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You may like to see the attached paper about the economies of Northern Ireland and the Irish Republic. It was prepared within the Treasury at my request - largely to satisfy curiosity which had been aroused by conversations with my Irish opposite number at recent EEC meetings. Humphrey Atkins' people have kindly checked the facts. The paper leads to no particular conclusions, but as background is not without some interest.

2. I am copying this minute to Peter Carrington and Humphrey Atkins.

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G.H.

7 September 1981

The economies of Northern Ireland and Eire

1. In economic terms Northern Ireland and Eire have much in common: they are small economies, highly dependent on international trade; they are both poor by European standards; they both suffer from high unemployment and a tendency to net outward migration most of the time; and they both benefit from income transfers from their richer neighbours. This note documents these features of the two economies and considers their relevance to alternative political 'solutions' to the Irish problem.

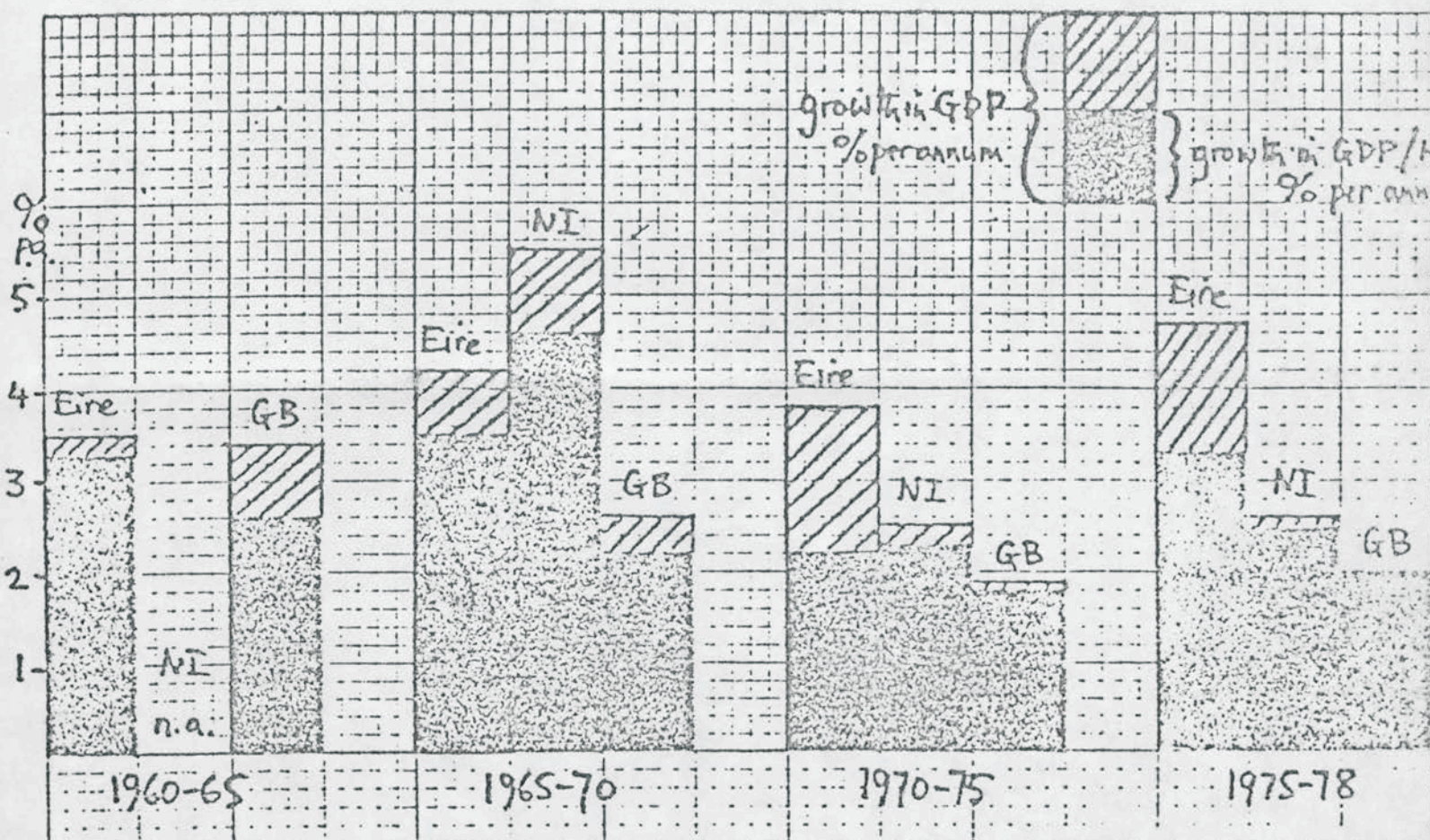
2. The small size and comparative poverty of Ireland can be seen from the following figures -

Population, Output and Personal Incomes in NI, Eire and the UK in 1978

	Population	GDP at factor cost	Personal Income	GDP p.head	Personal Income p.head
	m	£m	£m	£	£
N.I.	1.5	2998	3131	1948	2034
Eire	3.3	5788	6022	1748	1819
U.K.	55.9	144442	142093	2587	2545

A comparison of GDP per head in the EC shows that only parts of Italy are poorer than Ireland and that the richest region, Hamburg, is three times better off.

3. As the following chart shows, GDP has grown faster in both parts of Ireland than in GB since the mid 1960s. The growth rate in the South was faster than in the North throughout the 1970s, a result being that GDP per employee is now higher in Eire than in NI. Eire's dependent population is, however, proportionately higher than that of NI. The outcome is that GDP per head of population remains higher in NI than in Eire, despite the rapid growth of the Republic's economy in recent years.

Growth in GDP and GDP per head, 1960-1978

4. In both parts of Ireland unemployment is high, the most recent figures being 17% in NI and 13% in Eire. One result of the failure of the two economies to provide a sufficient number of jobs for a rapidly growing population has been net emigration from Ireland. However, the 1970s saw a change in the pattern, since Eire gained rather than lost population.

Net migration per 1000 population

	<u>Eire</u>	<u>N.I.</u>
1951-61	-14.2	- 6.6
1961-66	- 5.7	- 5.2
1966-71	- 3.7	- 4.6
1971-79	+ 2.9	- 5.7

The causes of the turn-around may have included the success of policies to attract new industry, the reduced 'pull' from GB, and an improvement in the level of social security benefits (expenditure on 'social security and welfare' increased from 8.8% of personal incomes in 1971 to 10.7% in 1978, and Eire's aim is said to be eventually to match the level of benefits in the UK). Net emigration has continued from NI.

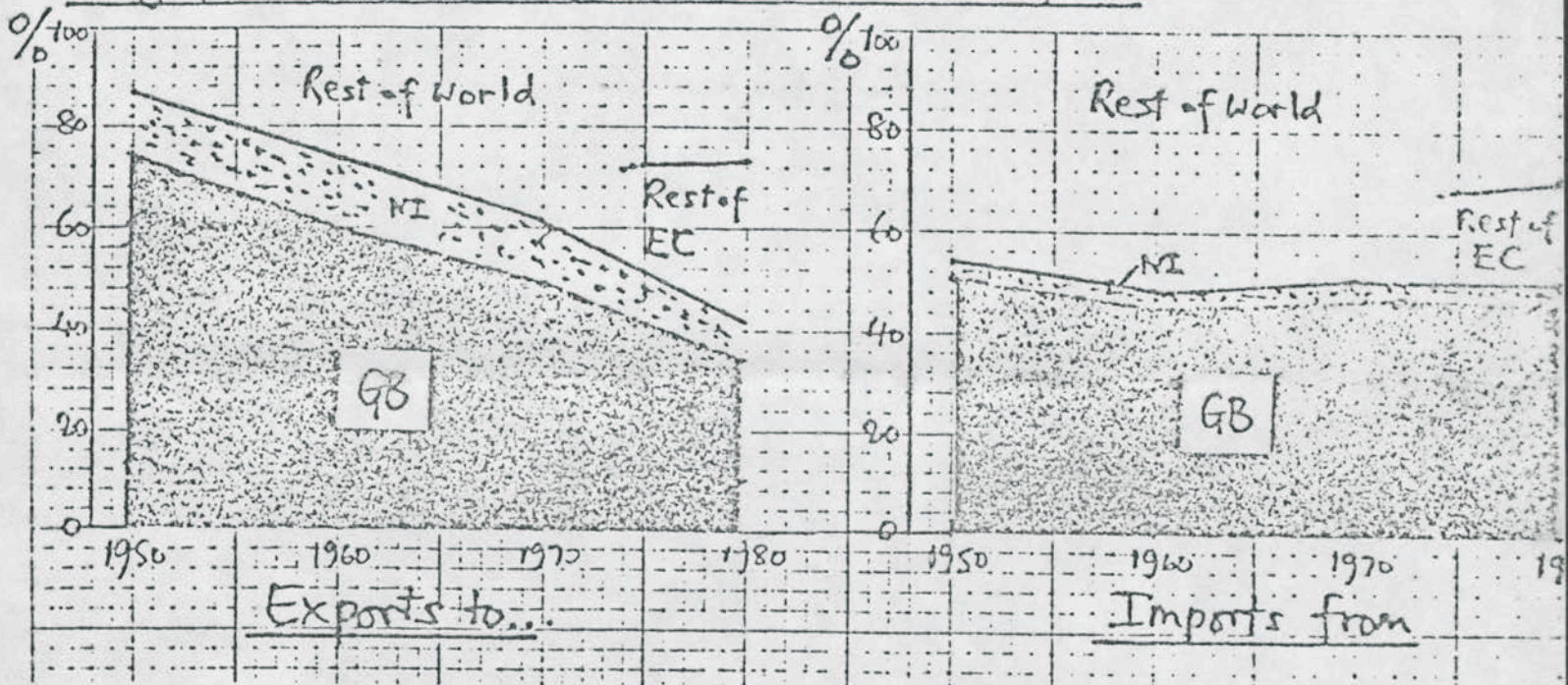
5. The industrial structures of the two economies have been becoming increasingly similar (see the table at the back showing the distribution of employment among broadly defined sectors). Agriculture's share of total employment has been falling faster in Eire than in NI but it is still double that of NI (22% as compared with 10%). Manufacturing accounts for some 20 to 25% of employment in both North and South; but the most vulnerable sectors, namely textiles, clothing and footwear, shipbuilding and other vehicle production account for 47% of manufacturing employment in the North as compared with 23% in the South. The services sector has a slightly bigger share of employment in NI than in Eire.

6. An academic assessment of the effectiveness of Irish industrial policy has concluded that it has made a very substantial contribution to net job creation in manufacturing, amounting to about a quarter of total manufacturing employment in NI, and just over one-third in Eire during the period 1960 to 1974. One result of this success has been that manufacturing output has grown very rapidly in Eire; it is now about three times higher than in 1962. The increase in NI has been much less impressive because the new industries were needed to offset the declining output of the old. Indeed in the 1970s the NI index of manufacturing output rose by only 4%. The current recession has hit manufacturing output and employment much harder in NI than in Eire. Between June 1979 and December 1980 manufacturing employment fell by 2.1% in Eire and by 14.8% in NI.

7. Both NI and Eire are very open economies, NI more so than Eire. Exports are equal to some 90% of GDP in NI and some 50% of GDP in Eire. Imports are similarly large. NI depends heavily on GB both for imports and exports: in 1974 82% of exports went to GB and 75% of imports came from there (the figures somewhat exaggerate the position since they include goods exported to and imported from third countries via GB).

8. Though Eire is still closely linked to the British economy as the chart below shows, it has been reducing its dependence on export sales to GB. A number of factors are responsible for the loosening of these ties - the broadening of the country's industrial base and the rundown of agriculture (which in 1955 accounted for 74% of exports, compared with 30% to-day); entry into the EEC; and now the break with sterling.

Geographical distribution of Eire's Exports and Imports



9. The two Irish economies are not particularly closely linked to one another. Eire sends 7% of her exports to NI and obtains 4% of her imports from NI. The most important

trade links between North and South involve the exchange of agricultural products and livestock.

10. The level of UK Exchequer support for NI is considerable: in 1981/82 it will be well over £1 bn. The main elements are a £785m transfer to the NI Consolidated Fund, £325m to pay for law and order and an, as yet unknown, transfer from the GB National Insurance Fund (worth £74m in 1979/80). The benefits to the Province from the CAP are not separately distinguished, but NI farmers received direct grants and subsidies from MAFF worth £40 m in 1979-80. In addition, the cost of maintaining the troops in NI is estimated to be £100m, and the Lord Chancellor's Department incurs expenditure on court services.

11. All in all, the transfers which the rest of the UK is making to NI are currently worth about one-quarter of personal incomes in NI. This is not to say that incomes would fall by a quarter without them - some of the benefits are passed to the consumers of NI products in the form of lower prices, some to "foreign" firms operating in NI in the form of higher profits; other parts of the transfer buy services which NI may not need indefinitely, most notably the present level of expenditure on law and order. Nevertheless, there can be no doubt that the UK subvention has enabled NI to achieve a level of income significantly above that which it could maintain on its own and retain resources which otherwise would have relocated in regions of greater economic opportunity. It has also supported a high and growing level of public sector employment: in 1974 the public sector provided 30% of all jobs in NI; by 1979 this figure had risen to 35% (the equivalent figures for the UK as a whole are 27% and 29%).

12. The South too relies on income transfers from "overseas", particularly from the EC. It has been estimated that Eire's benefit from the CAP amounted to some £600m in 1980. In addition there were receipts of some £100m in 1979 in respect of industrial development.

Political 'Solutions'

13. Three political 'solutions' with variants have been canvassed from time to time, namely (i) independence for NI, (ii) some form of union between North and South, and (iii) closer co-operation between North and South within the existing political framework. The first point to make about these is that, although any of them would be beneficial in economic terms if it led to a restoration of peace and a more settled environment in which business could be carried on, none of them would 'solve' the economic problems of low income and high unemployment. Indeed if they caused an interruption or scaling down of fiscal transfers to Ireland they could exacerbate the Island's economic problems.

(i) Independence for NI

14. So long as NI relies as heavily as it does on the GB economy both as a source of raw materials and as an outlet for its final products, it is hard to see how it could be in any worthwhile sense independent in economic terms. In particular it could not gain by devaluing the NI pound against the pound sterling; and it would be bound to experience the same cyclical fluctuations as GB. Moreover if independence meant forgoing the fiscal transfers which NI at present receives from the UK, it would have a high cost in terms of national income. In sum, economic independence looks to be a non-starter.

(ii) Some form of political union between North and South

15. The economic and monetary unification of North and South would raise all the problems which have so far prevented the economic and monetary unification of the EC as a whole. In particular, the necessary harmonisation of tax structures and rates and the alignment of social security payments, would cause considerable difficulty. Harmonisation could not take the form of a levelling up of social security payments and a levelling down of taxes if the

budget balance were to remain undisturbed. Thus there would be difficult compromises to be reached and considerable upheaval.

16. The problems of harmonisation alone would take time to resolve. In addition there would be currency changes to consider and ^{most important of all,} the future of the income transfers to N.I. which are currently being made by GB. Enthusiasts for economic and monetary unification would say that none of the problems which would arise is insoluble. But they could scarcely deny that the preparatory work to be done is very considerable and that a smooth and orderly transition would take a number of years. At least for the immediate future, by far the most promising 'solution' is the third one, closer co-operation. This could be a step on the way to eventual economic and monetary unification; or it could be the framework for a long-term preservation of the political status quo.

(iii) Closer Co-operation

17. The joint planning of roads, electricity supplies and other physical links could obviously be beneficial to both sides; and with the return of more settled conditions there would presumably be a backlog of such projects to be carried out (the border areas having been particularly unsettled). The joint promotion of tourism is an obvious example of another form of co-operation which would be easier if tensions were less. More generally the case for closer co-operation is to take advantage of economies of scale in an island too small to justify the separate development of North and South.

18. Although EC membership may have generated some cross-border traffic in agricultural produce to take advantage of differences in green exchange rates, the graphs on page 4 of this note do not suggest that membership has caused trade between North and South to grow particularly fast. The fact is that the economy of N.I., like that of the other regions of this country, is oriented over-whelmingly towards the rest of the UK, whereas, as the first graph on page 4

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shows, Eire has been steadily diversifying its trade away from the UK ever since World War II. It is entirely possible that unsettled conditions may have delayed an adjustment to EC membership which will come about once normality has been restored.

19. In economic terms the Government's role is to ensure that the natural forces making for closer co-operation between North and South are allowed to run their course. Beyond that, the big question concerns the future of the present Exchequer contributions to NI. Whether NI should be aided indefinitely to the present extent raises broad issues going beyond the scope of this note. It is, however, relevant that the NI economy is adjusted to the present level of subvention and that there would be considerable difficulty in scaling down this level quickly.

18 August 1981

(percentages)

DISTRIBUTION OF EMPLOYMENT AMONG SECTORS

	<u>Eire</u>		<u>NI</u>	
	1968	1978	1968	1978
Agriculture	29	22	12	10
Mining	1	1	1	-
Manufacturing	19	20	31	24
Food, drink, tobacco	5	5	5	4
Chemicals and allied ind.	1	1	1	-
Engineering and metal ind.	2	3	6	4
Shipbuilding	-	-	2	2
Vehicles	1	1	2	2
Textiles	2	1	8	5
Clothing	3	2	4	3
Timber and furniture	1	1	1	1
Paper, printing, publishing	2	2	1	1
Bricks, pottery, cement	1	1	1	1
Miscellaneous	1	2	1	1
Construction	7	8	10	8
Gas, electricity, water	1	1	2	2
Services	38	41	39	46
Public Administration	4	6	6	9
<u>Total</u>	100	100	100	100