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PANEL RESPONSE: GROWTH POLICY

Honohan and the Comparative Perspective

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I INTRODUCTION

It is highly appropriate to have an economic historian such as myself participating in a celebration of Patrick Honohan's life and work. To most observers Patrick is a macroeconomist, financial economist, and central banker, and of course he has been all of those things in his time and an outstanding one to boot. But Honohan's career is also deeply enmeshed with economic history. First, he has helped to make it, both when acting as advisor to Garrett FitzGerald in the 1980s, and in his role as Central Bank Governor during those very dark years that now (in part thanks to him) seem so long ago. Second, during the 2000s he wrote the first draft of the economic history of our crisis, in several frequently cited papers and reports that will be a key source for future historians (Honohan, 2009a; 2009b; 2010). And third, he has made fundamental contributions to Irish economic history (Honohan and Ó Gráda, 1998; Honohan and Walsh, 2002; FitzGerald and Honohan, 2023). This reflects a genuine interest in the past, which manifested itself *inter alia* during the regular cliometric workshops held at the Central Bank during his tenure there. Patrick has been an active and valued participant in many economic history meetings over the years, and economic historians are proud to have him as an honorary member of our tribe.

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One feature of Patrick's work to which I want to draw attention is its comparative nature. There are two ways to present any country's economic history, including that of our own. The first would start by describing the policies of the generally liberal but austere Cumann na nGaedheal, contrast this with the protectionist governments of de Valera and Lemass, go on to the opening under Lemass and Whittaker, note with regret the fiscal excesses of the 1970s, celebrate Ray McSharry and the advent of the Celtic Tiger, shudder at the failures that led to our crash, and breathe a sigh of relief at the stabilisation that followed under Kenny and Honohan. No doubt there is something to be said for such an approach, but we were not alone in closing in the 1930s, opening in the late 1950s, experiencing turmoil in the 1970s and 1980s, crashing in 2008, and recovering slowly thereafter. Perhaps the Irish experience is part of a bigger story, and perhaps we can only really understand it by comparing Ireland with other countries. This is my preferred approach, and so in this note I will mostly argue that Ireland is not so different, before acknowledging that (like any country) it is also different in interesting and important ways.

II IRELAND IS NOT SO DIFFERENT

One of Patrick's most useful recent contributions is a bracing response to hyperbolic and exceptionalist takes on the Irish economy (Honohan, 2021). Ireland is not in fact the most prosperous country in Europe – it ranks somewhere between 8th and 10th in the EU, making us a rather ordinary part of an admittedly very rich continent. (The fact that commentators sometimes get this wrong is of course a reflection of some very odd features of our economy and their implications for our economic statistics.) And if we have ended up with rather run-of-the-mill European living standards, the causes of the growth that led there were also quite typical. As Honohan and Walsh (2002) point out, our growth was based on convergence on the richer countries of the day, as were all the European post-war growth miracles (Crafts and Toniolo, 1996; Eichengreen, 2007).[1]

So far, so typical, as were several details associated with the Irish convergence experience, notably the role of education and the transition from traditional agriculture to modern industry and services (Temin, 2002). As Honohan and Walsh (2002) put it (p. 4), "At one level, therefore, Ireland's achievement does not seem all that special." The wage moderation stressed in their account has its counterpart too in the corporatist structures that limited wage increases in post-war continental Europe (Eichengreen, 2007).

[1] Such a convergence perspective is inherently comparative – Irish growth depends not only on whatever may be happening inside the country, but on the relationship between the Irish economy and economies elsewhere.

The challenge, as they point out, is to explain why Ireland's convergence only took place in the 1990s, whereas in continental Europe it occurred during the 1950s and 1960s. Was this due to an unusually dysfunctional policy environment? Again, I would argue that for long periods of Irish history its economic policymaking was, while certainly not optimal, very typical of the time (O'Rourke, 2017; Ó Gráda and O'Rourke, 2022). During the 1930s our tariffs were average by the standards of the period, and our quotas were lower than average. We were slow to liberalise during the 1950s, but so were our natural comparators, the other European peripherals (Greece, Italy, Portugal and Spain). Spain's autarkic regime lasted until 1959, when it joined the OEEC and started to liberalise; Portugal became a founder member of EFTA in 1960 but retained protection for many of its most important imports; Finland started liberalising in 1957 and reached an agreement with EFTA in 1962; and Greece negotiated an Agreement of Association with the EEC that came into force in 1962. Ireland applied to join the EEC in 1961, although the application was unsuccessful. In all these cases governments were motivated by a recognition that existing trade policies could no longer continue as before, in a European environment that had been transformed by the Treaty of Rome.

Irish trade liberalisation did start to lag behind during the 1960s, and – crucially – such liberalisation as we did undertake then was vis-à-vis the United Kingdom, then the sick man of Europe. This could hardly have had the same growth impact as deeper integration with continental Europe. The other peripherals liberalised more broadly, and their growth rates accelerated in response. But it would be harsh to blame the Irish government for de Gaulle's veto in 1963 of the British application to join the EEC. That decision delayed our accession by a decade, which helps explain why Ireland's growth performance was so disappointing in a convergence perspective during the 1960s: as FitzGerald and Honohan (2023) argue, membership of the European Common Market, and later its Single Market, were transformative in their impact on the Irish economy.

III IRELAND IS DIFFERENT

As Honohan (2021) and others have highlighted, Irish economic statistics are highly unusual, due to the role played by multinationals in our economy. The same could be said for our tax base, and both these issues are the subject of considerable policy and academic debate today. What about the past? If much of our post-war economic history can be said to be typical, the timing of our convergence on the leaders was not. Aside from the delayed Irish integration with the European mainland noted earlier, what other factors might explain this costly difference?

One of the reasons for poor Irish economic performance in the 1950s and early 1960s was a series of macroeconomic crises associated with balance of payments difficulties. The most notable of these was the macroeconomic crisis of 1955-1956, which Honohan and Ó Gráda (1998, p. 52) describe as the “defining event of post-war economic history”. On the one hand, Ireland was hardly the only country during the Bretton Woods era to experience the macroeconomic consequences of “stop-go” policies: these were also very evident in post-war Britain, for example. It is also true that the Irish and UK economies were highly inter-linked during this period. But on the other hand it is also true that misguided monetary policy played a major role in the 1955-1956 crisis, as Honohan and Ó Gráda show, and that UK macroeconomic shocks had a bigger impact on Ireland’s CPI than on its GDP (Stuart, 2019).

Strikingly, as Honohan and Walsh (2002) point out, the fact that Ireland’s growth miracle post-dated accession to the European Communities by some two decades can also be explained by macroeconomic factors. Ireland was indeed not alone in facing severe macroeconomic challenges in the 1970s, but severe fiscal policy errors magnified the impact of the disinflation that followed in the early 1980s. In a striking passage, Honohan and Walsh (p. 7) comment that:

> *The whole period since 1973 thus appears as a long business cycle, with a deep and prolonged trough in the first half of the 1980s and a climacteric around end-century, superimposed on a secular transition in the population structure and in the patterns of labor force participation and employment.*

It thus seems that the quality of Irish macroeconomic policymaking was poor at several key stages of our post-war economic history, and that this can help to explain our delayed convergence. And domestic policymaking was also poor in the early 2000s. Was it necessarily worse than elsewhere? I have not seen comparative metrics of the quality of historical policymaking that would allow us to answer such a question. But if the Irish economy has responded to global shocks in a highly exaggerated fashion, then that is surely down in large part to domestic macroeconomic and financial policy errors. So while it is important to take account of the wider picture, purely domestic factors also mattered.

IV CONCLUDING COMMENTS

Let me conclude with a question and a comment.

The question is whether some of the mistakes of the early 2000s might have been avoided had policymakers taken on board the logic of the convergence process stressed by Honohan and Walsh (2002). Convergence is self-limiting: once you have caught up, and are rich, you can no longer catch up, and growth will slow sharply. This is what the experiences of other countries will tell you, and it would be foolish to assume that your country will be any different. But policymakers in the early 2000s had become used to very high growth rates and did what they could to maintain them. And perhaps the rest of society was less concerned than it should have been by the unsustainable nature of the growth after 2000 because it too regarded it as natural, failing to distinguish between the convergence of the 1990s and the bubble of the 2000s (Honohan, 2009a).

The comment is that when Honohan explains Irish phases of growth with reference to macroeconomic policy mistakes, he is putting back together again the short run and the long run that were sundered by Solow in 1956. Maybe economists should do that more often.

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