MULTINATIONAL COMPANIES AND ECONOMIC DEVELOPMENT: ASPECTS OF THE IRISH EXPERIENCE

T.A. Boylan and M.P. Cuddy*

The rapid growth of foreign direct investment has become one of the most controversial topics of debate in recent decades. The problem at the technical level is that economic theory to date has been unable to provide a unified theory of the multinational firm. Consequently the theory of the multinational firm remains effectively an eclectic one, drawning largely on two branches of economic theory, industrial organization and international trade theory, respectively. But the behaviour of international investment through multinational firms impinges on most areas of economic behaviour, and at times well outside the economic realm. Consequently, restricting the conceptual perspective for examining the multinational firm to industrial organization and international trade does not convey the full extent of the 'eclecticism' actually involved.

In addition to the absence of a unified theory of the multinational firm there is the larger perspective of the contribution of foreign direct investment to overall economic and social development. From this perspective the behaviour of the multinational firm remains one of the most emotive topics within the realm of public policy discussion, and negotiating this ideological mine-field is extremely hazardous. This paper neither attempts to synthesize the extraordinary disparate literature on foreign direct investment nor to arbitrate between the conflicting ideological views of the multinational firm. Its aims are altogether more modest. The central objective is to provide an economic overview of foreign direct investment in the Irish economy, followed by a more speculative discussion of what we deem to be the more significant issues viewed from an economic perspective. By way of historical perspective we provide a brief account of the background to foreign direct investment in Ireland. The structure of the paper reflects these objectives.

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*The authors are, respectively, Lecturer and Professor in the Department of Economics, University College Galway.

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Major Phases of Foreign Investment

Three phases of investment by foreign firms in Ireland have been identified by O'Malley (1986). The first phase was up to 1950 when firms located in Ireland to sell to the Irish market which then enjoyed considerable protection from outside competition. The second phase was between 1950 and the late 1960s. These firms specialised in "technologically mature" products which were labour intensive and did not require contact with advanced industrial areas. The third phase which commenced in the late 1960s and still continues, involves newer and more technically advanced products. The fact that they lack many of the key technical and business functions has given rise to significant discussion in the Telesis Report (1982) and its aftermath. The foreign firms in Ireland today are dominated by those which belong to the set which forms the third phase.

Nationality and Employment of Foreign Firms

There are 883 foreign firms in Ireland employing 78,000 persons or 42% of total manufacturing employment (Table 1), with U.S. firms being the most significant in terms of numbers and employment, accounting for 46.6 per cent of total foreign employment. The U.K. and W. Germany are in second and third position, respectively. These three countries account for 76 per cent of employment by foreign firms in Ireland. There has been a significant shift in the structure of foreign firm employment since 1973. This reflects the changing circumstances and the domination by U.S. firms of the third phase of foreign firm location in Ireland referred to above. In 1973 the U.S. accounted for only 25.3 per cent of foreign firm employment while U.K. firms employed 45.7 per cent of the total.

Although the net job increase in foreign firms since 1973 has been only 19,000 the gross increase has been considerably more. Between 1978 and 1984, for example, the total job gains in foreign firms was 55,600.

Table 1: *Foreign Firms by Nationality and Employment, 1985*

Nationality	No. of Firms	Employment	% Employment
United States	327	36,000	46.6
United Kingdom	202	14,000	17.9
West Germany	129	9,000	11.5
Netherlands	38	3,000	3.8
Sweden	26	2,000	2.6
France	23	1,250	1.6
Japan	9	1,200	1.5
Other	129	11,150	14.2
TOTAL	883	78,000	100.0

Source: White, P., 1985

Consequently there have also been very significant job losses in foreign firms. Since 1981 job losses have exceeded job gains by 5,000. This volatility of employment by foreign firms has always been viewed with concern. However, when the losses exceed the gains there must be cause for alarm.

Sectoral Employment

Foreign firms, although engaged in a wide range of sectoral activities, are concentrated in a small number of sectors which they tend to dominate. These are the sectors producing the newer and more technically advanced products. At present 46 per cent of total foreign firm employment is in the metals and engineering sector and it accounts for 61 per cent of employment in that sector. Within metals and engineering, foreign firms account for 90 per cent of total employment in the computers and office machinery sub-sector; 74 per cent in electrical engineering and 94 per cent in instrument engineering.

Chemicals and artificial fibres is another high technology area which is dominated by foreign firms and which accounts for 74 per cent of employment in that sector.

Interestingly, footwear, which is a more traditional sector is also dominated by foreign firms (74 per cent of employment), while food,

Table 2: *Numbers Employed by Foreign Firms and as a Percentage of Total Employment by Sector, 1985*

Sector		No. Employed		% of Total	
Metals & Engineering			35,900		61
of which:	Computers & Office Machinery	11,018		90	
	Electrical Engineering	8,610		74	
	Instrument Engineering	7,064		94	
	Mechanical Engineering	3,307		52	
	Motor Vechicles & Parts	2,214		58	
	Metals	756		68	
	Other	2,931		13	
Chemicals and Articifical Fibres			8,989		74
Footwear			1,166		73
Rubber Products			1,721		86
Food			6,350		17
Textiles			4,300		39
Other			19,574		18
TOTAL			78,000		42

Source: Derived from Table 1, White, P., 1985. Table 2, O'Malley, E., 1986 and Central Statistics Office 1986.

another traditional sector has only 17 per cent of its employment in foreign firms.

Direct Contribution to Economic Activity

The results of a survey carried by the Industrial Development Authority (1985) of manufacturing firms provide an important source of information to evaluate the contribution of both foreign and Irish firms to economic activity in Ireland. The survey covering the 1983 accounting year included all manufacturing firms having more than 30 employees. The population survey accounted for 86 per cent of manufacturing employment with 76,000 employed by foreign firms and 96,000 employed by Irish firms. That is, the ratio of foreign to Irish firms employment was 0.79.

The gross output per employee is about 11 per cent higher in foreign than in Irish firms with foreign firms producing £4.5 billion and Irish firms producing £5.2 billion worth of output (Table 3). A more accurate

Table 3: *Gross Output, Gross Value Added and Wages and Salaries for Foreign and Irish Firms in Manufacturing Industry, 1983*

	Foreign	Irish	Foreign/Irish
	(£m)	(£m)	
Gross Output	4,549	5,190	0.88
Gross Value Added	1,627	1,327	1.23
Wages & Salaries	738	978	0.75

Source: Derived from Table 1 and Appendix II, Industrial Development Authority, 1985.

measure, however, of the contribution to economic activity is value-added and here we see that the contribution of foreign firms is significantly greater than Irish firms. The ratio of foreign to Irish firms gross value added is 1.22 despite the fact that the employment ratio is almost the exact inverse of this. However, recognising the fact that a very large percentage of profits, and perhaps even cash flow, is repatriated by foreign firms, the wage and salary payments are a more accurate measure of direct contribution to economic activity. Here we see that the contribution by manufacturing firms to wages and salaries is generally in proportion to their employment share. It is interesting to note, however, that despite the predominiance of foreign firms in what may be called the high technology sectors, requiring, by implication, a higher level of skill from its labour force, the average wage paid by these firms is approximately five percent below the average wage paid by Irish firms. This perhaps is partly explained by the absence of some of the more highly paid technical and business functions from the foreign subsidiaries located in Ireland.

Inter-Industrial Linkage

One of the most significant differences between foreign and Irish firms is the level of inter-industrial linkage. Despite having a level of gross output which is only 12 per cent less than Irish firms, foreign firms purchase only one-third the amount of Irish raw materials (or intermediate product) purchased by their Irish counterparts (Table 4). This arises from the fact

Table 4: *Linkage of Foreign and Irish Manufacturing Firms, 1983*

	Foreign Firms	Irish Firms	Foreign/Irish
	(£m)	(£m)	
Irish Raw Materials	745	2,379	0.31
% of Total Raw Materials	0.36	0.77	
Irish Services*	526	732	0.72
% of Total Services	0.63	0.93	

Source: Derived from Table 1 and Appendix II, Industrial Development Authority, 1985.
*Includes fuel and energy.

that they purchase only 36 per cent of their raw material requirements from Irish firms compared with 77 per cent in the case of Irish firms. Here tremendous potential exists for the expansion of these linkages which is a major concern of current industrial policy. Raising inter-industrial raw material purchase by ten percentage points would translate into an additional £206m in actual purchases.

There is considerably less imbalance between foreign and domestic firms in the purchase of Irish services. Foreign firms purchase £525m worth of Irish services which is £53m less than might be expected on the basis of employment share. However, foreign firms spend about 20 per cent more on services in total than Irish firms. However, they purchase only 62 per cent of their services in Ireland compared to 93 per cent by Irish firms. Again there exists the possibility to exploit more successfully the service needs of foreign firms. This might be more difficult however, since much of these service payments are to other subsidiaries or to the parent companies in return for a technical or business function contribution.

Contribution to Trade and the Balance of Payments

One of the most controversial topics in recent times in respect to foreign firms has been in relation to their contribution to exports and the balance of payments. On the face of it, it would appear that foreign firms make a very substantial contribution to exports, £3.7 billion in 1983, which is over twice the contribution made by Irish firms (Table 5). However, imports by those same firms is 44 per cent of exports, leaving a net trade balance of £2.1 billion. It is interesting to note that this ratio of imports to exports also holds for Irish firms. Although this common ratio is

Table 5: *Net Trade and Net Foreign Balance for Foreign and Irish Manufacturing Firms, 1983*

	Foreign	Irish	Foreign/Irish
	(£m)	(£m)	
Gross Exports	3,730	1,765	2.11
Imports	1,651	752	2.19
Net Trade Balance	2,079	1,013	2.05
Profits Repratriated (Maximum)	731	—	—
Net Foreign Balance	1,348	1,013	1.30

Source: Derived from Table 1, Chart 7 and Appendix II, Industrial Development Authority, 1985.

coincidental it does suggest a way of approximating the degree of transfer pricing practised by foreign firms. It might be expected that having adjusted for production mix and the export share of total sales that the two ratios would be approximately equal. Deviations away from this would indicate the degree of transfer pricing being practised.

It is true that much of the profits accruing to foreign firms is repatriated. If the maximum for 1983 which was £759m (the actual amount appearing in the balance of payments for 1983 was £625m) was repatriated this would leave a net foreign balance of £1,318. This is the net current contribution of foreign firms to the earnings of foreign currency which is paid to Irish labour and for goods and services produced in Ireland. It is in fact 30 per cent greater than the net foreign earnings of Irish manufacuring firms. This contribution by foreign firms to the Irish economy is extremely significant and indisputable.

The Regional Impact of Foreign Firms

The regional distribution of employment in foreign firms follows fairly closely the urban hierarchy. The East region which includes Dublin has one third of foreign firm employment (Table 6). The South-East, which includes Cork, has the second highest percentage, while the Mid-West, which includes Limerick, has the third highest percentage. Nevertheless, there has been significant dispersal to the less urbanised regions. The policy to regionalise industrial employment has depended very heavily on the dispersal of foreign firms. Foreign firms account for the highest percentage of total manufacturing employment in those regions which showed the fastest rate of growth in industrial employment over the past 20 years. Thus the Mid-West, West and North-West regions have the heaviest dependence on foreign firms for their total employment.

Table 6: *Employment by Foreign Firms and Percentage of Total Manufacturing Employment by Region, 1981*

	Numbers	% of Total
Donegal	1,054	16.1
North-West	2,287	46.8
West	7,344	48.1
Mid-West	10,798	52.6
South-West	14,032	37.3
South-East	7,295	25.3
East	28,171	30.1
North-East	6,684	36.8
Midlands	5,463	36.7
Ireland	83,128	34.6

Source: O'Suilleabhain, M., 1982.

The heavy dependence of a region on foreign firms has some immediate implications. There is first of all the stability of employment, particularly in situations where the firm has limited its operations to an assembly type operation. Secondly, there is the impact which these firms have on generating regional economic activity through the purchases of production materials and services. It is clear, first of all, that where there is a heavy concentration of foreign firms in a region there will be a low level of these purchases because of the generally low level of inter-industrial purchases in Ireland by such firms. But it is also clear, however, that those less developed regions which have experienced recent industrialisation have a lower capacity to capture those linkages than the more developed regions. For example, while the chemical and metals and engineering sectors, which are dominated by foreign firms, spend an amount equal to 27.0 per cent and 25.3 per cent of total sales, respectively, on the purchase of materials and services in Ireland, generally, the picture is quite different at the regional level (Table 7). Purchases by the chemical sector is only 2.0 per cent of sales in the North-West region and 5.5 per

Table 7: *Inter-Industrial Linkage in West,[1] Northwest[2] and Ireland[3] in Chemical and Metals and Engineering Sectors*

	North-West	West	Ireland
Chemicals	0.020[4]	0.055	0.270
Metals & Engineering	0.088	0.194	0.253

[1]1980 Source: Boylan, T. and Cuddy, M. (1983)

[2]1983 Source: Cuddy, M. (1986)

[3]1983 Source: Derived from Industrial Development Authority (1985) and Central Statistics Office (1983).

[4]Proportion of total sales.

cent of sales in the West region while purchases by the metals and engineering sector is 8.8 per cent of sales in the North-West and 19.4 per cent in the West. It is evident therefore, that the indirect effect of foreign firms located in the less developed regions is generally more important to other regions than to the regions themselves.

The examples given here highlight the fact that, despite the concentration of efforts by the Industrial Development Authority to decentralise industrial activity in Ireland, the more developed region and in particular the East region captured a substantial part of the spin-off generated in the less developed regions.

Summary and Conclusions

Foreign firms have contributed very significantly to the Irish industrial base both directly and indirectly. They employ directly 78,000 persons or 42 per cent of manufacturing employment and contribute £737m annually in wages and salaries. They dominate the more technically advanced sectors which begs the question as to whether Ireland could have participated to any significant extent in these sectors in the absence of foreign firms. It is not of course surprising that U.S. firms should be at the forefront of foreign direct investment given its technological superiority and its desire to have a foothold in European markets.

Two important indirect contributions to the Irish economy are made by foreign firms. 1 Firstly, they purchase approximately £1.3 billion of Irish goods and services into their production process. This represents a major stimulus to the Irish economy despite the fact that significant improvements can still be made in increasing it. 2 Secondly, there has been a substantial impetus given by foreign firms to technology transfer and innovation. It is difficult to quantify this latter contribution. However, through the demand for inputs into their production process specific requirements and standards have to be met by Irish firms which very often require the enhancement of technology levels and a certain level of innovation. The skills of workers in the foreign firms have been significantly enhanced. Many former employees of foreign firms now form an importtnt segment of our stock of indigenous entrepreneurs. There has also been an important "demonstration effect" on Irish firms with respect to 'best practice' in the various technical and business functions of firms. The demonstration effect has also spilled over into educational and training institutions which have responded in their programmes to the more sophisticated needs of foreign firms. 3 A final significant and very positive element has been the contribution of foreign firms to our foreign exchange. earnings; the minimum net foreign earnings being of the order of £1.3 billion per annum on current account.

This is of course 30 per cent greater than the net contribution by Irish firms to our balance of payments.

There are, however, a number of problems in relation to foreign firms. There is the question of our high level of dependency on these firms, combined with the problem of the instability of these firms' production decisions. There has been a very high rate of job turnover or a very high level of gross to net job creation in foreign firms. This ratio has been growing and over recent years has been less than one. There has been increasing competition for a decreasing volume of foreign investment world wide. Among our EEC partners we are losing ground not only on the absolute level but in our share of new foreign investment (O'Malley, 1986). This situation will become increasingly critical if the EEC continues its push towards the harmonisation of competition throughout the Community in the absence of an effective EEC Regional Policy. If the diagnosis of a shortening of the life cycle of foreign firms is correct then there will be an increasing shortfall in the net job creation by foreign firms. Can Irish firms, with their newly augmented capital and human technology, rise to the challenge of making up this shortfall?

The additional major problem with respect to foreign firms has been profit repatriation which has been ascribed the term "black hole" mainly because of identification problems in the balance of payments. The problem is not the rightness or wrongness of this activity on the part of foreign firms since they are responding to opportunity of investment or otherwise. The problem is the failure of the Irish economy to retain this potential source of investment. A certain amount is remaining in Ireland; in 1983 for example, the profits made by foreign firms was £759 million while the corresponding outflow in the balance of payments was only £625 million. There was therefore a retention or net investment by foreign firms (apart from a new firms setting up) in Ireland that year of £134 million. As to how we can attract more of this potential investment is naturally a question to which the government and the Industrial Development Authority is devoting considerable energy.

A final problem which emerges is the inherent weakness in the overdependence on foreign manufacturing industry as a vehicle for regional development. Although it is evident that the dispersal of foreign firms to underdeveloped regions has an important direct impact, it is clear also that indigenous firms in these regions have been unable to respond absolutely in meeting the linkage demands of these firms. The slowing down of foreign investment will certainly not be offset by the expansion of the indigenous firms in these regions. And the foreign firms that will locate in Ireland are unlikely to be attracted to these less develop regions given the reorientation of industrial policy and the weakening of the regional dimension of this policy. The harmonisation of EEC competition policy will have its impact even more forcefully in these lesser developed regions of Ireland. Taking these various strands together the implementation of effective regional policy at EC and national level becomes imperative for the economic survival of the less developed regions in Ireland.

Overall the contribution of foreign direct investment must be judged to have made a considerable contribution to Irish post-war economic development, both directly and indirectly. As we have demonstrated in the previous section multinational firms have contributed substantially to major aspects of our economic development, be it in industrial export growth, or net foreign earnings, or net employment creation.

Notwithstanding the overall positive view, which we have taken towards the contribution of foreign direct investment to Irish post-war economic development, three qualifying comments are warranted. Firstly, Ireland in common with most countries which have been hosts to foreign direct investment, has undoubtedly entered into a new set of dependency relationships with foreign mobile investment, where a great deal of the decision-making is totally outside our control. This calls into question the adequacy of the structures available to the nation-state to encounter and manage a process which has clearly transcended such structures. Ireland being a particular sub-species of the nation-state, i.e. a small-open economy, is particularly vulnerable in this regard. Ours may not be the dependency as articulated within third world countries, but that is surely a matter of degree rather than of kind. Secondly, it would be naive of us in Ireland to expect that multinational firms operating in Ireland would not engage in what must be regarded as normal practice for such firms. The fact that we should now belatedly regard such processes as transfer
2 pricing or repatriation of profits as problems is an interesting measure of our lack of understanding of how such firms operate. In the absence of some fundamental rethinking on the part of Irish policy makers such practices by multinational firms must be regarded as being perfectly consistent with the terms agreed with these firms from the outset. Finally, the wisdom of continuing to rely on foreign direct investment in the form
3 in which we have to-date has been called into question in the post-Telesis examination of industrial policy. The response of policy-makers in re-directing industrial policy to engage these problems will be of immense and long-term significance to the future of Irish economic development.

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