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Influence of the EU (and the IMF) on domestic cutback management: a nine-countries comparative analysis

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\textbf{ABSTRACT}

The influence of the EU (and the IMF) on domestic cutback management were studied in nine European countries. In this concluding article, a cross-country comparative analysis is presented. The influence of the EU and the IMF being most evident in bailed-out countries, we first take a closer look at the loan programmes in Greece, Ireland, Portugal, and Spain, plus the hardly-known earlier bailouts in Hungary and Latvia. We then turn to two factors that influence cutbacks and reforms: economics and politics. Finally, the concept of the influence of the EU (and the IMF) is differentiated into degrees and types of influence.

\textbf{KEYWORDS} EU governance; EU and IMF influence; fiscal consolidation; cutback management; bailouts; nine-country comparative analysis; political circumstances

\section*{Introduction}

In the preceding articles of this special issue, the influence of the European Union (EU) (and the International Monetary Fund: IMF) on cutback management in nine countries in Southern, Western, and Eastern Europe – Greece, Ireland, and Portugal; Spain and Italy; Hungary and Latvia; and the Netherlands and Estonia – have been analysed by academic experts in the respective countries. In this concluding article, a comparative cross-country analysis is presented.

The issue of EU influence on domestic state affairs is nowadays highly contested, fiercely debated, and strongly politicized. A wave of scepticism about the EU has swept over large swathes of Europe. Former Communist East European countries like Poland and Hungary, which adopted a pro-Western and pro-Europe stance immediately after their independence from Soviet Russia, are reverting to a populist, nationalist, and patriotic standpoint against what they perceive as EU interference. Britain has voted in a referendum to leave the EU. In many Western European countries, nationalist populist anti-EU parties are gaining popular support. Southern European countries like Greece, Portugal, and Spain also protest against EU interference, as their bailouts resulted in harsh austerity measures, high unemployment,
and reduced living standards. In this special issue, we have investigated one particular facet of EU influence, albeit a very significant and relevant one: domestic cutbacks and reforms at the time of the crisis. How did Brussels influence cutback management by governments in the countries affected? The bailouts in Greece, Portugal, Spain, and Hungary led to massive public protest, violent demonstrations, and widespread social unrest, characterized by indignation, condemnation, defiance, and resistance. In our study, we have sought to avoid the normative, ideological, and political prejudices about country cases by presenting an empirical analysis based on facts and figures, especially an international comparative analysis. As stated in the introduction to this special issue, we hope that this empirical academic analysis of EU influence can somehow nuance the current populist prejudices about Brussels’ perceived meddling and interfering.

The central research question in our study was: What was the influence of the EU (and the IMF where applicable) on domestic cutback management?

Although the financial-economic aspects of fiscal consolidation are paramount, in this special issue we were primarily interested in the politics of cutback management – the domestic governments’ political decision-making about cutbacks and reform: How did the EU (and the IMF) influence cutback management, both in countries that were bailed out and in those that were not?

EU and IMF influence on domestic cutbacks is most obvious in countries that received loans because of sovereign debt defaults. The loans were provided on strict fiscal, financial, and structural reform conditions imposed by the EU and the IMF. In this concluding article, we first take a closer look at these financial assistances (loan) programmes, the so-called bailouts. How big were the loans, what were the loan objectives, and what were the loan conditions, relating to both fiscal and structural reform? And what were the outcomes? What were the similarities and differences, and how can these be explained? First, the fully-fledged 2010–2011 bailouts in Greece, Ireland, and Portugal are considered, plus the more restricted 2012 banking sector bailout in Spain. The earlier 2008 bailouts in Hungary and Latvia, which were not widely publicized in the Western media, are then addressed.

The factors that influence and possibly explain the cutbacks and reforms are subsequently examined. Besides the influence of the EU (and the IMF) – our main focus of interest – we identify two factors: economics and politics.

The economic, financial (banking), and fiscal situation in a country were the prime determinant of its economic and fiscal crisis in general, and sovereign debt crisis in particular. Excessively large state debt was a main cause for sovereign debt payback default, as illustrated in the Greek case. An excessive budget deficit was another main cause of the fiscal crisis, and an important factor in determining the extent of consolidation necessary. An ailing financial banking sector, holding private (household and corporate) debt, was the underlying cause of a number of debt defaults. The economic, financial, and fiscal circumstances in the run-up to the crisis are summarized and analysed across countries.

Economics alone is not sufficient to explain the crisis. Credit rating agencies, whose downgrading triggered countries’ debt defaults, explicitly take politics and government into account to estimate a state’s ability to repay debt and make timely interest payments. So, we also take a closer look at the political situation in the countries studied. We look at the party-politics during the run-up to the crisis, the negotiations with the EU and the IMF about loan programmes, and the implementation of the loan
conditions, that is, the austerity measures and structural reforms. The anti-austerity protests, the massive and often violent demonstrations, strikes, and social unrest are only briefly touched upon in this article, although the harsh, painful, and detested austerity effects of the bailouts to a large extent determine the ultimate ‘societal success’ of the financial assistance programmes. Success is not only about deficit reduction and economic growth, but also about unemployment, poverty, and social inequality.

Finally, we focus on the main point of interest in this special issue: What was the influence of the EU (and the IMF)? Degrees and types of influence are differentiated according to the degree of an economic, financial, and fiscal crisis in a country, and according to the governance instruments at the EU’s disposal (Ongaro 2014). We further differentiate the degrees of influence according to the particular political circumstances in the various countries.

The analytical framework used here is summarized in Figure 1.

The financial assistance programme

The worldwide banking crisis was triggered by the fall of Lehman Brothers in September 2008. Although some initiatives were taken in Europe towards international coordination (G-20 meeting and Euro summit in October 2008), each country addressed its own banking problems. The ensuing economic crisis that surfaced in Europe in 2009 was again managed by each country on its own; and the subsequent fiscal crisis that most European governments began facing in 2010 was tackled by each government on its own. The EU had little influence on the fiscal cutbacks and reforms at the time, except through its Excessive Deficit Procedure (EDP).

Bailouts in 2010–2012

The Greek sovereign debt crisis in 2010 could not be solved domestically. Greece had become a debt defaulter and made an appeal to the IMF for financial assistance (Featherstone 2011; IMF 2013b). Greece being a Eurozone member, the EU and the European Central Bank (ECB) were also involved (contagion from the Greek default to the entire Eurozone was a major reason for granting the loan), leading to the novel
construction of the Troika: the European Commission (EC), the European Central Bank, and the International Monetary Fund. The EU, particularly its informal leader, Germany’s Chancellor Merkel, had insisted on the IMF being involved because the Fund had ample experience and standard operating procedures for these crisis situations, whereas the EU did not. Following the usual IMF procedures, the Troika worked out a programme that defined the loan amount, the objectives, and the so-called conditionalities (Featherstone 2011; IMF 2012; Spanou 2017). The loan conditions consisted primarily of the fiscal and financial policies to remediate the deficit and banks, and of so-called structural reforms (see below).

At the end of 2010, Ireland became a debt defaulter and asked the IMF, the EU, and the ECB for help. Ireland had misinterpreted the 2008 banking crisis and given overly generous bank guarantees that proved to be so costly that the state itself had to ask for financial help. The bank crisis thus became a sovereign debt crisis (Hardiman and MacCarthaigh 2016).

Early in 2011, Portugal had to ask for financial assistance, more or less for the same reasons as Greece: the bad economic and fiscal circumstances caused the bond interest rates on the large and foreign-owned debt to rise to unsustainable levels. Portugal’s ability to refinance its debt on the financial markets had come to a halt (Araujo 2017).

A major concern during the sovereign debt crisis (also called the Eurozone crisis) was that the defaults in the smaller Southern Euro-member states would be followed by defaults in the large member states Spain and Italy. A fully fledged bailout package for these large countries would be extremely costly, maybe even impossible. In 2012, Spain asked the EU and the ECB for a bailout of its banking sector. Initially, €100 billion was held in reserved for the recapitalization, restructuring, and resolution of the banks and in the end €41.3 billion was expended, less than 4% of Spanish GDP, about a tenth of the relative size of the other three bailouts (Kickert and Ysa 2014). It was hoped that the moderate-sized help would be sufficient. The Spanish bailout concerned only the banking sector; nevertheless, the EU enforced the conditionality that Spain should fulfil the European Semester requirements (fiscal and structural reforms) (Badell and Ysa 2017).

### Loan size, objectives, and conditions

Table 1 summarizes the key elements of the loan programmes (bailouts) in the Eurozone in 2010–2012. The key elements are now compared to reveal the similarities and differences.

The (relative) size of the loan programmes (as a percentage of GDP) was rather similar, initially. That changed when Greece did not succeed in exiting the loan programme and needed a second loan in 2012 (and a third in 2016, not covered in the table). The Greek debt has by now become so unsustainably high that the IMF is proposing debt restructuring (writing-off loans) (IMF-IEO 2016), but the EU (with Germany and the Netherlands to the forefront) is currently strongly opposing this.

It is clear that the programme objectives were similar: restoring confidence in the banks and the sovereign state. Restoration of economic growth did not need to be targeted in the Irish case, as its economy was sound (contrary to that of Greece and Portugal).

### Ownership of loan programme

The table summarizes the support and cooperation of national authorities during implementation, officially called ‘ownership’. The Greek authorities only half-heartedly
<table>
<thead>
<tr>
<th></th>
<th>Greece</th>
<th>Greece</th>
<th>Ireland</th>
<th>Portugal</th>
<th>Spain (banking)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approval date</td>
<td>May 2010</td>
<td>March 2012</td>
<td>Dec 2010</td>
<td>May 2011</td>
<td>June 2012</td>
</tr>
<tr>
<td>Expiry date</td>
<td>March 2012</td>
<td>Jan 2016</td>
<td>Dec 2013</td>
<td>June 2014</td>
<td>Jan 2014</td>
</tr>
<tr>
<td>Amount from IMF (percentage of total)</td>
<td>€30 billion (27.3%)</td>
<td>€28 billion (16.2%)</td>
<td>€22.5 billion (26.5%)</td>
<td>€26 billion (33.3%)</td>
<td>IMF not part of programme, but gave technical assistance</td>
</tr>
<tr>
<td>Amount from EU</td>
<td>€80 billion</td>
<td>€144.7 billion</td>
<td>€45 billion</td>
<td>€52 billion</td>
<td>€100 billion (9.6% GDP) €41.3 expended by European Stability Mechanism (3.9% GDP)</td>
</tr>
<tr>
<td>Total amount (percentage of GDP)</td>
<td>€110 billion (48.6%)</td>
<td>€172.7 billion (90.4%)</td>
<td>€67.5 billion (40.4%)</td>
<td>€78 billion (44.3%)</td>
<td></td>
</tr>
<tr>
<td>Programme objectives</td>
<td>Restore financial market confidence in sovereign and banking sector</td>
<td>Same as May 2010</td>
<td>Restore financial market confidence in sovereign and banking sector</td>
<td>Restore financial market confidence in sovereign and banking sector Return to economic growth</td>
<td>Long-term resilience of banking sector Recapitalization, restructuring, and resolutions of banks Regulatory and supervisory system Return to economic growth</td>
</tr>
<tr>
<td>Implementation</td>
<td>Ownership was limited Administrative capacity to implement reforms was very weak</td>
<td>High ownership Special unit under prime minister Full cooperation Pro-active implementation</td>
<td>High ownership Special unit under prime minister Full cooperation</td>
<td>High ownership Special unit under prime minister Full cooperation</td>
<td>High ownership Cooperation Bank of Spain central role</td>
</tr>
</tbody>
</table>
supported the loan programme (*lack of ownership*). This is understandable, as the harsh cutbacks and deep economic recession led to high unemployment, poverty, and social inequality. Public protest and social unrest were massive and violent (Spanou 2017). In 2010, there had been no consultation with the opposition. In 2011, the technocratic Papademos government did have cross-party support, but even so the opposition was strong. There is still no end in sight for the Greek crisis and bailout.

Although the *Portuguese* sovereign debt crisis resembled that of Greece in many respects (weak economy, large deficit and debt, and polarized politics), the bailout was successfully exited in time (EC 2016b). The Troika undertook the loan negotiations with a caretaker government and consulted the opposition and social partners, resulting in wide and cross-party support. Portuguese authorities created a special coordination unit directly under the prime minister (*high ownership*) (Hardiman et al. 2019).

The *Irish* bailout did not cause party antagonism. Although there were disagreements over its implementation, there was cross-party commitment to rapidly solve the default crisis. A special inner cabinet committee was created directly under the prime minister to pro-actively cooperate with the Troika (*high ownership*). The Department of Finance was split to create a new department, responsible for expenditure control and managerial reform (Hardiman and MacCarthaigh 2016; MacCarthaigh 2017; MacCarthaigh and Hardiman Forthcoming). Ireland successfully exited its bailout before the planned end date (EC 2015).

**Bailouts in 2008**

Whereas most West Europeans were informed by the media about the Greek bailout, and now and then about the Portuguese and Irish bailouts, hardly anyone has ever heard about the IMF–EU bailouts of two years earlier, right at the outbreak of the worldwide financial crisis (*Table 2*). In October 2008, EU member (not Euro member) *Hungary* applied for help from the IMF, which together with the EU and the

---

**Table 2. Bailouts in Central Eastern Europe in 2008.**

<table>
<thead>
<tr>
<th></th>
<th>Hungary</th>
<th>Latvia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approval date</td>
<td>October 2008</td>
<td>December 2008</td>
</tr>
<tr>
<td>Expiry date</td>
<td>2010 ended before completion</td>
<td>2011</td>
</tr>
<tr>
<td>Amount from IMF</td>
<td>€12.5 billion (64.1%)</td>
<td>€1.7 billion (22.6%)</td>
</tr>
<tr>
<td>Amount from elsewhere</td>
<td>€6.0 billion: EU €1 billion: World Bank</td>
<td>€3.1 billion: EU £0.4 billion: World Bank</td>
</tr>
<tr>
<td></td>
<td></td>
<td>€1.9 billion: Nordic countries €0.4 billion: EBRD and others</td>
</tr>
<tr>
<td>Total amount (percentage of GDP)</td>
<td>€19.5 billion (18.2%)</td>
<td>€7.5 billion (30.8%)</td>
</tr>
<tr>
<td>Programme objectives</td>
<td>Substantial fiscal consolidation to restore confidence in government debt sustainability</td>
<td>Stop liquidity crisis while maintaining fixed exchange rate</td>
</tr>
<tr>
<td></td>
<td>Liquidity support and bank capitalization to restore confidence in banking sector</td>
<td>Resolution of systemic Parex Bank</td>
</tr>
<tr>
<td></td>
<td>Reduce the risk of regional contagion</td>
<td>Restore confidence in banking sector</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Reduce fiscal deficit to Maastricht criterion</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Restore competitiveness under fixed exchange rate</td>
</tr>
</tbody>
</table>
World Bank devised a loan programme (the first-ever case of joint IMF–EU support) (IMF 2011; Torok Forthcoming). In December 2008, EU member Latvia asked the IMF for help (followed by Romania and Ukraine, not covered here) (IMF 2013a). In both countries, foreign exchange debt problems (bank loans in foreign currency for household mortgages, plus foreign-owned private and public debt) formed the core of the debt-default crisis (Cepilovs and Török 2019).

**Loan size, objectives, and conditions**

Table 2 shows that the (relative) size of both early loan programmes (as a percentage of GDP) was lower than the later 2010–2011 loans. The IMF’s contribution to the Hungary loan was much larger than that of the EU (first time ever confronted with a bailout). In the Latvia bailout that quickly followed, the IMF involvement was less, and in the later 2010–2011 bailouts the IMF provided about 25 to 30% of the total loan, with total loans amounting to about 40 to 45% of GDP.

The programme objectives of both early loan programmes were different from those of the later 2010–2011 programmes. Bank liquidity and foreign currency exchange were the main problems to be solved. The difference between both countries was that all the large banks in Hungary were foreign-owned (with parent banks providing liquidity), whereas Latvia had a large insolvent domestic bank (Parex) to be rescued. Moreover, Hungary devaluated the Forint, whereas Latvia insisted on maintaining the fixed currency peg (Cepilovs and Török 2019).

**Ownership of the loan programme**

Regarding ownership of the loan programmes, that is, the domestic authorities’ support and cooperation, the Latvia bailout was initially confronted with political problems (prime minister resigned, upcoming elections), and early in 2009 street protests broke out. However, the loan programme was successfully exited (Cepilovs 2017). There was much less public protest and social unrest in Latvia than in Hungary. Ownership of the Hungary bailout was controversial. It was requested by a minority government, the remnants of a coalition break-up. In April 2009, the prime minister resigned and a technocratic government was formed. Then, the April 2010 elections were won (with a two-thirds majority) by the nationalist-populist opposition party, which, like the population at large, fiercely opposed the loan programme. The IMF loan programme was soon ended, as a result of disagreement about the new government’s fiscal measures; and a number of unique (and disputed) one-off cutback measures resulted in Hungary leaving the EU’s EDP. The nationalist populist Prime Minister, Viktor Orbán, resented foreign interference. The influence of Washington (IMF) and Brussels (EU) was to be restrained (Torok Forthcoming).

**Outcomes of bailouts: success or failure**

Were the loan programmes successful in solving the countries’ crises? This methodologically difficult question is hard to answer. Success and failure are affected by many factors other than the loan programme alone, especially the international financial and economic markets. Moreover, as stated in the introduction, success and failure is not only about bank solvency, deficit reduction, and economic recovery, but also about social and political factors like unemployment, poverty, social inequality, and the resulting public protest and social unrest. Table 3 summarizes the
outcomes of the loan programmes as detailed in the official evaluation documents of the IMF and the EC (references below Table 3), and therefore mainly framed in economic terms.

Two loan programmes stand out as clear failures. First, the Greek case failed because the loans did not succeed in remediating the Greek state finances and even less so the economy (IMF 2013b). The massive cutbacks requested in the loan programme further deepened the economic recession, resulting in high unemployment, poverty, and social inequality. Second, the Hungarian case failed, as the newly elected nationalist-populist government terminated the IMF loan programme before completion and also prematurely exited the EU’s EDP. Hungarian economic sustainability is disputed (IMF 2011).

One loan programme stands out as a clear success. The Irish loan programme not only succeeded in restoring confidence in the banking sector and public finances, but also resulted in Ireland’s economic recovery. Its underlying economy was highly productive and competitive (EC 2015).

The Portuguese and Latvian loan programmes were successful in the sense that confidence in the banks and the state were restored, but the weaknesses of both economies in terms of low productivity and weak competitiveness persevered, resulting in disappointing economic growth and unemployment in the years following the bailouts. The structural reforms to cure the economic weaknesses were insufficient and unsuccessful (IMF 2013a; EC 2016b).

The banking bailout in Spain was successful in the recapitalization, restructuring, and resolution of the banks. Whether the fiscal and economic outcomes were successful can be disputed; in the short term not, in the longer term maybe (EC 2016a).

From the point of view of the unemployed and impoverished crisis victims, especially the large number of unemployed youth in Southern Europe – revealingly called the ‘lost generation’ – the ‘success and failure’ of the bailouts looked quite different, as evidenced by the considerable social unrest and protest movements (see below).

**Economic background to the bailouts**

The initial economic conditions of each sovereign debt defaulter were the same: large state debt and deficit, combined with negative economic prospects, led international credit rating agencies (Standard & Poor’s, Moody’s and Fitch) to downgrade the relevant countries, leading to unsustainable interest rates on foreign-owned state bonds. The differences in economic and financial circumstances between the countries are now considered.

**Economic situation**

In Greece and Portugal, joining the EU resulted in easy and cheap access to foreign capital, further enhanced by joining the Eurozone. The influx of foreign capital, which initially fuelled substantial economic growth – the main incentive for joining the EU and the Eurozone –, then began to have negative effects. Growth supported by the EU structural funds was driven mainly by domestic consumption and not invested in productivity and competitiveness. The Greek and Portuguese economies were in bad shape (EC 2016b; IMF 2013b).
<table>
<thead>
<tr>
<th>Expiry</th>
<th>Fiscal outcomes</th>
<th>Economic outcomes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greece</td>
<td>Large deficit reduction achieved (cuts in public sector wages, pensions, and social benefits)</td>
<td>Economic downturn more severe than expected</td>
</tr>
<tr>
<td></td>
<td>Fiscal structural reforms failed</td>
<td>Unemployment also higher than expected</td>
</tr>
<tr>
<td></td>
<td>Debt unsustainable</td>
<td>Structural reforms insufficient to restore competitiveness and growth</td>
</tr>
<tr>
<td></td>
<td>Banking sector increasingly vulnerable</td>
<td></td>
</tr>
<tr>
<td>Ireland</td>
<td>Main focus on restoring confidence in banking sector</td>
<td>Productivity and competitiveness of economy sound</td>
</tr>
<tr>
<td></td>
<td>Deficit reduced (public sector wage bill)</td>
<td>Economic growth restored</td>
</tr>
<tr>
<td></td>
<td>Confidence in public finances restored</td>
<td>Structural reforms not critical and thus limited</td>
</tr>
<tr>
<td>Portugal</td>
<td>Vulnerable banking sector strengthened</td>
<td>Productivity and competitiveness low</td>
</tr>
<tr>
<td></td>
<td>Confidence in banks and state restored</td>
<td>Economic inefficiencies too broad and deep to cure with loan programme</td>
</tr>
<tr>
<td></td>
<td>State-owned enterprises inefficient loss makers</td>
<td>Low economic growth and high unemployment</td>
</tr>
<tr>
<td></td>
<td>Fiscal structural reforms insufficient</td>
<td>High income inequality</td>
</tr>
<tr>
<td>Hungary</td>
<td>Foreign parent banks' support Access to foreign financial markets restored</td>
<td>High foreign debt exposure</td>
</tr>
<tr>
<td></td>
<td>Fiscal measures balanced budget but contested</td>
<td>Long-term sustainability of economy dubious</td>
</tr>
<tr>
<td></td>
<td>Domestic bank liquidity crisis solved</td>
<td>Economic growth low</td>
</tr>
<tr>
<td></td>
<td>Foreign parent banks' support Confidence in banks restored</td>
<td>Unemployment high</td>
</tr>
<tr>
<td></td>
<td>Fiscal measures effective</td>
<td>Structural reforms reversed after programme termination</td>
</tr>
<tr>
<td>Latvia</td>
<td>Banking bailout linked to fiscal consolidation (EDP)</td>
<td>Competitiveness of economy low</td>
</tr>
<tr>
<td></td>
<td>Fiscal measures effective</td>
<td>Economic growth below potential</td>
</tr>
<tr>
<td></td>
<td>Budget stability law</td>
<td>Unemployment high</td>
</tr>
<tr>
<td></td>
<td>Independent fiscal authority</td>
<td>Structural reforms in labour and product markets</td>
</tr>
<tr>
<td></td>
<td>Deficit and debt still high</td>
<td>Economic circumstances still unfavourable</td>
</tr>
<tr>
<td></td>
<td>Fiscal consolidation slowing after programme termination</td>
<td>Very high unemployment</td>
</tr>
<tr>
<td>Spain</td>
<td>Banking bailout linked to fiscal consolidation (EDP)</td>
<td>Productivity still low</td>
</tr>
<tr>
<td>(Banking)</td>
<td>Fiscal measures effective</td>
<td>Economic recovery long-term prospect</td>
</tr>
</tbody>
</table>
Ireland, on the other hand, had made use of the EU structural funds and foreign capital to develop a highly productive and competitive economy. The economy was strong and growing fast (EC 2015).

The Hungarian economy did not fare well after its transition to democracy and the free market. The economy plummeted and unemployment soared. External financial assistance was needed. Hungary had four IMF loan programmes in the 1980s and six in the 1990s. Hungary’s hitherto loose fiscal discipline was only tightened after Hungary’s accession to the EU in 2004, when the EDP was instantly enacted (IMF 2011).

Since early 2000, Latvia had enjoyed an economic boom, further boosted by joining the EU in 2004. Growth was, however, driven mainly by domestic consumption, resulting in high inflation, a housing bubble, and a large deficit (IMF 2013a).

Financial (banking) sector situation

In Greece, the financial (banking) sector was not initially considered problematic. In Portugal, the banking sector had collapsed and was rescued at a high cost. Of the €78 billion Portuguese loan programme, €12 billion was destined for the banking bailout (EC 2016b).

The crisis in Ireland resulted mainly from the overly generous and costly banking sector support provided by the Irish government in 2008. The relatively large Irish banking sector was strongly exposed to real estate, and the outbreak of the worldwide banking crisis led to the bursting of the housing bubble. The bank rescue measures resulted in a steep rise in state debt, thereby turning the banking crisis into a sovereign debt crisis.

In Spain too, the main problem was banks’ high exposure to real estate and a housing bubble that burst when the financial crisis broke out in 2008. Banks collapsed and had to be rescued. A boom–bubble–bust cycle materialized, like in Ireland (EC 2016a).

At the time of the 2008–2010 banking and Eurozone crisis, the Italian banking sector was considered sound. The relatively conservative risk-averse Italian banks had not ventured into the complex and risky financial constructs causing the fall of Anglo-American banks. Only more recently, in 2016–2017, were Italian banks confronted with mounting toxic assets.

In Hungary and Latvia, the financial sector circumstances leading to the defaults were different (Cepilovs and Török 2019). There, the main cause of the debt defaults emanated from the financial sector, particularly the foreign exchange market crisis. In Hungary, state debt was largely foreign-owned, and residents held large foreign currency loans (mortgages). The foreign exchange market collapsed with the 2008 worldwide banking crisis. In October 2008, Hungary requested a bailout from the IMF to prevent a financial meltdown and possible regional contagion. In Latvia too, state debt was mainly foreign-owned. Bank loans were in foreign currency, mainly for household mortgages. The 2008 banking crisis led to a bank run, a liquidity problem, and a foreign exchange crisis.

The difference between Hungary and Latvia in the banking sector was that, in Hungary, all (larger) banks were foreign-owned, with foreign parent banks solving the liquidity crisis, whereas in Latvia many (larger) banks were foreign, but the second largest bank (Parex) was domestic and had to be rescued by the state.
Political background to the bailouts

Political effects and causes of cutbacks

The political effects of fiscal consolidation found in an earlier study of 14 European countries (Kickert and Randma-Liiv 2015, 186) were confirmed in our country cases. First, incumbent governments that planned hard cutbacks nearly always tended to lose the next general elections. Secondly, coalition governments that planned hard cutbacks often broke up, resulting in minority coalitions. Thirdly, coalition governments that made hard cutbacks and broke up nearly always tended to call early elections. The remarkable exception was Estonia, where, at the second cutback round, the coalition broke up and a minority government took charge but did not call early elections and won the regular elections (Savi and Randma-Liiv 2015).

Kickert and Randma-Liiv’s (2015, 172) findings about political causes of fiscal consolidation were also confirmed. The assumption that right-wing governments tend to take harder and swifter cutback measures than left-wing governments are false. The political orientation of governments (right-centre-left) hardly matters for cutbacks. Neither does the margin of parliamentary majority (minority-normal-grand) have much influence on cutbacks. The primary factor explaining the size of cutbacks is, virtually by definition, the size of the budget deficit and debt.

We now discuss a couple of political factors that clearly had an influence on cutback management: first, the politicization and polarization of decision-making; second, the change in political landscape caused by the rise of protest parties.

Politicization and polarization

In Greece and Portugal, the decision to request financial assistance from the IMF and the EU was characterized by politicization and polarization – the usual features of Southern European political systems (Kickert 2011; Sotiropoulos 2017).

In the Greek polarized political party landscape, it is customary for a newly elected incoming government to engage in a political blame game, accusing the previous-ousted government of manipulating the economic and fiscal statistics. In 2010, the new socialist prime minister attempted to persuade his European colleagues of his fiscal reliability by openly doing penance for the falsified national deficit and debt statistics. It is doubtful, however, whether that really helped him in the subsequent negotiations about the bailout conditions (Featherstone 2011). The negotiations about the financial assistance programme were characterized by mutual mistrust. Greek protests and opposition were to no avail (Spanou 2017).

In Portugal, the socialist prime minister responded to the banking crisis and ensuing economic recession by public investments in economic recovery. A bailout was out of the question. After the outbreak of the Greek sovereign debt crisis in 2010, the government had to reverse its course and go for outright cutbacks. It negotiated three subsequent austerity programmes (Stability and Growth Pacts) with the EU. The fourth cutback package was rejected in parliament by the centre-right Social Democrat party, leading to the resignation of the socialist prime minister. The neoliberal and technocratic centre-right Social Democrats, who actually favoured the conditions of the fourth austerity package, forced the outgoing prime minister to ask for a bailout, resulting in a Memorandum of Understanding (MoU) containing more or less the very same conditions (Araujo 2017). Opposition, protest, and obstruction
against the Troika proposals were much less extensive in Portugal than in Greece. The new Social-Democrat-led Portuguese government cooperated fully in the implementation of the bailout conditions (cutbacks and structural reforms); and it successfully exited the bailout programme on time (EC 2016b).

Like in neighbouring Portugal, the Spanish socialist prime minister responded to the banking crisis and economic turndown by investing public funds in economic recovery. The word ‘crisis’ was a political taboo. Austerity measures were out of the question. In 2011, the EU intervened and told the prime minister that Spain could not count on continuing to receive financial support (ECB buying up endangered Spanish bonds) unless it displayed fiscal discipline. In May 2011, the socialist prime minister unexpectedly announced a cutback package, resulting in massive protests by backbenchers in his party, leading to his resignation and the loss of the November 2011 elections to the centre-right Popular Party. The new prime minister soon introduced larger cutback measures (Badell and Ysa 2017; Kickert and Ysa 2014).

In Ireland too, the government for long denied the severity of the banking crisis and refused to ask for financial assistance, despite ECB pressure. It was the Central Bank of Ireland that eventually precipitated the loan request. Moreover, officials had been drawing up plans for a national recovery programme, and the MoU essentially mirrored that plan (MacCarthaigh and Hardiman Forthcoming).

Hungarian national politics were also characterized by political polarization and deep distrust between the Socialist Party (former Communists) on the one hand and the opposing nationalist, conservative, and liberal parties on the other, dominated by Viktor Orbán’s centre-right nationalist-populist party (Fidesz) (Lendvai 2012). After the 2006 elections, the new Socialist-Liberal coalition grudgingly commenced to take major cutback measures to meet the EU deficit ceiling. The highly unpopular measures were strongly opposed by the populist Fidesz party. Then, in 2008, the government was forced to call for external financial assistance, resulting in the October 2008 bailout. The ensuing harsh cutback measures led to more protest and unrest, resulting in the Fidesz party winning a sweeping two-thirds majority election victory in 2010 (Torok Forthcoming).

Politicization and polarization did not take place in Latvia and Estonia, or in the Netherlands.

In Latvia, from its independence in 1991, centre-right and nationalist parties dominated in parliament (until 2016). After the January 2009 street protests against the austerity plans, the government coalition broke up, and in March 2009 a cross-party technocratic government, headed by a former Bank of Latvia chief economist and former finance minister, was formed to negotiate the loan conditions with the IMF and the EU (Cepilovs 2017).

In Estonia, the centre-right-left coalition government implemented its first hard cutback measures in June 2008. Then, cutback rounds in February and June 2008 led the social democrats to leave the coalition, but the remaining centre-right minority government did not call early elections and won the normal March 2011 elections (Savi and Randma-Liiv 2015).

The Dutch political system is characterized by deep-rooted and long-time compromise and consensus (Kickert 2004). That did not change at the time of the fiscal crisis. Moreover, the Dutch budget crisis was rather moderate and so were the cutbacks (Kickert 2015).
Change in political landscape: anti-austerity protest movements

Anti-austerity protest movements emerged in Europe in the aftermath of the global financial crisis. Governments were taking cutback measures to manage their fiscal crisis, and austerity began to lead to rising unemployment and falling living standards, especially in countries that were bailed out (Fominaya and Hayes 2017).

In Greece, the crisis resulted in a collapse of the traditional two alternating-parties system, with government power always in the hands of either the socialists (PASOK) or the conservatives (New Democracy). In the 2015 elections, these two parties were almost obliterated by the electorate for their apparent inability to handle the crisis. The newly established left-wing (Marxist) party, Syriza, was the clear winner and formed a government. Syriza was a protest party opposing the severe and painful cutbacks enforced by the Troika each time another loan tranche was due. Moreover, the political landscape was changed by the use of referenda against Troika-imposed cutbacks. A first attempt in 2011 to hold a referendum against the Troika austerity measures was effectively blocked by the EU. In 2016, the new Syriza government held another referendum against the Troika cutbacks, which it won clearly. Nevertheless, the Syriza government was forced back to the negotiation table in Brussels and for further loans had to accept the very same conditions that had been voted down in the referendum (Spanou 2017). Table 4 juxtaposes the situation of protest parties in Hungary and in Greece.

The Spanish political landscape was likewise changed. Since the transition to democracy, political power had always alternated between the socialists (PSOE) and the conservatives (Popular Party: PP). Coalitions were alien in Spain. The brutal economic recession – with huge (youth) unemployment and massive social unrest (15M movement) – led to the creation of new protest parties on both the right (neo-liberal pro-business Ciudadanos) and the left (Podemos). The 2015 and 2016 elections twice resulted in a hung parliament. After the first elections, both PSOE and PP refused to cooperate and mutually blocked possible multi-party coalitions, resulting in yet another general election. Again, parliament was hung, and neither party was willing to form, or capable of forming, a coalition. Eventually, and partly to avoid a third round of elections in less than two years, the PSOE, after removing its leader, finally decided to allow a minority government of the centre-right PP to be voted into office by the parliament (Badell and Ysa 2017).

In Italy, the political landscape had radically changed in the 1990s after corruption scandals. The traditional parties were wiped out by the electorate, and newly created parties entered the stage, most notably the populist centre-right party combination (Forza Italia) led by Berlusconi. By the end of the 1990s, political scientists tended to conclude that Italy had entered a phase characterized by the layering of new and old institutions without any veritable transition to a new republic (Bull and Rhodes 1997, 2013), a state of affairs that has come to be characterized as a politico-administrative

<table>
<thead>
<tr>
<th>Table 4. Success and failure of anti-austerity protest parties.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hungary FIDESZ (Viktor Orbán)</td>
</tr>
<tr>
<td>Existing populist, nationalist, patriotic party</td>
</tr>
<tr>
<td>Against IMF–EU-imposed austerity and reforms</td>
</tr>
<tr>
<td>Won elections (two-thirds majority)</td>
</tr>
<tr>
<td>Quit IMF loan and ended EU’s Excessive Deficit Procedure</td>
</tr>
</tbody>
</table>
context in motion (Ongaro 2009). When the crisis hit Italy, resulting in a harsh recession, enduring economic decline, rising unemployment, and social unrest, several protest parties entered the political scene and managed to attract the electorate’s support (notably the populist Five Star Movement, M5S). The fiscally unreliable Berlusconi government was overthrown to make way for the independent technocratic Monti government, supported by all main parties. That support lasted only until the following elections, won by a small margin by the centre-left Democratic Party, which was able to secure a majority only in the lower house (Di Mascio, Natalini, and Stolfi 2013; Badell et al. 2019) and then eventually lost the subsequent elections in early 2018.

Conclusions and discussion

EU and IMF influence on domestic cutback management

The main question addressed in this article was the influence of the EU (and the IMF where relevant) on domestic cutback management. We first differentiate degrees and types of influencing according to the degree of an economic and fiscal crisis in a country, and according to the EU’s fiscal governance instruments. Second, we further differentiate the degrees of influencing according to the particular political circumstances in a country.

Degrees and types of influence

The degree and type of EU influence depends primarily on the severity of the economic and fiscal crisis in a country. Different degrees of economic and fiscal crisis call for different EU fiscal governance instruments. As long as a country has a balanced budget and a debt brake, there is no EU intervention (apart from regular EU monitoring).

When the fiscal situation exceeds certain thresholds, the Excessive Deficit Procedure (EDP) comes into effect. The 2011 EDP successors, European Semester, contains not only fiscal corrective measures, but also recommendations for structural reforms. That is, the EU not only intervenes in fiscal and economic affairs, but also ‘recommends’ public sector reforms, such as in the labour market, pensions, and so forth.

When a country’s economic and fiscal situation deteriorates so much that the international financial markets start losing confidence in that country’s creditworthiness (credit rating agencies), and bond interest rates are rising to alarming heights, the European Central Bank (ECB) can intervene by buying up the endangered bonds, thus calming the markets. In return for such monetary support, the ECB and the EU make ‘recommendations’ on fiscal affairs and reforms.

When the economic and fiscal situation becomes so unsustainable that a country loses its creditworthiness and defaults on its state debt (sovereign debt crisis), an appeal can be made to the IMF and the EU to provide a temporary loan (bailout). The loan programme is provided on conditions. The Troika intervenes in fiscal and economic affairs, and also requires a country to carry out structural reforms in, for example, the labour market, pensions, and tax administration.

No direct influence in Estonia and the Netherlands

Estonia was hit hard by the fiscal and economic crisis. The Estonian government implemented extensive and hard cutback measures at an early stage. Its strong desire to join the
Eurozone further enhanced its already strict fiscal discipline. Estonia managed to stay out of the EU’s EDP, so there was no direct intervention by the EU. Indirectly, however, the EU did exert influence because of the strict fiscal requirements for accession to the Eurozone, which was top of Estonia’s political priorities (Kickert and Randma-Liiv 2019).

In the Netherlands, the fiscal and economic crisis was relatively mild. It did enter the EU’s EDP, but was easily capable of overcoming the mild crisis with relatively moderate measures. Interference from the EU was virtually non-existent. The Dutch Ministry of Finance considered itself to be more capable than Brussels of handling the crisis. Regarding budget discipline, it was rather the Dutch influencing Brussels than the other way round. The Dutch, together with the Germans, had always been pushing for stricter budgetary rules, ever since the Maastricht Treaty and even more so since the crisis (Kickert and Randma-Liiv 2019).

More influence in Italy and Spain

In countries with more serious economic and fiscal problems and allegedly less fiscal discipline, like Italy and Spain, the influence of the EU on the national government was stronger (Badell et al. 2019).

Italy was not bailed out, but in summer 2011 the fiscal and economic situation became dramatic, resulting in soaring bond interest rates. The ECB on a large scale bought up endangered Italian state bonds. This monetary assistance came at a price in terms of EU–ECB interference in Italy’s fiscal affairs. Berlusconi was known to have been furious about foreign interference in Italian sovereign (fiscal) affairs (ECB–Bank of Italy letter of recommendations).

In Spain, the ECB also bought up endangered state bonds, and apparently the Spanish government also received an ECB letter of recommendations. The Spanish prime minister was forced by the EU to reassure the international financial markets of his fiscal discipline by taking austerity measures. EU influence in Spain further stepped up with the banking bailout. The Spanish banking sector bailout, with the ECB and the EU monitoring and controlling a bank rescue and reform operation, contained the conditions stipulated in the EU’s European Semester. Therefore, the EU had more influence on the fiscal affairs of Spain than on those of Italy.

Bailouts and the Troika

In countries that were so seriously affected by the crisis that they had to be bailed out, the influence of the EU (and the IMF) on the government were different. There, a Troika of IMF, EU, and ECB was established to monitor and control domestic fiscal decision-making. The IMF had ample experience and standard operating procedures for financially assisting countries with balance-of-payment troubles. At the outbreak of the Eurozone crisis in 2010, the EU had no experience in financially assisting troubled states (the IMF had taken the lead in Hungary’s and Latvia’s 2008 bailouts).

Reverse influence: domestic influences on IMF–EU loan programmes

The influence of the EU and the IMF on domestic cutback management was obviously paramount in the loan programmes. Nevertheless, domestic actors managed to exert influence on the loan programme conditions, albeit in varying degrees.
In Ireland, once the government was forced to recognize the real extent of the banking crisis and therefore to request financial assistance, the loan programme’s MoU coincided to a large extent with the national recovery programme already conceived by Irish finance ministry officials. So, Irish domestic influence on the loan conditions was significant.

In Portugal, the neo-liberal managerial social democratic opposition party forced the socialist government to resign by voting down an austerity and reform package, which it actually favoured, and which the Social Democrats managed to get inserted in the loan programme’s MoU. Moreover, the loan programme was implemented by a social democrat government. So, the influence of Portuguese domestic (opposition) politics on the loan conditions was considerable.

The Greek case, however, seems an example of domestic authorities being coerced into austerity and reforms, which they in vain contested, protested, and obstructed. The anti-austerity Syriza party won the elections and won the anti-austerity referendum, and yet, in the end, was forced to accept the EU–IMF loan conditions.

In Hungary, the newly elected government so much resented being coerced by the EU and the IMF into cuts and reforms that they prematurely abandoned the loan programme. Foreign influence on domestic affairs was to be terminated.

Table 5 presents a schema of the degrees and types of EU (and IMF) influence.

Discussion: political economy not value free

The conditions that the Troika attached to its financial assistance programmes were contested in the ‘helped-out’ countries, most notably Greece and Hungary, with fierce public protests and widespread social unrest against the harsh consequences in terms of lay-offs, salary cuts, pension cuts, unemployment, and poverty. The dominant economic frame of reference used in the EU, more specifically in the EC’s Directorate-General for Economic and Financial Affairs (DG EcFin) (Buti and Carnot 2013), which took the lead in Brussels, seems to be the mainstream economic thinking in north-western European countries rather than that prevailing in southern European countries. In other words, the countries paying the bill for the bailouts, Germany and the Netherlands upfront, seemed to be imposing their economic views on the loan-receiving countries, which resented the harsh loan conditions.

The predominant economic rationale in Brussels (and Washington) is that fiscal consolidation based on spending cuts, rather than tax increases, is more likely to reduce budget deficits. Moreover, consolidation on the spending side rather than on the tax side is less likely to create an economic recession (Alesina and Ardagna 2010). Numerous empirical studies have been used to underpin these claims (Alesina 2010, 2012; Alesina, Favero, and Giavazzi 2014). Spending-based consolidation could even contribute to economic growth when accompanied by cutbacks in the costs of administration, that is, cuts in size and pay (Alesina, Favero, and Giavazzi 2014). Economic policymakers employed these findings in the debate about how much consolidation was needed, how fast, and with which instruments (Sutherland, Hoeller, and Merola 2012; Molnar 2012; Blöchliger, Song, and Sutherland 2012).

A salient political aspect of fiscal consolidation is the question of whether harsh fiscal austerity in times of economic recession is the right approach to adopt. The fervent condemnations by Nobel Prize winner Paul Krugman are well known. The basic argument is that a weak economy will be further harmed by deficit reductions,
Table 5. Degrees and types of EU (and IMF) influence.

<table>
<thead>
<tr>
<th>Economic and fiscal situation</th>
<th>EU (and IMF) fiscal governance instrument</th>
<th>Degree of EU (and IMF) influence</th>
<th>Further differentiation of degree of influence per country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deficit and debt balanced</td>
<td>None (except regular EU monitoring)</td>
<td>Fiscal consolidation without direct EU influence</td>
<td>Estonia indirectly influenced because of Euro access priority</td>
</tr>
<tr>
<td>Deficit and debt above ceilings</td>
<td>Excessive Deficit Procedure, European Semester</td>
<td>Fiscal consolidation with direct EU influence</td>
<td>Netherlands in EDP, but fiscal influencing was rather other way around</td>
</tr>
<tr>
<td>Economic and fiscal situation alarming. Financial markets reduce confidence in creditworthiness</td>
<td>ECB buys up endangered state bonds</td>
<td>Fiscal consolidation with direct EU and ECB influence</td>
<td>Italy and Spain received letter of recommendations. Spain received banking bailout with European Semester conditions</td>
</tr>
<tr>
<td>Economic and fiscal situation unsustainable. Financial markets lost confidence in creditworthiness Debt default</td>
<td>Loan programmes with strict conditions: financial, fiscal, and structural reforms</td>
<td>Fiscal consolidation with direct IMF, EU, and ECB influence</td>
<td>Greece no influence at all on loan conditions. Portugal somewhat influenced loan conditions. Ireland strongly influenced loan conditions. Hungary quit loan programme to end EU and IMF influence</td>
</tr>
</tbody>
</table>
whereas economic growth is a good cure for deficits, so it is preferable to stimulate economic growth than to engage in cutbacks. Unfortunately, this debate is often largely political-ideological, with debaters presuming to possess the moral prerogative to condemn or justify fiscal consolidation. In the economics discussion platform VoxEU, the danger of fiscal austerity leading to another economic recession was discussed at the time by European economists (Corsetti 2012; De Grauwe 2013; Gros 2011) and top officials of the IMF (Cottarelli 2012) and the EU (Buti and Carnot 2013; Buti 2014).

The political economy ‘findings’ about the fiscal effects of spending cuts rather than tax increases, and the alleged beneficial fiscal effects of public sector cuts, may seem to be amply empirically grounded, but political economy is not value free. The seemingly neutral purely empirical findings are actually normative. The debate about fiscal austerity and economic recession is heavily burdened with political ideology. Nevertheless, it is an undeniable fact that mighty international institutions like the EU, the IMF, the World Bank, and the OECD (and the credit rating agencies) have been and possibly continue to be outspoken advocates of these ‘mainstream’ political economic ‘insights’.

Disclosure statement

No potential conflict of interest was reported by the authors.

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