Achieving the Fastest Rate of Productivity Growth of Any EU Country

A Roadmap for the Next Phase of Irish Economic Policy

Paper Presented by

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1 Introduction

It is wonderful to realise that there is a new generation in Ireland which has never faced the hardship of high levels of unemployment, or the horrors of weekly riots and bombs in Northern Ireland, or the bleak depression of forced emigration. Many individuals in the public and private sector and successive governments, and not just the current Government, have contributed to these hard won achievements. In framing policies for Ireland for the next decade let everyone know that Ireland will not lightly give up these successes.

We will never again accept actions by individuals or groups which threaten the success of the Irish economy or the undoing of a nation at peace. As a people we will resist reckless economic policies or inappropriate fiscal actions and will oppose vested interests who attempt to damage the remarkable success of our economy. Regardless of the short term political attractions or otherwise, or how we are faring in the media or opinion polls, the Government are committed to focusing on maintaining our success and to start the journey of addressing new challenges for Ireland. We will also work vigorously to ensure that European policies enhance and do not damage the success of Ireland and of other member states.

Ireland is, however, a small and very open economy and it would be foolish in the extreme to think we are isolated from international developments. Today's economic landscape presents unique challenges for Ireland. World market problems include risks in international banking and credit markets, record energy prices, and market volatility, which make the future economic path of Ireland and many industrial economies more uncertain than just a few years ago. Additional issues, such as the value of the dollar/euro rate, pose particular challenges for firms in Ireland who are dependent on the US market.

Ireland is, however, in a position of strength to meet these challenges. The economy has been transformed to Europe's second richest (in GDP per head). Growth in GDP this year and forecasts for next year indicate that despite the slowdown in construction, Ireland will continue to be among the faster growing economies in the EU. Growth, however, will be lower than we have experienced recently. As a result of this there is a need for a marked reduction in the rate of growth in current expenditure. The percentage increases which we have been accustomed to will not be feasible. We must nonetheless, continue to protect vulnerable groups in society. It is also essential to maintain the rapid growth in capital expenditure.

Fifty years ago, Ireland was one of Europe's poorest countries. Policy makers of the time mapped a route that laid the foundations for economic prosperity. The key to the policy was openness to trade and international competition, the attraction of foreign investment and an emphasis on education. Ireland's recent success is due to the hard work and skills of our people facilitated by supportive policies. The idea that Ireland's success is unwarranted or unsustainable is a fallacy, although the economic context is now more difficult and risks remain.

Against this background it is essential to implement sensible and evolving economic policies and with our skills and flexibility continuation of success is feasible. We have an awareness of what we have achieved and the commitment to ensure we maintain these successes. The achievements made will not be overturned by sectoral readjustments in the economy or by moderation in Ireland's exceptional growth rates.

While we must not underestimate the task of ensuring that our economic success continues, I want in this Indecon Public Policy Lecture to focus not on short term economic forecasts but rather on what I believe are new challenges and priorities for future economic policy in Ireland over the coming decade.

Challenges of Productivity, Equity and the Environment

Three priorities which I believe we must put more focus on over the next ten years are productivity, equity, and the environment in which we live. As a nation we must now use the basis of our recent success to make significant progress in these three areas. My objective is to work to ensure that by the 100th year of commemoration of 1916, Ireland will be a country at peace which is characterised by very high productivity, enhanced equity and one in which we promote and safeguard our environment. The scale of these challenges are comparable to those which we have faced in other areas and we must begin to ensure what ought to be is achieved.

We need to treat the tasks of increasing productivity, enhancing equity and improving our environment with the same commitment that we tackled the objectives of peace, full employment and the prevention of forced emigration.

These ambitions will not be realised by running down what has been achieved or by regarding a slower growth rate as amounting to the collapse of the economy. This is not to suggest that short term growth will be as rapid as in previous years and this is no time for petty political point scoring, no time for a lack of self-belief and no time to expect the Government on its own to achieve our ambitions. The ambitions for Ireland I believe should include securing the fastest growth in productivity of any EU country, while also increasing equity and an improvement in the environment. These may appear idealistic but I do not apologise for this and working towards achievements of ideals is the only way we can enhance our economic success.

In this paper I would like to focus in particular on two of these three priorities, namely accelerating productivity and equity, but I would like to reinforce the importance which we need to attach to the environment. We need a determined set of integrated policies to improve our environment. These will need to address not only our physical environment and Ireland's commitment to reducing the CO_2 intensity of the economy, but will also need to address other aspects of the physical and social and built up environment which influence our daily lives. These include crime, health, education, planning, transport, architecture, recreational facilities, social integration and the numerous other factors in our environment which influences our experiences. These require innovative and ambitious policies and will influence the type of society we establish by 2016. I, however, intend in this paper to focus in detail on the other two priorities of accelerating productivity and improving equity. Success in these areas will assist in enhancing our environment.

2 Productivity

The foundations of Ireland's past economic success (and previous failures) have been largely related to productivity. In the late post-war period, when Ireland was inward looking, we lagged behind other EU countries in productivity. The major EU countries enjoyed a so-called post-war 'golden-age' in productivity gains as Europe started catching up to the US. In recent years, Ireland's productivity growth in certain sectors has been truly impressive but much more is needed and an economy-wide drive for sustained and accelerated productivity growth is required.

Facilitating rapid productivity improvements in Ireland over the next decade must be a priority for economic policy. Productivity increases are the foundation for increased living standards and for the continued growth in the economy. Almost every policy area must be judged at least in part by its productivity performance impact and only in this way will the much-talked-about need for competitiveness be achieved while simultaneously increasing our living standards.

Productivity comes in two forms: labour productivity and a more complete measure of productivity which I understand economists refer to as total factor productivity. Labour productivity is total output divided by total labour input. Total factor productivity is defined as total output divided by total input. Labour productivity is in part a function of the level of capital per employee. Labour productivity growth in Ireland will require 'capital deepening' which will mean that investment must exceed the rate of growth in labour inputs. Overall increases in total factor productivity growth will require increases in scale and scope economies, learning by doing, improvements in technology and production techniques, and the reallocation of inputs from low productivity to high productivity activities. How policy facilitates this is a key challenge for Ireland.

Competitiveness is typically defined in terms of unit costs vis-à-vis competing producers in other countries. Thus competitiveness is the total quality-adjusted unit cost of production multiplied by the appropriate exchange rate, vis-à-vis the cost from competitors. Our exchange rate is outside of Ireland's control and many cost elements, such as international energy prices, are determined elsewhere. How productively we use resources must therefore be the key policy issue. The level of total factor productivity will impact directly on the total unit production cost and is essential to addressing competitiveness issues.

Both overall productivity growth and labour productivity growth have implications for Irish economy policy. All else equal, total factor productivity growth for the Irish economy would mean falling unit costs. For the internationally traded sector, a faster productivity growth compared to competitors could result in improved competitiveness. Labour productivity has similar desirable properties. Incomes and living standards can rise at the rate of labour productivity growth without compromising competitiveness or sustainability.

Ireland cannot, and indeed should not, attempt to compete on the basis of costs with low cost countries such as India or China. Our competitive advantage must lie in other areas. This will require us to increase our capital intensity in certain areas and also develop an increasingly skilled and educated workforce. Thus, capital deepening in Ireland should take the form of increased net fixed investment by both foreign-owned and domestic firms, increases in infrastructure, and increases in human capital. Our competitive advantage will also be a direct result of how effectively inputs such as capital, energy, materials and employees are utilised.

For those who think Ireland's economic success has been due solely to the expansion of the construction sector, I would point out that Ireland's economic performance has been a reflection of a rapid annual growth in productivity and we have achieved much faster growth in productivity than other EU countries. We have also achieved total factor productivity growth levels above the US.

Total Factor Productivity Growth (Per Annum)

	2000-05
Ireland	2.2
Denmark	0.0
France	0.9
Germany	0.7
UK	1.3
USA	1.7

Another measure of productivity growth is GDP per hour worked. Data on this for Ireland shows an impressive performance but there are marked variances by sector. One key issue for policy arising from this is to ensure that productivity gains are economy-wide and that productivity is not seen as simply an issue for the manufacturing sector.

Growth in GDP per Hour Worked (Per Annum)

	2000-05
Ireland	2.9
Denmark	1.0
France	1.4
Germany	1.4
UK	2.0
USA	2.2

Some sectors such as public services, transport and hotels and restaurants have shown relatively low productivity growth, while other areas such as some of the high technology sectors have shown impressive annual growth in productivity. This is influenced by the nature of the output provided and the level of capital investment and numerous other factors. Similar findings have been evident in these sectors in other countries but I believe we need to accelerate productivity gains in all sectors of the economy and policy must facilitate this objective.

In an internationally traded global economy Ireland will have to find innovative ways to build on our strengths and to focus on ways of radically enhancing productivity. A major national drive to increase productivity in all sectors of the economy will take time to realise and will require multifaceted policy actions. I believe this must be pursued with the same commitment that we as a nation invested to tackle unemployment and to secure peace in Northern Ireland.

This will include the following:

- Continuing high levels of capital investment in the internationally traded sectors
- Increasing the economic returns on investment
- Acceptance of the need for ongoing structural change in the manufacturing and non-traded traded and services sectors

- Providing an attractive environment for highly skilled knowledge employees to work and live
- Reform of the public sector
- Investment in first, second, third and fourth level education
- Maintenance of a stable public finances and a tax system conducive to enterprise and investment.

Continuing High Levels of Capital Investment

To achieve the objective of being the most productive economy in Europe with the fastest productivity growth, Ireland will need to continue with a high level of capital investment. Investment, at its most basic level, involves delaying current consumption for the possibility of increasing consumption in the future. Investment is the flow of capital into the net stocks of physical and human capital. Investment takes place because of the expected after-tax risk-adjusted rate of return it provides. Investment can be undertaken by governments, private companies, or individuals. Investment has been a significant contributor to Ireland's recent economic success but Ireland needs to invest more in a number of categories.

Ongoing high levels of Irish and foreign investment in physical capital by private firms will be essential to meet the productivity challenge. Foreign multinationals in Ireland in certain sectors display high rates of investment and high levels of capital per worker and facilitating the continuation of these high rates of investment will be a key element of ongoing policy. Irish firms, with many notable exceptions, have lower levels of capital per employee and this will need to be addressed.

In the next phase of transformation of the Irish economy, the importance of investment for economic growth and productivity cannot be underestimated. As an illustration it is worth remembering that the majority of US economic growth over a long period has been due to increased investment and the majority of productivity growth has been due to capital deepening.

Policy in Ireland will continue to provide a very attractive environment for private sector corporate investment in internationally traded activities and with the right policies the prospects for such investment remain very positive. Let there be no doubt that supportive measures for such investment will remain a feature of Irish economic policies and Ireland will never accept European or Irish proposals which could damage our pro-enterprise corporate tax regime and our ability to respond in a flexible manner as is required in an ever changing global environment. In a more general context, European Member States will not, and should not, ever agree to give up their rights to design and implement their own personal and corporate tax policies appropriate to their citizens.

We will also consider how to facilitate individual private investment in activities which contribute most to national productivity gains in internationally traded areas. Some realignment of private investment from the Irish and overseas property sector to manufacturing and international traded services and to infrastructural investments would have positive implications for productivity growth and this will be encouraged.

In addition to accelerating corporate and individual investments in appropriate capital projects, the Government, through the National Development Plan, are also committed to a high level of ongoing investment in completing the infrastructural transformation of the Irish economy. When this programme is completed, and it will be completed on time, we will see a transformation in Irish infrastructure with resultant gains for productivity.

The Government are committed to implementing the infrastructure capital projects in the NDP without delay and in this context we will consider, if necessary, whether public finance deficits are appropriate to help complete this programme. Deficits in public finances which are a result of mismanagement or of payments for current spending which cannot be afforded can be very damaging for an economy and we have plenty of lessons on this from past Irish experience. However, deficits which reflect investment in capital infrastructure which provides net economic returns can, in the appropriate circumstances, be justified to maximise productivity and the productive potential of the economy.

Increasing the Economic Returns on Investments

As well as accelerating the level of capital investment or capital deepening in the Irish economy, which will improve labour productivity, we need to focus on how to increase total factor productivity and the related issue of the economic returns on investment.

One area which I believe is particularly important in this context relates to measures to ensure value for money and effective management of public sector investments.

Maximising the contribution of Ireland's capital investment programme means that the state must secure value-for-money for the investments. I have introduced initiatives to deliver value-for-money in both current and capital programmes and it is essential that these initiatives are consistently implemented and are further developed.

These initiatives *inter alia* comprise the following:

- Full acceptance of the need to improve value for money and to ensure that every euro is well spent
- Fixed price lump-sum contracts becoming the norm
- Ex-ante evaluations, including economic cost-benefit appraisal for all projects over €30 million
- For large projects over €30 million, formalised contracts review by the Departments concerned with reports to their Minister and with provision for audit by my Department
- More vigorous competition for public sector contracts
- Additional specialised training for the Civil Service and State Agencies
- Open recruitment of a number of full-time specialists to the public sector in Capital Project Evaluation and Management
- Allocation of single individual responsibility for all major capital projects
- Better use of compulsory purchase orders
- Performance table for Government Department and State Agencies regarding the extent of project outcomes versus budgets on contract.

These and other initiatives will be vigorously implemented to maximise the productivity impact of scarce public sector resources.

Acceptance of the Need for On-Going Structural Change

A high productivity economy will necessarily involve ongoing structural change in manufacturing and internationally traded services and in other sectors. This will inevitably mean a continuous process of job turnover, gains and losses with firm closures and new start ups. No market economy can achieve sustainable growth without such continual adjustments. It is far better for us to ensure that our gains exceed our losses and that measures are taken to assist individual employees and regions that are faced with the fall-out from such change.

We also need to have a balanced view of how Ireland is performing in different sectors and to give equal prominence to new jobs created as well as job losses. Policy in Ireland has in recent years recognised the need for ongoing structural change and this must continue if we are to accelerate productivity growth. Advance planning to support employees who are faced with such job losses and to enable them to re-enter the labour market must continue to be a critical element of our policies.

Environment for Highly Skilled Knowledge Employees

Ireland has succeeded in attracting both Irish and non-Irish immigrants and in encouraging our best and brightest to remain in Ireland. This reversal of Ireland's historical brain drain is of key significance to productivity growth in an environment where highly skilled knowledge employees have numerous international opportunities. The task of providing an attractive location for skilled knowledge employees will remain a priority in our drive to accelerate productivity and to maintain our economic success. We must also work harder to unlock and harness the often as yet un-tapped potential of many of our newly arrived workers. Addressing this occupational gap will ensure that migrants are effectively employed and yield a productivity dividend for us all.

This will be reflected in flexible and appropriate education and training policies for workers, new and old. It will also be reflected in the continuation of a pro-work personal taxation system but will also require the provision of quality public services and the numerous factors related to enhancing the environment in which we work and live.

Reform of the Public Sector

Public sector productivity will also need to be a priority for Ireland over the next decade. This will impact on the cost and quality of providing services and will also impacts on the internationally traded sector. A rapid growth in productivity in the public sector will enable Ireland to secure better services and to ensure that costs are not imposed directly or indirectly on the traded sector.

I do not have much time for often ill-thought-out criticisms of the thousands of committed and talented public servants, whether they be civil servants, nurses, teachers, gardai or local authority employees. However, it is clear that if we are to accelerate economy wide productivity, ensure value for money in our public services and improve quality and access then major on-going public service reform is needed.

In my view this will require a long term and radical plan. Elements of this are likely to include:

- A universal acceptance that public services are there to serve the public
- Structural and organisational changes
- Redesign of rules on accountability and of incentives for performance
- Training and skill development
- Open recruitment for an increasing number of posts and other initiatives to facilitate interchange between public and private sectors
- No tolerance for inappropriate vested interest actions which impact on the public
- More evidence based analysis and increased adaptation of what has worked internationally
- Dilution of boundaries between departments, agencies and local authorities
- Private sector provision in certain areas where this is more cost effective
- Review of our regulatory agencies and what activity is regulated and the specific approaches used
- Focus on solutions rather than blame
- Significant cultural and value changes
- Enhanced performance measurement.

The forthcoming OECD Review of Public Services in Ireland will represent the first step in the next phase of the development of Irish public services and acceleration of productivity, enhancing quality, access and value for money must be the key targets. Delivering on these targets will be a priority focus for policy.

Investment in First, Second, Third and Fourth Level Education

High quality education is crucial for Ireland and any other country which aspires to high standards of living and high productivity levels. It is also essential to enable individuals to realise their potential. Ireland will continue to invest in education and to nurture the development of a well-educated population and continuous training and education.

In previous Budgets I increased direct and indirect funding for third and fourth level education as well as supporting significant increases in first and second level education. A high level of ongoing investment in all stages of education is a prerequisite to Ireland's continuing economic success. Repeated studies have demonstrated the importance of education in increasing national and individual productivity. All elements of the education sector must be supported and a disproportionate investment in say, universities at the expense of first and second level education, or indeed second chance adult education, would result in a very inegalitarian society. We also have, however, to recognise the special role of third and fourth level education in acquisition of technologies and in supporting the drive towards accelerating productivity growth.

Maintenance of a Stable Public Finances and a Tax System Conducive to Enterprise and Investment

Ireland has used our exceptional growth rates to effectively manage the public finances in a way which has reinforced economic prosperity.

The remarkable performance in Ireland's public finances can be best seen in a comparative context by reviewing government deficits/surplus as a percentage of GDP. While the average for the EU was a deficit in 2006 equal to 1.7% of GDP, Ireland recorded a surplus of 2.9% GDP. I expect a further surplus of the General Government Balance this year. This compares with significant deficits elsewhere in Europe.

General Government Deficit/Surplus as a Percentage of GDP 2006

Ireland	2.9
Euro Area	-1.6
EU	-1.7

Source: ECB

The successful management of our public finances can also be seen in the trend over time. This gives Ireland the ability to manage the challenges we face arising from the inevitable slowdown in revenues related to the adjustment in the construction sector.

There has also been much talk about general government expenditure in Ireland, which has increased in recent years reflecting the growth in the economy, but as a percentage of GDP expenditure has fallen over the period since 1995 and is lower than the average for the EU or Euro Area countries. Increases in current government expenditure will, however, have to be lower than in the recent past and there can be no unnecessary structural loosening of fiscal policy; but we must continue to invest in our infrastructural programme.

General Government Expenditure as a Percentage of GDP

	1995	**2006**
Ireland	41.0	34.1
Euro Area	50.6	47.3
EU	49.4	46.7

Source: ECB

While in periods of surplus we have been able to support an ongoing expansion in public expenditure with current expenditure increases last year of around 12%, in a more difficult fiscal environment continuing with such a rate of increase would be damaging for the economy and will not be accepted.

It is my intention to moderate the level of increase in current expenditure in a planned way. In that respect, I believe that the increase in current expenditure next year should come down to around 8%. In doing so, such a rate of increase will be a staging post in a continuing process of adjustment.

Looking beyond 2008, I believe we should continue to ease current spending growth towards the rate of growth in the overall economy. Even in that scenario, we will still be able to increase Government spending by a number measured in billions every year. It will be important that

Government departments and Ministerial colleagues continuously consider the relative merits of all their programmes and prioritise spending in a way which ensures that the programmes with the greatest benefit to society are the programmes which attract the greatest resources.

I wish to emphasise, however, such limits should not and will not extend to the investment arena. I have made it clear time and again that my first priority is the delivery of the National Development Plan. Its implementation in full is central to our long-term economic prospects. That is why I am planning to increase capital spending growth by a number well in excess of current spending growth and in 2008 I believe that we can prudently allow for growth in investment of the order of 12.5%.

The Pre Budget Outlook confirms that we will be providing for a moderate deficit next year. I believe it is right to maintain capital expenditure at planned levels even in the face of below-trend economic growth. In the past, capital investment always bore the brunt of fiscal restraint when the economy was growing at less than its potential clip. Cutting back on investment might have been the politically easy option but it was the wrong choice for Ireland. To cut back on our capital programme in 2008 would be damaging to productivity and the underlying growth trends in the economy and I do not intend to do so.

The trends in general government debt in Ireland also reflect careful and prudent economic management. General government debt as a percentage of GDP has fallen from 31.2% in 2003 to 24.9% in 2006. The 2006 figure compares to 61.7% for the average of the EU and 68.8% for the Euro Area. Short term developments must be placed within this context.

General Government Debt as a Percentage of GDP

	2003	2004	2005	2006
Ireland	31.2	29.7	27.4	24.9
Euro Area	69.2	69.6	70.5	68.8
EU	61.8	62.2	62.9	61.7

The low level of government debt in Ireland in recent years has given us the freedom to be able to manage the slower growth in revenue without the crippling costs of high borrowing and our financial strength will continue to enable us to invest significantly in infrastructure. While private sector debt in Ireland has increased, this reflects the favourable environment for investment and the growing wealth and asset accumulation of the private sector. In considering private sector debt it is essential to take account of the rising ratio of net household assets to GDP. In framing economic policies for the next decade, there should be no doubt that the maintenance of stable public finances will remain the cornerstone for Irish economy policy. This will also be accompanied by a tax system which will remain conducive to enterprise and investment. Both of these are essential to our aim to secure the fastest growth in productivity within the EU.

In managing our public finances we have not in the past and we will not in the future plan the public finances around the assumption that tax receipts from the property and wider construction sector will continue to grow in future years as they have done in the recent past. It is important to put the increased contribution from stamp duties and capital gains tax in context. The Budget forecast of the yields from stamp duties and capital gains tax combined, in 2007, represent about 15 per cent of tax revenues overall. In contrast the "big four" taxes – VAT, Income Tax, Corporation Tax and Excise Duty – were expected to account for close to 85 per cent of total tax revenues this year.

It is important to point out that the property related taxes are not the only taxes which have been growing strongly. In the period 2001 – 2006 Income Tax increased by just over €3 billion and Corporation Tax by just over €2.5 billion. These are indications of a strong economy – more people in work and more companies returning healthy profits. Available resources will of course be more constrained due to the revenue decline related to the adjustment in the property sector.

In addition, keeping day-to-day expenditure within affordable levels is and will remain the cornerstone of Irish policy. Similarly, in tighter economic environment it is unrealistic to expect the type of tax cuts which have been a feature of recent years and only taxation reductions which are consistent with the prudent management of the economy will be considered. Interest groups seeking changes in our tax system which would reduce tax revenues at this time must recognise that such actions would not be appropriate. The priority of any changes in taxation must be to ensure that we target our efforts where the need is greatest. This brings me to the priority challenge of enhancing equity.

3 Progressing Equity

The way in which our resources are distributed must meet a shared concept of legitimacy if Irish society is to work together to become the European economy with the highest productivity growth. Of course differences will exist arising from variance in hard work, talent, skills and other factors. In financing economic policies for the next decade I want to signal that more will be done to ensure equality of opportunity. The ending of inequality of opportunity is a legitimate objective for the Irish Republic over the next decade and policies will need to be adjusted to give reality to this ambition. A Republic is a country where citizens come together to agree the rules under which the Government are mandated to advance all individual interests equally. The sustainable enhancement of these interests require gains in productivity which can best be achieved by market forces, but while markets work, they don't work perfectly for everyone. There have been major gains in improving opportunity in recent years but we need to move to a position of full equality of opportunities. Even when we do this it may not guarantee equality of outcomes. While we have achieved a remarkable rising tide of economic activity, it has not lifted all boats by the same amount, nor done so equally between individuals, different socio-economic groups or between regions.

Severe poverty has, however, been radically reduced and socio-economic mobility has been increased. The creation of a full employment economy has been a major contributor to the marked advances in equity. However, areas of poverty and social exclusions remain and equality of opportunities has not been achieved.

To further enhance equity we need to pursue a wide range of policy measures. These include:

- Maintenance of public expenditure on health and education;
- Address areas where existing systems have failed individuals or certain groups particularly in terms of access to services;
- On-going priority to tackling inequalities faced by citizens with disabilities or vulnerable groups;
- Keeping those on minimum wage from the tax net;
- Reform of the taxation system to remove inequalities;

- Mechanisms to support working families and individuals on low incomes.

Maintenance of Public Expenditure on health and Education

As a nation we cannot progress equity without ongoing public investment in areas such as health and education which impact on our most vulnerable citizens and also the prioritisation of measures such as targeted pre-school education. Government spending on health and education will be protected in the forthcoming and subsequent Budgets to the extent feasible within public finance constraints. We need, however, to ensure that value-for-money is obtained for the very significant investment which is being made and that our systems support high productivity. Ensuring that more expenditure is translated into higher standards will remain a key challenge for policymakers and this will require an acceleration in productivity gains.

Address Areas where Existing Systems have Failed

Ireland's health, education and other systems have sometimes failed to meet the expectation of individuals or certain groups in obtaining appropriate access or quality of service. While millions have benefited from our public health and education expenditure, we need to address weaknesses in our systems where access has been inappropriately delayed or denied. Sometimes this can be a result of unfortunate human error but it can also be due to systems which have not adapted or to vested interests. Enhancing equity will require innovative and determined policies to address such issues.

We also need to be intolerant of a failure to secure universal secondary education and this needs to be a priority for the next decade. Supporting those who have been left behind in terms of literacy or other basic rights in our educational system must also be given increased attention. Similar initiatives are required in other areas.

Inequalities faced by Citizens with Disabilities or Vulnerable Groups

In all my previous Budgets I have ensured that our most vulnerable groups are protected. Citizens with disabilities had historically been left out in the prioritisation of expenditure and taxation charges and the process of reversing this will remain a priority. Ways to remove the inequalities faced by individuals with disabilities or those faced by other vulnerable groups will be a major challenge but one which we must address.

Reform of the Taxation System to Remove Inequities

Consistent with the Programme for Government I will be setting up a Commission on Taxation and I expect it to be up and running next year. This commission will consider the efficiency of our tax system but I also intend that it will identify reforms needed to remove remaining inequities in the tax system.

In all of my Budgets I have been addressing the need to review and evaluate existing tax incentives and other aspects of our tax system. In this regard, I have introduced a cap on total allowances which limit the amount any individual can claim from tax incentives and have discontinued certain incentives that are no longer needed. The impact of this will be increasingly seen over time. The focus of changes in the tax system to remove those on lower incomes which I discuss below and the targeting of tax reductions on those on the standard rate of tax have resulted in significant improvements in the equity of the tax system and this is an ongoing challenge.

Removal of Those on Minimum Wage From Tax Net

In the past individuals on very low incomes in Ireland faced personal tax on these incomes. While this situation still applies in some other countries, it has been addressed in Ireland. This has removed disincentives to work and is justified on equity grounds. In forming recent Budgets the Government were determined to remove as many individuals as feasible from the tax net and we have succeeded in being able to apply a zero tax on individuals who had incomes equal to the minimum wage and have been able to maintain this policy even with increases in the level of the minimum wage. Keeping those on the minimum wage out of the tax net will remain a policy objective.

Mechanisms to Effectively Support Working Families and Individuals on Low Incomes

It is recognised that even when one removes individuals from personal tax, there may be a case for providing other public expenditure supports if they are on very low incomes and do not benefit from tax credits. While some have suggested refundable tax credits these can have significant problems and may not be the most efficient means of equity optimising our tax policy. There is, however, a challenge for policymakers to find other mechanisms to effectively support those on low incomes.

Measures to enhance economic-wide productivity will be assisted by the indirect impact on increasing incomes, but in my view, it will be appropriate over coming years to consider other mechanisms. These could include reforms of the Family Income Supplement Scheme or other initiatives.

4 Conclusion

Since the late 1950's Ireland has come a long way economically. By almost any measure, Ireland has transformed itself from a poor, inward looking country to one of the world's most vibrant and dynamic economies, with high living standards and high rates of growth. This success, achieved over many years and not without missteps, is grounded on sound economic fundamentals.

While the Irish economy continues to enjoy success and still is growing strongly, today's economic horizon presents us with considerable economic challenges for the future continued prosperity improvement of the nation. The openness of the Irish economy means that we must be more careful and plan for the future with great care. The future of Ireland holds so much promise but much remains to be achieved.

Countries which are skilful in economic management will benefit their own citizens and also provide models which other countries can follow. Ireland intends to continue to show leadership in this area and to advance a model designed to accelerate productivity growth.

Ireland's institutions will need to evolve and to be embedded in a social and political context which prioritises productivity, while also promoting equity and the environment. This will be essential to the next phase in the transformation of the Irish Economy.

Ireland has distinct competitive advantages including our geographic location (although sometimes this was seen as a disadvantage). Our advantages include proximity to other wealthy nations, our membership of the European Union, our educational infrastructure, our English language speaking population and our history of openness to trade and investment over the last 50 years. The record of inward investment in high tech manufacturing and services sectors, our ability to be flexible, our pro-enterprise taxation system and most importantly the skills and imagination of our people are also competitive advantages. Another advantage is our relationships both within Ireland and internationally although these are often undervalued. More work will be needed to maintain and develop

Ireland's international and commercial relationships and innovative ways to re-enforce links with the Irish diaspora merit consideration.

As a nation, we need to build on our traditional values of co-operation, trust and support to develop the most productive economy in Europe and to use this productivity to support equality of opportunity. This is the challenge for Ireland for the next decade. Irish people have shown an ability to adapt and we need to find the mechanisms to ensure that people operate in a way that promotes productivity.

Ireland in 2007 is one economically, which I imagine, the founding fathers of the State would have been proud of. They would have applauded many of Ireland's economic achievements but I also imagine they would instruct us now to think of what remains to be done for all our people.

Thank you for your attention.