1. INTRODUCTION

The issue of privatisation and the related themes of this symposium - liberalisation, competition and regulation - are part of a broader discussion on the kind of economic system and indeed the kind of society we wish to construct in Ireland. This discussion in turn takes place in the context of a broader global debate on evolving economic systems, a debate that has been accelerated by enormous change in Eastern Europe and by the emergence of China as a market economy but which nevertheless is far from finalised. Over the last ten years a strong strand of argument has developed that a single system of economic organisation, namely a particular model of market capitalism is now in effect the main paradigm of a global economy.

In a debate characterised by much certitude it is constructive to remember that the current manifestation of capitalism offers more than a single uniform model. In particular, the distinctive European model - the Social Market model - offers significant government intervention in pursuit of social and economic objectives in clear contrast with the Anglo-American variant. Hutton and others have argued that the version of capitalism operating in the developed countries of East Asia and in certain developing economies in the region, constitutes another substantial variant. Advocates of general equilibrium theory tend to dismiss these divergences as transitory aberrations en route to the uniform global capitalist system. In particular they assume and actively advocate rapid convergence between the European Social Market model and the Anglo-American variant.

It is undoubtedly true that there is a dynamic of convergence and that further convergence of models will take place. The ‘Blairite Third Way’ constitutes an attempt to map the road to convergence. However, there is body of considered
opinion, Rhodes and van Apeldoorn (1997) being but two of the representatives, which argues that the European model will persist, albeit in modified form.

The core characteristics of the European model currently include relatively high levels of government expenditure and traditionally have included the presence of substantial state owned enterprises. Levels of government expenditure have fallen slowly in Europe over the last decade and have stabilised now at a figure of just under 45 percent of GDP. This average figure masks a range, stretching from around 60 percent for Scandinavian economies, to Ireland’s figure of 28 percent, not only the lowest in Europe, but the lowest in the developed world.

The commercial state companies are the other significant component of the public presence in economies. Until 1990, these typically accounted for 10 percent of GDP in EU countries, although in some individual states such as Austria, the sector accounted for as much as 20 percent of GDP. Britain, where state companies now account for some 2 percent of GDP, is the most obvious, and to an Irish audience the most visible, example of dramatic reductions in this sector. The decline of the overall significance of the state sector is less rapid in other EU countries, but nevertheless, the trend is significantly downwards.

In an overall perspective, if the measure of the significance of the public sector is based on the aggregation of government expenditure and the role of state companies, Ireland now has the most privatised economy in Europe, if not the developed world.

2. IRISH PUBLIC ENTERPRISE

The history of public enterprise and of individual state enterprises in Ireland is relatively well documented. Sweeney (1990) has argued that in the early years three interrelated principles guided the thinking behind the establishment of state companies:

- That natural monopolies would be better in state ownership,
- Public Enterprises would counter market failure, and
- Individual state companies had a role as National Champions.

Many of those present will remember a time, perhaps no further back than the early 1970s, when state companies enjoyed considerable prestige and it would not be overstating the matter to say, a measure of public approval. The achievements of the companies were a source of national self-esteem in an otherwise bleak landscape, a concrete demonstration that economic competence and commercial performance lay within the grasp of economy and society. As recently as 1993 a survey of Ireland’s most admired companies carried out on the Fortune magazine template rated a number of state utilities very highly across the full range of evaluative criteria offered in the study. Indeed several state companies were ranked
as being amongst the best managed companies in Ireland in their opinion of their private sector peers.

Over time additional factors emerged which tended to further bring these companies into economic prominence and locate them at the centre of important debates, as for instance in the area of industrial relations. State companies became highly unionised, with unions generally succeeding in getting above average employment conditions for their members. It may be argued that the manner in which the union strength was used in some state companies was detrimental to the overall case for the companies in the period since 1960. In the 1970s, turbulent industrial relations often earned disproportionate black marks for public utilities and it is generally forgotten that in the conflict-based model of industrial relations which seemed to be current at that time, major private companies such as banks also endured prolonged strikes - the two interminable banks strikes being as welcome to many small businesses as the loss of electricity was unwelcome.

It certainly is the case that the strength of trade unions in state companies increased the overall strength of the trade union movement with a direct spillover effect on the strength of the union movement in the private sector. This gave enhanced status to the overall trade union movement in negotiations with government. This direct benefit to trade unions coupled with a left perspective, ensured trade unions became very supportive of state companies. Conversely, in the eyes of some commentators unions may have become too closely involved in the interests of the state sector, a perception that is not always borne out by examination of the key data from that period. Nevertheless embedded views and perhaps prejudices, still colour the debate about the role, the autonomy and the efficiency of state companies and form a part of the privatisation case.

3. INDUSTRIAL POLICY

Industrial policy between the early thirties and the late fifties involved a two-stranded approach. State companies became the drivers of large ambitious projects while protectionist tariffs and associated measures were designed to develop the indigenous private sector. The state companies, besides being important in the overall industrialisation process, also were agents of supported regional and social policy. The benefits to the midlands region of the Bord na Mona and the ESB are cases in point. This is in direct contrast to the situation in the UK where nationalisation of smoke stack industries, which were in serious commercial decline, was in many ways the direct antithesis of the entrepreneurial green-fielding that characterised the Irish situation. It is often forgotten that these elements, which contribute to one part of the British privatisation debate, have little direct application in an Irish context.

Over time, the limitations and failure of the policy element directed toward the indigenous private sector ultimately led to foreign direct investment (FDI) being
adopted as the primary driver of economic development. Thus from the 1960’s onwards the option of establishing new state companies as instruments of policy was no longer on the agenda. The only wholly new organisation created was Bord Gais with the nationalisation of Dublin Gas representing a one-off and highly pragmatic decision. The new policy of FDI reliance generated very visible results but also generated concerns about the emerging nature of Irish industry.

Irish industrial policy has been subjected to formal review by government in two significant exercises in the last twenty years. In the early 1980’s, The Telesis Report and the subsequent White Paper on Industrial Policy (1984) argued that an essential component of a policy with the stated objective of creating high quality self-sustaining economic activity is the presence of strong indigenous exporting companies. Ireland lacked a sufficient number of such companies and it was unlikely that a policy substantially relying on FDI would lead to their development.

In 1990, the Culliton Review focussed on the same issue as part of its analysis. It concluded that ‘the attraction of foreign investment is not a sufficient basis for developing a national advantage in advanced industries’ (Culliton, 1992). It further stated that ‘If industrial policy is to be successful in helping to generate a competitive industrial structure which can sustain long-term employment growth and living standards the focus must shift decisively to indigenous companies’. With regard to state companies Culliton remarked that ‘These (state) enterprises include some of the very few reasonably large industrial enterprises in the state’. In effect Culliton argued that large indigenous companies were necessary for a successful industrial policy in an Irish context and that state companies composed a significant element of our narrow base in this area.

The problem of the dominant role of FDI in recent economic success has receded in debate. This is understandable, as economic success of the kind recently experienced tends to ensure that little attention is paid to those voicing negligible reservation about the driving force. The Celtic Tiger – real or mythic – is a much-praised species, but the heady enthusiasm of commentators has occluded the fact that it is not so much a celtic cat as a collection of international tigers, the majority of US origin, residing in a benevolent celtic mist. In reality over seventy percent of Irish exports are now accounted for by FDI and this must give us food for thought in shaping future policy.

4. PRIVATISATION IN IRELAND

Since the late 1980’s arguments in favour of privatisation of state companies have been voiced and the tone of the debate has become increasingly assertive and perhaps somewhat strident. Lee has commented with characteristic astringency on the lack of intellectual originality in the debate on economic and social policy formulation in Ireland in the past. In the case of the privatisation debate it might well be argued that the analysis so far has faithfully reflected this long dreary
tradition of mediocrity with an evidently unshakeable appetite for the retailing of second hand ideas. Most of the argument has simply followed international trends without any critique as to the merits and suitability of such a policy to the particular circumstances of the Irish situation.

It is instructive to briefly examine some of the more concrete arguments advanced. Certain drivers of privatisation in other economies no longer apply in Ireland. In the UK the then current budgetary requirements in the 1980’s needed the proceeds of privatisation. This has also been the case in France in relation to meeting Maastricht criteria on budget deficits for single currency qualification. While these arguments had validity in Ireland until the mid-1990s, they obviously are no longer relevant in the context of very large budget surpluses.

Given that borrowing by state companies is classified under the Public Sector Borrowing Requirement (PSBR), it could be argued that privatisation of companies may reduce the PSBR and improve the total debt/GDP ratio. Again this argument now has little immediate relevance in Ireland following the dramatic drop in the total debt/GDP ratio of recent years. As Vickers (1990) points out there is a certain illusion implicit in the argument for reducing the borrowing requirement by privatising elements of it because “in macroeconomic terms, it ought to matter little whether a firm is in public or private ownership, when it does a given amount of borrowing”.

In Ireland there has been little rigorous debate to date on the rationale for privatisation and what discussion there has been has lacked real hard evidence about the merits of the proposal. The advocates liberally invoke the word ‘pragmatic’ but there is a lack of acknowledgement that pragmatism is rarely value free. The arguments advanced in Ireland for privatisation; tend to rely either explicitly or implicitly on a set of inter-related propositions.

1. Privatisation will automatically (but in some unspecified way) improve efficiency and lead to lower prices for consumers. This argument is largely contingent on the assumption that competition accompanies privatisation. If change in competition is part of the transformation, then there is a distinct possibility of such outcomes. However is must be recognised that even when such competition emerges, former monopolies may retain significant market power. As Vickers (1990) argues ‘it would appear that no general claim can be made as to the economic desirability of privatising firms with market power’. The issue of market power is well illustrated in Ireland in traditional and wholly private sectors of the economy such as beef-processing, banking (until the recent advent of the Bank of Scotland) and the cement manufacturing industry until the early nineties.

2. Private sector shareholders will demand continuing delivery of rising dividends and growth leading to improved management and corporate performance and
lower prices. This is relatively true if the comparison is with the muted commercial demands of a single indulgent state shareholder, which certainly has been the case in the past. There is no reason however why a state shareholder with focussed requirements could not be as demanding as a private shareholder. In recent years the dividend payment by Aer Rianta to the government offers a model of what might be achieved in this regard.

It should also be remembered that demanding shareholders may ultimately have their demands met at the expense of consumers. The case of banking in Ireland offers a salutary example. Furthermore the ‘short-termism’ of financial markets may be destructive to the quality of services provided by privatised industries particularly in area of public utility. Some of the water utilities in the UK are evidence of this, where early harvesting and under-investment has led to serious problems.

There is ample evidence of price reductions in industries which have been privatised. But concurrence may not prove causality. For example in the telecoms sector, technological change is undoubtedly a significant factor. In electricity provision, the most recent generation of highly automated combined cycle gas turbines, achieving very high efficiency levels of fuel utilisation, have dramatically reduced production costs.

3. It is argued that the government as shareholder often imposes conflicting objectives on state companies. As Vernon stated, state companies have “a confusion of goals, that may be unreconciled and unreconcilable”. However, governments in recent years have achieved a more focused approach and have recognised that the companies in turn must maintain focus. Nevertheless there is an argument that new structures, for instance, the possibility of putting state companies in a holding structure within the National Treasury Management Agency (NTMA), could eliminate most of the difficulties in this area.

In the final analysis one should not altogether rule out the desirability of pursuing multiple objectives. It may grate on the tidy mind but it may be justifiable in a broader vision.

4. The role of a government department in being simultaneously policy maker for an industry, having the ultimate remit for regulation and being the main shareholder (particularly in a regulated liberalised sector) may present conflict of interest issues. The shareholder remit can readily be resolved by the proposition of a holding structure offered above.

5. A related argument lies in the proposition that state companies lack the opportunity to be truly commercial because of their relationship with government departments. Slow decision making processes when approvals are being sought hamper commercial freedom. Much of this criticism is true. It
substantially arises from ambiguous attitudes by the state and by certain key decisions makers as to the role of state companies. The comparison made in this argument between a clear-cut private shareholder driven agenda and an ambiguously motivated state shareholder may well be valid in current circumstances. No organisation can thrive on the basis of restrictive and muddled thinking. In some state companies there has effectively been an ‘investment strike’ by the state shareholder. This has occurred under governments of all complexions in recent times. It has taken several forms with varying degrees of subtlety; a refusal to contemplate equity injections, refusal to sanction investments even when provided from the state companies’ internally generated funds flow and tortuous approval processes.

A more valid comparison is surely that between a supportive state shareholder with clear growth and development objectives and supportive private shareholders with the same objectives.

6. There is a popular perception that the EU Commission is opposed to state firms and, in particular, to the injection of capital to such firms by the state shareholder. The EU is in fact neutral on the issue of whether state firms should exist. Furthermore, it does not prohibit the injection of equity capital provided such injections abide by the “market investor” principle. In any event in the Irish context, with the exception of Aer Lingus, no state company has received or needed equity injections in recent years.

7. Some state companies are perceived as lethargic, inflexible and doggedly committed to maintaining old-fashioned hierarchical structures and particularly inappropriate cultures. Privatisation, it is argued is necessary to transform these organisations. There is no doubt that some of these characteristics describe aspects of the performance of some state companies. However, the empirical evidence in the UK, especially on the encompassing culture issue, is not strongly supportive of the view that privatisation is an irresistible instrument of change in this area.

The arguments proposed above are not particularly specific to Ireland. They have characterised debate in most European countries. But there are in fact issues specific to Ireland which have advanced the cause of privatisation.

5. THE IRISH SOCIO-POLITICAL-CULTURAL CONTEXT

The socio-political cultural paradigm pertaining in Ireland provides a supportive cultural context within which the privatisation debate is framed and this represents a non technical factor or force for advancing this change. Ireland has never been a full subscriber to the European Social Market model. While the limited resources of an underdeveloped economy may be cited as a factor in the failure to put in place
the kind of social infrastructure characteristic of the European Social Market model, a more important determinant may have been the philosophical disposition of the leadership cadre.

Earlier in this paper reference has been made to the limited nature of the intellectual effort at official level which was directed towards development of economic and social policy in Ireland over a long period of years. Where such a gap exists, an easy substitute was the importation of ideas and our near neighbour with whom we share a common language and media landscape provided a flow of ideas in the absence of a truly indigenous creativity. But the UK even before Thatcherism subscribed only to a weak and incomplete version of the European Social Market model. For example, labour market policies and employment protection measures were never as well developed in the UK as in northern European countries.

This context, coupled with Thatcherism in the 1980’s, the poisoning of the merits of government expenditure and thereby much government management, through reckless deficit budgets in the late 1970’s and 1980’s, a certain affinity with the US through emigration, extensive US FDI investment in Ireland with non-union human resource management policies, all have contributed to a much more significant shift in the socio-political culture towards the Anglo-American model than has taken place in most other European countries. Advocates of privatisation have sought to reinforce this shift in the socio-political paradigm by campaigning for other elements of policy supportive of the shift, such as reduced government expenditure, and have utilised the shift to further the privatisation agenda.

6. FUTURE OF PRIVATISED COMPANIES AND INDUSTRIAL POLICY

There is, however, a specific issue in the privatisation debate that should be central to any decision made in the Irish context. To-date the issue of industrial policy has barely merited discussion.

The Irish state companies as noted earlier (Culliton, 1992), form a core element of large-scale indigenous industry. Privatisation is not just about a change of ownership from the state to popular share ownership by individual Irish people, Irish institutions and foreign institutions. It opens up the very distinct possibility of take-over. The Irish state companies are not large by international standards, and in many cases can constitute a useful building block for very large companies building European and Global organisations. But such take-over will not just be a simple further change of ownership. They will be fully integrated into the global organisations and shareholder requirements will necessitate significant cost reductions. Economies of scale will be achievable in key management areas and these will be located and consolidated at the corporate centre. This will not be located in Ireland. Thus over a relatively short period of time, the Irish operation will become simply a branch operation of a large multinational company. They will have little or no influence on decision-making in relation to development and
expansion. This is the very criticism that has been levelled at the role of FDI in Ireland.

There are many recent examples of this behaviour in the private sector internationally. The car manufacturing company, Rover, taken over by BMW in 1996, has seen some of its critical business functions transferred to Germany over a three-year period. The British operations are rapidly been reduced to production operations and local distribution.

This is not to argue that state companies should be left in some kind of closeted environment in Ireland in a mark-two version of the policies of the 1930's. Rather they should be exposed to full competition where possible and with a supportive shareholder encouraged to internationalise. Aer Rianta and the ESB are examples of companies, which have already made useful tentative steps at such internationalisation. This analysis of the role of state companies in industrial policy is not exclusive to Ireland. The less enthusiastic steps of the French in the direction of privatisation reflect in part this consideration.

It has been argued by Vickers (1990) that privatisation has adverse distributional effects in that wealth formerly held in the common ownership is concentrated in fewer hands. There is a specific additional factor in Ireland in the privatisations to date. Employees have been given substantial shareholdings in privatised companies through Employee Share Ownership Programmes (ESOP) or promised such shareholdings where privatisation is under consideration. The arguments for this have been largely dressed up in the current fashionable clothing of stakeholder theory. They undoubtedly constitute such an approach, but the reality is that it is a concept effectively being used as a bribe to facilitate privatisation, and stakeholder considerations are not the prime objectives of the decision makers suddenly converted to stakeholder theory. Technically, the adverse distributional effects are even more severe than in the case of non-ESOP containing privatisations. On the other hand, the Irish privatisations to-date have not contained some of the outrageous senior management benefits that characterised UK privatisations with their obvious distributional consequences. One suspects the main motivation in this decision is fear of outrage rather than concerns for equity.

7. CONCLUSION

The privatisation debate in Ireland has been characterised by conventional wisdom, received ideas and unsustained assertion. It is largely advocated by a relatively small group of opinion formers and potential beneficiaries. Rigorous analysis has been largely absent. For instance there is an easy and incorrect association proposed between the idea of privatisation and the achievement of a more competitive market place. The significant issue of overall industrial policy has not featured in the discussion. In many ways privatisation runs contrary to established policy objectives in this area, policy which has developed from repeated rigorous analysis. The
debate has seen a disproportionate focus on a sector now accounts for about 3-4 percent of GDP. One might sceptically observe that it represents opportunity for wealth accumulation through privatisation of capital assets or through the utilisation of other assets such as licences, in an economy where the indigenous private sector has failed in the entrepreneurial task of wealth creation, as it pertains in most other developed countries.

References


DISCUSSION

Dr. John Fingleton: The message of John Kay’s presentation appears to be that liberalisation in the form of competition policy and deregulation is of central importance. So it is somewhat disappointing at a seminar on “Competition, Regulation and Privatisation” that most of the emphasis has been on privatisation. The costs of market failure are large and invisible and, although there is an increasing recognition of the importance of corrective policy measures, insufficient progress has been made in this area. Liberalisation in Ireland is proceeding very slowly. Let me give some examples.

First, policy changes have frequently been forced by EU legislation or by strong producer interests. The first is exemplified by the Irish two year derogation in the opening of telecommunications to competition and the second by its premature ending because of the perception that foreign investment was being lost. Second, the government is somewhat slow to establish the proper institutions, as illustrated by transport, especially taxis, and the generally last minute establishment of regulators in the energy and postal sectors. Third, where institutions are established, they are not given free reign to do the job properly. The Competition Authority was restrained to deal with innocuous vertical agreements for its first five years and even now is severely constrained by lack of adequate finances, especially to recruit the highly-skilled talent it requires. The Office of the Director Telecommunications Regulator (ODTR) can punish a telecom operator who breaches the rules by a fine of £3,000 or by withdrawing the licence. The former is small both relative to the potential social cost and to the private benefit of breaching the rules and the latter is not credible because it would simultaneously punish consumers. The appeal of the ODTR’s decision on the third mobile licence illustrates how unclear appeals processes and the unwillingness to delegate proper decision-making power has potentially enormous costs. Fourth, structural regulation, such as breaking up former monopolies, has generally been avoided, despite the fact that this could enhance the speed at which competition develops. The State’s lobbying in Brussels to allow Telecom Eireann to keep Cablelink is just one such example.

Across the board, it is clear that policy in this area is driven by producer not consumer interests. Sometimes these are coincident when both buy in the same market, as with taxis where consumers who have long suffered may now benefit because business in Dublin was increasingly adversely affected by the lack of taxis, or when producers pass on the benefits to consumers. However, policy needs to take on board the idea that the costs of monopoly, when borne directly by the consumer, are frequently large and invisible. Error at present is more likely to benefit inefficient monopolists.

So what do we need to do? I would make a few simple suggestions.

1. More structural regulation should accompany privatisation where possible.
This is relevant at present with broadcasting, and is likely to arise in the transport area generally.

2. Policy should be clearly focussed on a consumer welfare standard. At a minimum, the legislation for utility regulators should clearly state that the regulator’s general objective is to maximise long run consumer welfare. This is consistent with the reason for having such regulators, namely to replicate the function that the market would perform were there not a market failure.

3. The powers of regulators need to be enhanced, not to make them above the law, but rather to enable them effectively to undertake the tasks that are delegated to them. At a minimum, this requires a wide range of credible sanctions that are related to the social costs of rule-breaking. The manner in which the ODTR and Commission for Electricity Regulation (CER) have been established on an independent footing with reporting to parliament sets a useful model for combining independence of function with accountability. This should be extended to the Competition Authority. In the same area, more resources may be required, especially where public bodies are competing for specialist skills in a tight labour market. Bad policy resulting from deficiencies in these areas could be worse than no policy.

4. Some consideration should be given to restricting the grounds for appeals of regulatory decisions, especially where appeal results in delay that is costly for society but possibly beneficial for a private interest. Limiting appeal to judicial review is one route. Another, perhaps more radical, might be to require coincident consumer injury in order to have standing for an appeal. In other words, the party damaged by the regulator would have to show that the consumer is also damaged at the same time.

5. The overall approach to competition and regulation needs to be coherent. Competition rules should apply to all sectors regardless of specific regulation but sector regulators should probably have the same enforcement powers within their sectors as the Competition Authority. Individual regulators, rather than commissions, have much to commend them in terms of independence and accountability. At the pragmatic level, Ireland is unlikely to find sufficient qualified specialist experts to staff a range of commissions. The focus should instead be on finding the best individuals, and measuring performance by the decision to re-appoint. John Kay has indicated how this has worked well in the UK. Areas that are synergistic, for example gas and electricity, should be included within the same regulatory body.

Telephone prices in Ireland have fallen by double-digit amounts in real terms while the range of products and services has been enhanced enormously. Taxi prices have risen and the supply remains restricted. The contrast between one sector where liberalisation has been forced and another where it has not illustrates the important role that politically independent regulatory institutions play in contributing to economic growth. Much more remains to be done. Policy that makes clear the importance of consumer welfare and that is implemented by efficient laws that are enforced by strong and accountable regulatory institutions should be seen as a high
priority.

Privatisation is, in my view, a secondary issue in all of this. Private ownership generally offers efficiencies over public ownership, but these are often overstated by comparing the worst of public with the best of private. Public ownership requires additional rules to level the playing field and further emphasises the need for regulation to be politically independent. The priority should therefore be on establishing competition within an appropriate framework.

**Professor John FitzGerald:** John Kay in his paper highlighted the diversity of experience in regulation in the UK, with success or relative failure being related to the matching of regulatory style with the varying industrial structure of the sectors considered. He also placed much emphasis on the need to promote competition, emphasising this over the issue of ownership. Moore McDowell, on the other hand, emphasised the importance of changing ownership, rather than competition, while not ignoring the importance of competition.

In agreeing with John Kay, I think that Moore McDowell’s approach is dangerous, especially where existing monopoly producers in State hands are being considered. There are two basic ideas which would find wide acceptance – the State is not very good at producing goods or services efficiently and monopolies, whoever owns them, are bad for consumers and generally bad for society, except, of course, where they are essential is scale economies are to be reaped. Applying these ideas in the Irish case - they would seem to indicate that the State should not be involved in owning banks, food processing companies, airlines, waste disposal companies, housing maintenance by local authorities, road maintenance, printers albeit of banknotes etc. All of these goods and services can be provided by private sector producers working in competitive markets.

The case is less clear-cut for other goods and services, which, because of scale economies or other factors, have substantial monopoly elements. The problem with such monopolies is that the price is set above its social optimum resulting in production being too low and consumers paying too much. The price is set to maximise the monopolist’s rent. This rent can accrue in varying degrees to the investor, in the case of most private monopolies and some public sector monopolies to the workers. This is the case in many public sector monopolies, and in the old Dublin Gas. In the case of suppliers of services rents accrue to the monopolist, this might characterise some aspects of the peat industry. The objective of public policy should be to eliminate these rents through competition. However, where there is a natural monopoly, if rents are inevitable, it is better that they accrue to the State than to private citizens. In the hands of the State they can be used to reduce distorting taxes whereas in the hands of private individuals this option is not available.

Ownership and competition are not synonymous and there are different ways of getting competition. In the UK the water industry has been privatised, while in parts
of France the ownership remains in the hands of the State. In France the provision of the service, operation and maintenance of the water supply using the state-owned infrastructure, is provided by private sector firms that compete for the job (Cordier, 1994). This ensures that competitive pressures are exerted on the labour input and that the costs of providing the service are transparent. The process of competitive tendering provides additional information to a potential regulator to allow them to set an appropriate price. This model is already applied by Bord Gais and Bord na Mona – they contract out, through a competitive process, much of the work previously done in-house. The ESB, while a monopoly provider of services in Ireland, competes for management contracts for electricity infrastructure, both generation and transmission, in the UK, Canada and elsewhere.

Where they are subject to competition there is evidence that the labour input is lower, with lower implied monopoly rents. Such a model, involving vertical disintegration, may be more suitable than privatisation to some services in Ireland, such as electricity transmission and distribution, management of gas transmission and operation of airports. A competitive tendering process in these sectors would reveal true costs to the regulatory authority and help ensure that monopoly rents are minimised. A change of ownership on its own would serve to transfer existing monopoly rents from the state to the private sector, leaving the regulator even more “in the dark” than at present.

Finally, the option value of holding existing State monopolies in State hands until a suitable solution is found may be worth more than the value obtained from a potentially botched privatisation. Once privatised, it is impossible to reverse the process and mistakes made at the time of privatisation are locked in. The experience of electricity privatisation in Northern Ireland highlights this danger. Consumers there will end up paying massively higher electricity bills than anywhere else in the EU for twenty years. Fortunately in the Republic the impulse to follow the Northern Ireland model in the early 1990s was resisted – we still have the chance of doing a better job, while at the same time electricity is on sale very much cheaper than in the North.

The small size of the market and the island nature of the system make some options, which work elsewhere, potentially unsuitable in Ireland. This applies in particular in electricity. However, that is no reason to despair of the possibility of using competitive pressures to eliminate monopoly rents. As I have indicated, the judicious use of the franchising model may be called for in Ireland and, as John Kay’s paper on the UK experience has indicated, a “one size fits all” approach to regulation and privatisation would be wholly inappropriate in the Irish case.

Reference

Dr. Sean Barrett: I wish to thank the Society for this choice of topic and our three speakers for a stimulating evening. John Kay made the vital point that the Conservative Governments of the Thatcher era were unusual in that they believed that there were areas of life where Governments did not know better than the rest of society. Most politicians like to meddle, to appoint their supporters to State boards, to rig markets in favour of State companies and to use them to promote projects in their own constituencies. Privatisation in Britain was started by Denis Healey, an able Chancellor, and is retained under Prime Minister Blair. It has been exported to well over eighty countries.

The practical results have of course been outstanding in Ireland. Irish Ferries now makes over £20m a year in profits where the B+I Line lost some £220m between 1965 and 1989. Greencore makes £50 million profits where the Irish Sugar Company lost as much as £50 million the decade before. The former RTE radio monopoly now has a market share of 49 percent ten years after deregulation, notwithstanding the annual licence fee revenue of £72 million that is not available to its new competitors. A steel mill, that cost the taxpayer many millions in subsidies, is now operated by an Indian company without recourse to the taxpayer.

Ryanair is worth four times as much as Aer Lingus despite the latter’s fifty year start. Compared to a cartel of two State airlines flying between Ireland and Britain up to 1986 fares are now reduced by two-thirds in real terms and passenger numbers have increased from 2 to 8 million. The increase in numbers flying has generated some 80,000 extra jobs in tourism here. When 8 million people save at least £100 per round trip between Ireland and Britain the savings are conservatively worth £400m a year. Eircom spokespersons estimate that the deregulation of that sector has saved consumers here some £450m a year. It is no surprise therefore that Frank Barry’s superb analysis *Understanding Ireland’s Economic Growth* attributes much of our recent success to policies of deregulation, liberalisation, privatisation and competition.

With gains from these market-driven policies worth £1,000 million a year in the sectors listed above it is obvious that the economists who supported market liberalisation have made a major contribution to economic efficiency in Ireland. Since the companies themselves had opposed market forces the credit belongs to the economists. A country which has increased its number at work by 45 percent since 1987 and has an unemployment level half that of other European countries has a lot to be proud of and much to tell the OECD. I draw attention to this point not to promote complacency in Ireland but as a caveat against the importation of failed economic policies from an EU mainland which has added no net employment for thirty years.

Mr Wynn is far too gloomy about economics in Ireland. He refers to “the limited nature of the intellectual effort at official level which was directed towards development of economic and social policy in Ireland over a long period of years”.

79
On the contrary the way in which Ireland has outperformed the European Social Market model espoused in Mr Wrynn’s paper shows that the intellectual effort used here to dismantle the social market model was convincing and successful.

When John Kells Ingram and his associates founded this society in 1847, it was some 38 years before the founding of the American Economics Association in 1885 and 44 years before the Royal Economics Association was founded in 1891. In 1864 Ingram wrote that “It was the pressure of social problems then imperatively demanding attention that led its youthful founders to attempt the establishment of such an institution. It has from the first applied itself, in the spirit of earnest enquiry, to the most important questions affecting the condition of the country.”

Our immediate past president Dermot McAleese attributed the change in Irish economic fortunes after 1987 to expansionary fiscal contraction. With the huge rise in employment since then and a large decline in the government share of GDP the merits of the analysis are obvious. Lowering the government share in GDP has improved the national competitiveness of the Irish economy and allowed tax cuts to secure wage moderation thus increasing output and employment.

Mr Wrynn’s gloom is also unfounded when he states that “in the case of the privatisation debate it might well be argued that the analysis so far has reflected this long dreary tradition of mediocrity with an evidently unshakeable appetite for the retailing of second hand ideas.” Irish economists have played a major role in the transformation of this country and play major roles in international organisations, both public and private. Moore McDowell and Frank Convery’s volume on Privatisation disproves his point. It is every bit as good as Vickers and Yarrow.

I support Moore McDowell’s case that liberalisation and privatisation have to be taken together. Public sector companies invariably accomplish regulatory capture of their sectors with both an unlevel playing field and a biased referee. Public sector companies have the inside track to free capital, mysteriously referred to as “equity” by them. The results from Britain show that the combination of liberalisation and privatisation has transformed the companies, reduced over-manning, reduced subsidies from the taxpayer and reduced prices. Bus deregulation reduced fares and subsidies and increased by 17 percent the number of vehicle miles run, an important statistic for those waiting at the bus stop. In the UK 85 percent of bus services are now commercial, requiring no subsidy. There is competition also on the subsidised bus routes through a competitive tendering system. The results of rail privatisation in the UK in 1995 have been most interesting given the large subsides paid throughout the EU to State railways in the other countries. According to Transport Statistics Great Britain 1998 by 1997/8 under rail privatisation the increase in freight has been 30 percent and in passengers by 19 percent. By contrast in the last eight years of nationalisation passenger numbers fell by 11 percent and freight by 26 percent. Punctuality and reliability are high and fares have risen in line with the
consumer price index.

The success of privatisation has its foundations in some basic economic tenets. The property rights of the owners of State companies are worthless. I am a conscript in holding shares in State companies. I cannot sell the shares. There is no return on any effort of mine to secure an improved managerial performance. This contrasts with shares in private company. The property rights in a private company allow a market in corporate control. Shares are traded daily. Corporate control by Government departments and parliaments is notoriously weak. Regulatory capture prevails. The efficiency of market enterprises is ultimately ensured by the bankruptcy constraint. With such built-in advantages it is not surprising that privatised companies improve their results once they leave the public sector.

I agree with Moore McDowell on education. The Irish second-level education system is virtually a voucher system in which funding follows consumer choice between several types of school both in the private sector and the public sector and with a choice of tradition. The system enjoys the protection of the Constitution. I believe that after over 150 years of service to this society the National University of Ireland colleges have long ago earned the right to be autonomous. I oppose both the antipathy of the last Government to the autonomy of Trinity College Dublin and the supine surrender of the College in its Private Bill currently before the Oireachtas. The last Government’s attack on creches by regulations which were so strict compared to those in primary schools precipitated a crisis in childcare. The meddling tradition in Irish Government is alive and well notwithstanding the success of privatisation here and in about a hundred other countries.

Mr. Pat Massey: I would like to make a few comments on the papers that we have just heard. Firstly James Wrynn has argued that privatisation is unnecessary and that the State could be a demanding shareholder. In similar vein John Kay has told us that UK experience shows that privatisation is not critical and that improvements in performance in UK public utilities in a number of cases pre-dated privatisation. He attributes the improvement in performance to the introduction of a “hard budget” constraint. My main concern here is whether such a “hard budget” constraint, whatever its impact in the short-run, is credible in the medium to long term. Governments change and policy priorities may shift.

Having said that I am inclined to disagree with Moore McDowell. I believe that it is competition rather than privatisation which is important in securing improved performance in public utility industries. In this respect, however, I think that what is disturbing is the apparent lack of a serious policy debate, in spite of attempts in this forum and elsewhere to generate such a discussion. At a policy level it seems that there has been little real consideration of the issues. Competition has largely been forced upon Ireland by the EU Commission and even then the official line has been to seek derogations delaying the introduction of competition. Similarly the tendency has been to permit the minimum level of competition required to satisfy
the Commission.

In the case of telecommunications Ireland sought a two year derogation from liberalisation. The Government subsequently did something of a U-turn apparently triggered by newspaper reports that a major industrial project had been lost because of inadequacies in the telecommunications network. Again in the case of the electricity industry, Ireland sought a derogation from liberalisation and competition is now only being permitted in the case of the three hundred or so largest users of electricity. In the case of natural gas, only eight customers will be permitted to choose their supplier, although admittedly these account for almost 80 percent of gas sales in volume terms. There has been no serious discussion of why competition is to be limited. Given that competition is beneficial the question needs to be asked why are the vast majority of customers to be denied the benefits of competition. While this symposium has debated the merits of privatisation versus competition, it appears that except to the extent it has been forced upon us competition has not been introduced and that, in my view, is the issue which needs to be addressed.