 24% in 1984.So employment is growing in area where pay has traditionally been low,union organisation weak and the work temporary in nature.Unfortunately union recruitment activity is concentrated around the margins of existing membership groups rather than in establishments where the union has no presence.It is clear that it is difficult to organise workers in an industry where there is high turnover of labour but it is also clear that it is workers in such industries who are most in need of union support.
Employees of small firms are far more vulnerable than employees of larger firms because of the personal nature of their relationship with their employer.Therefore they need an independent representative who will raise issues with an employer in their behalf.There is ample evidence that part time workers are poorly paid and a disproportionate amount of these workers are female,unskilled and, in multiracial socities ,tend to come from minorities.A survey conducted by Wendy Richards showed that some home workers earn as little as 30-50p per hour while, the average industrial wage is £4.75 per hour.In 1979 a select committee in homeworking found that only 15% of the people surveyed earned more than £1 per hour.Part-time

workers(less than 18 hours per week) are not even covered by employment legislation and so they are particularly in need of trade union representation,but the unions have been slow to move into these areas.

Trade union leaders are anxious to protect and defend their members' jobs and due to the increase in unemployment and the decrease in union membership they have been unable to do this.This is why we find the ICTU voting 181 in favour and 114 against edorsing the National Plan for Economic Recovery.Outlandish promises to create 100,000 jobs have been given in return for agreements that 2.5% is the maxiamum pay increase that will be sought in either of the next two years.The interesting thing is that while in the late 1970s and early 1980d trade unionists had high hopes for the employment targets,today they know that it is unlikely that they will be met.Unions are not blind to what is going on,they just lack the power to do anything about it-and this is in part their own fault.Early in the 1980s they stood back and watched while their rights were slowly taken away from them.They did not seek to recruit new members in new industries amd now they are paying the price.Unions badly need to adapt to their new environment;otherwise their future looks very bleak,especially when we consider the eloborate systems of labour relations and "human resource management" being drawn up by employers.

Since 1979 Margaret Thatcher has used state power to restrict workers combinations so that markets could be safeguarded.However,she would not have succeeded in doing this if other conditions had not existed(e.g. the high unemployment rates which were not entirely her own creation).The wider socio-economic environment,as well as the political and legal systems all interact to set the conditions which decide the patterns of industrial relations.Perhaps future governments will use state power to even out the balance of power between trade unions and employers but with increasing unemployment and increasingly weakened trade unions this seems a long way off,and unions don't have time to wait.It is up to them to strengthen their organisation to cater for the needs of people employed in service industries and other sectors which badly need trade union representation(e.g. part time workers,home workers,people who work on small family farms ,factories etc.).If trade unions want to survive and contribute to the changing patterns of industrial relations this is the challenge they will have to meet.

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IS INDUSTRY BEING DEUNIONISED?

Mairead McDonnell.

"Is industry being de-unionized?". This topic has given rise to much controversy in recent years and is central to industrial relations today. Brian Donaghy's recent article in the Irish Times shows only too clearly the dilemma facing not only the Irish unions but those in Britain and America.

1. "On present trends the Irish Congress of Trade Unions is in dire danger of becoming little more than a talking shop, an organization holding an ever increasing number of conferences but commanding less and less attention......
In the US trade unions have almost been wiped out, with less than 20% of the workforce now carrying trade union cards.......
In Britain the unions have been severely mauled by the Thatcher government and despite the years of cutbacks in the "social wages" of state provided health, education and social services, there is little public suppport for the union movement."

The above quotes would appear to point towards the fact that support for the trade unions is in decline. Does this mean indutry is being de-unionized?

We will begin our discussion of de-unionization by firstly defining briefly what we mean by de-unionization. This of course deals with trade unions so we will define what a trade union does. We will then go on to examine the trends in trade unionism over time, highlighting the de-unionization process. The various factors giving rise to these trends will then be looked at paying particular attention to those leading to de-unionization. The conclusion willl briefly discuss the reaction of trade unions to recent trends and any measures taken to relieve the situation.

De-unionization occurs as the result of a reduction in one of two variables. It can quite simply mean the reduction in the overall membership of trade unions. Alternatively de-unionizastion can also mean the reduction in the power of a trade union i.e. it can no longer carry out the function for which it exists to fulfill.

What is the function of a trade union?

An organization's function may be defined as the role or task it is required to perform and the means employed to carry it out. In essence a trade union may be defined as:

1. "any organization of employees which first has one of its main objectives negotiating with employers in order to regulate the pay and conditions of its members and, second, is independent of the employers with which it negotiates or seeks to negotiate."

Alternatively we can lool at the Webbs' classical definition of a trade union

2. " a trade union is a continuous assocaition of wage earners for the purpose of maintaining or improving the conditions of their working lives."

Whatever their role trade unions are a product of all Industrial societies. They have existed for over one hundred years and much study has been done on trends in the development of trade unions.

In order to examine whether industry is being de-unionized we must decide on certain indicators by whcih we can measure the growth and power of trade unions. One of the most common indicators is trade union membership and the pattern of membership.

Between 1945 and 1984 trade union membership in the Irish Republic practically tripled form 170.8 thousands to 501.8 thousands. This increase was charactized by periods of rapid and gradual growth up to 1981 but since then there has been a sharp reduction in union membership. In the decade 1961-71 new membership of 58,000 was achieved (18%) but this was improved upon 1971-79 when membership increased 29%. Union membership then dropped 1979-81 by 6%.

This pattern of growth and decline was matched by that shown in Britain during the same period. In America the day of doom came much sooner as pointed out in the Industrial Relations Journal in an article called "The mid life crisis of the American Labour Movement". Total union membership reached a high point of 30.5% in 1968 and has declined ever since. Up to 1980 the total number of unions grew annually but because growth in the total labour force was even greater, the annual percentage unionized figures showed a steady decline . Subsequent to 1980, the percentage decline was made more severe by actual reduction in the number of union members.

As indicated above in the American statistics a better measure of trade union membership levels is union density:

union density=the ratio of total number of members to total number of employees and total registered unemployed i.e. we are taking account of changes in the size of the labour force. If we just look at increases in the membership they could simply be due to increases in the labour force.

In the 1960s in Ireland union density increased. From 1971-79 the upsurge in membership was reflected in higher density levels (1979 highest density level 54%). Post 1979 the density levels dropped with a value of 48% in 1981.

The growth in union power up to 1979 and decline post '79 was demonstrated by a number of clearly observable trends. These include:

1. degree of collective bargaining
2. growth or decline in the number of trade union representatives and their participation in managerial decision making processes.
3. Government intervention in the national economy and involvement of the trade union
4. Employment laws - advantageous of disadvanatageous to the trade unions.

Pre 1979 there was an extension of collective bargaining in employing organizations and at the workplace level. This led to a decrease in managerial power to make decisions without the go ahead of trade unions. There was a growth in the number of trade union representatives and their increasing participation in managerial decision making and day to day administration at the work place. Government intervention at this time clearly involved the trade unions thus increasing their overall clout. Any employment laws passed at this time were advantageous to the unions and led to their increasing power. Therefore up to 1979 in observing trade union activities we would concluded that they were a powerful group in society.

Post 1979 the situation was reversed. This period saw the weakening of trade union power in favour of employees and management. The unions have effectively been excluded from influencing government policy making and are threatened by economic recession.

In order to understand the recent de-unionization process we will examine the factors which have caused it. This involves a close examination of the environment in which trade union activities take place. One word of caution from Jackson before we proceed would perhaps be appropriate:

"It is clear that trade unions flourish in certain conditions rahter than others ..... However, while the environment in which unions operate is important it is not in itself a sufficient explanation for the growth and development of trade unions. The reactions of union members, and probably crucially union leaders, to these conditions, is also important. Unions may or may not take advantage of favourable environmental conditions : favourable conditions do not make union growht inevitable, simply possible or, at the most, likely."

Numerous writers have provided lists of factors which affect the growth and decline in trade union membership and power. Some of these include:

Economic factors, - 1. inflation
- 2. unemployment

Sectoral changes in Employment, - manufacturing to services
Composition of workforce, - 1. white collar workers

2. education level
3. female participation
4. move from primary to secondary industry
5. permanent to partime work

Technology, -Shift to new microelectronics, - New non-union industry
Management beginning to manage
Growth in the range of Employment Law
Politics

We will begin our study by examing economic factors. During the 1970s Ireland experienced high inflation.. In this situation employees' living standards were threatened. Therefore the pressure from trade unions to protect living standards through wage and salary increases encouraged new membership. Similarly redunancies, short-time etc. would have prompted many employees to join unions.

The economy has new entered a period of downward wage and price adjustment. Analysis of pay settlements in 1982 range from 5 - 9% with the 'norm' at 7%. The reduction in the rate of inflation has had a dampening effect on the ability of trade union negotiation to conclude large wage settlements. This makes the benefits of collective bargaining less apparent eg some companies have zero 'norms' - Hoover and British Airways. eg Pan Am pracitising claw-back bargaining where a reduction in terms and conditions has been agreed reluctantly on the part of the labour force.

We are now seeing trade union negotiators who are willing to sign pay deals which are to last for two or three years. This means there has been a significant decline in the power of the unions and there is less incentive to join.

Unemployment is the result of an overall worldwide recession but has been exacerbated in Britain by government economic policies which have been designed to eradicate inflation. Trade union membership fell by greater than 1 million in 1981 and 82 largely as a function of job loss.

This is, however, linked up with another factor affecting unionization. Job losses were disproportionately concentrated in the heavy manufaturing industries or as they been called 'engine room industries'.

These industries are concentrate in particular areas. and the affects of the job losses are felt particularly in a number of towns and villages in the northern region of Britain.

Northern region 1951 - 75 average UE 3.52%
1982 " " 16.5%

Loss of union membership here represents a loss of tradition, history and culture which reflects more than a mere loss of trade union card holders for a temporary period. Occupational restruturing has occured due to the destruction of these indutries and there is no evidence to suggest that where employment is taken up in a new sector trade union tradition and culture is automatically transferred to the new employement.

Since 1945 there has been a decline in the 'other' manufacturing plants and an increase in employment in the service industries.

John Kelly would look at these developments as producing an increasingly "inhospitable climate" for trade unionism. Traditionally the service sector was as area where trade unionism was relatively weak. In the period 1969-79, however, inroads were made in this area and the rapid trade union growth was partly a result of new members coming from the public sector ie more white collar workers.

Post 1979, however, the trade unions are not making substantial inroads into the white collar and private services employment. There are two kinds of service employment - highly skilled, high status jobs and low skilled, low status jobs. At both ends of the scale there are problems. Both ends are characterized by a lack of tradition of trade unionism. At the upper end workers have some misconception that they belong to an "upper, middle class elite". Some headway has, however, been made into this sector on the part of trade unions eg ASTMS has now included the financial sector which had been totally nonunionized.

Similar problems have been faced by America as outlined by Hoerr. He maintains that union power will remain strong in industries such as autos, mining, steel, construction retail food, railroads, airline and trucking. These forces of strength, however, are crumbling and

"unions are making little headway in organising such growth industries as financial services, and high technology. Union membership in privcate industry has been dropping .... in public employment the levels of white collar unionization are high."

In the lower service sector in Britain eg contract cleaning there is no great trend in unionization. This ties in with another factor affecting trends in unionization, namely education.

In general those whose education extends beyond the minimum school leaving age and those who obtain formal qualifications are less likely to join trade unions than those who leave school at the legal minimum age. The main exceptions are teachers and nurses who belong to highly unionized professions. In America growing numbers of well educated white collar employees are adding to the pressures for protective labour laws.This is further

reducing the power of trade unions as will be seen later when we study labour law in detail.
Other characteristics which may lead to a decrease in the power or membership of trade unions concern the composition of the labour force.One fact that is commonly accepted is that women do not join trade unions to the extent that males do.In recent years there has been a significant move from promary to secondary employment.The secondary labour force is predominantly female as they are often only interested in having a parttime job.Why does this trend towards part-time work lead to de-unionization?The answer lies in the fact that it is not financially feasible to organise this type of worker.Constant effort would be required ro recruit new members as the employees changed and it would be difficult to continue representing the previous employees.The wages of these employees are normally low therefore the union dues would be lower(assuming a pro rata subscription system).Also employers tend to discourage unionization in these industries.
Trends however,do show that female union membership density has increased from 24% in 1948 to 39% in 1979.A lot of this is due to increases in female white collar work which increased from 30-46% in the same period.These statistics are for Britain but similar trends can be seen in Ireland.Because of the shift in employment patterns some 54% of all union members now work in the public sector,a sector employing 36% og the working population.
To summarise the findings so far.De unionization has been caused by:a decrease in inflation,a decline in manufacturing coupled with the rise of the services sector,an increase in white collar workers and in female participation rates.
Another important factor is technology.Technological advances normally lead to a decrease in the required workforce as
"oppoptunities afforded through technology allow companies to significantly increase output with a stable or reduced labour force."
This reduces the scope for union activity as more and more employees are declared redundant,and technology can't be de-invented.This kind of situation existed in the printing industry as told in "Fleet St. moves on".Here,changes in the economic environment facilitated by technological developments were of decisive importance to trade union power.Reduced cost of entry to the market and the breakdown in oligopoly meant that other newspaper houses had to overcome the competitive advantage of new entrants with a reduced cost base.Employers cannot maintain oligopoly in the long term,therefore they have to change any restictive practices regardless of union power.To

conclude,technology has led to a breakdown in oligopoly in the newspaper business and makes it easier for employers tp produce without a trade union.This pattern has been repeated in many industries.

Another factor associated with technology is that in many hi-tech industries ,trade unionism is not the tradition.It is not encouraged and a paternalistic style of management is often adopted.to reduce the perceived need for a trade union among the workforce.The shift to microelectronics in Ireland has been dominated by American multinationals.These large companies refuse to deal with trade unions and this is facilitated by the IDA.One exception in Digital which will negoatiate with reference to non-specialised employees(those engaged in menial tasks)There must be some benefit for the employee and it is normally in the form of good employer-employee relations plus other incentives.One of the best known companies using this warmarmpit approach is IBM.

In America,more and more companies are basing their labour policies on the IBM model.

"this means paying competitive salaries and benefits,providing amenities such as recreation facilities,involving workers in decision making and treating them fairly-nonunion companies in particular are instituting formal systems similar to union greviance procedures,that enable workers to solve job related problems.And no layoff policies are spreading"(Hoem,Beyond Unions)

No layoff policies imply that the worker has a job for life if he "works hard".Firms also often decrease wages and increase worker benefits,whick amounts to a subtle form of exploitation.Nonunion firms with more "assertive" management are becoming more accaptable.Historically firms were associated with a multiunion pattern,there is now a growing trend towards sigle union deals.Multinationals are in a particularly strong position in this regard-either they get their single union deal or they go somewhere else with their factory.This is precisely what Ford did in Dundee.

This trend has been enhanced by changes in labour law.In Britain recent developments since 1979 have added more power to the elbow of management than unions and have thus enhanced deunionization.Below is a summary of the labour law changes that have given managemant more confidence(allowed "managemant to manage").It was claimed that between 1974 and 1976:

"Labour enacted a militants charter of trade union legislation.It tilted the balance of power in bargaining throughout industry away from resposible management towards unions."(Bright et al.,1983)

Election success in 1979 for the Tories saw the beginning of a program of amendments of existing statute law and largely directed at restricting the power of trade unions.This programme was carried out in three phases.First statutory instruments were passed.This extended the "continuous service qualification" for unfair dismissals claims to one year and reduced the minimum period of consultation which must be given by employers to recognized trade unions where mass redundancies are planned.Some potential applicants for unfair dismissals were now excluded and in a period where unemployment has more than doubled,reducing the consultation period considerably affects the power of the trade union.

Second,the Employment Act 1980 narrowed the definition of lawful picketing making it more difficult for a trade union to take effective industrial action.It also set out codes of practice for certain areas of law e.g. union secret ballots and closed shop agreements etc.Third,the Employment Act 1982 further restricts union power in areas associated with industrial conflict and union organisation.Some other adverse legal developments are the Social Security Act 1980,the Abolition of Fair Wages Resolution and the reduction in the effectiveness of wages councils.Trade unions are still learning to cope with this new legal environment,and splits within the TUC as to how to cope have not helped matters. At the same time the traditional functions of unions are being encroached upon by the legal system.Closer European harmonisation has resulted in new unfair dismissals rules and other laws regulating the work place.In one sense this is a testimony to the success of trade unions in having their traditional (and onetime subversive) demands enshrined in public legislation,on the other hand it wouls seem to obviate the need for their existence.The Tory legislation has often taken the form of strengthening individual rights in precisely those areas where it would hurt unions most-the closed shop and strike ballots.Thus unions are facing a loss of both power and resposibility,and rethink of what their role should be is required.

Another influence affecting the power of trade unions is in the political sphere.Often trade unions meet government to discuss national issues.This phenomenon has been labelled corporatism;but it is important to emphasise that it is not aform of joint management.It is only recently that trade unions have started to react to what they see as a hostile government.

"More generally the government is determined to deny the trade union movement any effective voice in the decisions which deeply affect working people.It has rejected any notion of engaging in genuine consultation with or reaching a broad understanding on economic and social policy"(Bright et al.,op. cit.)

Increasingly some trade union members are urging withdrawal from the corparate policies of the government.In Ireland numerous unions are being urged to affilate with apolitical party.Unions however are not meant to be political parties so such an arrangement would be questionable.As an example of such a demand,Charlie Douglas(ATGWU) asked

"Is it not time that we said clearly to our members that their needs as consumers,as parents and as free citizens,can be met(only) in part by trade unions in a conservative political system?"

John Carroll also sees a need for radical action.This push for a political role for unions is a fight for their survival,an attempt to prevent the ongoing deunionization processes from continuing indefinitely.It is clear that there is a strong need for the unions to acquire some worthwhile political influence if they are to survive.

One final question worth discussing is "Are the changes we are witnessing temporary changes resulting from a recession or is a more fundamental shift underway?.If thet are permanent then the question of a future role for trade unions is of paramount importance.From the membership point of view,unions are going to have to launch new recruitment drives.A study by John Kelly surmises that failure to make any inroads white collar and private services employment can be traced to alck of effort on the part of trade unions.Activity is often concentrated around the margin of existing membership groups rather than in areas where the union has no presence.The sluugish response of the trade unions could be due to a number of factors.Naturally, a failure to immediately realise that this was the best source of new members must be mentioned.A shortage of finance(bearing in mind that subscriptions would have been falling in this period) was also a factor.Finally if the union organises a constant proportion of a declining workforce,the stability of union density may preserve its bargaining power.They would therefore have little interest in expanding membership.As Bright points out

"With regard to recruitment patterns we would expect that mergers will continue and recruitment strategies will largely be based on openness and a search for new sectors."It will be in the trade unions' own interests to make themselves attractive to potential members.Unions are no longer expected to deal with just wages and conditions.Working peoples' expectations have risen and workers are now demanding more of a voice in union affairs.If unions are to improve their capacity for decision making then according to Fogarty they will have to

(1)double union dues and have much more professional expertise in union offices

(2)ensure one clear channel on employee representation in each organisation
(3)take a new look at union procedure.
Perhaps most importantly,they should recognise that a problem does exist.Whatever the approach they take,it will be a long time before we can regard trade unions as Clegg did as
"one of the most powerful forces shaping our society and determining our future"

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NORTH - SOUTH: BRIDGING THE DIVIDE

Rosemary Ward

(This is the text of the inaugural address given by the Auditor of DUBES for the 59th session)

I have chosen for my inaugural topic the economics of less developed countries (or LDCs),which in my opinion must itself be the most under developed topic in economics. According to the World Bank in 1982 there were 143 developing countries in the world, as opposed to 29 being "developed". In other words, over 80% of the world is defined as "developing". A priori one might perhaps think that 80% of economics would then be devoted to LDCs, in fact more than 80%, since a science concerned with the allocation of scarce resouces would surely then be concerned most of all with allocating them where they are most needed. This is, of course, not the case. The most vibrant debate in Development Economics is the subject's right to exist all, and The Economist tells us that "the subject is out of vogue" with universities struggling to fill their professorships when they fall vacant. This lack of interest in development economics is surely reflected in the fact that after 48 years trying to close the gap between the rich industrial market economies and the less developed economies, the gap has not narrowed but widened. Yet, in many ways, this seems to have just happened, as opposed to being the result of any specific plan. It is almost unanimously accepted that it is everyone's interests if the so-called North-South divide is bridged. For the developed countries, a closing of the gap would mean the following :-

1) - It would lead to increased to increased political stability and reduced political tensions in the world.

2) - It would greatly expand world export markets and provide all countries with the opportunity to boost their economies.

3) - It would help control world population growth because economic and social development themselves seem to reduce fertility rates. Given these compelling reasons for helping LDCs to develop, I will be asking tonight what is the best way for LDCs to develop? And what can we, the developed world, do to help in this process?

The first question a Less Developed Country must ask about its development is whether it should try to become self-sufficient or whether it should interact with the rest of the world.

Dependancy theorists have argued that increased interdependance will only benefit the richer countries, and that the presence of contacts with developed countries somehow prejudices the growth of LDCs. However, these ideas are contrary to massive empirical evidence, and the most prosperous regions and sectors of the less developed world at present are those with which the developed countries have most contact. The developed countries can offer human and material resources, skills and capital to the LDCs, and just as importantly, can engender a new outlook towards material possessions and the means of obtaining them. Of course, contacts with the world economy are simply a prerequisite for growth, and many other factors are also necessary, but the first step for a less developed country must be to look out at the world, and find the context in which it must develop.

Contacts with the world will mean the importation of goods and services, and a corresponding need to find goods and services which can be sold on world markets. It has traditionally been one of the Less Developed Countries greatest problems that the opening of their economies led to huge balance of payments problems. One of the reasons for this was that many LDCs relied on a few primary products for revenue to pay for imports. The Prebisch-Singer thesis showed however, that, over time, the price of primary products is bound to fall relative to the price of manufactures. Therefore, it is not enough for an LDC to open up, it must also industrialize. The attempts to industrialize have been along two general paths. The first, Import Substitution, tried to replace commodities that were being imported, usually manufactured goods, with domestic sources of production and supply. However, as in Ireland, import substitution failed in most of the countries where it was attempted without the stimulus of, competition , it frequently created an inefficient industrial sector, operating far below capacity, and generating very little employment, very little foreign savings, and very little prospect of further productivity growth. The quantative controls on trade, usually associated with import substitution, also caused governments to ignore the exchange rate, thereby making foreign bank loans seem cheaper, and it is probably not a coincidence that Brazil, Mexico and Argentina, the big debtor countries now, all supported import substitution policies in the 1960s and 1970s.

The other strategy for industrialisation has been export - orientation. While the LDCs that have tried this have had mixed results, it has brought genuine development in many instances and, in my view is the only long term strategy which can bring long - term development. For LDCs, as a a whole, manufactured exports grew from 6 % of toital merchandise exports in 1950 to 42 % in 1980.

The view that export orientation is the only real way forward is officially accepted in most quarters now. the World Bank report of 1987 called for 'outward oriented' trade policies on the part of developing countries. It argues persuasively that countries that have adopted outward - oriented policies, notably the 'Little Dragons' of East asia - South Korea, Singapore, Taiwan and Hong Kong - have outperformed the countries that have adopted other policies. Given that outward - oriented policies represent the best chance of development for LDCs in the future, I will devote the rest of this speech to discussing how this process should come about, showing: first of all, how developing countries themselves must adjust, and secondly; what we, the developed world, can do to help in the process.

The main impetus for development must come from within the country itself. The first thing a developing country must have is an uncorrupt political system. If political favour is a necessity for business success, then companies will invariably take a short - term view of their business, since governments will obviously come and go. And a long - term view of business is vital for development. The four Eastern Dragons all have saving ratios of over 20 %, as they plough back their current profits into the futures of their companies. These high investment rates are very important in the early stages of development, and business people must be confident that their investments will be allowed to bring results in the future.

The second problem for an entrepreneur in a devolping country is getting capital. Getting bank loans does not seem to be particularly difficult; - many developing countries have quite sophisticated banking networks, backed by government owned development banks. But few aspiring entrepreneurs starting out, especially in Africa, are prepared to sink equity into their projects. Typically, their main asset will be land, and they may need the say - so of an extended family before they can pledge it to a business scheme. So businesses tend to start out much too highly geared , with the entrepreneur under pressure to make as quick a return as he can to pay back the bank.

Thirdly, it is very important that professional management is employed when the company gets to a certain stage. Many of the companies that have succeeded in the Third World have done so because they have attracted excellent managers from outside the ranks of the founding families. If top management positions are kept within the family, then erratic results will follow.

Fourthly, much of the developing world is over-regulated for its level of economic activity. Much of this is the result of the colonial - bureaucratization which was handed on by the Spanish, French and British. An aspiring entrepreneur, for example, may have to pass legal tests before forming a company, meet tax obligations, minimum wage standards, environmental controls etc.

It is in the context of these internal changes necessary for development that I believe foreign aid has a role to play. Much has been written about aid and its alleged disincentive effects on developing countries. However, in the early stages of development, those which I have just been talking, the South needs, above all, finance. Interest - free loans for the first few years of a project could get over the problem of high gearing, and finance in general could make a massive difference to infrastructure. Most countries of the North have accepted the target of 0.7% of their GNP in the form of official development assistance, and if the aid was monitored, there is no real case, I believe, to doubt its effectiveness. The present Irish government has, as you know, reduced the % of GNP given to developing countries, and I feel that although this has received much less publicity than many other cutbacks, it must surely be one of the most harsh. Of course, Ireland is not the only country to cut back its contribution - many European countries have; and Ronald Reagan has shamefully reduced America's aid programme. The Chairman of the US House of Representatives Committee on Europe and the Middle East, Lee Hamilton, wrote in 1983 that "if a developing country is unable to present its needs in terms of East-West rivalry, its chances of receiving American aid are diminished." It is surely not too much to ask that if developed countries have agreed to give a certain amount of aid, they could at least keep their word on the issue.

However, I believe that the biggest help the North can be to the South is in the area of trade barriers. The area of trade is overseen by GATT, the General Agreement on Tariffs and Trade, an international treaty dating from 1947 and GATT attempts to help Southern countries develop through a "Generalized System of Preference", i.e., putting lower than usual, preferential tariffs on imports from developing countries. However, like the aid situation, while both the EEC and the US seem committed to the idea in principle, in practise the system works nothing like it should.

First of all, the American scheme, set up in 1976, can decide not to give preference to any country it likes, if the developing country, for example, does not co-operate with US anti-drug policies. A lot of very important goods for LDCs are excluded - for example textiles, watches, electronics, shoes and glass. A country can have its preferences taken away if it is too good at exporting in one single year, which obviously tends to penalize countries just as they are becoming successful. Also, about half the goods eligible under the scheme don't actually apply for it, due to the baffling complexity of the scheme's rules.

The EEC is no better. In principle of course it is totally in favour of GSPS, and Community blurb on the Lomé Convention, signed in 1984, proudly declares that "99.5% of the products of African, Carribean and Pacific countries have duty free access to the Community markets with no reciprocal concessions being demanded! In practice this is far from being the case. A massive 75% of all goods eligible for preference do not in fact enter Europe duty free. Again the complexity of the rules must be blamed, and one has to ask - could either a simple system or a good guide to the present one surely be drawn up? The European scheme is hedged around with quotas and ceilings of every kind, one set for each member of the EEC. And in Europe, the quotas are allocated not to firms in exporting countries but to importers; quotas are awarded to first comers. This encourages the importer to benefit from the GSP, and not the developing country.

The GATT system of helping developing countries, then, is nothing more, in my opinion, than a sham. The World Bank Development Report of 1987 agreed, albeit in politer terms - "In exchange for preferences" it says, "which brought them limited and risky gains, developing countries have given up a voice in reciprocal trade negotiations and left themselves open to attack by industrial countries, who accuse them of unfair trade." The whole GATT system seems geared to suit the North as much as the South - it soothes the industrial countries' consciences while bringing negligible benefit for the developing countries. The current Uraguay round of talks doesn't promise much change.

Of course, the GATT doesn't cover all the trade restrictions. We all remember, last June, the debate about the Single European Act, when it was claimed that the abolition of the non-trade barriers within the EEC could reduce the costs of our exports by over 1% of GNP. And this is within a common market! Last summer GATT identified 135 of these 'grey area' measures - voluntary export restraints, market-sharing deals etc. - and also pointed out the two largest offenders - the United States and the European Community.

What I am saying then is that, while aid is important, and should be increased to the UN-reccommended level, a determined approach to reduce trade barriers for developing countries exports would be just as beneficial in the short-run, and probably a lot more so in the long run.

The final subject I want to discuss tonight is on multinational corporations. There is no doubt that multinationals are a fact of life in the world economy today, and are neither good nor bad in themselves. There is also no doubt however that many have engaged in unethical political and commercial activities - the attempt to bring down the Allende regime in Chile, the illegal payments by oil companies to goverments in various parts of the world; the support given by certain corporartions to illegal regimes in Africa and so on. However, the main fear about multinationals is that they have become so pwerful that they cannot be controlled by nation - states any longer.

As we know in Ireland, a multinational always contains the ultimate bargaining card - if the going gets tough, it can always pull out and set up somewhere else. It is the power of multinationals to set states competing against each other that is their ultimate power. Eight years ago, the Brandt Report called for effective national laws and international codes of contact to provide a framework for the activities of transnational corporations. The huge benefits of setting up on a transnational basis will ensure that very little investment will be lost on aggregate, but developing countries would get a greater share of the wealth generated.

To summarize then, I believe that there are three steps which the North should take to help bridge the gap with the South :-

(1) It should increase aid to the minimum level recommended to the United Nations.

(2) It should reform its trade regulations and make them work the way many of their originators intended them to.

(3) It should, through negotiation with the South, provide a code of conduct.

Ladies and Gentleman, everything I have argued tonight has been argued on the basis that it is in the interests of the North that the South should develop, and that everyone will gain if developing countries gain. I have no doubt but that this is the case, but I must ask if everything we do for developing countries must be based on our own self interest. Especially as far as the poorest people ,and the poorest countries are concerned, surely we must consider human solidarity and international social justice. We should stop debating whether development economics has a right to exist and treat the real issues with the urgency they require.

LATIN AMERICAN TRADE AND DEBT

Eoin Lonergan.

The term "Latin America" is very misleading in that it gives the impression of a coherent geographical economic and cultural unit.In area it stretches from the southern U.S.A.(in cultural terms it extends even north of this) to the Cape of Good Hope,5000 miles away,taking the distinct regions of central America,the tropical rainforests of the Amazon to the First World modernity of Rio de Janeiro and Brasilia.The people of the region come from many different ethnic backgrounds and in political terms the area has produced everything from the most vicious right-wing dictatorships to the world's first democratically elected Marxist government.Nonetheless they do face many problems in common and this sense can be treated as a whole.The most pressing of these problems are those of trade and debt-how can they generate enough income to prevent sliding into bankruptcy and its attendant consequences?In this essay I concentrate on this issue,with reference to "Dependency Theory",arguably the most suitable framework for analysing post colonial LDC's.

The issues of trade and debt are heavily interlinked and can be seen in terms of a vicious circle.A country must borrow heavily in order to finance infrastructural improvements which would hopefully encourage industrialisation and allow it to reap the benefits of foreign trade.Conversely when the cost of servicing these debts becomes large,the same country must increase production and exports simply to repay the loans.Latin American countries must borrow to develop production to finance borrowing.The OECD in its report,puts a heavy emphasis on statistics but (necessarily) plays down the human and political factors so relevant to the development of Latin America.It ignores the responsibility of the rich North for past and present injustices ,which seem to dominate media coverage of that region today.

One of the effects of the post colonial legacy is that Latin American countries have little or no control over the direction of their economic future.Development of trade in these countries is a reflection of and is consequent upon expansion in the core countries of the North.The mushrooming of Latin American debt recently has reinforced the hold of the industrialised world on Latin America,which was already firmly in place via Trans National Corporations (TNC's) whose wishes always had to be considered when formulating economic policy and in an extreme case led to the downfall of a democratically elected regime (Chile 1973).In many cases however these governments are far from democratically elected and wouldn't serve the interests of the majority even if they could.A consequence of dependency is the existence of the clientele classes who act in the interests of foreign capital in order to ensure financial and sometimes military backing for the status quo,which typically involves the existence of a wealthy elite amidst dire poverty amongst the masses. These characteristics can be seen most glaringly in countries such as Chile ,El Salvador ,Argentina and Columbia but this characterisation is less accurate with respect to e.g. Brazil which has a large and growing educated middle class whose interests are typically more diverse than those of the super rich .In general though it can be said that the internal dynamics of dependency are as much a function of domination as are the more explicit pressures placed on LDC's by immediate financial circumstances.

The OECD report stresses the the problems facing Latin America cannot be analysed without reference to the troubled world economy.It identifies three shocks that affected world trade since 1970:ecxhange rate instability,balance of payments disequilibria as a result of oil shocks and the universal increase in non tarriff trade barriers.

The breakup of the Bretton Woods system of fixed exchange rates has caused a large degree of price instability on world markets.The huge devaluations which resulted from the floating of exchange rates meant the beginings of Latin America's most persistent problem-inflation.As countries such as the U.K. and Italy well know,a devaluation (resulting in a rise in the domestic price of imports and thus inflation) can form the beginings of an inflationary spiral as workers seek pay rises to compensate for the rise in prices which in turn causes a further rise in prices.In countries where confidence in the ability of money to retain its value in not high(perhaps as a result of previous hyperinflations or political instability) this can quickly lead to incredible(by post war western standards)rates of inflation.For example in 1986 Argentina's inflation rate was estimated at 1300% per year and 100% a year seems to be quite acceptable.This inevitably results in further devaluation which compounds the problem even further.Governments have proved unable to provide lasting solutions ,sometimes because of their populist orientation which makes them reluctant to implement measures whiach are bound to hurt somebody.Brazil's recent attempt to impose wage and price freezes(the "cruzado plan") lasted three months before collapsing under the strain of public outrage with the black marketeering and scarcities which ensued.

Another problem posed by exchange rate instability is in relation to Latin America's large external debt.It is very difficult for these countries to assess their ability to repay the debt when its value is changing with every fluctaution in whatever currency it is denominated in.In Brazil's case a one cent rise in the dollar means an additional $1.5billion of debt.As the domestic currency depreciates the burden of interest payments becomes more severe .This also means that the countries export earnings are uncertain and a depreciation tends to reduce these earnings given that these countries are often reliant in exports of primary products for which the world demand has been depressed for some time.
Many of these exports are not price sensitive in that the lowering in (say) the $ price which such a depreciation entails fails to produce a sufficient rise in demand to compensate for the lower value of existing exports.Obtaining foreign currency can often be very difficult and a black market selling foreign currency at way above the official rate is a standard feature.
After the oil shock of 1973, existing balance of payments disequilibria were exacerbated and new ones appeared.Oil importing countries now faced a massively increased import bill with the oil-shock induced recession depressing export earnings.In this respect Latin America cannot be treated as a unit because oil rich countries such as Venezuela,Mexico and Peru benefitted from the price rise.At the same time the countries of South East Asia (Newly Industrialising Countries) were beginning their big export-led push into Western markets which finally relected itself in the massive trade surpluses we see today.Latin American countries themselves have doubled their imports from the NICs in the last 20 years.Unfortunately they did not follow the example of export-led growth but concentrated on austere demand management policies coupled with import substitution.However not every country can pursue an export led growth strategy-if they did everyone would end up worse off(Of course this is no reason not to pursue such policies).These policies resulted in a massive fall in imports e.g. in Brazil exports fell by 25% in real terms.The policies seem to have been motivated by the simplistic view that "exports good,imports bad" which in not true especially if you stop importing capital goods thus preventing the modernisation of domestic industry and hampering its ability to compete on world markets i.e. less imports now means less exports in the future.It should now be rocognised that a major shift in world purchasing power appears to be taking place away from the North America and Western Europe towards the large surplus countries such as Japan and Taiwan.The Latin American countries need to reorient their export markets towards these potentially profitable markets and

away from the U.S.A. which is going to face severe adjustment problems as it tries to cope with its own very considerable balance of payments problems.

The third problem facing Latin America involves widespread increases in non-tariff trade barriers which affect the export markets that these countries need so badly.There is little point in financing huge capital expenditure in export industries if there are no open markets.As world opposition to free trade relaxed during the 60s and after in particular due to the general agreement on tariffs and trade(GATT) tariffs were lowered worldwide.However in recent years a general rise in nontariff barriers has been noticeable.Quotas,strict regualtions,red tape and automatic tariff hikes for processed goods are now the biggest barrirers to free trade.

The development and strengthening of the European Community(EC),the European Free Trade Association(EFTA),and the relatively closed nature of the Asian NICs means that new policies will be needed by the richer countries if LDCs are to penetrate these markets.Another problem facing LDC exports is the structure of tariff barriers that discriminate against processd goods.Many primary products such as rice can be exported duty free to the EC ,however products can face a 13% tariff if they are partly processed.This is a huge obstacle to Latin American countries who have the potential to process their own commodities,thereby increasing employment,diversifying industry and earning more export income.Instead these countries are forced to export these commodities in a raw condition minimizing value added within the country.For Latin American countries who earn 50-60% of their export income through primary raw materials,this is a heavy burden.Often the only processed goods that reach the world market from Latin America are those products produced by subsidiaries of TNCs.As we in Ireland are acutely aware increases in the profits earned by TNCs in the periphery countries accrue largely to non nationals and have little beneficial effect on the economy as a whole apart from the provision of immediate employment(often low pay and/or low skill).

TNCs have a huge stake in Latin America today.Most of them are U.S. owned and export most of their output to the European and North American markets.Although they introduced much needed capital to Latin America and provided employment it seems that in the long run their cost outweigh their benefits.These TNCs tend to become less and less beneficial over time to their host countries.Increasing concentration of capital and resources through horizontal and vertical integration means that the spinoff effects are reduced as time progresses and native contractors lose out.Although Brazil produces almost 50%of the world's coffee output the whole process is controlled by non Brazilian owned firms from the planting of seeds in TNC plantations to the labelling of jars.A small number on TNCs e.g. Nestles reap most of the benefits of Brazil's huge coffee exports.It is very rare for the producer country to receive more than 25% of the final price charged to consumers.As these TNCs diversify they fill more niches in related markets.Indigenous industries find it impossible to compete with these TNCs due to the latters' massive economies of scale,which produce organisations with formidable market power,control of which remains in the core countries.All of these characteristics of TNCs give rise to the shared interests among them in the countries in which they operate.Their need to control all aspects of the production process eccourages them to plan for the long term.Inherent in this plan is the need for TNCs to have some influence on the governments in their subsidiary countries.This is a further constraint on Latin American countries in their quest for independent development.However, the government and the TNCs may appear to oppose each other on certain issues-this may often be for appearances sake to allow the regimes to preserve some credibliity in a region renowned for its political instability.

As regards foreign trade the OECD report categorises four output sectors-minerals,agricultural produce ,services and manufactures. The growth of service industries throughout the world has been very rapid in recent years.Expenditure on services tend to rise as countries become richer-indeed the service sector has accounted for most of the oft boasted about increase in employment during the Reagan years in the U.S. However the growth of the service sector has not had much impact on the composition of world trade and there does not appear to be much potential for development in this area for the LDCs.It is important not to confuse services and nontraded goods.Service goods are typically nontraded-unless a haircut is outrageously expensive you won't travel to another country to buy it.However many services are traded e.g. financial services,consultancy services etc.But these all rely on existing expertise and advantages so there may not be much potential for development for LDCs in this area.In fact where services are exported it is usually from the richer countries to the LDCs.The large percentage of students from LDCs studying in Ireland and the export of Irish professional expertise to LDCs bears witness to this.

The world trade in minerals appears to have reached its peak.Efforts made to economise in the use of the mineral products following on the oil shocks have caused a fall off in demand for many minerals in recent years.The prime exported mineral from Latin America is oil,the bulk of which comes from Mexico,Venezuala and Peru.These countries benefitted from the high price of oil up until the early 1980s but with the falloff in demand for oil and the plunge in oil prices these countries have suffered a sharp decline in their terms of trade (the amount they need to export to pay for a given amount of imports).The associated falls in their exchange rates vis-a-vis the rest of the world have further reduced their export earnings.The risks associated with dependence on one commodity are well known.When the price of copper plumetted by 60% in 1975 it caused near bankruptcy for Zambia which depended on copper for an incredible 94% of its export earnings.There is potential for high earnings for exports of minerals from LDCs but the demand has been reduced by the drive for self sufficiency in energy in the core countries.It has been established that today 90% of world expenditure on exploration is in the rich countries of the world.Since exploration is a long term costly activity,this trend could leave LDCs with a serious gap in their export earning ability in the coming years.

The most important area of trade for most Latin American countries is agricultural produce,be it timber ,fruit,cocoa,coffee etc.Non tariff barriers represent a large obstacle to development in this area,especially in relation to processed goods.This is a problem that should be familiar to Ireland as we export raw agricultural produce to be processed in the core countries of the EC.The prices of raw agricultural produce are highly volatile leading to unstable incomes and associated long term planning difficulties.Some kind of price control would obviously help,and the absence of such controls partly explains why so many farmers in Colombia and Bolivia have turned to exporting cocaine for a living.This give them a guaranteed income and their collective actions this year could amount to production of $25bn worth of cocaine valued at New York street prices.Economists can hardly question the rationality of switching production from commodities whose price is highly unstable to a commodity which experiences stable or increasing demand and thus a stable price.There is a sad irony in the fact that the Latin American countries,having been largely left out of the "petrodollar" boom of the 1970s are now at the centre of the "narcodollar" boom of the 1980s.

Although demand for agricultural imports is falling worldwide;Japan imports half what it used to 20 years ago,the U.S.A. 1/3.With this in mind Latin American countries shuold move towards higher value added produce,but this brings in the core of the trade-debt problem.The West cannot expect Latin America to pay of its debts to western banks and at the same time close their import markets through trade associations such as the EC, EFTA or the USA.50% of world trade is subject to nontariff barriers and this figure must be reduced if we are really committed to free trade and co-operation.While we are quick to reccommend free market remedies within LDCs(via the IMF) we seem less willing to implement free market measures between countries.The message seems to be that LDCs must be free to buy our exports(on credit if necessary)but that they mustn't be free to import to us in return.Scare mongering by politicians in the West warning of unemployment if LDC imports are given free access to "our" markets has not been substantiated by fact.Richer countries have benefitted from lower priced imports in the form of low inflation.On the terms of the "New Right" this of itself should be a good thing.Britain for instance has proved willing to sacrifice at least 1.5m jobs for the goal of low inflation-if this is represenative of the value that the West now places on low inflation then cheap imports are surely a good thing.In addition many LDC imports don't compete with developed country goods anyway-though this is partly due to the response of European and American industry to low price competition i.e. by moving into the upmarket,value added sector.

To conclude with a comment on a current topic :the Stock Market crash of 1987.The uncertainty in the markets which contributed to the crash can be traced to at least two factors-the enormous U.S. trade and budget deficits and the enormous Latin American foreign debt.The year 1987 brought the realizations that (1)much of the Latin American debt would never be paid back (2)the correction of the U.S. twin deficits would probably precipitate a world recession.The second factor shows that the issues of trade and debt are not purely confined to Latin America.These two issues are often treated separately but they are closely linked.On the one hand,Latin American countries need to export more in order to pay back their debts and/or develop their economies.on the other hand we have the massive trade imbalances between the U.S. and Japan and other Far Eastern countries.The traditional Latin American export destination i.e is the U.S. faces severe balance of payments,budgetary and excange-rare adjustments.As has already been mentioned they need to reorient their exports towards the booming "Pacific Basin".More generally we need to redistribute existing trade flows and get away from the Japan-U.S. nexus .Apart from anything else it is economically unsound to have the world's two largest economies overly dependent on each other.Of course such a reorientation requires money which brings us back to where we started.Perhaps this could be achieved by a new "Marshall Plan".The original post World War II plan incorporated the essential vision that it suited the U.S. to engineer a recovery in its largest potential export markets,even if these countries would one day compete with the U.S. on its home ground.If a similar plan was implemented with respect to Latin America they could buy more U.S. goods thus alleviating the trade deficit and also export more to each other and the U.S. thus giving them the necessary earnings to pay back their debts and in turn stabilize world financial markets.On reality things would be as simple as that .For one thing Europe started with a clean balance sheet,and also current Latin American policy indicates that the U.S. would attach strong political conditions to any aid.It took a shattering war to precipitate the introduction of such a bold and imaginative plan in 1945;one wonders what further tragedies Latin America will have to endure before some real effort is finally put into ensuring that the region can fully realise its enormous potential.Whatever steps are taken they will involve risks,but given the greater risks we face if no action is taken,not to mention our collective responsibility to the poverty stricken nations of the Southern hemisphere,some action is imperative.

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THE TAIWAN ECONOMIC MIRACLE

Finbar McDonnell.

If there were a competition to find the country with the strangest economic history in the last 40 years, Taiwan would surely stand a good chance of winning. In 1949, Chiang Kai-Shek led what remained of the Nationalist army, after the Chinese civil war with Mao Tse Tung's communists, to this small island, situated off the south-east corner of China. There, the ' Republic of China ', which had previously constituted the 35 provinces of China, was limited in soverignty to one, while Mao's ' Peoples' Republic ' exercised sovereignty over the other 34. For the Republic of China (Taiwan) to be still in existence after 40 years is in itself amazing. For it to have a GDP per head of over 40 times that of the Peoples' Republic, to have foreign-exchange reserves of over $75 billion (the world's second largest after Japan), and to be the world's 13th largest trading nation is astounding.[1] For the economic growth to have been compatible with an improved distribution of income during *every* phase of the transition from colonialism to a modern developed economy simply completes the miracle.[2] It is as though Sinn Fein, anticipating defeat in the War of Independance in 1920, fled to the Blaskets, and now boasted one of the world's top economies, with a GDP per head of £250,000, massive foreign reserves AND a high degree of equality ! (This helps one understand how amazing it is that Taiwan hasn't been invaded by the Peoples' Republic, if only because of how infuriating the little island must be !). This amazing transformation is the first reason I was drawn to Taiwan in writing this essay.

The second is because, in many ways, Taiwan has been a liberal economist's dream for the last four decades. There are four reasons for this. (1) Since the Peoples' Republic was avowedly communist, Taiwan was avowedly capitalist and would stay that way. (2) With a well equiped army (comprising some 2% of the population) the country's boundaries were as secure as they would ever be. (3) Also, the country was politically very stable, with really only two rulers up until this year. Chiang Kai-shek, the man who led the rebels in 1949 was a (fairly) benevolent leader until 1975, and his son Chiang Ching-Kuo continued in his footsteps (after a short interim period) until he himself died this January. (4) Since the Yuan (or parliament) maintains that it represents all of China, no elections have been held since 1949. This means none of the wasting of money for political purposes,

or political footballing with economic issues which we have experienced in Ireland have been present in Taiwan (I am not arguing against democracy but just saying that in Taiwan , their 'situation' politically has certainly been economically beneficial - if the leaders had not been benevolent and uncorrupt , as they would not have been had they not kept the dream of a unified China as their uncorrupting goal , then the lack of elections could have brought appaling results) . In other words ,' a climate was created , as Friedman talked of when describing the benefits of steady monetary growth " favourable to the effective operation of those basic forces of enterprise , ingenuity , invention , hard work and thrift that are the true springs of economic growth ."[3] Not only was the climate created , but to believe or even pretend that the dream of a unified China is real implies , as *The Economist* says " the discipline that produces economic miracles . "[4] Furthermore , Taiwan was blessed with excellent planners . I believe Ireland , another small open economy , could learn an awful lot by studying the economic development of Taiwan , which was planned and executed brilliantly . It has never tried to have too much too soon , but has been restrained , diligent , yet always dynamic . The planning took (and takes) the form of four-year documents , the first of which was for 1953-1957 , and the ninth is currently running , from 1986-1989 .
For the purposes of this paper , I will divide Taiwan's development process into three phases ;
Phase(1) - the 1950's preparations for "take-off" and the import substitution policies .
Phase(2) - the 1960's "take-off" , which continued into the 1970's , with export orientation , the arrival of multinationals , and the successful penetration of foreign markets .
Phase(3) - the 1980's move 'upmarket' , the new science-based industry , and the problems of Taiwan's "affluent society" .
The third phase is obviously the most difficult to discuss since there is no historical perspective , but I shall try to do so , and also tentatively examine possible future directions for Taiwan , in the light of its new political leadership (a Mr. Lee Teng-Hui) , the pressure to raise (further) the value of the Taiwanese dollar , and the pressure to reduce Taiwan's tariff levels . However , I will begin at the beginning ; the place is Taiwan , a small provincial island off China , and the time is the early 1950's .

In the early 1950's , the Taiwan economy was in an awful state . The current value of GNP per capita was only $48 ie. less than half that of the world's economy in 1987 .[5] The economy had just experienced severe hyperinflation ; prices rose at an annual five-fold rate in 1946-1948 , and then accelerated to about a thirtyfold increase in the first half of 1949 .[6] The savings rate was under 5% of National Income and even the most basic infrastructure was nonexistent . On top of this , almost all of the land was held by a small portion of the population .The starting point for development was very low therefore , and the 1950's , which for our purpose really runs from 1949 to 1962 , was basically a time of preparation for the "take-off" which followed

This preparation comprised of three policies - Price stabilisation , Land reform and the setting in place of some basic infrastructure .

Given the massive inflation rates of the late 1940's , the most urgently needed action , more vital than any other , was price stabilisation.Stabilisation policies were implemented by various measures . (1) The old Taiwan currency was devalued at a rate of 40,000 to 1 , and the value of the New Taiwan dollar (NT$) was linked with that of the US dollar at the rate of NT$5 = US$1 . The currency was backed 100% by gold , silver and foreign exchange . Various other monetary reforms were also made However , a large government deficit meant this rate left the NT$ very much overvalued in practice , and reduced the effectiveness of monetary reforms . (2) Preferential interest-rate savings deposits were introduced in 1950 . These gave high interest-rates on deposits , of 7% per month , which , if compounded , would amount to 125% per year . As Kuo has pointed out " Although the interest rate was actually still below the inflation rate in 1950 , the setting of such a high interest rate required intelligence and diligence on the part of the government ."[7] This scheme was very effective , and when the interest rate was (gradually) reduced to 2% per month by 1952 , 44% of the money supply was in such deposits . (3) A great effort was made to achieve a balanced budget to eliminate economic instability , and the budget was in surplus every year (albeit with the help of US aid) . Sound fiscal policies were implemented with a firm determination .

Land reform restructured the whole agricultural industry , boosted productivity , and allowed for the influx to industrial work of many farmers after 1962 . Land reform was carried out in Taiwan , Kuo tells us , in three stages[8] ; (1) Rent reduction took place in 1949 . It legally limited the amount of farm rent on private tenanted land to 37.5% of the harvest . Before the implementation of this programme , tenant farmers in Taiwan had to pay a land rent amounting to more than 50% of the total harvest .(2) The sale of public land to tenant farmers was successfully implemented in 1953 to 156,000 tenant families , at a price fixed at 2.5 times the annual crop price . (3) A limit was set to individual land holdings , with dispossessed large farmers reimbursed with government bonds and stocks . The area transferred from landlords to tenants through the "Land to the Tiller" programme amounted to 71% of the total area of public and private tenantad land . The fact that this took place without social unrest was due both to the fact that the reformers had political control in the country ,and also to their determination that nobody should lose out in the reforms .

The third policy , the setting in place of basic infrastructure , was limited by the lack of funds available in the 1950's . The average ratio of net domestic savings to national income from 1951 to 1959 was only 5% , and from 1960 to 1962 had grown only slightly to 8% .Domestic savings are but one source of investment and Taiwan also received U.S. aid during this time.This aid which partly as already mentioned,went to financing government deficits,helped to bring the ratio of net domestic investment to national income to over 10% for each year in the 1950s.This investment went to infrastructural programmes such as electricity,transportation and communications but also into private sector projects such as mining and manufacturing.

These policies,designed to strengthen the domestic economy were combined with an overall government policy of reducing the sizeable trade deficit by import substitution.First,import restrictions and high tariffs drove up the price ratio of imports to exports appreciably in the 1950s.For example,the relative price of textiles,a major import,to rice,the primary export rose from 2:1 to 5:1,allowing the textile industry room to grow raoidly.Secondly,the exchange rate was used to encourage import substitution,and the use of exchange settlement certificates(ESCs) meant the government could allow in important inputs at a cheap price but place a high price on unwanted imports.The import substitution policies did work to some extent but the basic deficits remained into the 1960s.In 1952 the shares of exports and imports in GNP were 8.6% and 14.8% respectively.In 1961 ,they were 11.2% and 18.5% respectively.[9] However,about 1958(as in Ireland) the limited domestic market and urgently needed foreign exchange called for a fundamental policy change in favour of export promotion and outward oriented policies.

The year 1962 is generally accepted as the year the economy "took off".This is using Rostow's famous classification,where he defines a take-off as requiring all three of the following related conditions(1)a rise in the rate of productive investment from say 5% or less to over 10% of national income;(2)The development of one or more substantial manufacturing sectors with a high rate of growth;(3)the existence or quick emergence of a political,social and institutional framework which exploits the impulses to expansion in the modern sector and the potential external economy effects of the take off and gives the growth am ongoing character[10].As we shall see,Taiwan satisfied these conditions admirably in the 1960s and 1970s.

We have already said that the ratio of net domestic investment to national income was above 10% each year in the 1950s,but that this was due to the contribution of U.S. aid.Considering this aid was terminated in 1965,and considering the importance of a structure which subsequently permits a high rate of savings to finance investment,the condition for the "take-off" is bound to be the domestic saving ability.In this respect,Taiwan's ratio of net domestic saving to national income rose from 7.6% in 1962 to 13.4% in 1963 to 16.3% in 1964 and has never looked back.In 1967 it broke 20% and in 1973 reached a massive 35%[11].In short,Taiwan has been able to finance its investment by domestic savings sice 1964,and in certain specific periods(1971-73 and 1976-79),because of great trade surpluses,domestic savings even outweighed investments.That is,part of domestic savings was not utilised within the country.This very high savings(and therefore investment) ratio came mainly from the private sector,however the government savings ratio was also high,and accounted for about 1/3 of total investment between 1962 and 1979.This was especially important for the construction of infrastructure and heavier industries,such as transportation,nuclear power generation and steel in the 1970s.

Private foreign investment was also important,but not crucial,amounting to under 6% of the gross investment in manufacturing in 1962-1969 period although differing as a percntage of total investment from sector to sector.The chemical,electrical machinery and textile industries,for example absorbed over 2/3 of foreign investment in the 1960s.In the 1970s(where figures are available for approved as apposed to actual foreign investment)the proportion of total investment from abroad increased to about 8%,again concentrated on the modern sector with about 1/2 going into electrical machinery industry and about 1/4 into chemicals.Of course,the contribution of foreign investment was not only financial but extended to better technical knowledge and opportunities to import supplies and increase exports.However the Taiwan miracle was mainly a home produced one and although there was aid pre 1965 and foreign investment after the bulk of the growth was the product of Taiwan's own people and money.

It was based on the development of several substantial manufacturing sectors.These in turn developed due to the excellent climate which was created for investment.In 1961,a "nineteen point economic and financial reform" was introduced and the the "Statute for the encouragement of investment" was enacted pursuant to these measures.This had the following implications(i)a productive enterprise was exempted from income tax for a period of five consecutive years(ii) the maximum rate of income tax including all forms of surtax,payable by a productive enterprise thereafter would not exceed 18%(iii)profits reinvested were not taxable(iv)the exchange rate was stabilised and procedures governing settlement of foreign exchange earned by exporters were improved.Add to these highly attractive incentives,the very low wages demanded by the labour force and the absence of almost all strictures regarding pollution and environmental care,and the background is in place for a manufacturing expansion.

Between 1950 and 1980,the number of factories in Taiwan increased from 5,623 to 62,474[12].This phenomenal increase was concentrated in several industries.In the early 1960s,the boom area was food processing,as an extension of agriculture and food processing comprised over 70% of manufactures exports.The industry was also boosted at this time by the protection barriers on imports allowing for expansion on the domestic market.The infant textile industries began to grow up and it was now their turn to expand greatly,with exports growing from under 10% of total exports to almost 30% by the mid 1970s,dropping back to 25% in 1980.This expansion,which ensured that the "Made in Taiwan" label reached all parts of the world,allowed Taiwan to reach full employment in 1971.But a country(even one which had grown by over 8% a year in the 1960s),as the *Economist* says "can only get so far with sweat shops,zeal and the ability to copy"[13].In the 1970s Taiwan moved into modern industry,and its most rapid expansion in production and exports took place in electronics.By 1980 it accounted for slightly over 1/4 of Taiwan's manufactured exports.The final growth industry over the period comprises a group of firms that can be lumped together by the descrition "those who took advantage of the lax pollution controls".Plastics,chemicals,petroleum refining,pesticides ,leather, tanning firms etc. all started up and Formosa plastics,a local company founded in the mid 1950s is now the world's largest producer of PVC.

The destination of Taiwan's evolved with its manufacturing sector.The food processing of the early 1960s meant Japan was the major export destination,taking 29% of all exports as opposed to the U.S. taking 21%.However by 1979 the growth in modern industry meant that only 14% of exports went to Japan,while 35% went to the U.S. and over 8% now went to Europe[14].These trends as we shall see later have caused one of Taiwan's main problems of the 1980s-a large trade surplus with the U.S. and a huge dependence on the U.S to buy what Taiwan is producing.

The massive expansion in exports was,of course,almost unique among world economies,but it had a few parallels,all geographically nearby.For example in the period 1965-69 when Taiwan's exports grew by 40.8% per year(on average),Japan's grew by 29.1% per year,Korea's by 46.3% and Hong Kong's by 24.4%.Kuo does a fascinating study of the different causes of export expansion in these countries[15].First,she gives the basic causes of export expansion in any country as (i)increases in world trade (ii)changes in the commodity structure of world trade (iii)changes in the area.distribution of world trade (iv)increases in competitiveness of a country's exports.She then draws up a table showing the contribution of each of these factors the these countries' export growth for the period 1965-69.

Item	Taiwan	Japan	Korea	Hong Kong
(i)	30.6	51.7	26.2	50.2
(ii)	-6.5	9.6	-2.7	5.4
(iii)	3.2	-22.5	-1.5	-4.4
(iv)	72.7	61.5	78.0	48.9

(Source:Shirley Kuo;The Taiwan economy in transition,p.177)

Although Kuo does not go into detail on these figures,it is seen that the main factor contributing to the export expansion of these four countries in this period was their increase in competitiveness in the world market(the increase in the value of world trade was also very significant for Japan,probably due to their being more "upmarket" at that stage than the others).This increase in competitiveness may have come from various factors.The inportant ones were increases in productivity,advancement in quality and sales of new products,all at wage rates which were low by international standards.

However the impression that Taiwan between 1961 and 1980 consisted of millions of poor workers being kept poor to maintain competitiveness is totally false.It is an incredible sight to see a country advertising "increased opportunities for Taiwan's 180 trade partners round the globe...Taiwan's new buying power is rich for tappping...the knock of opportunity is loud and clear"[22].In fact the country made considerable advances in narrowing the income gap in the midst of rapid economic growth.Simon Kuznets' famous study had said that this was almost impossible for a developing country,but in two studies(that of Professors Chenery and Ahluwalia and that of Fei,Ranig and Kuo)Taiwan is identified as one country where inequality has narrowed with development.In the 1950s,Taiwan's family distribution of income[16] was not very different from the unfavourable levels present in most LDCs in their early years of transition.The following table shows how the distribution of national income changed as it grew:

Income share of	1964	'66	'68	'70	'72	'74	76	78
Lowest 20%	7.7	7.9	7.8	8.4	8.6	8.8	8.9	8.9
2nd lowest 20%	12.6	12.4	12.2	13.3	13.2	13.5	13.6	13.7
Middle 20%	16.6	16.2	16.3	17.1	17.1	17.0	17.5	17.5
2nd richest 20%	22.0	22.0	22.3	22.5	22.5	22.1	22.7	22.7
Richest 20%	41.1	41.5	41.4	38.7	38.6	38.6	37.3	37.2

(Source:Fei,Ranis and Kuo,pp34-35)

This increased equality is emphasised all the more by looking at the following table.It shows that real family income showed a considerable increase in all income brackets.However, the rate of increase was far greater for those in the poorest income brackets and smallest for those in the richest income brackets.

Families	Rate of increase between 1964-79(%)
Lowest 20%	231.0
2nd poorest 20%	223.0
Middle 20%	213.0
2nd richest 20%	208.0
Richest 20%	181.0

(Source;Fei;Ranis;Kuo p.38)

Without going into detail,I will qoute the conclusion of Kuo[17];"the specific characteristic of the Taiwan economy was a more equitable income distribution amidst rapid industrialisation and urbanization.The narrowing inequality within the nonfarm group was the most influential causing the reduction in nationwide income inequality.The rapid absorbtion of the labour force contributed substantially to the rise in relative incomes of the lower income families,both urban and rural.Industrialisation and urbanization have brought in their wake significant welfare benefits;higher per family income,higher employment rate,higher productivity and a higher standard of living."
That the Taiwan economy has "taken off" cannot be doubted,but just before I turn to Taiwan in the 1980s,I will look at how the different sectors of the economy have fared through the years.In 1952 agriculture's share of GDP was 32%,industry's share 22% and services accounts for 48%.By 1980 this had changed to about 10% for agriculture,45% for industry and 45% for services.The changes in shares of employment have been even more dramatic.In

1952,agriculture comprised 55% of the labour force,industry 18% and services 27%.By 1980 these figures were 18%,42% and 40% respectively[18].These changes reflect the "modernisation" process which took place in the 1950s and 60s in Taiwan.

So what then of Taiwan in the 1980s,and indeed the future?The era of low wages has long passed,due to the achievement of full employment in 1971.The average textile worker's wage of $2.37 per hour puts Taiwan way above the LDC norm(nearby Thailand's $0.58 per hour for example).Newcomers in the international market are accelerating their exports of cheap labour products.Taiwan has recognised that the only way to increase its competitiveness in the future is through advancement in technology and the industrial structure so as tp produce and export higher value added and more sophisticated products which utilise more skilled labour.Therefore the 1980s have seen an attempt to move from labour intensive light industries to skill intensive heavier industries.As ever,the planners are in control,and this structural change of the economy has been pursued in several directions;

(1) in 1978 work began on the "Twelve New Development Projects" to give Taiwan the infrastructure necessary for its move to an industrial market economy.The 1980s have seen a mass rapid transit and underground railway system developed for Taipei,the construction of a fourth nuclear power station,more motorways,new reservoirs and such an intense program in general that *The Economist* has spoken of Taiwan "sinking from the weight of its own infrastructure"[19].

(2)71 industrial estates are now in operation and another 8 are under construction.These include a massive "science based industrial park" near Taipei designed to foster areas where scientific and techmological investment will bring a commercial payoff.This park,established in 1981,now boasts 70 companies,many being to the forefront of the world hi-tech industry.

(3)The labour force is more educated than ever before and a lot of money has been spent in this area.The proportion of the population with degrees has risen to 12% from 4% in 1968 and the proportion finishing second level is now 22%(as against 10% in 1968)[20].Not only have the numbers increased,the quality of education has also been improved and vocational schools have been better equipped and their co-ordination with industry actively planned and implemented.

(4) Once again the country is busily creating the right "investment climate",and five year tax exemptions ,offers of venture capital from the state, low interest loans etc. all are

being used to attract hi-tech firms.With a highly educated workforce,Taiwan will once again be the cheap labour (in its field) destination.

(5)Attempts are currently being made to turn the Taipei stockmarket into a sophisticated world market.The idea is to channel Taiwan's huge savings into the most profitable investments possible,and also to provide equity for the hi-tech sector.Recent laws have granted permission for foreign brokerages to open a branch in Taiwan and to deal directly on the stockmarket.

While it is still too early to say whether these measures have been successful they appear to be moving Taiwan relatively smoothly into an "industrial market economy " category.The average GDP growth per head between 1980 and 1986 was 6.8% and last year's trade surplus was the largest ever.Taiwan is certainly confident it can make the transition-the Council for Economic Planning and Development forecast a GDP per head of $13,400(in current terms)by the end of the century,and the new president Mr.Lee Teng Hui has said he wants the figure to be $17,000[21].

However,while the future seems very bright there are two large problems Taiwan must deal with in the next fifteen years.Both are problems associated with its success.The first problem is the huge trade surplus.When combined with the fact 44% of Taiwan's exports go to the U.S.,it makes for bad international relations and means that U.S. demands for a revaluing of the NT$ over the last few years must be treated very seriously.In fact in the last three years the exchange rate has appreciated from about NT$40=$1 to about NT$26 to $1.However this has not really affected the surplus because profits have simply been cut on exports and Taiwan buys very little from the U.S. anyway.This indicates that further recaluations will probably be necessary and Taiwan will obviously be trying to minimize damage to its competitiveness.The U.S. pressure has also reduced the tariff levels,many of which were an overhang from the 1960s.The average tariff rate in real terms is now about 4% but is much higher in specific areas(e.g . the 55% tariff on imported cars).If Taiwan is not to have action taken against it by the U.S. and others(GATT etc.) it will have to reduce these tariffs and its trade surplus fairly rapidly.

Taiwan's second problem is pollution.The lack of environmental control measures which helped the boom of the 1960s and 1970s now means that Taiwan's area is now officially considered harmful to health for 17% of the year and the country has the highest rate of hepatitis B in the world. Taiwan has become an effluent as well as an affluent society. A solution to this problem is very difficult to find.Most of the polluters are small firms who could not afford to change their chimney stacks.While the government has set up an "Environmental Protection Administration" last year,many doctors are predicting a horrifying increase in cancer rates over the next 20 years.

In 1988 Taiwan has decided it is time to give development aid.It is to start by giving about 0.4% of GNP for the next five years[22].In many ways ,this is an indication that Taiwan is ending the development process.This process has not fallen neatly into any one category:aid was needed,import substitution policies used but export orientation was the dominant policy.The lesson to be learned is that no one strategy is suitable and that long term planning and a willingness to make sacrifices is required.In a sense,Taiwan is a shining example to other LDCs ,in many ways it is a testament to how hard it is to achieve growth.So many conditions were right in Taiwan that may not be right elsewhere.However,what must please Taiwan most is that with 2% of the population of China it is 40% of the national income.Taiwan has rejected out of hand a "one country,two systems" approach.The dream of the Republic of China encompassing the 35 provinces again is still alive and this patriotism will probably fuel Taiwan's economic miracle into the 21st century.

Footnotes.

1.Taken from various "Economists" who cull the statistics from their own sources and national statistics.The excellent World Bank development report does not give any statistics,presumably because Taiwan will not join any organisation which recognises China.However the same report does give statistics on other nonmember countries e.g. the USSR so unless the Taiwan govt. has called for their statistics to be excluded I am at a loss to know why they are excluded.

2.The economist;5-11 March 1988;A survey of Taiwan p.1

3.Rnis and Kuo,The Taiwan success story,p.143

4.in "The role of monetary policy",AER,LVIII,no.1

5.As footnote 2

6.The Taiwan economy in transition,Shirley Yuo,1983,p2

7.ibid,p.289

8.ibid,p.27

9.ibid,p.137

10. Rostow,The stages of economic growth,1960,p.39

11.Fei,Ranis and Kuo,op. cit. p.10

13.ibid,p.9
14.Yuo,op. cit. p.140
15.ibid,ch.8
16.Fei,Ranis and Kuo use family income as their measure of equality.
17.Yuo,op. cit. p.133
18.The Economist ,op. cit ,p.9
19.ibid.,p.13
20.Kuo,op. cit. p324
21.The Economist,Feb27-Mar4,p.46
22. ibid ,Mar5-11 ,1988,Taiwan survey
23.ibid,Feb27-Mar 4,p.46

GOVERNMENT INTERVENTION IN THE IRISH ECONOMY

Margaret Doyle.

"A state comes into existence because no individual is self-sufficing ,we all have many needs".(Plato)[1]

Economics and politics are inextricably linked.The question of government intervention in the Irish economy cannot be seperated from the broader one concerning the role of the state in the modern world.This is not a question of individual vs. collective behaviour;man being a social animal has assured the existence of familial,tribal religons and economic groupings.We are ,rather,faced for the first time in history with the government of an educated mass public .Experiments this century have ranged from totalitarian fascism to totalitarian communism with varying methods of social and economic organisation.The world is still in a state of flux and great anxiety exists over the proper role of the state in today's society.

Ireland is a small open economy,a state midway between centralism and liberalism.It has a quite high(53.7%) public sector share(public expenditure expressed as a percentage of GDP).This figure includes all government expenditure less intergovernmental transfers.Half of it is comprised on transfer payments and the rest on the administration and provision of government functions of defence,policing,health,education and infrastructural provision.

During the 1970s there was a massive increase in the PSS from 39.5% in 1973 to 55.6% in 1982.This was due in parts to increases in transfer payments which increased both in number and the level of benefit and was also due to a tremendous expansion in numbers employed in the public sector(now over 200,000) largely due to the soaring unemployment rate in the wake of the oil crises.This increase is PSS was funded both by the increasing proportion of income taxes taken by the state as nominal income increased,and by borrowing to finance current spending.

This decade has seen a widespread reaction against high levels of government intervention.It has its intellectual expression in such books as "The Road to Serfdom"[2],"Bureaucracy and Representative Government"[3],and "Free to Choose"[4] which,though not new ,have achieved new prominence in the 1980s.In Ireland such intellectual ideas are accepted as people see the Irish economy as being

trapped with the burden of national debt,due mainly to an enlarged public sector.
The problems identified for the public sector are firstly that it is overexpanded,i.e. it is bigger than people actually want.Due to fiscal illusion(the phenomenon whereby inflation pushes wage earners into higher tax brackets which are fixed in nominal terms) people did not perceive the true costs of a public sector;if they had,they may have reduced their demand for public services.Secondly productivity in the public sector has grown slowly relative to the other sectors of the economy.However, a fundamental cotroversy centres on whether such a phenomenon is inherent in the nontechnologically progressive nature of services such as health ,policing etc. or whether it is due to the "economic bureaucracy "[5]i.e. civil servants obdurate stance against efficiency in favour of aggrandisement.
I believe that the backlash outlined above should be perceived in its proper context.It is merely the swinging of the pendulum of public opinion away from the unquestioning acceptance of "the omniscient,altruistic public official implicit in the market failure arguments for state intervention" towards the reality of "vote seeking politicians and self intersested civil servants"[6].There are undoubtedly problems with government intervention but those outlined above are one of practice ,not of principle,and so may be mitigated,if not eliminated by reform.Democracy offers the people a most potent instrument to shape and mould Irish society and in particular its economy on which so much else depends.During the present swingeing cutbacks(which in their unplanned and random nature bear many of the faults for which the growth in the PSS in the 1970s was criticised)the beneficial nature of gonernment intervention should not be forgotten.J.M. Keynes is said to have declared that"The political problem of mankind is to combine three things-economic efficiency,social justice and individual liberty".In this essay I shall outline how the government can and does fulfill these functions in the Irish economy.
The most vociferous proponents of the market are those who oppose "big government".Accepting the regulating mechanism of the invisible hand they hold that a social optimum can be achieved with a minimum of government intervention.However,in reality divergences from the theory of perfect competition occur with the existence of imperfect competition,natural monopolies,missing markets and externalities.
The state produces public goods.Merit goods are produced because of externalities i.e. unpriced effects external to the market.Because private and social costs and benefits are not equal,equilibrium in the market is not optimal.Thus the state may

provide merit goods such as health and education which it will believes will benefit society as a whole.It is ignorance(in the economic sense)which leads to underconsumption of such goods(as well as their long term nature as an investment relative to individual time preference),and ignorance also leads to overproduction of demerit goods.Government may discourage such activities through exhortation or legislation e.g. against smoking.
Social goods are goods to which the twin principles of the market,exclusion and revealed preference,do not apply due to jointness in consumption and the free riding problem whch distorts revelation of preference.These goods include defence,streetlighting and public parks.Many public goods are also a source of civic pride.
Natural monopolies throw a spanner in the works of perfect competition.The state may institute anti-trust legislation or it may nationalise the industry for several reasons e.g. to avoid overpricing and exploitation of the consumer or because many such monopolies constitute infrastructural industries and form a direct part of the cost structure of most other economic activities.As in other underdeveloped countries Ireland also took over natural monopolies because the pragmatic considerations of a low capital base and a low willingness to invest induced the state to develop an industrial base in the early years of the Free State.This involvement was also used as a device to bring about social justice through interregional equality by locational planning.The dispersal of such industries has had a profound effect on rural towns otherwise reeling from severe migration,and provided opportunities for employment and thus enhanced liberty through choice.The state also provides equality of opportunity(and thus again enhances liberty) through anti-discrimination legislation.
The third area in which the government can substantially aid economic efficiency is is in the area of planning and growth.An optimal allocation of resources at all dates in the future(i.e. optimal economic growth)requires knowledge of all future prices and if there aren't futures markets in all commodities then this is not possible.This is the problem of "missing markets".One way of tackling this problem is for the state to gather and publish information relevant to the growth of the economy.The costs of such information gathering would be prohibitive for all but the largest firms.This was the rationale behind the introduction of indicative planning at the end of the 1950s.It must be added that planning has a bad name,particularly in Ireland.Politicians now boast of "pragmatism" and "dealing with situations as they arise"[7] which is a rather shortsighted approach to take.Planning would not be what Ritchie Ryan described as "least realistic of

my tasks [being based on] prejudices about the past,hunches about the present and prophesies about the future" if some fundamantal reforms were implemented.The first is an improvement in the statistical base both in coverage and processing time.The second problem is that plans become politically tarnished because of overoptimistic targets(and thus casts doubts on the credibility of all government functions).In the Netherlands a Central Planning Bureau independently reviews and costs all plans.Such a body would be veru useful in Ireland(indeed one of the criticisms that T.K. Whittaker made of the short lived planning department was that it divorced planning from costs)
The last more intractable problem is that Ireland is an SOE and so government control over the economy is limited.However,planning can be useful for endogenous variables such as the money supply and would be excellent for the public sector.The publication of such a plan would provide certainty for businesses regarding taxation and expenditure and would disarm the criticism that that "the more the state plans,the more difficult planning becomes for the individual"[8].This criticism would not hold if the government published the parameters within which it was constrained,the targets which it hopes to achieve,the means by which it hopes to do so and a routine report on its progress.Ironically ,this proposal should be readily accpepted by some of the strongest opponents of state intervention-the New Classical Marcroeconomics/Rational Expectatations school who attach great importance to maximising the information available to the private sector.Such planning would lead to a medium term approach which is now absent from the annual budget.It would involve a co-ordination of government departments now lacking and lastly it would fulfill the political function of preventing a government from being elected without policies and thus having a "mandate" to act as they wish.
Most monetarists lambast the Keynesian approach as being too interventionist and allege that high government intervention is "antithetical to liberty"[9].However,Keynes held a contrary view;he saw individual liberty being advanced by stabilisation policies;"the enlargement of the functions of government" Keynes would defend "both as the only practicable means of avioding the destruction of existing economic forms in their entirety and as the condition of the successful functioning of individual initiative"[10].One could also argue that the libertarian arguments employed by Hayek,Friedman and Nozick would in practice enhance the liberty of the capitalist at the expense of those without capital because of its scarcity value.However this a matter of impassioned ideological controversy and is outside the confines of this essay.

Lastly both social justice and individual liberty are enhanced by government redistributionary policies.These include more than transfers,though transfers are the most salient aspect.Transfer payments are just in that they redress the imbalances caused by inequalities of wealth and obviously enhance the liberty of those who would otherwise be in destitution.The universal provision of social and merit goods also provides a degree of categorical equity.The arguments for direct tranfers instead of these may be refuted because they would lead to decreased use of these services by the poor and also to a two tier system of provision.Lastly,a service often neglected by economists is the legal system.Independent of the Oireachtas and posessing a proud tradition of ots own it treats all citizans equally.Free lagal aid also helps the economically powerless to challenge the powerful.
In conclusion it should be warned that"it is not sufficient to contrast the imperfect adjustments of unfettered private enterprise with the best adjustments that economists in their studies can imagine.For we cannot expect that any public authority will attain or will even wholeheartedly seek,that ideal.Such authorities are liable alike to ignorance ,to sectional pressure and to personal corruption by private interest"[11].Once we ahve recognised this we may keep a close and watchful eye on the government and thus mitigate ,if not eliminate,its most glaring flaws.Then government,through benevolent intervention may work for the general good.Those who fear the demise of capitalism should note that "capitalism did not survive in the United States or in the other industrial countries,because of a rigid adherence to the individualist precept-the sacrifice of those who could not make it in a stern competitive struggle.It survived because of continuing and generally successful effort to soften its hard edges-to minimize the suffering and discontent of those who fail in the face of competitive economic power,ethnic disadvantage or mental,moral or physical incapacity"[12].

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8.Hayek,ch. VI
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LONG TERM TRENDS IN EQUITY PRICES

Jonathan Wright.

This model is inspired by the historic tendency of the ratio of yields in gilt and equity investments to average 2.Deviations outside the 1.5 to 2.5 range in the U.K. have always presaged sharp correction.The model focusses on yields,not earnings incorporating retained earnings into future yield expectations and seeks to establish rational price levels in equity markets by comparing their returns over time to those available in other investments,particularly gilts.

The model assumes that all investors have expectations of future interest rates and dividends of which they are certain (or at least risk of deviations from these expectations is symmetric on either side),that they are rational,and that after some point in time in the future,perhaps the very distant future,expected interest rates and dividend growth rates become constant over time (e.g. our expectations of these variables in 2200 are the same as those in 2250).β and r represent yield dividends and interest rates respectively which are functions of time(t).By the last assumption there exists some t' such that if t>t' r=r' ,$\beta=\beta'(1+k)^t$,where β,k and r' are constants.

The model requires expected equity returns to be equal to expected gilt returns over all time periods or turning this on its head it requires the price of an equity at a point in time to equal to its price and cumulative return at any other point in time discounted at the interest rates implicit in gilt prices.the valuation at t=0,P_0 is given below.t=(1,2,..........)

$$P0=\int_0^1\frac{\beta dt}{(1+r)^t}+\frac{\Delta P+P0}{\int(1+r)^t dt}=\int_0^1\frac{\beta\, dt}{(1+r)}+\frac{P1}{\int(1+r)^t dt}\qquad[\Delta P=P1-P0]$$

$$\frac{P1}{\int(1+r)^t dt}=\int_1^2\frac{\beta\, dt}{(1+r)^t}+\left[P2-\frac{P1}{\int(1+r)^t dt}+\frac{P1}{\int(1+r)^t dt}\right]\frac{1}{\int_1^2(1+r)^t dt}$$

$$=\int_1^2\frac{\beta\, dt}{(1+r)^t}+\frac{P2}{\int_1^2(1+r)^t\, dt}$$

$$\text{similarly, }\frac{Pi}{\int_{i-1}^{i}(1+r)^t\, dt}=\int_i^{i+1}\frac{\beta\, dt}{(1+r)^t}+\frac{Pi+1}{\int_i(1+r)^t dt}$$

$$\text{Therefore }\quad P0=\int_0^1\frac{\beta}{(1+r)^t}dt+\left(\int_1^2\frac{\beta\, dt}{(1+r)}+\left(\int_1^3\frac{\beta\, dt}{(1+r)^t}\right.\right.\ldots\ldots\ldots\ldots$$

$$\text{i.e. }\quad P0=\int_0^\infty\frac{\beta\, dt}{(1+r)^t}=\int_0^{t'}\frac{\beta\, dt}{(1+r)^t}+\int_{t'}^{\infty}\frac{\beta'(1+k)^t}{(1+r')^t}dt\quad\text{..Deduction 1}$$

But P0 is infinite if $\lim_{t \to \infty} \frac{\beta'(1+k)^t}{(1+r)^t} \neq 0$

P0 is finite,therefore $(1+k)^t < (1+r')^t$ for all t, t >t'

therefore k<r' ...... Deduction 2

If t+t' and dividends are paid only where t=1,2,.............(i.e. is an integer) then

$$P0 = \sum_{t=0}^{\infty} \frac{\beta'(1+k)^t}{(1+r)^t} = \sum_{t=0}^{\infty} \frac{\beta'(1+k)^t}{(1+r)^t}$$

Therefore $P0 = \left[\frac{1}{1 - \left(\frac{1+k}{1+r'}\right)} \right] \beta'$ (Sum of geometric progression to infinity)

$$= \frac{\beta'(1+r)}{(1+r)-(1+k)}$$

Therefore $P0 = \frac{\beta'(1+r)}{r'-k}$ ....Deduction 3

Deduction 1 essentially means that a rational valuation of an equity in this model involves looking only at its future yield because these will cause price fluctuations.Deduction 2 is more interesting;it means it is irrational to expect dividend growth rates to exceed interest rates for ever.This is a very significant conclusion as it is almost certainly defied in respect of long dated gilts in countries with low interest rates e.g. West Germany or Japan.Deduction 3 applies to a special case even within the model i.e. where expectations of interest rates and dividend growth rates are that they are constant over time.It would indicate however that where r' and k are close extreme sensitivity of price to changes if r' and k is rational.

Although this model may partly account for long term equity trends it does not adequately explain volatility in contemporary equity markets ,because these add on risk premia.These are not primarily because of uncertainty in predicting the r and β functions but because of feared irrationality in the markets.Risk premia imply further irrationality so irrationality and rationality are both self fulfilling prophesies.Hence we can develop the above model to include features of cobweb models in it;movements towards or away from the model itself are self perpetuating and lead ultimately to stability or wild volatilty.

EQUALITY AS A POLICY OBJECTIVE

Margaret Doyle.

"The idea if inequality is both very simple amd very complex"

Amartya Sen[1].

Andrew John(Economy of Ireland,ch.2)interprets the policy aim of intragenerational equity as a proximate aim of equality.The reason for any policy objective is to change society in its imperfect existence and move towards the "proper order" of things.Philosophers through centuries have described their own forms of Utopias.Most argue passionately for fairness,distributive justice-in short,equity.Plato advocated a form of communism and yet his "Republic" was to be ruled by an educated elite.Aristotle maintained that "equality consists in the same treatment of similar persons"[2] where similarity is based on one's position at birth.Thomas Jefferson was author of a constitution guaranteeing equality before the law,but not for negro slaves.Rousseau and Marx hold that individuals are potentially equal and that social relations should be derived from this premise, whereas Locke and Nozick hold that people are entitled to the fruits of their natural endowments.

Nowadays,there are two basic definitions of equality.I shall define the two in turn,examining what each means,outlining problems of measurement and also considering the desirability of each.I shall finally consider the equation of intragenerational equity with equality.

The first definition of equality is equality of opportunity or a system that is fair in its operation.This has widesread support and yet there is immense subjectivity in assessing its extent.Most would note inequalities in material inheritances but from an ethical point of view ,is the posession of an inherited skill not as equally inequitable?However,as Friedman as noted "literal equality in the sense of identity is impossible" and hence measures taken to ensure equality of opportunity are generally concerned with education.

Why is equality of opportunity so favoured?There are two strong arguments behind it.The first is economic and states that equality of opportunity is complementary with efficiency and the free market system and thus with the optimal production of goods and services.Friedman if fact equates free market capitalism with equality of opportunity.Funnily enough Plato also favoured equality of opportunity(even of the sexes!) not on principle but because of its beneficial effects on production.

The second argument is that equality of opportunity is ethically just and is grounded in the premise of equality before God and equality before the law as "All men are created equal".Even Locke may have approved of keeping earned income only(thereby excluding inherited inequalities) by maintaining that natural resources are held in common.

There are two reservations about equality of opportunity as above interpreted.The first is that opportunity seems to mean "economic opportunity".Friedman even admits that in a free society where there is equality of opportunity "social practices unquestionably gave special advantages to persons born in the 'right' family,of the 'right' colour and practising the 'right' religon.[4]Education is supposed to eliminate such practices.Pigou described this as "the *locus classicus* of liberal theories about the relation of education to social class" in which we "will use education to abolish class by assimilating all men to the rank of gentlemen."[5]I doubt that either deproletarianisation or embourgeoisement will be strong enough to counteract the natural forces puling towards a pyramidal structure.As Ken Livinstone recently remarked,the main difference between the upper and lower classes is the immense confidence possessed by the former,something that is not always passed on in comprehensives.

One's second query is whether equality of opportunity is possible to have without equality of welfare.Equality of opportunity at one stage in life may by chance lead to further inequalities of opportunity.Secondly power is generally equated with money.Assuming equality of opportunity results in inequalities of wealth,can equal treatment e.g. before the law be guaranteed?Thirdly if intergenerational transfers of wealth are permitted it is difficult to implement equality of opportunity for subsequent generations.

The second definition of equality is equality of welfare.Welfare however is immeasurable and so we must choose a measurable proximate policy objective,e.g income or wealth.Economists generally choose income as wealth itself generates income.Also in Ireland information on wealth is limited to that from those who die above the CAT threshold.However using income as a proxy raises the distinction between earned and unearned income as the former probably involves disutility(having to get up in the mornings),and also wealth provides intangible benefits such as security and prestige.We then have to ask:Over what period do we equalize income-weeks,months,years or a lifetime?What groups are to be the basis of our study?-Individuals would be the most logical choice but again we are constrained in that far more information pertaining to households is available.Again two households may have the same income but a different breakdown of earners to dependents.Lastly our true devotion to equality may be tested by guaging our response to its extension from national to global equality.Despite Minister McSharry's statement that"My country has always been very supportive of of aid measures aimed at the most distressed low income countries"[6] Ireland's aid fell to 0.19% of GNP in 1986,compared with 0.7% recommended by the U.N.

What are the arguments in favour of equality of outcome?Andrew John makes the valid point that from the four assumptions of welfare theory and particularly the third which states that individual welfare depends on the goods and services consumed,"at least over a significant and relevant range inequalities of welfare and inequalities of income will be associated"[7].After all,despite Friedman's reassurances that although "life is not fair ..it is important to recognise how much we benefit from the very unfairness we deplore"[8],this is scant comfort to the destitute.Nor does it feed them to know that members of their class will,in future generations become increasingly well off.

One argument in favour of equality is the social one.Equality is desirable because inequalities cause alienation and hurt us all.Secondly because of human compassion we may desire to allevate poverty and thus reduce inequalities.This is consistent with Pareto-efficiency.

The second viewpoint is a philosophical one.Rousseau and Marx take an egalitarian view of society based on a humanistic view of the equal worth of each individual.Equality of welfare is achieved on the basis of the famous maxim"from each according to his ability,to each according to his needs"[9].The problem is determining what precisely needs are since they will be subjective.

Utility is taken into account in the argument in that if one assumes diminishing marginal utility of income,utility is maximised by an equal distribution of income.This premise may be flawed in treating money as having DMU.Unlike other commodities money is very flexible and may not be subject to DMU,at least to the extent imagined.

Sen rejects the utilitarian framework and concurs with Andrew John that needs rather than "desert" "would appear to have far greater use for the complex idea that we call humanity"[10].The market exacerbates existing inequalities whereas his weak equity axiom[11] would call for the opposite distribution.

The final argument rests on a philosohical experiment carried out by John Rawls.He posited that if placed in an "original position" we would be infinitely risk averse and choose the configuration that maximises the welfare of the worst off person(maximin).Given a fixed total income,this calls for total equality of income.

The arguments against equality are ,as Sen noted,generally made on non-distributional grounds.They generally concern the "size of the pie" and problems of redistribution.Friedman dismisses equality of outcome as impracticable,the pursuit of which would be economically and socially catastrophic.Economically,because unlike the Dodo in "Alice" who declares"everyone has won and all must have prizes" in the real world we are faced by the questions "where are the prizes to come from?",and "what incentive is there to work and produce?"[12].Socially,it will result in a state of terror and will drive out the "ablest,best trained,most vigorous citizens" and will cause a "growth in crude criminality"[13].

We cannot but make value judgements when considering distribution."In one way or another usable measures of inequality must combine factual measures with normative ones"[14].Thus Sen raises the issue which I briefly touched on earlier which is the equation of intragenerational equity and equality.There are the non-income determinants of welfare to be considered.As Andrew John said inequalities of welfare and income are connected "over a significant and relevant range".It is undoubtedly true that the MU of income is infinite for a starving ,penniless pauper yet once a certain level of income is reached other factors become dominant.These may be tangible factors such as one's environment,one's work,one's fellows and indeed one's personality.We must also consider intangibles such as liberty which will undoubtedly be limited by by any attempt to pursue equality.The USA has plumped for a mixture of the two often termed categorical equity,where equality is treated for a merit good and everyone has the right to subsistence.[15].It is an attempted solution to the trade off between equity and liberty.It is not perfect,but then the idea of equality is very complex.

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1.A.K. Sen,On Economic Inequality,preface.
2.Aristotle,Politics,Book II,Ch.7
3.M.Friedman,Free to Choose,Ch.5
4.ibid.,Ch.5
5.Pigou,quoted in F.Hirsch,The Social Limits to Growth.
6.In a speech to the UN quoted in the Central Bank Review,3rd quarter,1987.

7.M.Friedman,ibid.

8.A.John,Economy of Ireland(ed. J.W.O'Hagan),Ch.2,p.84

9.Karl Marx,quoted in A.John,ibid.

10.A.K. Sen,op. cit.,Ch. 4

11.The weak equity axiom states that if person i has a lower level of utility at each level of income than person j then person i should receive more income in an optimal solution.

12.M.Friedman,op. cit.,Ch.5

13.As 12

14.Sen,Ch.1

15.The Economic Report of the President of the USA,1974-"Those who produce more should be rewarded more;and no individual or household should be forced to fall below some minimum standard of consumption regardless of production potential".

INSIDER OUTSIDER LITERATURE - AIMS AND ACHEIVEMENTS

Mark Walsh

Introduction.

In recent years a growing body of literature has developed in macro labour economics focussing on the distinction bteween insiders and outsiders and the economic implications of this disparity.In such work,insiders are generally held to be currently employed workers (at a given firm) and outsiders are those currently unemployed.From such an analysis comes,it is claimed,explanations and possible solutions to current unemployment problems.Our aim in this paper is to offer an analysis ot the two quite seperate paths that this research has taken,discussing their respective aims and achievements,with critical comments where justified.

In section one we assess the "hysteresis" work of Blanchard and Summers,whilst section two considers Lindbeck and Snowers research.Both of these sections contain a brief insight into the theoretical basis of the relevant models and a critical appraisal of them.Finally section three offers some concluding comments and possible further research developments.

Section One-Insider-Outsider analysis and Hysteresis.

The recent European emplyment experience has led many economists to believe that we are observing hysteresis in the labour market.what this entails is that far from there being a natural rate of unemployment to which the economy will return we are experiencing an employment ratchet effect :once unemployment falls to a new low this low then becomes the economy's equilibrium position.[1] Blanchard and Summers have developed an insider outsider model to support this view.

The key assumption of this work is that only insiders are involved in the wage setting process-outsiders have no direct influence.However what is meant by insiders is a somewhat flexible concept.Taking a simple model we can analyse the basic implications.Assume there are many firms in the economy,and demand facing each firm is a function of aggregate demand,which itself depends on real money balances and the firm's own price relative to the general price level.Assuming that the only potential source of fluctuations in the economy is nominal money, and that our variables of interest are employment (n),output(y),price(p),nominal money(m) and the wage (w) (an i subscript refers to firm i,an unsubscripted variable is economy wide),then formally the demand facinf firm i is given by

$(1) y_i=(m-p)-a(p_i-p)$

If firms operate under constant returns to scale $\Rightarrow y_i=n_i$ and given constant marginal costs and constant elasticity of demand,profit maximisation implies $p_i=w_i$.

From this we can obtain a derived demand for labour for firm i of

$(2) n_i=(m-w)-a(w_i-w)$

Now associated with each firm there exists a group of insiders with membership n_i^*;only they are involved in wage bargaining and they have priority in employment.Assuming that in each firm the group of insiders is sufficiently strong to set the wage unilaterally,and sets it so as to make expected employment equals membership size we have

$(3) E(n_i)=n_i^*$

Thus from (2) we have that $E(m)-E(w)-a[w_i-E(w)]=n_i^*$.Given that all firms and groups of workers are the same and that the only shocks are aggregate nominal shocks then all groups will choose the same nominal wage.Thus $w_i=w=E(w)$ which implies

$(4)\ n=n^*+[m-E(m)]$

i.e employment =membership + a disturbance equal to the unanticipated component of the money supply.

Consider the membership rule.In an extreme pure insider model this would be only workers employed at the time of bargaining i.e. $n^*=n(-1)^*$ which implies

$(5) n=n(-1)+[m-E(m)]$

Hence employment follows a random walk,innovations being due to unexpected movements in aggregate demand.In reality though membership rules will not be this rigid,it may take a few periods to gain or lose insider status.Under such circumstances employment dynamics become more complex e.g. a long sequence of unexpected shocks can generate a change in membership but this is likely to be a rare event.Thus on average employment is stable at its equilibrium until such a sequence occurs to change the equilibrium (be that positively or negatively),hence the insider model can generate persistence effects.

This simple model can be extended to take account of outsider effects on wages via employment in new firms (something which is more likely in boom periods).This leads to employment following a first order process around the level of the labour force and if the labour force evolves slowly over time unemployment also follows approximately a first order auto regression.Similarly,if we believe that only the short term unemployed can exert downward pressure on wages(due to discouraged worker effects etc.) then assuming that short term unemployment is roughly equivalent to the chenge in employment then (3) becomes

(3)' $E(n_i)-n_i^*=b[n(-1)-E(n)]$,$b>0$

i.e' assuming wage pressure from outsiders depends on expected short term unemployment,then solving for aggregate employment gives

(7) $n=n(-1)+[m-E(m)]$ -employment follows a random walk.Again allowing for the more realistic nature of the complex dynamic relationship between short term and total unemployment we can move away from this full persistency result to a more stepped ratchet effect.Thus the Blanchard and Summers work has generated an insider outsider model with persistence effects for unemployment ,and which implies that any attempts to reduce actual unemployment will serve to reduce equilibrium unemployment as well.To succeed such policies must be aimed at generating a series of positive shocks to the economy,possibly via monetary expansion in this simple framework,in an attempt to re-enfranchise the unemployed,particularly the long term unemployed.

Whilst persistence effects are important in analysing unemployment as any simple regression will show ,this insider model suffers from three major problems.In its pure insider form it implies that at the disaggregated level sectoral wages should largely depend on sectoral conditions and previous employment history in the sector ;but evidence suggests that economy wide influences actually play the dominant role in sectoral wage equations.Also,these wage equations suggest that wages are inversely related to labour force size-on this model they shouldn't.Thirdly and possibly most importantly,there is the turnover problem:each year firms lose many of their employees through voluntary quits.If wages were fixed to ensure continued employment of the insider group alone i.e. not entrants we would expect to observe continually falling employment.However despite these criticisms the insider outsider analysis seems to have made a lasting contribution to wage theory,and given the infancy of hysteresis theories we can only expect this field to expand and enhance its theoretical basis and empirical robustness over time.

Section Two:turnover costs.

In the theory of involuntary unemployment the following two questions are of fundamental importance:

(i)Why do involuntary workers not succeed in underbidding their employed counterparts?

(ii)Why do employed workers accept being laid off when times are bad rather than take a cut in their wages?

In the cintext of the free market economy an answer to these questions can proceed along one or both of two routes
(a)it can explain why employers have no incentive to accept lower wage bids ,or,
(b)it can show why the unemployed have no incentive to underbid.
Efficiency wage theories tahe the former route,union models the latter,and implicit contracting notions both.The insider outsider analysis of Lindbeck and Snower offers an approach to both routes.It attempts to capture the notion that
(i)workers might not try to underbid their fellow workers,because they believe that the latter would respond by making their working life unpleasant for them ,or
(ii)firms may refuse to accept wage offers of underbidders because to accept would be unprofitable i.e. it might reduce insider morale hence productivity; entrants may require training and the wage differential may be less than this expense for example.
As such this branch of insider outsider analysis is designed for a completely different purpose from that of section one.Also as we shall see it seems to offer a better microeconomic foundation from which to assess current events,Lidbeck and Snower's analysis starts from the premise that currently employed workers have,in the firm's eyes a cost advantage over outsiders.This stems from the insiders' ability to impose a turnover cost on their employer if they are to be laid off or entrants recruited.
Turnover costs are generated in three ways.Firstly there are hiring and firing costs.If we assume that there exists three homogenous groups of workers :insiders,entrants and outsiders and entrants are associated with the same hiring cost and go through a fixed initiation period after which they become insiders and thus associated with firing costs.Assuming that contracting is only possible for the initiation period and no longer,also that "entrant fees" are not available for whatever reason,then it can be shown that insiders can exploit their bargaining strength to us this cost advantage and gain some of the .firms monopoly rent.Thus we should observe the insider wage>entrant wage(but by no more than the firing costs) and the entrant wage>outsider wage (but by no more than the hiring costs).Clearly we have a situation where the insider wage as above the market wage but due to the costs entailed in recruitment etc.-it is not firm's interest to hire workers who are seemingly undercutting currrent employees.Assuming that all firms are identical and aggregating we generate a situation with labour supply>labour demand i.e. unemployment.

Expanding this to encompass ability differences,measured by the diffrential between marginal products net of indispensable labour costs,we can show that whenever this differential is less than the differential between the insider wage and tge reservation wage,then outsiders may be identified as involuntarily unemployed.This unemployment will persist whenever the ability differential net of dispensable and indispensable labour costs is greater than the wage differential.In that event the firms have no incentive to replace insiders by outsiders.
A second turnover cost is generated by co-operation and harassment activities of insiders which can affect each others' productivity.Given firms' inability to contract against such activities,due to monitoring difficulties,insiders can use such methods to generate economic rent which they can exploit in wage determination to prevent underbidding being successful.
Consider co-operation alone:entrants offer to work at their reservation wage and insiders attempt to gain a wage above this.The wage diffreential is only sustainable so long as it is less than the insider-entrant marginal product differential generated by the disparity between insider-insider co-operation and insider-entrant co-operation. Assuming co-operation has no direct utility cost to insiders then it is insiders interests to maximise this disparity;given that co-operation enhances productivity this implies co-operating only with insiders.Given this situation persistent involuntary unemployment may exist because outsiders suffer a reduced choice set-they are unable to compete on the same productivity grounds as insiders due to a lack of co-operation,leaving them as lower productivity workers;thus it wouldn't be in the firm's interests to hire them for they would only become employed outsiders still failing to receive productivity enhancing co-operation thus only being worth the reservation wage.
Similarly harassment activities can achieve these results.Insiders can keep unemployed workers from underbidding by creating a credible threat that the underbidders will be harassed with its associated disutility.Thus outsiders will have a higher reservation wage than insiders ,hence their choice set evev allowing for their abilities is less favourable than that of the insiders,and they thus may be considered involuntarily unemployed.
A third cost induced by turnover is the adverse morale effect on employees such behaviour generates leading to a fall in productivity.If the firm's remuneration package consists of (a)wage (b)cut off productivity then the firm can increase turnover by raising the cut off productivity.This reduces expected future return to current effort for each employee ;the effect on

effort depends on the income and substitution effects.the substitution effect causes effort to fall-the employee works les hard since he is more likely to be fired and therefore less likely to be compensated for effort;whilst the income effect raises effort because the worker works harder in order to avoid being fired.Thus turnover has an adverse effect when the substitution effect dominates the income effect.If this is the caes an insider can gain some of the economic rent and there may be involuntary unemployment.

We can model the above process as follows.We have three distinct groups outsiders,insiders and entrants (subscripted o,i,e).The variables of interest are employment(L),output(Q),the cost of firing insiders(C_0),the cost of hiring entrants (C_e).Finally,m is the incumbent workforce(inherited insiders)and A is the productivity diffreential between insiders and entrants.We assume that long term wage contracts committing entrants to not becoming insiders are unenforceable and that an imperfect capital market exists.Then if outsiders are perfect competitors for jobs with a firm then the entrant wage W_e will equal the reservation wage R.We have three functions,the production function $Q=f(AL_i+L_e)$, $A>1$;the C_i function $C_i(m-L_i),C_i>0$ and the C_e function $C_e(L_e),C_e>0$

Thus the firm"s problem is to

$\max \Pi=Pf(AL_i+L_e)-W_iL_i-W_eL_e-C_i-C_e$.

The first order conditions are

(i)$PAf'-W_i+C_i'>0$

(ii)$Pf'-W_e-C_e'<0$

For simplicity assume that insiders bargain individualistically and that they gain all the economic rent available,thus

$W_i=\min[(PAf'(m)+C_i^*),(W_e+C_i^*+C_e^*)]$

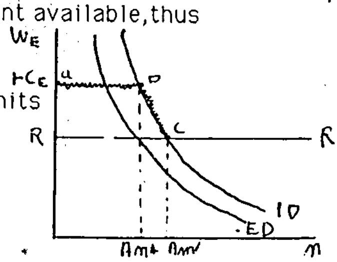
Thus graphically we have

n=AL_i+L_e=employment in efficiency units

ID=demand for insider labour

ED=demand for entrant labour

=hiring condition



Clearly from such an analysis we are presented with three cases.

(1)$0<m<m^*$ i.e the incumbent workforce in initially small enough to allow both insiders and entrants to be profitable => $L_e>0$.Insiders can't force their wage W_i up to the point at which their marginal profitability is 0 because in doing so it would be worthwhile for the firm to replace them by entrants.Thus insiders raise their wage to the level at which their marginal profitability is equal to that of the entrants $W_i=W_e/A$,thus ab+short run equilibria but only point b is long run equilibrium,due to entrants becoming insiders after the initiation period.

(2)$m^*<m<m'$ i.e entrants are now unprofitable at W,but insiders are marginally profitable at that wage:$L_e=0$ and $L_i>0$ hence outsiders can't compete for insider jobs,the insider wage is driven up to the point where the marginal profitability of the insiders is zero,i.e. on the ID curve hence bc equals both short and long run equilibria.Any current stock of insiders in this range perpetuates itself.

(3)$m'<m$ i.e. now both insiders and entrants are marginally unprofitable at R.Thus insiders are fired to the point m' and $W_i=R$ which is both a short and long run equilibrium.

To close the model W and R must be determined endogenously.We can let R be inversely related to the insider wage

$R=-dW_i \quad ,d>0$

and with respect to the entrant wage,assuming entrants capture all of the available economic rent,and that the ratio of the marginal product of outsiders to entrants is a constant b where $0<b<1$ then

$W_e^*=(1/b)R$

Thus in our analysis the line abc can be seen as an effective labour demand curve.Now assuming there exists a fixed number of firms all identical(n)and that there are s workers in the economy then we can aggregate the above labour demand curve to obtain an aggregate labour demand function.Clearly if $s>nm'$ and the current aggregate level of employment$<nm'$ then there is persistent unemployment.

If we define involuntary unemployment to have occurred when workers are unemployed who are prepared to work at a lower efficiency wage than that prevailing provided they can work in identical conditions to those currently employed;then involuntary unemployment is said to exist when

$W_e+C_i+C_e<W_i/A$ for identical conditions of employment, =>

$W_i>(W_e+C_i+C_e)/A$

Thus,this model generates a rationale for involuntary unemployment from an insider outsider analysis as well as addressing the initial questions posed.Returning to these points,it can be seen from this model that involuntarily unemployed workers are unable or unwilling to underbid their counterparts for a number of reasons.Firstly hiring costs generate a gap between insider and entrant wages which the firm can't remove.Secondly,morale effects amongst insiders could lead to the hiring of entrants decreasing overall productivity,whilst

finally harassment activities of insiders towards outsiders could generate such a disutility that the reservation wage is raised above the insider wage,hence they won't offer themselves as undercutters.Similarly Wage cuts will be refused by laid off workers because insiders remaining would object,thus leading to further harassment and alienation etc.-as such their effective reservation wage is now above the insider wage.
Also this model can shed some light on the hysteresis type developments.At the aggregate level,if labour demand falls this implies that the insider and entrant demands will shift inwards-in this simple model the insider group will choose to maintain a rigid wage and decrease its size leading to persistence of unemployment at a higher level;similarly expansion of demand generates a constant insider pool with rising wages,preventing a recovery in employment.As such we ahve a model which implies that to tid the economy of unemployment we must either attempt to expand the informal sector of the economy where insider outsider distinctions are less powerful,or we must attempt to weaken the insiders' grip on the wage setting process.
However it would be wrong to make snap policy judgements from such a simple model.Some of its assumptions especially about the bargaining process are very restrictive and perhaps should be weakened;also some evidence on the strength of the income and substitution effects would be useful.More importantly the movement from a well defined micro model level to a broader macro model leaves a lot to be desired e.g. we generate an economy with only two wages.However this work has made a positive contribution and such problems as there are can be ironed out.

Section three:conclusion
Each half of the insider outsider developments have offered new appraoches to their respective problems.Whilst these initial findings have been interesting and enlightening it must be asked how far such models can go.The hysteresis work appears to offer no explanation of wage dispersion as yet.We need to allow wage bargaining strenghts to vary from firm to firm thus creating a set of insider wages reflecting the strength of each firm's insider union.Also some analysis to voluntary quit process as observed is also necessary-why don't insider groups perpetually shrink over time?Such questions need to be addressed in future research for this line of thought to offer a feasible model.
The Lindbeck and Snower analysis also must face up to such stylized facts and it makes some very bols assumptions which aren't easily justified.For example their work assumes that entry fees aren't payable by an outsider i.e. if the outsider could offer

an entry fee equivalent to the insider reservation wage differential summed over expected working life then the firm would have an incentive to recruit that outsider.Such entry fees would remove all involuntary unemployment in this model.Whilst imperfect capital market ideas and moral hazard arguments can be used to justify such an entry fee elimination this doesn't prevent internal labout markets being designed by the firm which offer implicit entry fees,i.e. a rising earnings profile over tenure;thus this model may not generate involuntary unemployment.Furthermore the insider outsider analysis presumes that contracts are not possible apart from at the entrants initiation period,an outsider can't contract to become an employed worker without attaining insider status and the associated awards.Why isn't this possible?-clearly we need to assume some level of market uncertainty preventing such explicit contracts from being signed,but such uncertainty must also affect the insider firm bargaining and thus may lead to a breakdown in our involuntary unemployment result or for that matter the persistency result.Such issues must be addressed if this is to become a more feasible model.
A possible further development might allow for multiple insider and outsider groupings within the economy,possibly even within a given firm.Such internal distinctions may arise at varying seniority levels in a given internal labour market with a structured hierarchical form.The two extremes of such a process are(i)each individual on the promotional ladder being a seperate insider grouping,leading to individual bargaining a la the classical model and (ii)one insider group with one insider wage a la Lindbeck and Snower.Another line of research could be to integrate this micro model more fully in a macro model possibly allowing for an informal or competitive sector where such distinctions don't occur,or allowing for sectoral rather than economy wide demand changes. However the literature is still in its infancy and there are clearly no lack of issues for a research program in the area in the coming years.

Footnote.

1.Such theoretical developments would offer support to keynes' notion of multiple unemployment equilibria i.e. under a persistence effect each new unemployment level immeditately becomes the new unemployment equilibrium.

EXTERNALITIES - THEIR NATURE AND POSSIBLE POLICY RESPONSES

Kieran Mcloughlin.

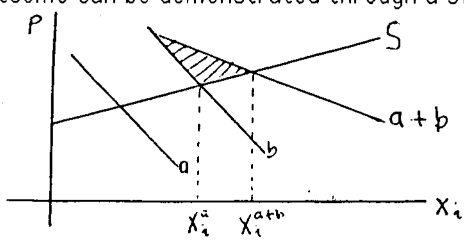
The free market has long been held to provide the most efficient method of maximising societal welfare in so far as it causes demand prices as revealed through marginal utility curves to be equated with supply prices,as revealed through marginal cost curves and thus brings about the optimal allocation of resources.

Naturally it therefore follows that if there is any distortion of this process,then the market will fail and "the link between optimality and competition is broken"[1] .There are a myriad of examples of market failure and whilst there is often disagreement on the specifics of particular cases it is generally recognised that the root cause of such failures is the presence of goods that display substantial degrees of "publicness" or "collectiveness"

Of such goods,the provision of some involves prohibitive transaction costs and while some are non rival in consumption all are non exclusive.An important category of these problematic goods/'bads' is that of externalities.

"an externality is said to exist if an activity of one party affects the utility or production possibilities of another party without being priced"[2] and the manner in which this creates a non pareto efficient outcome can be demonstrated through a simple example.

Figure 1.



Imagine we have 2 consumers,a and b.A consumes goods x and y while b consumes only y but A's consumption of x confers benefit on him.the utility functions are as follows

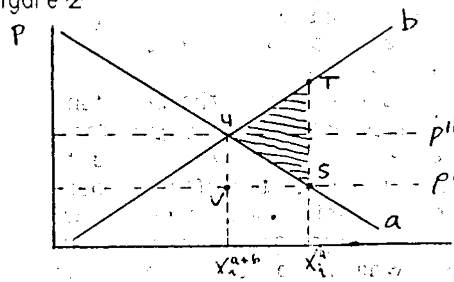
$U_a=f(x^a+y^a)$

$U_b=f(y^b+x^a)$

Now since A consumes and pays for x his demand curve for x determines the market supply .But the benefit enjoyed by b is not registered by the market :thus the true quantity demanded by a and b,i.e. x^{a+b} is not produced causing a welfare loss represented by the shaded triangle.

Similarly,a welfare loss would result if a's consumption of x caused b to suffer a disutulity which wasn't priced.

Figure 2



In the above example a chooses to consume x^a by equating his marginal valuation with the marginal cost,as represented by the price line.Of course this decision takes no account of the costs imposed on b causing over production of x and a welfare loss again indicated by the shaded area corresponding to the differerence between welfare levels at the actual consumption point and the socially optimal consumption point.
Therefore while there are many different types of externalities-positive or negative,originating in production or consumption etc.-they are all resposible for the market failing to achieve the social optimum by causing a divergence between private and social costs.thus to achieve the social optimum some corrective measure must be found.
Such a solution is immediately suggested by figure 2,namely the enactment of a mutual agreement between the parties to reduce A's consumption of x from x^a to x^{a+b}.After all,with such a move b would stand to gain an increase in utility represented by the area STUV while A would lose only SUV,leaving a net gain of STU,the exact distribution of which would depend on the bargaining power of the parties.in this situation it would be in both their interests to engage in a form of commercial logrolling whereby b would bribe a to reduce his consumption to the socially optimum position by offering him part of the surplus utilty STU and eliminating the externality.However this solution ignores distributional issues which could form an important part of the social welfare function and the gain in efficiency could be offset by a worsening of the distribution of income e.g. if a was a landlord and b a peasant.As is usual the economist *qua* economist ignores such considerations.
This does not mean that this solution is economally sound-in fact its practical feasibility is rather limited.Firstly,for such an agreement to be possible we must assume that transaction costs are low(relative to STU);however the existence of high

transaction costs is often one of the causes of market failure in the first place.Also,such a bargaining process can be undermined by strategic behaviour and untrue preference revelation,with for example a overstating his marginal valuation of x and b overstating the disutility he sustains,each trying to maximise their gains.Thus the chances of a move to a non pareto efficient position or no move at all are high.

What we are discussing is essentially the solution offered by R.Coase who argued thar externalities were best dealt with by a market in which externalities could be traded through the imposition of property rights with the affected party paying a bribe or receiving compensation depending on wherein the property rights were vested(which some may see as an arbitrary or unjust criterion),and whether a cost or a benefit is being generated.What Coase is suggesting is not so much that we need to revise our theory of externalities ,but rather that some phenomena that are normally seen as externalities really are not.But this is evading the definition of an externality,because if the good or "bad" can be traded in a market then it is not an externality,by definition.The puzzle then is why a market such as one Coase suggested does not exist,and if the government must intervene to provide it,then his argument loses a lot of its *laissez-faire* force.His approach is basically a one sided approach to a two sided problem,meaning that "the payment of compensation only involves the payer taking into account the costs he imposes on others,failing to make the receiver take account of the costs he imposes on the payer"[3] thus mutual costs and benefits are still not equalised and an externality persists.

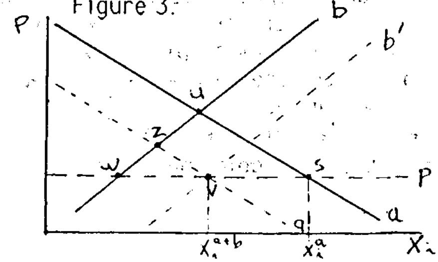
So it would seem that bargaining solutions are of dubious value in attempting to overcome the problem of externalities and that some form of coercive measures might be needed.Such measures of course could only be enacted by the government and an example would be the physical internalisation of an externality as first occurred in the case of the Tennessee Valley water authority.But while such policies can be of considerable success when applied to productive enterprises they would be wholly useless if they were tried on a multiplicity of households.

Another possible approach the government could adopt,which is in fact a derivative from Coase's suggestion would be for it to assume the property rights to a certain resource and then sell quotas to firms.the difficulty is that this would favour large firms who might concentrate their production or use of the resource in a particular area thereby conferring costs or benefits on the inhabitants of that area disproportionately relative to the rest of the population who through the state,are supposed to be owners of the resource.

Yet another alternative would be for the government to set the socially optimal output at a certain level(assuming this could be calculated given the usual problems of untrue preference revelation etc.) and then restrict all firm's output below this level.This approach to is fraught with difficulties.There would be a persistent tendency to "free-ride",indeed this is why there is a problem in the first place;thus there are very serious enforcement difficulties.The state may not pick the right limit on output and thus needlessly drive up its price,or drive firms out of the business,leaving us in a worse position than when we started-tyre factories may cause pollution,but we need some tyres.

All in all then government intervention ,apart from the infringement of property rights is seen to be problematic.The traditional solution to the externality problem which seems to overcome these difficulties is the so-called "Pigovian tax".

Figure 3.



In figure 3,as in figure 2 initial equilibrium is at point S with a's consumption of x causing b a disutility.But if the state were to impose a Pigovian tax on a's consumption of x equal in value to the marginal damage sustained by b then a"s demand curve should shift back to a' with equilibrium being re-established at point U causing the socially optimum quantity x^{a+b} to be demanded,and the apparent disappearance of the externality.But in fact equilibrium would not settle at U but rather at Z because there would now be an incentive to bargain with a loosing UZW but with b gaining VUW thus representing a net gain to the two of VUZ.Buchanan and Stubblebune in realising that the positing of a unilateral tax would not achieve the social optimum suggested that the affected party,here being b,should also be liable for a tax equal in value to the reduction of a's consumption thus shifting his demand curve back to b' which intersects a' at U,the socially optimal level.

Certainly the imposition of such a bi-lateral tax would not be without difficulties,not least of which would occur in the setting of rates which would require true preference revelation while what is known as the conscience effect also has to be taken into

consideration,but nonetheless it would seem to be a more viable and realistic measure than those already discussed..,
In conclusion therefore,we have looked at the nature of externalities and various market and policy based responses to them.Not surprisingly since externalities are a market failure,the market oriented responses did not fare too well.Policy responses at least had some chance of mitigating the externality and given the marginalism on which traditional welfare economics is based,were found to be something of a blunt instrument.A tax of some sort was suggested as "the best of a bad lot".Another problem would seem to be the lack of an adequate theory of externalities .This can be traced to the inconsistency of discussing the problem of one agent's actions affecting others in a framework that assumes that no-one's actions affect anyone else.The essence of an externality in interdependence,which is assumed away in perfect competition .Theories of oligopoly which explicitly allow for the interdependence of actions would seem to be more relevant for our purposes,and this in turn implies that game theory also has an important role to play.However work in this area is very limited and we are left with the depressing conclusion after 50 years of effort that
"it is likely that different external effects will be solved by differerent methods,including that of doing nothing."[4]

Footnotes and Bibliography.

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2.Boadway and Wildasin,p105.
3.Ng,p184.
4.Ng,p176.

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THE MICROFOUNDATIONS OF KEYNESIAN ECONOMICS

Dermot Nolan

INTRODUCTION

This essay will be concerned with examining the set of models which are generally known as Keynesian, and evaluation of their choice-theoretic structure from a microeconomic viewpoint. It is not primarily concerned with assessing the intrinsic worth of such models, nor, indeed, will the actual worth and relevance of microeconomics itself be considered. The essay can be broadly split into two sections. The first section starts with a methodological discussion of the need to have well-specified and theoretically valid microfoundations for aggregate models, and in doing this will attempt to identify the fundamental basis behind microeconmics. I shall then briefly discuss general equilibrium theory, the "hard core"[1] of microeconomics; and will then move on to consider what exactly Keynesian economics is, and is it possible for it to have microfoundations. This section concludes with a discussion of the microfoundations problem with reference to the Post-Keynesians, such as Davidson, and possibly Shackle.

The second section opens with a very brief historical survey of some of the earlier attempts to root Keynesian economics within a microeconomic framework. I then move on to consider some more recent attempts to obtain Keynesian results using microeconomic foundations; Clower and Leijonhufuud are both considered and the school of predominantly French economists who developed fix-price theory. We will focus on the importance of money in Keynesian models, and on the question of whether Keynesian economics is a 'general' theory. I will finish by looking at some more recent, and perhaps less ambitious attempts to develop microfoundations. One further point before starting; this is essentially a survey essay and, as such, will not attempt to provide any new insights or develop new models. Any technical elements will be relegated to an appendix.

Section I:

The first task is to try and define what is meant by microfoundations. As I see it, the core of microeconomics is that its basis lies in choices made by individual traders. These traders are assumed as being rational and optimizing, by which it is meant that traders try and maximise their own welfare. This basis then leads to theorizing about exchange and production, in fact to all that constitutes microeconomics. I am not going to venture an opinion on whether it deals with these questions satisfactorily; there are obvious flaws, notably that it tends to concentrate too much on equilibrium positions. How does microeconomics link in with this? The common, rather vague, definition of macroeconomics given in textbooks is that it is concerned with economic aggregated e.g. output, unemployment, inflation etc. Thus macroecomonics deals with aggregated markets[2], but often it has dealt with them with methods totally different to that of microeconomics. I believe that this is a mistake and that if macroeconomics is to form part of a coherent discipline of economics, it should use the same basis as microeconomics i.e. the rational, optimizing individual.

If we accept the need for microfoundations, then what form should they take? Most writers have seen general equilibrium as the main connection between the two areas. General equilibrium, first conceived of by Leon Walras and given its present form first by Hicks and then Arrow and Debreu, can be conceived of as the 'hard core' of macroeconomics. This phrase is derived form Imre Lakatos' view of scientific progress and is meant to indicate that at the heart of any discipline there exist propositions, assumptions and beliefs that are taken as irrefutable by all members of the scientific community[3]. This, I should add, does not mean that economists believe general equilibrium models are descriptive of the real world, merely that it is the basis against which all other theories are judged. The specifics of the general equilibrium model are well known and I shall not discuss them here. I shall only note that it is essentially timeless; posits instantaneous price adjustment through the famous tatonnement process, and supposes complete certainty and perfect information on the behalf of all transactors. This last point means that a complete set of futures markets exists and thus the future does not prevent the existence of an equilibrium. To the commonly made (and true) point that the assumptions are unrealistic, I would reply that this is only natural, since they were designed as sufficiency conditions; thus the rules of the game were fixed to ensure an equilibrium outcome. Whether or not one agrees with the idea of general equilibrium, I think that it is inevitable that any attempt to root microeconomic foundations on macro models must use a general equilibrium framework, since it is so much of the heart of microeconomics.

The next task is to define what I mean by Keynesian, and to ask what are the essential insights of Keynesian economics. When using the words "Keynesian model" I mean a model which not only permits, but tends to generate a situation where markets fail to clear and there is less than full employment of resources. I do not intend to become involved in semantic discussion about the difference between Keynesian economics and the economics of Keynes. Such a distinction may be interesting but I do not believe it is particularly useful. The presumption in Keynesian models is that the market system will fail to clear due to co-ordination problems, and that if it did clear the economic situation would be ameliorated. In this I follow Hahn: "In a real sense Keynesian economics is about co-ordination failure which leads to outcomes which can be Pareto improved"[4]

Early Keynesian models tended to very ad hoc and to generate results without a firm theoretical basis. Due to the influence and power of the Keynesian school these faults tended to be overlooked. But if the arrival (or revival) of neo-classical models has done nothing else, it has at last forced Keynesians to examine their models closely and has made them search for new foundations.

Before concluding this section I wish to examine briefly the type of economics which has come to be known as Post-Keynesian. I feel the term "Fundamentalist Keynesians", as used by Coddington[5] is more useful here, and I wish to divide them into two groups, even though such a distinction is hardly all-encompassing.

(a) Writers such as Shackle, Davidson who emphasize uncertainty, massive dynamic shocks to the system etc. Much of their objection to microfoundations is based upon the idea that economic systems are inherently unstable and thus cannot be modelled adequately. With this approach it is not surprising that they have little use for microeconomics and its emphasis on equilibrium.

(b) The Neo-Ricardians; here I am thinking primarily of the Cambridge school and people such as Joan Robinson. Much of their work attacks marginal productivity analysis and asserts that there is a need for a return to macro theories of distribution. Here the emphasis is on class; the division between workers, capitalists and landowners is the basis of much of their theories. As such, they reject reductionist theories which seek to base economics on individual choices and, thus, they have little use for microfoundations.

In order to emphasise the huge gaps that exist between orthodox theorists and fundamentalist Keynesians I shall refer to the proceedings of a conference on the microfoundation of macroeconomics. Professor Davidson claims that the general equilibrium model could not resolve the "interesting macroeconomic question of money, inflation and unemployment"[6]. Professor Nell claims that "the distinction between micro and macro would have made no sense to the classical economists"[7] and calls for a theory which emphasized individual social class.

I should point out that these theories are useful, indeed pssibly more useful than orthodox economic theory. But I believe that they are not part of economics per se, as they employ a totally different framework. Thus if Keynesian ideas develop within the economic discipline, they must do so from a reductionist basis. This view-point is made by Hahn when in discussion of his work:"(1) I am a reductionist in that I attempt to locate explanation in the actions of individual agents.(2) In theorising about the agent I look for some axioms of rationality. (3) I hold that some notion of equilibrium is required and that the study of equilibrium states is useful."[8]

Section II

I shall start this section with a brief survey of early attempts to root Keynesian insights within a macroeconomic framework. The logical place to start is with Hicks and his classic text "Value and Capital" - Hicks was the first to introduce the notion of a fix-price market, where prices would not move to clear markets, though he did not indicate why this might happen. Perhaps his most important insight was the idea of temporary equilibrium, which allows expectation to enter into his model. Expectations are assumed given at the start of a Hicksian week and may not be changed until the start of the next week. With the absence of some futures market, this severely weakens the stability of a general equilibrium system, which provides a strong link to the ideas of Keynesian economics. Unfortunately Hicks' shown time period is highly arbitrary; and this, together with some mathematical problems with his models, meant that he had not solved the microfoundations problem.

Other attempts to link micro and macro were made by Oscar Lange and Laurence Klein, but I will pass these by and move to the work of Don Patinkin. Using the real balance effect, Patinkin proves that if all prices are flexible a Walrasian equilibrium will be reached. [9] However, if any one price is inflexible unemployment may exist. Given that prices tend to be inflexible the conclusion obviously was "that as a practical economist Keynes was undoubtedly correct in his diagnosis of disequilibrium and the need for integration in markets by governments to stimulate demand.'[10]

This conclusion however was not very satisfactory as it asumed price rigidity occured, but made no real attempt to explain why. This left classical reasons such as union restrictions, monopolies, etc. as the only reason for unemployment. To try and redeem Keynesian ideas, work was done on trying to explain price rigidity, and most of it focused on specifically non-tatonnement ideas, e.g. the Walrasian auctioneer who was presumed to instantly change prices, if needed, was abandoned.

The most important work was done by Robert Clower in his paper "The Keynesian Counter Revolution" by using his dual decision hypothesis. The theory of this will be developed in the appendix, but its essence is that if a consumer finds him/herself unable to sell as much labour as s/he wishes, his/her demand for goods will be smaller than it would otherwise have been. This distinction between notional and effective demand for goods ensures that since prices move only in response to effective demands, a situation can exist where excess supply can appear on one market, but there will be no excess demand to counteract this in another market. This provides an explaination for price rigidity in the face of unemployment.

The problem is obviously due to consumers being unable to provide information to producers, that they would buy more if they could work more. Clower and other writers initially tended to blame this information problem on the fact that trades were usually conducted in monetary terms. This prompted Clower to write another paper "The Microfoundations of Monetary Theory" in which he emphasized this point and made the now infamous dictum 'money buys goods, and goods buy money, but goods do not buy goods'. Taken to its logical conclusion this seemed to imply that there would be no umployment in a barter economy, an idea plainly ridiculous. This idea about the unique importance of money has been firmly rejected by Hahn, who pointed out that any non-reductible asset that people buy, such as land and Old Masters, is enough to upset Say's law. Money is important in Keynesian economics, but simply blaming all unemployment on it is not the answer. As Drazen has pointed out, Clower probably wishes he never wrote that paper.[11]

The dual-decision hypothesis is at the centre of his work and it does have a considerable power. Hwever in terms of its choice-theoretic structure it is highly unsatisfactory. The constraint introduced does not allow for any cash balances and, as such, falls into the realm of ad hoc economics. If one accepts the dual-decision hypothesis, then an individual unable to obtain a job would demand nothing; this is surely incorrect as a model of individual behaviour. Clower is also extremely vague abput whether the end-position is an equilibrium or not; I think it would be unreasonable to suppose that information would not travel eventually to start the market moving towards equilibrium. Clower's work spawned a variety of other models; the most well known set being that which constitute fix-price theory. (He subsequently 'disowned' fix-price theory).[12] Fix-price theorists, many of whom are French, assume that prices are fixed in the short run (a la Hicks) and therefore it is highly unlikely that the economy will be in a Walrasian equilibrium position. Given these fixed prices, agents are likely to face constraints in any particular market and to be rationed in the quantity which they wish to buy or sell e.g. if prices are below equilibrium values on the goods market then consumers will be rationed on the quantity of goods they can buy. This is based upon the idea that the short side of the market is dominant and that no agent can be forced to buy more that s/he wishes to at the prevailing price; a not unreasonable assumption.

The microeconomic structure of fix-price models can be split into two main groups. The first, owing its origin to J.P.Benassy, sees a consumer looking at one of N markets and percieving N-1 constraints in the other markets, but ignoring any constraints s/he thinks may exist in the Nth market. Given this, s/he then makes his/her offer in this Nth market, and then moves on to the next market and repeats the process. This scheme allows the consumer to violate constraints in a market when s/he makes the offer in that market, and thus the scheme does allow for a theory of excess demand. Under some fairly standard assumptions an equilibrium, with less than full employment, can be proved to exist. The problem with this theory is that it does not appear to have a very rational way for an agent to behave. The consumer goes from market to market and forgets everything s/he has done in the previous market. Thus the Benassy scheme is not a very convincing theory of consumer choice.

The other main theory, formulated by Dreze, is preferable in the sense that the consumer is behaving perfectly rationally. Here the consumer receives a market signal telling him/her of the constraints in all markets and s/he formulates his/her demands and supplies accordingly. Again, an equilibrium can be proved to exist at these fixed prices. However, this scheme has problems also, as no agent is allowed to violate their constraints. This means that there is no excess demand on any market, which hardly corrosponds to a realistic portrayal of a market with rationing. Another problem is that there is no exchange of information in the process, which there really should be.

What of the contributions of fix-price theory in a wider sense? It has helped Keynesian economics in that rigorous modelling is employed for perhaps the first time, and there is an attempt, however unsatisfactory, to provide microfoundations to their models. There are some problems with describing them as Keynesian, as monetary policy works equally as well as fiscal policy in attempting to restore the economy to full employment level. The real problem with fix-price theory is that there is no justification for assuming prices to be fixed. Admittedly, they are only presumed fixed in the short run but, again, there is no comment on how short the short run actually is. This leads to a further problem in that their notion of equilibrium is highly dubious. Do the models imply that prices are actually fixed and that the equilibrium is a genuine state of rest or is there the implication that prices are moving but very,very slowly so that the whole process is really a disequilibrium process, and not an equilibrium at all? In fairness to fix-price theorists, it must be said that much of this is due to technical problems. We will return to this point later.

We have seen that Keynesian economics has run into considerable problems, notably in its inability to posit a reasonable price-adjustment mechanism. I personally believe that the vital question which has not yet been answered is how to accurately model the information and uncertainty problems which are at the centre of the Keynesian idea. Much of this failure is due to the obsession with attempting to provide a more 'general' theory, which encompasses the classical theory. This has meant that writers insist that the Keynesian model must include the limiting (and patently unrealistic) case of perfect competition, and this is definitionally impossible. For one of the assumptions of the perfectly competitive system is that every agent is perfectly informed. But this is the very shortcoming of mardet systems that Keynesian economics is based upon. Axel Leijonjufuud's famous thesis is a good example of this. In chapter 2 he announces that Keynes' theory is a 'general' theory; he bases this upon Keynes reversing the speed of price and quantity adjustments which Marshall had taught. At first he literally pulls this assertion out of nowhere, but later he defends it by using job-search theory as formulated by Alchian. This is a useful framework for analysis but since it is based upon a theory of incomplete information it cannot be instantly construed as a general theory.

If Keynesian economics is to have a future, then I agree it must deal with a specifically non-tatonnement situation where the auctioneer is not present. This means that some form of price-setting behaviour by firms must be explicitly used in models. To briefly give some examples, Negishi postulates fixed prices due to firms perceiving a kinked demand curve. Many of the French economists, such as Grandmont and Laroque, have given up fix-price theory and are using models with imperfectly competitive firms. Even with flexible prices, non-Walrasian situations may occur due to uncertainty about future interest rates; this is one of the main messages of Grandmont's book "Money and Value". I am not claiming that these models are perfect or constitute the full message of Keynesian economics. I do think that they are 'the way forward' , so to speak, and that, at first, Keynesian economists will have to be content with less ambitious goals than providing and instant 'general theory'.

Before concluding, I wish to discuss some of the technical problems with Keynesian models. I think that ultimately, full price rigidity may have to be abandoned and thus there will be a need for a reasonable price adjustment equation. Unfortunately this will be very difficult to theoretically justify and is likely to create many technical problems in already complicated models. Indeed the technical difficulties associated with modelling Keynesian systems are, I believe, responsible for much of the downfall in Keynesian economics in the past decade or so. In support of this, I would like to quote Thomas Sargent, one of the foremost of the non-classical economists (and in my opinion, one of the few who is not ideologically motivated):"one reason in favour of the equilibrium models is that it solves lots of technical problems." [13]

Despite this I believe that purely because of technical problems Keynesian economics should not be abandoned. I think that market failure is a major problem that cannot be just ignored, and thus for economics to be a useful discipline it will always need to be able to explain, and hopefully correct, market failure.

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BOOK REVIEW

Aebhric Mc Gibney.

"The Performing Arts and the Public Purse-an Economic Analysis"
Professor John O'Hagan
Christopher Duffy.

This timely Report ,commisioned by The Arts Council,provides an objective economic framework for discussing the much neglected policy area of whether the government should intervene in the financing the performing arts via public funding.

It may be asked why economics should concern itself with a topic that would seem to have little relation with the allocation of real tangible goods.Indeed the book begins with a warning from Galbraith that "art has nothing to do with the sterner preoccupations of the economist".This attitude could be a legacy of the classical economic viewpoint as expressed by Adam Smith that the arts were the ultimate in unproductive luxury expenditure,disappearing at the moment of performance.Economics has finally come around to the view that just because a good is intangible doesn't mean it is not worth while and with this has come a change in the attitude to the arts as epitomised by the subsequent conversion of Galbraith.Evens the economics guru Keynes himself was first chairman of the Arts Council of Great Britain which may add further legitimacy to the study.

A possible limitation of the analysis that is clearly stated at the outset is that only the live ,labour intensive,classical performing arts are considered such as ballet,orchestral concerts and theatre.The reason given is that to include the arts as a whole would have raised too many questions and issues to be adequately discussed in the short space provided.Clearly it is better to deal with one area well than to provide a scanty treatment of the whole spectrum.

The Report is divided into three parts.

Part One considers the general issue of public funding for the performing arts- arguing that because the collective social benefits far outweigh the private benefits to individual consumers the amount of this public good that is provided may be way below the optimum level.Among such collective benefits listed are a distinctive national culture and a rise in tourism;there are others require deeper breaths to swallow.Other reasons given for public funding are possible distortions in the market and the question of equal access ,which is developed later.Also considered in Part One is what form the public funding might take either directly,indirectly or through other government budgets such as an employment scheme.Such a plan was implemented in the U.S. in the 1930s to get the dole queues down and it might be well for Ireland to consider such a scheme in the present economic climate.An interesting side issue is the question of funding through the National Lottery and the danger that such income might be included as part of the total funding of the Arts as opposed to additional revenue.

Part Two looks at the main direct source of public funding,the Arts Council itself.It critically examines the aims of the Council and looks at the issues of what level and what distribution of funding is best.This part concludes by looking at the main item of expenditure by the Arts Council,the theatre.

Part Three continues the specific appliction of the general issues raised in Part One looking at the policy areas of Equal Access,Arts Festivals and Community Arts.Of most interest is the question of equal access in terms of socio-economic and geographical equality.Also there may be a need to change present individual prferences by educating people as to what they are missing.Using what data is available the authors show that the one link the Irish have across all barriers of integration is traditional Irish music which is enjoyed as much by the urban working class and the farmer.

The Report is written in a clear progressive format following the traditional essay style of "say what you are going to do,do it,and say what you have said".However despite the intention to appeal to a wider audience than economists alone it is inevitable that certian economic jargon and concepts arise which may make some chapters more accessible than others.Nonetheless each point discussed is explained in as clear and as logical a manner ,with examples,as I believe could be possible.This is a commendable achievement on the part of the authors as the most difficult test of understanding is in the teaching or explaining of knowledge to others.Although no definite conclusions on these "matters that are ultimately issues of values and political judgement" the aim of the Report is clearly achieved in that a framework is provided for considering the funding of the Performing Arts from a public funding viewpoint.Now that this framework is in place the way is open for further research in this important area.