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The Politics of Fiscal Squeeze

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Putting the Politics of Fiscal Squeeze into Perspective

It is commonly implied that the great financial crash of 2008 and the dramatic policy changes that followed in many countries were unique in the history of the world. Many have commented on the sheer scale of the financial pressures on many governments in terms of deficit and debt and on the drastic monetary responses by central banks, setting their official lending rates at historic lows and printing money on an unprecedented scale (see, for example, Swagel 2009; Greenspan *et al.* 2010; Reinhart & Rogoff 2011).

We do not want to underplay the significance or the dramatic nature of those adjustments. But even so, historical comparisons are instructive. For example, the fiscal travails of the early United States in the early 19th century (when half of the states then in the Union had to default over their debts, mass protests had to be contained, and new unpopular taxes imposed in the middle of an international trade slump) merit some attention by those who think there are no parallels to the Eurozone debt crisis of the early 2010s (Roberts 2012: 204). Indeed, the experience of the Ottoman Empire after it defaulted on loan repayments to its foreign creditors in 1875 goes far beyond anything witnessed in the Eurozone countries in the 2010s so far (see Birdal 2010: 6–10). In that case, a large independent (ostensibly private) bureaucracy run by the Empire's European creditors was set up by the Decree of Muharrem issued by Sultan Abdülhamid II in 1881 to collect taxes that were paid directly to those creditors. Even in more recent times, experiences such as that of Mexico in 1995 in consequence of its so-called 'Tequila' crisis can provide some partial parallels to the problems experienced by crisis-hit countries in the 2010s. The currency slumped by almost 50 per cent after a pre-election spending splurge in 1994 had been financed by debt indexed to US dollars, with GDP then falling by some 7 per cent and industrial wages by 30 per cent in a single year, leading to a hasty 'bailout' (arguably mainly benefiting international creditors) organised by the United States, the IMF and the Bank for International Settlements (Humphrey 2000).

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Of course there is always something unique about the circumstances of any given time. But even so, comparisons across space and time, both in the aftermath of major financial crises and in other conditions, can help us understand what we here call 'fiscal squeeze', explore the politics behind such processes and see what if anything they have in common. That is what this book aims to do. But first we need to explain why this book focuses on *fiscal squeeze*, why it is the *politics* of fiscal squeeze we want to focus on, and what we mean by putting fiscal squeeze into *perspective*.

Why *Fiscal Squeeze*?

This book is mainly concerned with efforts made by politicians and governments to correct the public finances by raising taxes or cutting spending or a mixture of the two. We put spending and taxes into the foreground and monetary policy into the background. But of course we recognise that the two types of policy overlap, for example when governments use inflation as a tax, or use default or devaluation as a way to deal with debt problems, as has often happened historically.

In this book we use the term 'fiscal squeeze' to denote political effort put into reining in public spending and/or raising taxes. Given that starting point, Table 1.1 indicates three basic possible varieties of fiscal squeeze, in terms of effort put into increasing revenue, cutting spending, or both at the same time. The possible types are three rather than four, because cell (1) of the table, with effort going into neither raising revenue nor cutting spending, does not constitute a 'squeeze'. We will later elaborate this very basic typology by adding subcategories, and it is worth noting that revenue-only fiscal squeezes (cell (3) of the table) seem to be extremely rare, at least in modern democracies.

We use the term fiscal squeeze because many of the terms used in the prevailing literature are ambiguous, politically loaded or have a technical meaning that refers to financial outcomes rather than political effort. For example, the term 'fiscal adjustment' is often used in practice by international econocrats as a euphemism for higher taxes and/or spending cuts, but it often means attempts to change spending relative to GDP, which is a measure of financial outcome rather than political effort.

Table 1.1. Some basic types of fiscal squeeze.

Effort going into revenue increases	Effort going into expenditure cuts	
	No	Yes
No	(1)	(2)
Yes	(3)	(4)

The same goes for 'fiscal consolidation', which similarly is often used as a technical-sounding euphemism for the same sort of measures. But it is also used more strictly to denote a reduction in the fiscal deficit (the difference between total revenue and spending or 'primary balance'—the balance struck before taking into account interest payments on the public debt). And both fiscal adjustment and fiscal consolidation in the more technical sense are financial outcomes that can come about as a result of economic growth rather than painful belt-tightening measures by governments. Contrariwise, those belt-tightening measures do not necessarily lead to fiscal consolidation if the overall economy contracts significantly, for example as a result of an international slump.

The term 'austerity' is perhaps closer to denoting the political effort that this book concentrates on, but it is ambiguous for several reasons. It is often used to denote what we here call fiscal squeeze, but it is sometimes used as a non-technical synonym for fiscal adjustment or fiscal consolidation. Moreover, it has recently come to denote a policy position associated with faster rather than slower attempts to correct fiscal deficits, and with an emphasis on correcting such deficits through spending cuts rather than tax increases, in the context of an economic slowdown or recession. Mark Blyth's (2013) attack on austerity as a what-to-do doctrine, and his account of its intellectual history and links to contemporary neo-liberalism more generally, is a telling recent example of this usage of the term.

But that is only a particular subset of what we here call fiscal squeeze.[1] So, in contrast to the normative associations (positive or negative) that 'austerity' has acquired, and in contrast to the financial outcomes that fiscal adjustment and consolidation tend to denote, we use fiscal squeeze as a neutral term to denote those fiscal changes that reflect political effort put into belt-tightening or loss imposition (i.e. spending cuts or tax increases imposed by governments, or both), irrespective of whether or not those measures reflect any particular doctrine or result in fiscal consolidation in the technical sense of deficit reduction.

It follows that fiscal squeeze is harder to measure than economic or financial outcome indicators, since the extent of the effort it denotes is not directly measured by financial outcome numbers, for at least three reasons. One is that economic outcome data tend to focus on *implemented* spending cuts or revenue increases, whereas in politics, *announcement* is often important as well as implementation. Another is that, as already noted, financial outcomes can

[1] There are other terms that could also be considered. For example, the term 'cutback management', used by some academics in the 1980s (for instance Dunsire & Hood 1989), is less euphemistic and circumlocutory than 'fiscal adjustment' or 'fiscal consolidation' and embraces much of what we are concerned with here, but covers only spending reductions or containment rather than what happens to taxes, charges or similar measures.

change for reasons unrelated to political effort, for example if revenues rise in an economic recovery as a result of higher incomes rather than by politicians putting tax rates up.

In particular, policies such as income taxes and welfare spending often act as ‘automatic stabilisers’ that dampen fluctuations in real GDP. For instance, when GDP falls in a recession, the budget deficit tends to increase as a result of falling tax revenue and increased welfare spending, which in turn keeps aggregate demand and national income higher than it would otherwise have been. Similarly during a boom, budget deficits often reduce as tax revenue rises and welfare spending falls. Such effects do not occur equally in all times and places, dependent on the extent of welfare entitlements and of obligations to balance spending and revenue in the short term. But where they apply, these effects are ‘automatic’ in that they occur without explicit government intervention, and hence an assessment of the political effort going into fiscal squeeze has to take into account the extent to which effort goes into overriding the cyclical effect of such stabilisers, as we do in our quantitative analysis in the next chapter.

A third reason why political effort involved in cutting spending or raising taxes (or both) is not automatically represented by reported deficit and debt numbers is that such effort depends heavily on context. A key part of that context is the preferences of political leaders and their core supporters as well as those of the voters. For example, it seems likely that in early 1976 Harold Wilson’s Labour government in the UK expended more political effort in persuading its fractious and divided governing party even to accept a (short-lived) policy of holding public expenditure constant than did Jean Chrétien’s Liberal government in Canada two decades later in substantially cutting federal spending in very different political circumstances. In principle, public spending cuts may require less political effort from ‘Tea Party’ style politicians who are committed to shrinking the state and whose core supporters have the same preferences, than in cases where government leaders find themselves applying policies that go against their own publicly expressed preferences and/or the preferences of their core party supporters.

Against that, however, is the so-called ‘Nixon goes to China’ phenomenon, often observable in politics (see for example Cukierman & Tommasi 1998). This phenomenon is named after the episode in 1972 when a Republican US President (Richard Nixon) who had hitherto maintained a strong anti-Communist stance initiated a rapprochement between the United States and the People’s Republic of China. As in that example, leaders who have declared preferences in a particular policy direction can sometimes win over core party supporters and voters more generally with lower political effort when they move in the opposite direction (by imposing spending cuts and/or tax increases) and represent that move as unavoidable, at least as a short-term expedient. The extra political effort involved in changing their own established stance may in turn mean lower political effort for political leaders in winning over voters or supporters. An analogy could be drawn with the amount of braking effort needed to slow or stop a vehicle going down a steep slope or at high speed, as compared to that needed when travelling uphill or at low speed; the extent of braking effort (as represented by the extent of decelerative force) is only imperfectly measured by how long it takes the vehicle to stop or indeed whether it stops at all. In that example, gradient and previous speed are the equivalent of political context, and that is why financial or economic outcome data can only be a rough proxy for the extent of the political effort put into restraining spending and/or raising taxes. As the poet Robert Burns more pithily put it, 'What's done we partly may compute, / But know not what's resisted.'[2]

Table 1.2 accordingly aims to bring out what a spectrum of *political* cost or effort might look like for tax increases and spending cuts. At the low end of expected political costs, it identifies situations where governments concentrate on 'inertia politics' or maintaining the status quo in the sense of existing tax or spending plans and resisting calls for tax cuts or spending increases or both. Higher expected political costs apply where governments impose losses through spending cuts or tax increases that are low in visibility, salience or

Table 1.2. Fiscal squeeze and political effort: indicative examples of the spectrum of political effort.

	Expected political cost or effort level		
Fiscal instrument	Fairly low (Mainly inertia strategies)	Medium (Imposition of less visible and salient losses)	Fairly high (Imposition of visible and salient losses)
Taxation	Resistance to pressure for tax cuts	Imposition of 'stealth taxes' (e.g. use of fiscal drag, fees or charges that are not formally counted as 'taxes', such as parking fines)	Imposition of visible tax rises or levying new taxes on key voters or funders
	Acceptance of tax rises or new taxes already in the pipeline	Imposition of taxes or tax rises that do not hit key voters, funders or supporters	Breaking key election promises over taxes
Spending	Resistance to pressure for spending increases	'Stealth cuts' (e.g. non-indexation of benefits, increases in qualifying periods)	Imposition of visible cuts in spending of high salience to key voters or funders
	Taking advantage of spending programmes already scheduled to end	Cuts in spending of low salience to key voters, funders or supporters (e.g. benefits to non-voters abroad or spending cuts targeted at opposition heartland areas)	Breaking key election promises over spending

[2] 'Address to the Unco Guid' (Burns, [1786] 2009: 18).

impact on their key voters, supporters or funders, for example in imposing high nominal tax rates on wealth or income far above the median-voter level. At the top end of expected political costs are situations where governments impose losses through spending cuts or tax increases that are high in visibility, salience or impact on their key voters, supporters or funders. We do not claim that such distinctions are always easy to draw, that they are readily represented by standard statistical measures, or even that the measures indicated in each of the columns of Table 1.2 will always represent low, medium or high political costs, given the issue of variable context mentioned earlier. The table merely aims to provide a point of departure for thinking about what political effort or costs mean in fiscal squeeze.

Given that fiscal squeeze, as defined earlier, can only be indirectly measured, we identify fiscal squeezes in this book in two ways. One is by qualitative judgements based on study of the politics of the time in a set of different places, for the case studies we introduce later. The other is by taking reported aggregates of spending and revenue as a rough proxy for political effort. For that second approach based on proxy measures, we go beyond the simple 'yes'/'no' classifications in Table 1.1 to identify two types of spending squeeze and two types of revenue squeeze. They are:

- 'soft' expenditure squeezes, when either (a) government spending falls relative to GDP, but such expenditure does not fall in constant-price terms or (b) expenditure falls in constant-price terms but not relative to GDP;
- 'hard' expenditure squeezes, when government spending falls both relative to GDP and in constant-price terms;
- 'soft' revenue squeezes, when either (a) tax revenues rise relative to GDP but such revenues do not rise in constant-price terms or (b) tax revenues rise in constant-price terms but not relative to GDP;
- 'hard' revenue squeezes, when tax revenues rise both relative to GDP and in constant-price terms.

We postpone all discussion of the technical issues involved in making these distinctions to Chapter 2, but we note here that when put together, those four types make multiple possible combinations, to which we return in the final chapter.

Why the *Politics* of Fiscal Squeeze?

Of course fiscal squeeze can be approached from many different perspectives. Economics tends to focus on assessing the best policies to be pursued by governments facing fiscal difficulties. Sociology and cultural studies tend to concentrate on the lived experience of fiscal squeeze, such as jokes, cartoons, graffiti or music. This book is centrally concerned with understanding the politics and political economy of fiscal squeeze—who gets what, how losses are imposed, who gets the credit and who gets the blame, and (relatedly) what, if any, longer-term political (or broader social) consequences follow from episodes of fiscal squeeze.

Fiscal crisis, pressure and contraction figured large in the political economy literature of the 1970s and 1980s in the wake of the economic and financial difficulties experienced by Western economies at that time (such as oil price shocks, 'stagflation' and de-industrialisation). For example, public policy scholars Richard Rose and Guy Peters (1978) asked *Can Government Go Bankrupt?* (then as now, the answer is both yes and no). Marxist scholar James O'Connor (1973) in his much-quoted *Fiscal Crisis of the State* modified the traditional Marxist theory of the state to argue that the state's role in supporting capital accumulation would increasingly come into conflict with its role in legitimating the capitalist system. From a very different intellectual perspective, public choice scholars James Buchanan and Richard Wagner (1977) in their *Democracy in Deficit: The Political Legacy of Lord Keynes*, argued that runaway government spending was the result of Keynesian ideas combined (fatally in their view) with democratic processes.

The administrative politics of spending cutbacks also figured large in the literature of that period. For example, Daniel Tarschys (1985) highlighted in a comparative analysis the way 'hard choices' tended to be decentralised within executive government systems through 'frames, envelopes, caps, ceilings and cheese-slicers'. Observing OECD experience, Tørben Beck Jørgensen (1987) analysed 'stages' of spending cutbacks as fiscal pressure continued over time (running from initial 'decrementalist' strategies, through 'managerial' remodelling to 'strategic' cutbacks). Peter de Leon (1983) analysed the politics of 'policy termination' from a US perspective (arguing that ideology was the commonest reason for policy termination, but that cost reductions and attempts to correct for programme inefficiencies also played a part). Andrew Dunsire and Christopher Hood (1989) analysed bureaucratic winners and losers in UK central government in the 1980s against a range of theories of the bureaucratic politics of cutbacks.

Many of those themes re-emerged in academic and public debate as pressures for fiscal squeeze developed in the aftermath of the financial crisis of the late 2000s (see, for example, 't Hart & Tindall 2009; Bermeo & Pontusson 2012; Bartels & Bermeo 2013; Streeck & Schäfer 2013). This book picks up on three issues that are more or less explicit in much of this literature, namely whether there is something special about the politics of fiscal squeeze, whether fiscal squeeze is a political blame magnet or a credit-claiming opportunity, and whether fiscal squeeze is highly consequential for political development or just one of those short-term ‘sugar rushes’ in politics whose effect quickly wears off.

Fiscal Squeeze as a Special Style of Politics

The first proposition is that there is something different, and perhaps especially challenging, about the politics of fiscal squeeze as compared to other kinds of politics. That, after all, is the assumption that led Aaron Wildavsky (1980) and others to conclude that only constitutionally entrenched limits on government spending could counter the ‘normal’ upward pressures on public spending in modern democracies (as reflected in an extensive but contested literature on the politics of long-term growth in public spending and taxation (Peacock & Wiseman 1961; Hood 1991)). Likewise, Alasdair Roberts (2012) sees US state politics in the aftermath of the financial crashes of the 1830s and 1840s as harsher, more brutal, less rewarding, even more violent than in more expansionary times:

> Politics was not an easy craft during the First Great Depression … Attention was seized by the … fundamental task of combating forces that were pulling political and social structures apart … Statesmen were occupied more than usual with the politics of denial: that is, explaining to powerful and angry constituencies why they had to be denied benefits or liberties, or why they were required to shoulder new burdens (Roberts 2012: 209–10).

The assumption here, chiming with well-known ideas about asymmetric preferences over losses and gains developed by Daniel Kahneman and Amos Tversky (1979) and others, is that loss imposition, where there are few ‘goodies’ to spread around, is more difficult and painful than distributional politics in times of plenty. From this perspective, we might expect fiscal squeeze politics to be markedly different from the politics of more expansionary times, for example in producing crises (that is, moments when political pressure is increased, usually as a result of disaster or political scandal (Tama 2011: 8)), abnormal ‘Nixon goes to China’ moments, and other departures from politics-as-normal.

The idea that fiscal squeeze presents challenges for democratic politics rests on plausible enough assumptions that raising taxes and reining in spending necessarily creates losers and that the imposition of such losses on significant numbers of voters makes fiscal squeeze politics a ‘difficult craft’. Loss imposition may not involve high political costs when (a) ‘maleficiary’ voters are diffused or losses hit those with a low propensity to vote, or (b) the stakes are low. But when high-stakes losses are imposed on mobilised groups, it is plausible to assume that such policies will strain established conventions and ties (for example to mainstream political parties), and perhaps even democratic ‘politics’ itself, as opposed to rule by technocrats or other groups ostensibly outside the 'political class'.

Against such claims, however, a contrasting 'null hypothesis' is that the politics of fiscal squeeze is no more, or less, different from the politics of fiscal expansion than (say) railway politics is from arts and media politics. One way of framing such a null hypothesis is to suggest that episodes of fiscal squeeze do not necessarily share major political characteristics, by analogy with the famous first sentence of Leo Tolstoy's *Anna Karenina*, which states that (in contrast to happy families) 'every unhappy family is unhappy in its own way'.[3] A slightly different basis for a null hypothesis—that there is nothing particularly special about fiscal squeeze—would be the proposition that all politics, about fiscal squeeze or anything else, involves clashes among contradictory worldviews (such as small-state individualism and those who favour various forms of collectivism), battles over who wins and who loses, and struggles by interest groups to protect their positions and by political actors to gain credit and avoid blame. It may be just another arena for observing the practice of 'heresthetic', that is, the pursuit of political strategies to open up new cleavages that change where majorities lie (McLean 2002), for example by dividing voters in low-paid employment from voters who are welfare claimants. From that perspective it might be argued that all politics is inherently about relativities, whether on the upside in good times or on the downside in bad times, and that the absolute level of resources is much less of the essence than the 'who gets what, when, how'[4] of whatever resources are available at any given point in time.

Fiscal Squeeze as a Political Blame Magnet or a Credit-Claiming Opportunity

Closely related to that first issue about what if anything is special about the politics of fiscal squeeze is the issue of how credit-claiming and blame-avoidance play out when governments are imposing losses rather than distributing gains. The post-2008 Eurozone crisis produced frequent repetition of an aphorism attributed to Jean-Claude Juncker, long-serving prime minister of Luxembourg and leader of the Euro group during a period of deep crisis in the currency union, namely that 'we [politicians in government] all know what to do; we just don't know how to get re-elected after we have done it'.[5] In the

[3] Of course, by the end of the book, several years and many pages later, Tolstoy reached a different conclusion.

[4] Harold Lasswell's (1936) famous definition of politics.

[5] *The Economist*, 15 March 2007, 'The Quest for Prosperity'. Later Juncker produced an addendum: 'For a long time, we didn't know what to do, and we still weren't re-elected' (*Der Spiegel*, interview with Jean-Claude Juncker, 11 March 2013). Prime minister of Luxembourg from 1995 to 2013, Juncker was chosen as President of the European Commission in June 2014.

same sort of spirit, it is said that in the 1980s the IMF's Fiscal Affairs Department had a 'rule of thumb' that the practical maximum of fiscal effort to be expected from governments was a 1 percentage point reduction of public expenditure relative to GDP each year.[6]

The implication of the much-quoted Juncker comment is that heightened distributional conflict (as tax burdens rise and/or government funding shrinks, raising the stakes in rival claims for resources) will tend to put the political 'blame game' into overdrive, with stronger pressure on incumbent office-holders of all kinds to shift or avoid the blame. The political science literature on blame avoidance stems in modern times from the work of Kent Weaver in the 1980s (Weaver 1986; 1988), which was later developed by other scholars, including Richard Ellis (1994), Raanan Sulitzeanu-Kenan (2007) and Christopher Hood (2002; 2011). From that perspective, if 'blame games' are accentuated during periods of fiscal squeeze, we could expect to see a number of developments in organisational arrangements, presentational strategy and policy design. Central or federal governments might delegate more fiscal responsibilities to lower levels of government, passing the political pain down the line or assigning responsibility for making painful choices to technocrats rather than elected politicians.[7] Political spin machines might be more active in orchestrating diversionary tactics or battening down the hatches when efforts to blame predecessors in office or inexorable outside forces reach their limits. Policymakers might develop more defensive approaches to policy, for example by making spending cuts or tax hikes that affect key voters harder to identify (such as by lengthening qualifying periods for benefits or letting third parties impose 'administration charges' that do not officially count as taxes).

But while those who follow the line of thought summed up by the Juncker aphorism see politicians who preside over fiscal squeezes in government as facing almost impossible blame-avoidance pressures, another line of analysis has tended to focus on the credit-claiming opportunities that successful handling of fiscal squeeze may offer to an incumbent government. In particular, Alberto Alesina and his colleagues have argued in numerous papers that successful pursuit of fiscal consolidation and adjustment (rather than courting voters with higher expenditure and lower taxes) can indeed allow incumbent parties to secure re-election, rather than face punishment at the polls by disappointed voters (Alesina *et al.* 2010). But Larry Bartels' (2013) comparative study of election results in periods of economic crisis in the 1930s and more

[6] Lord (Nick) Stern, who was a Visiting Fellow in the IMF's Fiscal Affairs Department in the 1980s, recalled this unwritten working rule in his opening remarks to the 2013 British Academy Conference at which the papers that form this book were first presented.

[7] This would align with depoliticisation initiatives even in good times, such as in central banking and economic regulation, designed to distance elected politicians from key decisions (Flinders 2005).

recent times concluded that outgoing governments tended systematically to lose elections in those circumstances.

Can these two approaches be reconciled? What if anything explains why some democratic governments (such as that of Canada in the 1990s) are able to implement fiscal squeezes and comfortably secure re-election, while in other cases (such as that of Ireland in the 1980s) governments pursuing such policies experience electoral defeats? Is it just some 'political leadership' *x*-factor, or are there other ways of explaining why fiscal squeeze sometimes seems to be a 'curse' for incumbent politicians but not at other times? There are several possible ways of explaining that. One possibility is that the politics of inertia offers more blame-avoiding opportunities than the politics of initiative (as argued by Rose & Karran 1987 and Rose 1990). If so we might expect governing parties that 'inherit' fiscal squeeze policies they can blame on their predecessors to experience a lesser degree of punishment by voters than those who both plan and carry through fiscal squeezes. A second possibility is that blame directed at governments may depend on constitutional and institutional arrangements, with division-of-powers and multiple-veto-point structures making it harder for voters to allocate blame to governments than in simpler structures (Anderson 1995).

More generally, blame outcomes might possibly vary according to the depth and provenance of fiscal squeezes. For example, it seems plausible to argue that there is more scope for blame to be attributed to outside forces—such as international bodies, financial markets, foreign governments—for those fiscal squeezes that occur during times of fiscal crisis (as in the case where currencies suddenly collapse or international credit is obtainable only at punitive rates or not at all) and can be represented as resulting from economic *force majeure* (or 'exogenous' forces in the jargon of social science). More problematic for blame avoidance may be those kinds of fiscal squeeze that occur during times of fiscal *stress* but not fiscal *crisis* and/or that seem to come from (endogenous) forces inside the political system, for example when tax revolts drive governments into cutting public spending. From a blame-avoidance perspective we might therefore expect apparently 'exogenous' pressures for fiscal squeeze to be played up or exaggerated by those domestic political players who favour spending cuts (or possibly tax rises) as a way to tackle long-standing political and institutional problems they see as stemming from an over-extended public sector.

A further aspect that may help to shape the politics of blame is the depth of fiscal squeezes. At the end of the previous section, discussing proxy measures for the political effort put into fiscal squeeze, we distinguished between 'hard' and 'soft' squeezes in expenditure and revenue in terms of whether these items changed both relative to GDP and in constant-price terms, or only in relation to one of these criteria. Of course, as already mentioned, politics is about relativities as well as absolute levels of spending. But if all else is equal we might expect squeezes that were 'hard' in those terms to be a greater magnet for blame.

Table 1.3 puts those two sets of distinctions together—that is, whether fiscal squeeze is triggered mostly by exogenous or endogenous pressures and whether, based on realised outcomes, it is 'hard' or 'soft'. As we go from exogenous to endogenous and from soft to hard types of fiscal squeeze, we might expect the blame risk faced by incumbent parties pursuing fiscal squeeze policies to increase. So the cases in the bottom right-hand cell (4) of Table 1.3—namely fiscal squeezes that are hard and endogenous—are particularly interesting for political analysis. How, if at all, can incumbents in government pursuing endogenous hard-squeeze fiscal policies shift or share the blame for the losses they impose on voters?

Stretching the concept of credit and blame beyond the issue of the electoral fortunes and political reputations of the political actors involved in fiscal squeeze are intriguing questions about who wins and loses the longer-term 'narrative' of fiscal squeeze events: for example, which policies come to be portrayed as successful 'best-practice' cases in the world of international econocrats, and which are written off as failures (Mauro 2011). This aspect of credit and blame reflects the interplay between expertise and politics, in terms of which studies or policy examples command widespread attention and which are ignored. Some countries' policies are presented as 'poster children', model cases to be emulated elsewhere, while others are ignored, and indeed, as we will see later, what can be dubbed a 'poster child' at one point in time can turn into a 'problem child' at another. The same goes for the credit and blame attached to experts and academics. For example, when the 2008 global financial crisis started to produce fiscal crises, political decision-makers looking for reputable evidence to support fiscal squeeze policies (Summers 2013) seized upon and lauded the (later much criticised) work of Reinhart & Rogoff (2010)[8] and also Alesina & Ardagna's (1998; 2009) theory of 'expansionary fiscal contraction'. A few years later those opposed to fiscal squeeze seized upon IMF research (Blanchard & Leigh 2012) that found that its previous estimates of fiscal multipliers had been too low (Portes 2012). So the 'credit and blame' game over fiscal squeeze goes well beyond the immediate party political battles. Narrative construction (Kahneman & Tversky 1984; Entman 1993; Riessman 1993) is central to the political framing of fiscal squeeze,

[8] In an OECD working paper, Égert (2012) was unable to reproduce the 90 per cent threshold on the debt/GDP ratio (above which growth is said to be damaged), which had attracted much political and official attention as confirming the urgent necessity of fiscal squeeze, notwithstanding the recession. Data errors were later argued to have compromised the Reinhart & Rogoff results (Herndon *et al.* 2013).

Table 1.3. Four types of fiscal squeeze politics.

	Type of trigger	
Realised outcome	Exogenous (squeeze triggered by outside forces)	Endogenous (squeeze triggered by internal developments)
Soft	**1** Scope for external blame: high Type of loss imposition: relative	**2** Scope for external blame: low Type of loss imposition: relative
Hard	**3** Scope for external blame: high Type of loss imposition: absolute	**4** Scope for external blame: low Type of loss imposition: absolute

with the technical debates sometimes proxy wars between competing visions about the scale and scope of the state.

Fiscal Squeeze as a Critical Historical Juncture or a Political Sugar Rush

Related again to the issue of how the politics of credit and blame plays out during fiscal squeeze is a question about the longer-term political and social consequences of such squeezes. The rhetoric of political debate during battles over spending cuts or tax increases tends to be full of fervent claims by proponents and opponents about the likely effects of such policies (whether beneficial, deleterious, or regrettable but necessary). Proponents present them as vital medicine for preventing collapse and improving social conditions in the medium or long term, while opponents present them as likely to unwind fundamental social compacts and unleash deep and irreversible social damage. Both sets of arguments tend to play up the 'never-the-same-again' consequentiality of such policies, and critics of fiscal squeeze naturally tend to highlight those groups and institutions who can be portrayed as winners and losers (for instance, federal or national governments versus local or state governments, technocrats versus elected politicians, private sector employees versus public servants, the employed relative to the unemployed) and to suggest that those losses will not be reversible.

Nor are such disputes confined to the politicians of the day. Some scholars and historians have made similar claims about episodes of fiscal squeeze as representing what historical institutionalists term 'critical junctures': landmark events or decisive forks in the road that are deeply consequential for policies and institutions long into the future (Cappoccia & Kelemen 2007). For example, Alasdair Roberts (2012), in his account of the United States' financial crisis and later fiscal squeeze in the first half of the 19th century, sees major long-term institutional developments, such as the strengthening of the executive relative to the legislature and the development of modern bureaucratic policing, as flowing from that episode. Robert Skidelsky (1967: 386–7) attributes the way the UK's 1929–31 Labour government handled the challenges of fiscal squeeze as 'determining' the politics of the subsequent decade, in particular by helping 'to create and confirm a mood of national self-doubt, of pessimism regarding the future, in which appeasement could flourish'. The implication is that some years later it will be easy to trace fundamental longer-term changes in politics and society to significant episodes of fiscal squeeze.

The alternative null hypothesis to that vision of fiscal squeeze as highly consequential in the long term is that such episodes, albeit much quarrelled over in the short term, tend to be 'blips' or political 'sugar rushes', quickly reversed in a longer-term pattern of government growth in spending and taxing. The implication is that after those episodes, spending starts to rise as soon as immediate pressure for restraint fades, normal party political competition resumes under the usual rules of the game, and path dependency in the main lines of policy development hardly changes in the long term.

Such questions of consequentiality are central to the politics of fiscal squeeze, but are typically easier to ask than to answer. That is partly because political effort will typically go into muddying the distributional effects of fiscal squeeze policies. But it is also because cause and effect are always difficult to establish definitively in history and social science. Claims about the long-term effects of such squeezes on the electoral fortunes of political parties associated with them, on broader public attitudes to egalitarianism, 'big government' or redistributive state spending and even constitutional or major institutional changes, are easier to make than to prove at a standard that would satisfy a criminal court. Counterfactuals (like Robert Fogel's (1964) famous attempt to imagine how 19th-century America might have developed without railways) can always be contested and it is easy to fall into the *post hoc, ergo propter hoc* fallacy (that is, that if B follows A, A must have caused B). That is part of the reason why consequentiality is so debatable.

The standard scientific way of dealing with this classic problem is by methods of sensitivity analysis and 'consilience' (a term which comes from Whewell (1840) and means putting together different strands of evidence and seeing if they point in the same direction). And when we apply that sort of approach, as we shall see later, we find that in some cases fiscal squeezes do not seem to constitute critical junctures; in other cases we can more confidently attribute significant political and social consequences to them; and in others again the links are debatable.

That in turn raises the question: if fiscal squeeze sometimes seems to be consequential and sometimes not, what accounts for that? Could it be that (like public service reform, argued by scholars such as Chapman & Greenaway (1980)) fiscal squeeze only produces long-term consequences if the 'austerity' agenda somehow connects with other pressures for major changes in political direction? After all, advocates of deep reductions in public spending have always existed, independent of whether there is a current fiscal problem. For example, Tanzi & Schuknecht (2000) judged desirable a return to the public expenditure levels of *circa* 1960 (when industrialised countries averaged below 30 per cent of GDP); they also commended the *circa* 20 per cent ratio of newly industrialised countries, doubting the value of recent redistributive activity beyond 'core activities'. But financial crises can sometimes give renewed traction to such views. The same can go for other policy changes, for example when the UK's fiscal squeeze under a Labour government in the late 1970s paved the way for subsequent decisive changes in political direction under the Conservative government led by Margaret Thatcher,[9] with implications not only for the UK but also for other countries to which privatisation, deregulation and marketisation were exported.

What Does it Mean to Put Fiscal Squeeze into *Perspective*?

This book is primarily an exercise in comparative public policy rather than one of the many 'how to do it' guides to fiscal management that have emerged since the late 2000s, and its aim is to put fiscal squeeze into perspective. Putting the politics of fiscal squeeze into perspective means at least three things. First, we need to understand episodes of squeeze against the background of what else was happening within the society concerned (for example, whether there was an accompanying financial crisis) and what was happening in the wider world. Second, we need to look at episodes of fiscal squeeze with the benefit of hindsight, looking at what happened afterwards to see whether the squeezes had the effects claimed of them. And third, we need to compare fiscal squeezes with one another to see what, if any, common patterns they display. We do that partly by comparing aggregate data for the nine country episodes in Chapter 2 on as consistent a basis as possible, given the range of the cases in space and time. But we also need to look at the more qualitative political story behind those numbers, to explore how the politics worked and how blame was attributed, deflected or avoided.

The purpose of careful contextualisation is to try to pin down the specific contingencies that shape the process and effects of fiscal squeeze—an obvious point but one often neglected by policy advocates looking for models whose success can be replicated elsewhere. For example, those policy advocates who at the outset of the current era of fiscal squeeze after 2008 saw the 1980s and 1990s policies of Canada, Sweden and Ireland as models to follow ignored features of those experiences that were distinctive to each country (such as the

[9] Gamble (1988) characterised the shift as towards the free market and the strong state, with the latter making the former possible.

lack of mainstream opposition in Canada) or to the era in which they occurred (such as a benign international environment in the mid-1990s), and that is an error that careful contextualisation can help us to limit if not avoid. History tends to be written by winners and spinners, so it is important to look critically at cases that have become 'poster children' as against those not so sanctified or considered as 'basket cases', to see how far claims of transferable 'best practice' can be justified (OECD 2011).

Our Nine Cases

This book aims to combine a 'spreadsheet' approach to comparing fiscal squeeze with qualitative accounts of a set of country episodes intended to explore the politics behind the reported numbers and to explore what if any medium- or long-term consequences might plausibly be attributed to those various squeezes.

The conventional econometric way of selecting cases for comparative studies of fiscal consolidation is to identify episodes using *ex post* data relating to reported financial aggregates and GDP outcomes, using stipulated statistical cut-off points. But, as we have already pointed out (and the same point has been made by numerous critics of the standard econometric outcome-based approach, for example by Dellepiane-Avellaneda 2010), fiscal squeeze—defined as pronounced political effort on the part of governments to improve their public finances—is harder to put into numbers, since political effort is not always translated into outcomes reflected in economic data. Fiscal squeeze may or may not lead to fiscal consolidation, and fiscal consolidation can occur with or without fiscal squeeze.

We chose our cases here on a quite different basis. We restricted them to a small enough number (nine) to be explored qualitatively within a book-length study. We chose cases that involved different state types and that took place sufficiently far back in time to allow us to explore what happened afterwards and assess the consequences of fiscal squeeze at least ten years after the event. Instead of basing our cases on deficit-reduction-based analysis, we chose cases that involved *both* substantial cuts in expenditure or revenue increases (as measured by outcome data) *and* fiscal squeeze in the sense of political effort (as judged by country specialists). All of those cases involve fiscal adjustments that can justifiably be described as large and unusual in that country's experience, involving dramatic packages designed to restore fiscal health. Where they differed was in the relative proportions of spending reductions and tax increases that went into the fiscal squeeze, the mixes of monetary policy and changes in market regulation that accompanied them, and in the international economic context in which they occurred: for example, whether currency devaluation was possible and whether key trading partners were growing strongly or suffering from comparable difficulties.

Finally, within those limits we chose cases that are puzzling or contested in some way. By 'puzzling or contested', we mean cases that (i) appear to go contrary to stereotype or involve a major change of path for governments and institutions; (ii) have acquired a 'poster child' or role-model status in the recent what-to-do policy literature that merits a more critical assessment; and/or (iii) would not necessarily be picked up by the standard methodology of the *ex post* approach. Table 1.4 summarises how the cases we discuss here can be rated on those three criteria.

Thus Alasdair Roberts in this volume analyses the fiscal squeeze following from state government defaults in the United States in the early 19th century, a case hitherto seldom discussed in the fiscal consolidation literature, but which left a profound constitutional and institutional legacy and has strong relevance to many of the issues now being discussed concerning the fiscal

Table 1.4. Nine cases of fiscal squeeze that are puzzling or problematic.

Case	Decades of hindsight	Counters stereotype or seems to involve change in path?	International 'poster child' meriting closer or more critical assessment?	Problematic for conventional *ex post* selection approach?
United States 1840s	18	Perhaps[a]	No	Yes[b]
United Kingdom 1920s	9	Perhaps[c]	No	Yes[b d]
Netherlands 1980s	2.5	Yes[e]	No	Yes[f]
Ireland 1980s	2.5	No	Yes	No
New Zealand 1990s	2	No	Yes	No
Canada 1990s	1.5	No	Yes	No
Sweden 1990s	1.5	Yes[g]	Yes	No
Germany 1990s–2000s	1	Yes[h]	Yes	No
Argentina 1990s–2000s	1	Perhaps	No	Perhaps[i j]

[a] Because the case has been little discussed and goes against contemporary assumptions about US hegemony.
[b] Because the case dates from before the time of modern national accounts.
[c] Because deep spending cuts were made to a budget already in balance.
[d] Because the case is not picked up by *ex post* deficit-reduction analysis.
[e] Because the country changed from a 'Scandinavian' to a more conventional Northern European fiscal profile over the 1980s.
[f] Because the squeeze in local government spending does not show up in conventional national-level numbers.
[g] Because the squeeze involved significant cutbacks in welfare entitlements in an archetypical welfare state.
[h] Because a major squeeze took place in a political system often characterised as slow-moving, with multiple veto points and consequent 'joint decision trap' features.
[i] Because currency collapse and default produces only one year of unambiguous spending cutbacks.
[j] Because the political effort prior to 2003 is not reflected in fiscal outcomes.

politics of the Eurozone. Christopher Hood and Rozana Himaz analyse the 1922 ‘Geddes Axe’ in the UK—a case nowadays often considered more as a ‘problem child’ than a ‘poster child’, in which the deepest cuts in UK civil spending in the last ninety years were made from a budget already in balance and in the middle of a deep recession. Walter Kickert explores cuts in spending by Dutch local authorities (which provide an important part of the Dutch public services) in the 1980s—a case which barely registers as a ‘fiscal consolidation’ since the local cuts are masked within overall national figures, and which reflects a process of fiscal repositioning over the 1980s that took the country from public expenditure/GDP ratios quite close to Scandinavian levels to levels more in line with non-Scandinavian Northern Europe. Niamh Hardiman analyses the severe fiscal squeeze in Ireland in the late 1980s (which made it a ‘poster child’ of expenditure-led fiscal adjustment and immediately preceded Ireland’s much-vaunted ‘Celtic Tiger’ period) and compares it to the ferocious fiscal squeeze applied in Ireland, under external supervision, two decades later, after it became an early casualty of the Eurozone crisis of the late 2000s.

Of the five more recent cases, those of New Zealand, Canada and Sweden in the 1990s (analysed here respectively by Robert Gregory and Chris Eichbaum, Donald Savoie, and Anders Lindbom) have been extensively canvassed as role models, both by international organisations and by those centrally involved in these country episodes, and so merit a careful reassessment more than a decade after the event. These cases bring out the very different political structures and situations in which fiscal squeezes can take place—for example, virtually no mainstream opposition in the Canadian case as against a precarious coalition in Sweden; a federal structure with provinces to be squeezed through unfunded mandates in Canada as against a highly centralised unitary system in New Zealand. They also bring out the often undiscussed fact that all of these ‘poster child’ squeezes took place in the context of a relatively benign international economic environment. The German fiscal squeeze some years after unification (analysed by Martin Lodge and Kai Wegrich) is also a ‘poster child’ case, as a much-cited example of successful adjustment at the core of the Eurozone. It is also politically significant because it goes against the conventional characterisation of the German political system that might be expected to militate against decisive and ‘hard’ fiscal squeeze. The most recent case in this collection, that of Argentina as it went through the throes of default and devaluation, is analysed here by Sebastián Dellepiane-Avellaneda. Again, this case involved massive political effort to correct the public finances (after deep currency crisis followed by default and the drying up of foreign credit) but it barely shows up as ‘fiscal consolidation’ on conventional measures because GDP was falling by more than public spending.

Of course this analytic approach to case selection does not constitute a representative sample in the conventional analytic sense, does not match fiscal squeeze episodes with non-episodes in the style of randomised controlled trials (often seen as the 'gold standard' for policy analysis and social science more generally (Cartwright & Hardie 2012)), and falls a long way short of the massive datasets used by scholars in some other comparative studies. But it allows us to look at data much more critically than such studies can normally do, and shows up the limitations of the available documentary data in what it can tell us about 'fiscal squeeze' rather than taking the conventional point of departure which assumes that officially reported numbers of financial aggregates are necessarily valid and reliable bases for elaborate statistical analysis. And while this approach necessarily allows only limited positive generalisations, it does provide us with a basis for disconfirmation of commonly asserted propositions, on the 'black swan' principle that it only takes one negative case to undermine generalising claims.

The Plan of the Book

Comparisons across space and time can never be perfect, as already noted. But even with all the inevitable limitations discussed in the previous section, a comparison of the politics of fiscal squeeze across nine cases of democratic government in different times and places can improve our understanding of the three analytic questions that we posed earlier, namely whether there is something fundamental that distinguishes fiscal squeeze from other types of politics, how episodes of fiscal squeeze affect credit and blame, and what, if any, medium- or long-term consequences for politics and the society more generally these episodes leave behind.

To help throw light on those analytic questions, each of the country chapters and the comparative data analysis in Chapter 2 explore what seems to have prompted fiscal squeeze in each particular case, how the process of fiscal squeeze worked and what, if any, longer-term political and other social consequences can be traced in retrospect to the squeeze episode. The first issue, of what prompts fiscal squeeze, can help us to assess whether such episodes all seem to be prompted by the same standard set of economic or financial circumstances—such as debt and/or deficit levels—that make fiscal squeeze 'inevitable', and how far politics plays into the decision to squeeze. The second issue, of how the process of fiscal squeeze works, can help throw light on whether and how far there is something distinctive about the politics of fiscal squeeze, for example whether and how governments crafted their policies in the light of constitutional or public-order challenges, and whether fiscal squeeze produced political crisis or was handled by some version of politics-as-normal. The third question, of what the political and social consequences of fiscal squeeze were in the short, medium and long term, can help to throw light both on the politics of credit and blame and on the 'consequentiality' questions discussed earlier. Were spending cuts and tax increases reversed and, if so, over what time period? How did the process affect intergovernmental relations, and with what consequences? Who were the long-term winners and losers from the process and what were the political and electoral effects in terms of political blame and credit accruing to political parties and their leaders? Is it possible to identify broader social consequences of fiscal squeeze, such as changes in the power of elites, threats to civil peace or even threats to democratic government?

We return to these questions in the final chapter, where we also discuss what if anything today's policymakers can learn from a contextual analysis of yesterday's fiscal squeezes.

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