Government Intervention in the Market

Chapter 8

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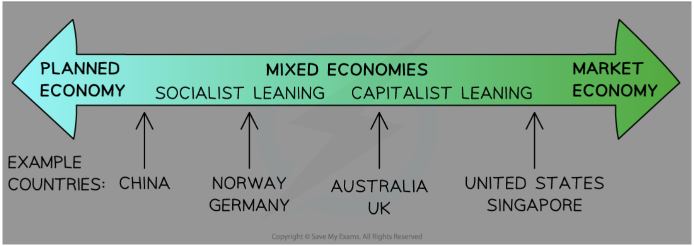
Learning Outcomes

In this chapter we will:

- evaluate the economic role of the government in a mixed economy
- evaluate how and why the government may use various interventions and incentives, such as taxation and legislation, to influence the price and quantity outcomes in particular markets
- evaluate the role and effectiveness of regulation in the Irish economy

Different Economic Systems



- **Free market/pure market economy** is one in which society's scarce resources are allocated on the basis of supply, demand and the price mechanism, with a laissez-faire or 'hands-off' approach to economic activity, leaving the production and consumption of goods and services entirely to the market.
- **Centrally planned economy** is one in which the government owns the entire means of production and is the only supplier/allocator of goods and services within the economy.
- **Mixed economy** combines aspects of both markets and government planning. The government is referred to as the public sector. The market forces make up the private sector.

Irish Economic System – Characteristics of Mixed Economy

1. **Social Partnership:** Dialogue between trade unions and enterprise allows government and partners to set targets, like moderating wage increases.
2. **Semi-state bodies and private enterprise work side by side** in areas like transport and energy. For example, Bórd Gáis Energy (a private company) operates on the national grid, which is managed by Éirgrid (state-owned body).
3. **Regulation:** Gov't regulates the private sector by setting rules and standards.
4. **Legislation:** Labour laws (like minimum wage), planning laws, Companies Acts, help to build fairness and accountability
5. **Fiscal policy** is used to achieve economic objectives (see next slide).

Objectives of the Irish Government

Create Full employment: this occurs when all those available, willing and able for work are employed in productive work at existing wage levels – exchequer benefits and living standards improve.

Sustainable economic growth: when GDP per capita increases from one year to next without fundamental change in the structure of society.

Price stability: Controlling inflation is vital in order to:

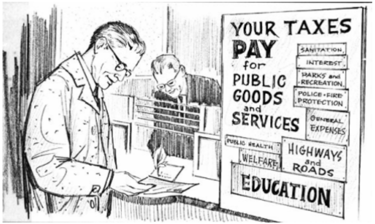
1. stable living costs,
2. moderate wage demeands,
3. maintain Ireland's international competitiveness.

Promote balanced regional development: the State wants all regions in a growing economy benefit from that economic growth. European Regional Development Fund aims to bring along all areas (esp. rural areas) which might otherwise lag behind via high-speed broadband, grants, improved access to education and training.

Environmental protection: the State imposes measures to educate, protect and preserve important natural resources.

Avoid market failure/intervene when markets fail – state steps in to allocate resources when supply and demand forces fail to do so.

How Governments Intervene in the Economy



Imposing and Collecting Taxes
A proper tax structure should shape consumer behaviour in a positive way. For example, steer demand from demerit goods (alcohol, cigarettes, sugary drinks) to build a healthier society.

Subsidising Certain Activities/Industries
Subsidies can make markets more competitive by re-allocating resources from bigger to smaller firms. However, they may distort markets & lead to inefficient outcomes.

Subsidies – Definition

Subsidies are direct payment by the state to reduce the cost of producing a particular good/service to encourage greater production of that good/service.

How Governments Intervene in the Economy

Public Provision
State companies may provide a product when there is an insufficient profit motive for the private sector, for example, Bus Éireann rural routes.

Action in National Emergency
During COVID-19, government acted quickly to enforce lockdown legislation and dispatched emergency supplies on a national level.

Redistribute Income: Measures like progressive taxation and minimum wages can help to allocate resources evenly and fairly, so everyone can benefit from economic progress.

Benefits of EU Membership to Irish Economy

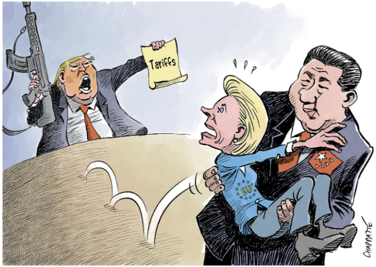
Trade Access & Export Growth
In 2023, €81billion of Irish exports were destined for EU markets; more than one-third of total exports, with the EU also accounting for over a fifth of imports Representation in Ireland. The EU is by far Ireland's largest trading partner, making up around 57.9% of exports and 60.7% of imports.

GDP per Capita Convergence
Since joining the EU in 1973, Ireland's GDP per capita has surged – from 89.5% of the EU average in 1973 to an impressive 290.2% by 2022.

EU Funding & Structural Investment
Ireland has received over €40billion in EU Structural and Cohesion Funds from 1973 to 2018, fuelling infrastructure, education, and capacity-building investments. In 1996, agricultural-related EU support amounted to about 3.5% of GDP, and the trade premium boost added an extra $\approx$ 1.2% of GDP.

Regional Prosperity
In 2024, Ireland ranked 2nd in the EU for GDP per capita at around €79,300, nearly double the EU average of €37,600. It contributes approximately 3% of EU GDP. The Eastern Midland region of Ireland stands among the richest NUTS-2 areas in the EU, with GDP per capita at approximately 245% of the EU average.

Benefits of EU Membership to Irish Economy



Sovereignty and Policy Constraints: Critics highlight loss of national autonomy due to mandatory compliance with EU regulations and directives, which can limit Ireland's ability to tailor domestic policies.
Economic Exposure and 'Leprechaun Economics': Ireland's inflated GDP – driven by multinational profit-shifting rather than underlying economic activity – has led to inflated EU budget contributions. In one notable episode, the "leprechaun economics" spike increased Ireland's EU GDP-based levy by up to €380 million per annum, before mitigation reduced that to around €280 million.
Overreliance on Multinationals & Structural Fragility: Irish economy leans heavily on US-based firms, especially in the tech and pharma sectors. An FT article notes 10 firms contribute $\frac{1}{2}$ corporate tax revenue, with 3 alone providing $\frac{1}{3}$ of that total. This poses fiscal risk if multinational activity declines.

Advantages / Disadvantages of State Intervention

Disadvantages

- Reduces entrepreneurial solutions: constant state intervention dampens risk-taking and innovation.
- Inefficient: state is spending taxpayer funds without the same incentive to maximise value as businesses.
- Bureaucratic: dealing with government departments is time-consuming and paperwork-heavy.
- Time barrier: the policy cycle is long and may delay desired outcomes.
- State workers not motivated by MRP: productivity may suffer if pay isn't linked to output.

Advantages

- Prevents monopolisation: regulation protects consumers from high prices and exploitation.
- Provision of services: e.g. Bus Éireann operating loss-making services for public good.
- Supplies public goods: State can step in to provide resources like street lights, flood defence, national security, where markets fail.
- Provides employment: the state employs people to manage and deliver services.
- Social welfare provision: ensures protection for vulnerable individuals like the elderly so they can live safely and comfortably.

Regulation & Regulatory Agencies

Regulation – Definition

Regulation is a mechanism to ensure the *safe, fair, and reliable provision* of goods and services, protecting consumer interests.
The Irish government sets up regulatory agencies to monitor and enforce these standards.

Key Agencies and Roles
Competition and Consumer Protection Commission (CCPC):

- Investigates price-fixing and abuse of dominance.
- Reviews and blocks anti-competitive mergers.

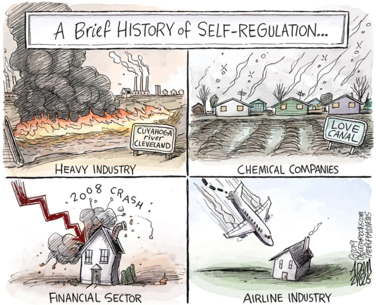
European Competition Network (ECN):

- Ensures fair and consistent application of EU competition law.

Commission for Regulation of Utilities (CRU):

- Protects energy consumers.
- Monitors gas/oil retail prices.
- Ensures fair and reasonable pricing.

Advantages/Disadvantages of Regulation



Disadvantages

Higher consumer prices: firms may pass regulatory costs on to consumers, particularly for goods which are price inelastic to demand.

Regulatory burden on small businesses: limited resources hinder compliance (e.g. small farmers).

Bureaucratic cost: the gov't owns most regulatory agencies, so taxpayers fund setup, training, and oversight of regulators.

Advantages

Public welfare: regulations ensure health, safety, and non-discrimination protections.

Ensures firm accountability: negligent firms face fines or closure.

Corrects information failure: regulators reduce asymmetry of information. General Data Protection Insurance (GDPR) can prevent insurers sharing sensitive client information.

2021 HL Paper – Q13 (b)

Explain, giving an example, one advantage of a government regulation. (6 marks)

3 marks	Clear, concise explanation
3 marks	Well developed example

Health and safety regulations
Consumers are protected from substandard and unsafe products through regulations imposed by the Irish Government and the EU.

Protects consumers from exploitation
Government regulation of large firms may help to reduce the likelihood of consumers earning large supernormal profits at the expense of consumers.

Prevent anti-competitive behaviour / growth of monopolies
Regulation can put an end to cartels between competing firms and can also assess whether or not a merger would be competitive within an industry.

Increases competition in the industry: Depending on how regulations are implemented in an industry it may lead to a reduction in the ability of firms to restrict supply and charge exploitative prices.

Environmental protection: regulations may lead to improved protection of the environment through reduced use of resources and generation of pollution.

2022 HL Paper – Q14 (c)

> *"However, the Living Wage Technical Group argued that €12.90 per hour is the minimum wage required for an acceptable standard of living."*

–Adapted from livingwage.ie

Discuss one argument for and one argument against the implementation of the 'Living Wage' €12.90 per hour as the National Minimum Wage for 2023. (8 marks, 4 + 4)

Arguments for:

Increase worker's standard of living. By providing for an increased minimum wage workers disposable income increases and their standard of living increases.

Increase the incentive to work. When workers see that pay levels are rising then it may attract more people into the workforce/help retain workers/boost productivity.

Boost economic growth. Higher incomes will mean increased spending within the economy and will help boost economic growth / employment.

Arguments against:

Increases the cost of business. Businesses and unions may argue against the implementation of the Living Wage as it would lead to an increase in their cost of production which may make it harder for businesses to survive.

Cost push inflation. Increasing the minimum wage up to the Living Wage may raise cost of production which may be passed on to the consumer in the form of higher prices.

May lead to decreased employment. Whilst more employees may be willing to work, leading to an expanded labour force, firms may decide to counteract the increasing costs through rationalisation of their workforce. This may leave fewer people employed than before the Living Wage was implemented.