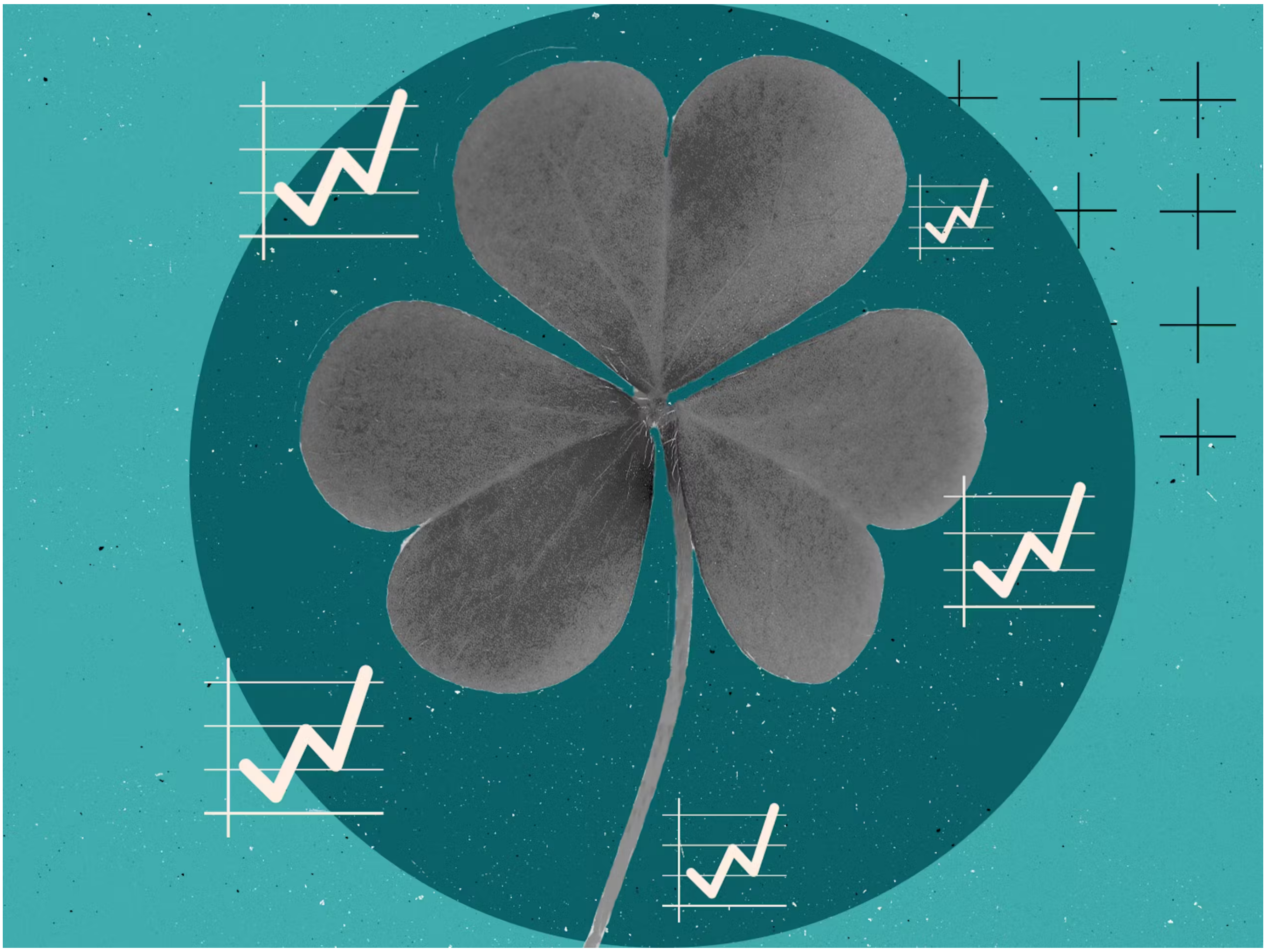
Miracle growth Irish economy does have an asterisk*

Joost Dobber

Ireland is recording sky-high growth figures and has so much money left over that it wants to set up a state fund. American multinationals are the engine of success, but they also make the economy top-heavy.



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In brief

- Ireland is posting economic growth rates that are much higher than elsewhere in the Eurozone.
- The American multinationals that have settled in the country are distorting the figures, but they are also driving the economy.
- There is so much extra tax revenue that Ireland now wants to set up a state fund.
- But dependence also makes the country vulnerable.

Ten words are enough to understand the success of the Irish economy: Apple, Microsoft, Google, Pfizer, MSD, J&J, Facebook, Intel, Medtronic, Coca-Cola.

The presence of these US multinationals has pushed Irish growth figures to un-European heights in recent years. No less than 12% was added in 2022, after Ireland's GDP had already grown by 13.6% a year earlier. A slightly more modest 5.6% is expected for this year. Still impressive, compared to the 1.1% subscribed for the eurozone as a whole.

In fact, the economic prosperity is so extensive that at the beginning of this month the Irish government presented a plan to set up a state fund, filled with the tax payments from US tech and pharmaceutical companies. At the same time, the tech giants are throwing the Irish economy off balance, at a time when it is already struggling with a serious housing crisis and a shortage of staff.

Vulnerable under the hood

"At first glance, you could say that our public finances are in a *sweet spot* ," said Treasury Secretary Michael McGrath of the curious economic situation in his country. "But dive under the hood, and it becomes clear that the vulnerabilities are piling up."

That story is mainly told by the development of Irish corporate taxation. At 12.5%, the Irish rate is very attractive, which is why those large American firms have settled on the island in the first place. The tech and pharma boom of recent years has exploded revenues for Ireland's treasury. So much so that corporate tax has overtaken VAT and has now become the second largest source of revenue after income tax. The aforementioned ten companies accounted for €13 billion last year, or 57% of the total.

Ierse belastinginkomsten | Groei vennootschaps

Multinationals worden melkkoe

Aandeel diverse belastingen in totale opbrengst (%)

Vennootschapsbelasting Accijns BTW Inkomstenbelasting Overige

That feeds a debate about how representative those spectacular Irish growth figures really are. When Apple decided to store its intellectual property in its Irish company in 2015, Ireland's GDP promptly skyrocketed by 25%. ' *Leprechaun economics* ', Nobel Prize winner Paul Krugman judged, after the leprechaun-like creature from Irish folklore.

"Our figures are rather distorted by the phantom exports of the multinationals," says founder Mark O'Connell of *foreign direct investment* consultancy OCO Global. “If Microsoft chooses to post a large amount of revenue to its European headquarters in Dublin, it will have zero effect on the Irish economy in the sense that there is no Irish productivity involved. But it will be in the Irish books.'

Highly paid

For that reason, the miracle growth comes with some caveats. Literally with an asterisk even, because the Irish prefer to avoid using GDP and opt for 'deglobalised' indicators such as gni* (adjusted gross national income) or mdd (adjusted domestic demand). In any case, Ireland is doing well, because the mdd also reached +8.2% in 2022.

"Too many people conclude that it's all about intellectual property that kind of goes around the world and isn't real," central banker Gabriel Makhlouf felt compelled to defend his country in the Financial Times. 'But that's not right. This happening, especially in pharma, is *made in Ireland* .'

The fact is that the multinationals certainly do not only contribute to the economy through corporate taxation; they also provide roughly 10% of the jobs. “There is a lot of real economic activity in the multinationals and it is also highly paid,” says economist Kieran McQuinn of the Economic & Social Research Institute (ESRI) in Dublin.

He points to the development of unemployment as an indication of the strength of the Irish economy. It rose during the pandemic, but then quickly fell again. "Now it is below 4%, which in fact has not happened since time immemorial."

Limits of growth

At the same time, this low unemployment is one of the signs that the country is reaching the limits of growth. The labor market is very tight and that makes it difficult for employers to find staff, especially if the multinationals offer high salaries. "The fear is that local companies will be forced out of the market because they cannot compete with the multinationals for personnel," said Davy chief economist Conall Mac Coille.

Add to that the fact that Dublin and the rest of Ireland are facing a major housing shortage, a legacy of the financial crisis, when Ireland nearly collapsed from its property bubble. This led to a devastation in the construction sector, which the country has still not recovered from. It has made Dublin a very expensive city, where students and workers from outside the tech, pharma and financial sectors are left out.

It leads to social discontent, which the left-wing opposition party Sinn Féin cleverly capitalizes on. In the 2025 elections, the party looks set to become the largest for the first time. That would be a landslide in a country where the conservative centre-right has always ruled the roost.

Still, the social problems are mainly a "symptom of Irish success," says chief economist Dermot O'Leary of brokerage Goodbody. 'The very favorable tax climate is an important reason for this, but there is more to it. Ireland has put a lot of effort into aligning universities and the labor market so that it is clear what skills will be needed in five years' time. And of course we benefit from the fact that there are so many high ranking Irish emigrants in the US.'

Another advantage: since Brexit, Ireland has been the only English-speaking EU country, making it an ideal entry point for Americans into the European market.

State fund

High corporate and income tax payments are expected to result in a budget surplus of €10 billion this year, plus another €16 billion next year. In an overheating economy, that money can't be spent without driving up inflation, and anyway the lineage of a handful of multinationals is too shaky to budget the money. That is why the government wants to set up a state fund of about € 65 billion in the coming years. This can then be used to absorb the effect of the expected increase in pension costs later this decade.

For example, the country that almost succumbed to the dominance of the banking and real estate sectors in 2008 is wary of renewed concentration risk. "I don't need to explain to you that when you're so dependent on a handful of companies, there's a vulnerability there," said O'Connell of OCO Global. 'If the fortunes of these multinationals turn, we will just be in a completely different situation. That is why it is important that Ireland focuses on developing local entrepreneurship, which fortunately the government also recognizes.'

Ireland already got a taste last year, when the big American tech companies implemented large rounds of layoffs. About 3,000 jobs also disappeared in Dublin, although plenty of staff are now being hired again.

A potentially greater threat is the Organization for Economic Co-operation and Development's (OECD) plan to introduce new global corporate tax rules, including a 15% minimum rate. "That new minimum shouldn't be a problem if it's introduced worldwide, and could even increase yields," says Esri's McQuinn. "But if the rules are tightened that profits must be made in the places where turnover is achieved, that could have a significant impact."