



22 Business, government and the economy

Learning objectives

In this chapter you will learn about:

- 1 The role of the government in the economy
- 2 The effect of the main economic variables on the economy

How the government intervenes in the economy

- **Legislation:** By passing laws, e.g. the Consumer Information Act
- **Government department decisions**
- **Local authority actions**
- **Semi-state bodies**

The role of government in the economy

- Enforces legislation
- Environmental protection
- Infrastructure development
- Provision of services
- Redistribution of wealth
- Regional development
- Regulation

The effects of government actions on business

- **Taxation policy:** Some taxes have the effect of creating work and expense for firms, such as collecting PAYE and VAT taxes for the state. Other taxes boost business investment and profits, such as low rates of corporation profits tax.
- **Spending policy:** When the government increases spending, this creates extra demand for goods and services, which firms can benefit from.
- **Government as employer:** As the biggest employer in the country, the wages paid by the state to its employees influence the rates of pay that private businesses will have to pay to their workers.

- **Decentralisation:** Moving government offices out of Dublin to rural locations will provide opportunities for businesses in those local areas.
- **Infrastructure:** Most of the infrastructure used by business is provided by the government.
- **Government planning:** Business benefits from the publication of government plans, whether they present opportunities or challenges.
- **National agreements:** The negotiation of national agreements gives business the opportunity to influence the future direction of the economy.
- **Public-private partnerships:** These arrangements for the provision of infrastructural projects give new opportunities for private firms to build and manage major projects in partnership with the state.
- **Regional development:** Businesses in less-developed regions benefit when the state takes action to increase economic activity in those regions.
- **Industry grants:** The government provides grants to businesses for capital investment, for training of staff and for feasibility studies through a number of different agencies.

State-sponsored bodies/semi-state bodies

These are organisations that are set up, financed by and are in the control of the state.

Top Tip!

You should be able to describe how the government can create a favourable climate for business.

Reasons for state involvement in commercial enterprises

- Develop the country's **natural resources**
- Provide **essential services**
- Develop the country's **infrastructure**
- Have control of **strategic industries**
- Develop industries requiring **high capital investment**

Important state agencies in Irish business

- Bord Bia
- CIÉ
- Enterprise Ireland
- Environmental Protection Agency
- Electric Ireland
- Fáilte Ireland
- Solas
- Health and Safety Authority
- Industrial Development Authority (IDA)
- Labour Relations Commission and the Labour Court
- RTÉ

Top Tip!

Ensure that you can refer to examples of state-sponsored bodies and their role in the economy.

Privatisation of semi-state bodies

Semi-state bodies are sometimes sold into private ownership by the government.

Reasons for privatisation

- The state may wish to sell a valuable business for **cash** so that they can use the money in another way.
- The original reasons for owning the business no longer apply.
- Private owners may be better able to make the firm more **efficient** and competitive.
- State-owned monopolies must be opened up to competition, i.e. **deregulated**, under EU regulations.
- The firm may require **capital investment** that private owners would be willing to invest.
- The state may wish to **promote investment in shares** among the general public.

Economic variables and their effects on business

Inflation

- Workers **demand wage rises**, pushing up costs for business.
- Purchase **costs will rise**, increasing cost of production.
- It will be more difficult to export goods to countries with lower rates of inflation

Taxation

- Increased income tax reduces workers take home pay and result in increased pay demands on business.
- Increased income tax reduces employees' incentive to work.
- Increased VAT increases prices overall and reduces demand for goods and services.
- Taxes on business profits may cause firms to move their business location to another country.

Interest rates (higher)

- There are increased costs of running the business, if the business has loans.
- Higher interest rates reduce everyone's disposable income and reduce demand for a firm's products.
- High rates will reduce the level of new investment as entrepreneurs won't want to borrow money for new projects.

Unemployment (rising)

- Demand for goods and services fall due to low income levels in many households.
- Income taxes collected by the government fall.
- The government has to spend more money on payments to help the unemployed.
- Wage rates may go down as workers are willing to accept lower pay to get a job.
- Some workers will emigrate to find employment.

Top Tip!

Ensure that you can refer to examples of semi-state bodies and their role in the economy.

Exam question

- 1 Discuss the effects of increasing unemployment on the Irish economy.
(2011, 20 marks)

Sample answer

The **demand** for goods and services is reduced and businesses may have to close down.

As people have less **discretionary income**, people will spend on necessities but luxury items will be sacrificed. This leads to falling business profits.

Government **current expenditure will increase** as the unemployed will sign on and claim social welfare benefits.

Emigration and falling immigration/'brain drain' (exporting of skilled labour).

Government revenue/tax take will fall as receipts from major sources of taxation will fall, e.g. VAT receipts will fall as there will be less consumer expenditure.

The **social costs** associated with unemployment will increase. Unemployment leads to social deprivation, rising crime, alcoholism and drug abuse. This can lead to increased expenditure for the government on health and law and order.

Long-term unemployed can lead to a large number of **deskkilled workers**.

Marking scheme

- Four effects: 4 x 5 marks – naming effect (2) + development (3) (5 = 2 + 3)

Questions

Higher Level long questions

- 1 Discuss the different ways in which the Irish government affects the labour force in Ireland. (2010, 20 marks)
- 2 Discuss how the Irish government could use the tax system to create a positive climate for business in Ireland. Use examples to illustrate your answer. (2009, 20 marks)
- 3 Evaluate, using examples, the arguments in favour or against the privatisation of commercial state enterprises in Ireland.

Key-points!

- Effects of the government on business and the economy
- Importance of semi-state bodies
- Reasons for privatisation
- Economic variables

Key-definitions!

fiscal policy: Refers to plans of the government for the collection of taxes and the spending of those tax revenues.

inflation: Rises in price levels from one year to another.

infrastructure: Refers to systems of transport, telecommunications, electricity, gas, airports, sewage, etc. which are developed in a country.

interest rates: The cost of borrowing money, usually expressed as a percentage per annum.

public-private partnerships: Development projects that are jointly owned by the state and private companies.

semi-state bodies: Companies that are owned and controlled by the government.