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Seán Ó Riain
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1 *Liberalism in crisis*

Ireland and the Great Recession: liberalism's crisis or liberalism betrayed?

In early 2013, as I completed this manuscript, the Great Recession was in its fifth year. The shock of the acute crisis of 2008 had given way to the recognition of the chronic, long-term character of the recession. The outrage of the early months of the crisis had turned into a deeper erosion of trust and legitimacy of private and public institutions, often accompanied by despair that either public or private institutions could deliver economic recovery, let alone reconstruction.

Europe was at the heart of the crisis, even if its economy as a whole was performing at least as well as others that were struggling to respond to the recession around the world. However, Europe's problems went deeper than specifically economic woes to the foundations of its socio-economic system, as the euro currency hung in the balance and the European project fractured in the face of economic crisis and political division. In the midst of this broader regional crisis, Ireland was one of the countries at the very centre of the economic storm. Not long before celebrated as the 'Celtic Tiger', Ireland was now experiencing one of the deepest and most sustained crises in Europe and beyond. After almost five years of recession and austerity, the Irish economy remained mired in an economic slump, with only fleeting glimpses of economic growth, burdened by banking and government debt and facing serious questions of solvency and sovereignty. Behind the public face of its status as the 'poster child' of austerity in Europe, Ireland was poised on a knife-edge between potentially unsustainable debt and the growing social and political costs of recession and fiscal consolidation.

In the five years of the Great Recession, Ireland had staggered from one historically memorable event to another, with each tumultuous occasion quickly passed over as new events took centre stage. The Irish

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state guaranteed the liabilities of its most significant domestic financial institutions in September 2008, in the face of a collapse in those institutions' liquidity and solvency and to the tune of over double the value of gross domestic product (GDP). In the following year, Irish citizens took on these private debts as their responsibility, with the costs of the banking bailout reaching at least €64 billion over the course of the recession. GDP collapsed with the bursting of the property bubble and as measures to cut the public deficit began to bite. Nonetheless, the Irish electorate approved the Lisbon Treaty promoting further European integration in October 2009, despite a sharp loss of trust in the previously popular EU and having rejected it just over a year before.

Almost uniquely among EU states, Ireland pursued a policy response that was focused almost exclusively on fiscal consolidation, particularly through expenditure cuts. This resolute commitment to 'austerity' was not enough to reassure financial markets, however, as uncertainty around the future of the euro and Irish banking debt saw interest rates on state borrowing rise sharply in 2010. Ireland entered a bailout programme in November 2010, involving detailed oversight of fiscal measures by the 'troika' of the European Union (EU), the International Monetary Fund (IMF) and European Central Bank (ECB) funders.

Ireland's electorate took their revenge on the parties that had presided over the bubble and the recession in March 2011, decimating the historically dominant Fianna Fáil party and returning a new coalition government of Fine Gael and Labour (the Christian Democratic and Social Democratic Parties, respectively). Once more in May 2012, Ireland faced a referendum on signing the fiscal treaty that brought together all these dilemmas of crisis, austerity and Europeanisation into a single vote on legally binding measures to control the public finances. Once more, despite the erosion of faith in the European and domestic elites, the electorate comfortably passed the Fiscal Treaty – with both Yes and No voters driven primarily by fear of the future rather than by positive agendas for recovery.

The Irish public deficit came down in 2011 and 2012 even as the economy stagnated and the social costs and political tensions grew. Despite some indicators of stabilisation and perhaps even growth in the economy, it was clear that many years of high unemployment lay ahead. With at least two years of significant cuts in public spending still to come, political difficulties remained. The growth in the number of home-owners with significant mortgage arrears prompted policies to

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allow for debt restructuring, but also offered the prospect of politically explosive home repossessions. A negotiated agreement with public sector unions to cut wages and change a variety of other payments and conditions faced great difficulty in getting union member approval. All the while, the EU was still capable of shooting itself in the foot as a proposal in March 2013 to impose part of Cyprus' bailout costs on ordinary depositors threatened for a time to fatally damage the prospects of a European banking union.

Much of the popular narrative of the Great Recession has focused on the frailties of national systems of economic management, or mismanagement. In particular, countries like Ireland suffered from major failures of regulation in the financial and property sectors, in developing the real economy and in the public finances. However, the Irish experience was only one of a number of similar stories that had unfolded across the European periphery over the previous five years. The various national economic stories combined into a European crisis. While the economies of Europe foundered in different ways, the politics of adjustment after the crisis – including the 'fiscal compact' of late 2011 and the European Stability Mechanism Treaty of February 2012 – fundamentally re-ordered European political relations. The question of the unequal development of the EU's regions and of relations between core and periphery had long been a sideshow in European politics – it now took centre stage.

Even more fundamentally, the European and international crises raised profound questions regarding the international financial system, the European and international economic orders, and the place of national governments and new forms of governance in shaping the political economy. Coming at the end of at least three decades of financialisation, Europeanisation and worldwide experiments in economic governance, the crisis cast a dim light on all these developments, placing economic liberalism profoundly in question. However, an economic crisis that seemed to signal the exhaustion of a period of aggressive international economic liberalisation has paradoxically reinforced liberal policy prescriptions.

This book explores these broader questions of liberalism, development and crisis through an analysis of the changing fortunes of the Irish economy, a poster child since the 1990s but one of the first to hit the rocks in 2008. Having spent many decades in the years after independence in 1922 as one of the laggards of the European economy,

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to everyone's surprise, Ireland became a model for economic growth and regional development in the 1990s. An economic crisis in the 1980s saw massive government debt accompanied by severe unemployment, immigration and weak labour force participation among women. Nonetheless, in the 1990s Ireland experienced rapid economic growth and, even more significantly, exceptionally high employment growth in the second half of the decade. The numbers employed in Ireland almost doubled between 1988 and 2008, increasing by one million jobs. The sources of this growth are of course controversial, with some seeing it as the outcome of Ireland finally 'converging' on European living standards through free market reforms, while others dismiss the gains of the period as unsustainable and rooted in a bubble inflated by liberal policies. Ireland's crisis since 2008 was sudden and severe, and appeared to bear out the argument of these critics. However, in the eyes of those who had seen the 'Celtic Tiger' years of the 1990s as a process of economic convergence, it was not continuity with those liberal policies that produced the crash but the departure from those policies in the 2000s through lack of discipline in public finances and weak prudential regulation in the financial sector.

This book shares the view that the Irish economy significantly shifted in its underlying dynamic between the 1990s and the 2000s. However, I argue that the growth of the 1990s was not due to a convergence on market-led orthodoxy, but to a partial move toward a European-style combination of industrial policy, social investment and social partnership. In the 2000s this dynamic was derailed by the financialisation of the economy, which was facilitated by economic and monetary union and financial liberalisation in Europe. National political compromises built this financialisation into the structure of the public finances. The property and credit bubble was already deflating from 2007 onwards, but the international crisis of 2008 produced a particularly dramatic crash in Ireland's economy.

However difficult it was to solve, the origins of Ireland's economic crisis appear to be no mystery. The crisis was fivefold (NESC, 2009). The core was a *financial* crisis – an unholy combination of property speculation by developers, reckless lending by bankers and a lack of governmental oversight and regulation created a property and banking bubble that brought the Irish economy to its knees when the international financial system ran into trouble in 2008. The liabilities of

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these banks were guaranteed by the state in 2008 and developer loans and assets have been taken under state management. A *fiscal* crisis mushroomed as the public finances were burdened with the cost of bailing out failing banks, but also with a growing deficit as tax revenues associated with the asset bubble disappeared. One of the largest austerity policies in recent history was undertaken in response (Whelan, 2010).

This was reinforced by an *economic* crisis. Despite widespread emphasis on problems of competitiveness, major deficits in productive investment and collapsing domestic demand were more significant economic weaknesses. These three crises drove a major *social* crisis based on negative equity and mortgage arrears, cutbacks in public services and disastrous rises in unemployment. Finally, Ireland faced a *reputational* crisis, particularly evident in the reluctance of international lenders to finance the government debt – culminating in an EU–IMF bailout in November 2010. Ultimately these crises hastened and were reinforced by a sixth, broader crisis of *political* capacity, solidarity and action (Kirby and Murphy, 2011).

A myriad of books and articles have traced the disastrous consequences of developments in these different spheres of property, banking and the state. There is still much to be discovered here regarding the cultures, coalitions and decisions that shaped each of these spheres. However, the most significant questions relate to the conditions that allowed the crisis to emerge, the reasons why the crisis took the form it did in Ireland, and why it has been so deep and persistent. Social and political institutions and the ways in which they are worked into everyday economic life are crucial to understanding these issues. Although my analysis focuses on the Irish national crisis, that story is itself woven with a number of broader and recurring threads.

The first is the increasing tension between financial and productive capital – where Ireland's boom of the 1990s, rooted in public and private productive investments, was sidelined by an asset bubble rooted in financial and property speculation in the 2000s. 'Development' and 'financialisation' competed as projects within the political economy, resulting in financialisation winning out with disastrous results.

The second recurring strand running through this story is forged from the linked processes of economic globalisation and regional

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integration. The EU has been the paradigmatic case of the trend in recent decades towards the emergence of dominant regional blocs. However, the crisis has been in part produced and intensified by deep structural fault lines in the relationships between core and peripheral economies and states within the EU – fissures that were only papered over by the European effort to promote integration through liberalisation. The European project involved the integration not only of different economies but also of diverse 'varieties of capitalism'. Monetary union and the European Stability and Growth Pact of the late 1990s attempted to manage this integration through a combination of market- and rule-based disciplines. However, these disciplines proved unable to manage the speculative market activity produced by European and international financial integration.

The third thread is the perennial tense embrace of capitalism and democracy. In principle, free market capitalism and representative democratic national government are complementary components of liberal societies. However, the economic inequalities and concentration of power produced by market processes have always posed a significant threat to democratic governance. This tension has been further intensified in the recent decades of global economic liberalism, leading Dani Rodrik (2012) to argue that all societies face an inescapable trilemma where they can choose only two out of deep economic integration ('globalisation'), national government and democratic politics. The only way to save national democracy appears to be to halt economic globalisation, while politics in an era of globalisation appears to offer the choice of democratic international institutions or negotiating and competing national governments. However, this trilemma may pose the question too dramatically. In practice, the experience of liberalisation has produced both powerlessness and fatalism, as well as experimentation with new forms of governance. Much as development and financialisation competed as counter-tendencies within Ireland's economy, experimental public action competed with aggressive liberalisation within Ireland's economic governance even as they were intertwined.

These three threads are linked by a deeper theme that runs through the entire analysis – the question of the economic liberalism that has dominated the global political economy since the 1970s. Throughout the analysis, I examine the role that economic liberalism played in the emergence of the crisis itself and ask in the concluding analytical

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chapter why the crisis has reinforced economic liberalism despite seeming to herald its demise (Crouch, 2011).

Political debates regarding the crisis largely pushed the question of liberalism to the sidelines. In Ireland, continuing revelations about a catalogue of governance failures in the public and private sectors led to a focus on cronyism and corruption rather than on the systemic dynamics of the Irish model. In Europe, the focus was on the problems in the design of the euro and the profligacy of national governments – as well as on the disastrous interaction between them. The increasingly liberal character of the regional integration process disappeared from view as a source of the region's difficulties. At a systemic level, while the tensions between capitalism and well-being have never been as obvious as they are to current generations, the prospects of generating shared social and political solutions to these economic problems have rarely seemed so remote.

This book attempts to understand economic liberalism not as a theoretical concept or as a political idea or programme, but as a particular way of organising capitalist economies, involving characteristic forms of economic organisation, government, welfare and social protection, and other elements of the political economy. I examine 'actually existing economic liberalism' through the case of the Irish political economy over the past three decades.

All political economies are mixtures of the various 'types' that research has identified – liberal, social democratic, developmental, Christian democratic regimes and so on. Ireland too mixes these types together – with a liberal emphasis on economic globalisation and the rights of capital combined with Christian democratic emphases on family, social democratic elements of universal social benefits, Mediterranean clientelist political cultures and the active industrial policy of developmental states. Nonetheless, there is enough internal coherence within these 'types' and enough differences between them that it proves useful to continue to use such typologies. Furthermore, most comparative analyses suggest that Ireland's economy fits the 'liberal' mix of characteristics most closely, with some notable exceptions in the areas of wages and active labour policy (Amable, 2004), industrial policy (Ó Riain, 2004), pay-related welfare benefits (Ó Riain and O'Connell, 2000) and some others. To understand real-world examples of economic liberalism, it is necessary to analyse not only the process of marketisation but also the social

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structures, political dynamics and institutional forms that are most common in liberal political economies.

Accounts of the Irish political economy usually place its apparent or desired liberalism at the centre of their explanations. Most 'orthodox' economic analyses emphasise the 'convergence' of the Irish economy in the 1990s as Ireland removed a number of obstacles to the operation of a market-led economy (Honohan and Walsh, 2002; Lane, 2011). Key policies here included spending cuts that stabilised the government deficit, an emphasis on wage competitiveness, maintaining low inflation rates and the pursuit of foreign investment and trade-oriented policies.

However, the 2000s saw a departure from these fundamentals. Spending increased, wage competitiveness and export performance declined, and the economy was allowed to overheat, in particular through the creation of a credit and property bubble – in this view, largely due to the weakness of even simple prudential regulation. Crucially, poor financial regulation and poor fiscal discipline spread, at just the time when membership of the euro currency imposed severe costs upon such weaknesses, eventually fuelling the crisis (Lane, 2011). While public policies play a role, in this view the critical variable is the extent to which policy and economic practices enable the operation of market processes. Prudence and disciplined enforcement of market processes and conditions are the critical elements of policy. When such policy characteristics are weakened, liberalism is weakened by political failure or, worse, cronyism.

Similarly, critical accounts of the Irish political economy often also place the liberal character of Ireland's political economy at the centre of the explanation (O'Hearn, 2001; Coleman and Coulter, 2003; Kirby, 2010; Kitchin *et al.*, 2012). In these accounts, liberalism is at the root of structural weakness in the Irish economy, but, more importantly, is also at the root of Ireland's social failures of income inequality, high poverty rates and weak structures of social protection. Ireland's political failures are associated with its liberalism in that cronyism is rooted in close ties to a dominant business sector, and the failure to develop a vibrant public sphere weakens the effectiveness and democracy of political institutions (O'Toole, 2009). Again, politics is present even in the liberal political economy, but primarily as a disciplinary mechanism that enforces market processes – acting as a 'competition state' (Kirby, 2002). The constraints of liberal forms of capitalism

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result in a variety of problems in Ireland that could be addressed through movement towards a different variety of capitalism (Kirby and Murphy, 2011) or through alternatives to capitalist organisation (Cox, 2011).

In keeping with these two competing perspectives, in this book I examine Ireland as a case of liberal political economy, an economy where market activity was taken to be the dominant and legitimate way of allocating resources and making economic decisions. However, rather than viewing liberalism as a fixed feature of Ireland's political economy, I analyse how that liberalism ebbed and flowed and how other political economic projects and tendencies contended with the overall liberal pattern of organisation. Specifically, I argue that developmental and corporatist institutions were critical in promoting growth in the 1990s, but were derailed by the property bubble of the 2000s fuelled by market liberalism and state boosterism.

Ireland is a fascinating, although surprisingly unusual, case of economic liberalism. It represents the clearest case of small country liberalism in Europe, perhaps the only case in Western Europe (with the possible exception of Switzerland). Even this classification of Ireland as liberal directs our attention to the historical specificity of liberalism as a form of national political economy. For, even though economic liberalism has had a sweeping and profound impact across the world, it is institutionalised in only a small set of advanced capitalist countries. Indeed, the subset of liberal political economies in advanced capitalism consists of the two historical hegemons (the UK and the US) and their former colonies and/or cultural and trading neighbours – Australia, Canada, Ireland and New Zealand.

Ireland's distinctiveness within this group is the result of certain characteristic features of economic liberalism. Apart from Ireland, these smaller variants of liberalism are distant from Europe. One of the ways in which the liberal world of capitalism is different from the others is that it is more geographically scattered. Unlike the social democratic, Christian democratic and Mediterranean versions, the geography of liberalism follows the footsteps of colonialism rather than the cultural clusters of European societies. This in turn reflects the close link between a policy and regime preference for liberal economic organisation and a country's power in the global political economy – the key promoters of a liberal trading regime have always been the hegemons of each era whose interests are favoured by the

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expansion of such regimes (Arrighi and Silver, 2000). While Ireland is among the most open advanced capitalist economies, this too is unusual as most of the liberal economies are more likely to operate as largely closed economies, despite a stated general policy preference for trade, financial and other market integration.

While Ireland is an exceptional case within actually existing economic liberalism, it is an important one. Countries that adopt liberal policy regimes in the contemporary economy are more likely to match Ireland's conditions as a small, open economy with significant legacies of post-colonialism and under-development (for example, see Mahoney (2010) for a discussion of Latin America's mercantilist and liberal forms of post-colonial development). Ireland's exceptionalism within the world of economic liberalism makes it a particularly significant case for the increasing number of countries across the world that pursue liberal policies.

Understanding liberal political economies

The following chapters explore the specific arguments offered from these perspectives in more detail. But in seeking to answer these empirical questions, it is necessary to tackle some profound conceptual issues. How should economic liberalism itself be understood? What kind of social structure and political programme is 'economic liberalism' and what are its key features?

In the field of comparative political economy, liberal countries occupy an unusual position. Liberalism is often the reference point from which others are seen to depart – with social democratic, Christian democratic or developmental states all seen as 'deviations' from the 'normal' state of lack of political intervention or social coordination. Partly as a result of this, liberal economies receive relatively little direct analysis compared to the other 'varieties of capitalism'. The economic dynamics, social institutions and political conditions of liberalism are perhaps less well understood and conceptualised than those of the alternative systems that seem more obviously 'social' or 'political'.

However, it still makes sense to talk about 'economic liberalism', both as a 'type' of national economy and as a transnational set of institutions and practices (Brenner *et al*., 2009). There are clearly liberal political economies – a number of them have been listed above. The last three decades have also seen the international spread of what

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