Withdrawal symptoms: an assessment of the austerity packages in Europe

—

Sotiria Theodoropoulou and Andrew Watt

Working Paper 2011.02

etui.

Withdrawal symptoms: an assessment of the austerity packages in Europe

—

Sotiria Theodoropoulou and Andrew Watt

Working Paper 2011.02
european trade union institute

Sotiria Theodoropoulou and Andrew Watt are
senior researchers at the European Trade Union Institute.

Brussels, 2011

Print: ETUI Printshop, Brussels

D/2011/10.574/21
ISSN 1994-4446 (print version)
ISSN 1994-4454 (pdf version)

The ETUI is financially supported by the European Union. The European Union is not responsible
for any use made of the information contained in this publication.

Contents

Executive summary

- For the years 2011 and 2012, the discretionary retrenchment measures planned correspond to 0.9% of GDP per year. The currently envisaged discretionary contraction is substantially greater than the 0.5% structural adjustment foreseen by the previously prevailing fiscal rules in the EU. This is in spite of the unusually slow recovery from this recession, the most serious experienced in postwar Europe.

- There is considerable variation in the size of packages across countries. By far the largest adjustment has been or will be undertaken by countries which either have sought external assistance from the EU/IMF (Hungary, Latvia, Greece, Ireland) or have been (or come close to) facing a public debt financing crisis in the markets (Portugal, Spain).

- The time span of the austerity packages often extends well beyond 2012 with the intensity of the adjustment being in many cases frontloaded to 2011 and 2012, that is, while the recovery is still predicted to be fragile and uncertain. This is especially the case in countries where the recession has been most severe.

- The distribution of measures between expenditure cuts and tax rises is skewed in favour of the former in most countries for which we received information. Social protection and public administration predominate among the areas of public expenditure which governments have targeted for expenditure reduction, while indirect tax rises predominate among the types of revenue that most governments have chosen to raise. A broad-brush evaluation suggests that, in most countries for which we received information, the austerity packages are likely to have regressive effects on income distribution. In France and Luxembourg, however, progressive distribution effects are expected from the measures which are focused on higher income taxes.

- Pensioners, public sector employees and welfare benefit recipients are among the groups in society likely to be most severely and adversely affected by the measures in most countries.

- It is questionable whether the planned adjustment in the public sector balances is compatible with changes in net private-sector savings-investment behaviour and net export performance that can be reasonably expected at forecast rates of GDP growth, given historical patterns within countries. In this respect, there are doubts whether the planned adjustments would alleviate the current macroeconomic imbalances within the EMU: countries with current account surpluses are currently planning to implement fiscal adjustment programmes that rely to a considerable extent on these surpluses increasing, making the adjustment of countries with current account deficits even more difficult.

– It is doubtful whether EU countries are willing and/or able to combine fiscal austerity with the measures required to achieve the longer-term goals of 'smart, sustainable and inclusive growth' set out in the Europe 2020 strategy. Of particular concern in that respect are planned cuts in public investment and in education and training expenditure. Some limited attempts are, however, being made to achieve consolidation using measures that promote 'green transition'. Given the combination of the direct effects of the crisis (especially high unemployment) and the regressive impact of the austerity measures in most cases, it is hard to see how, under such conditions, any substantial progress in reducing (relative) poverty, along the lines envisaged in the Europe 2020 strategy, can be made in most EU countries over the next few years.

– In most countries for which we received responses, while some form of social dialogue did take place prior to announcement of the austerity packages, in the final outcome the views of trade unions were largely ignored. In several member states, what is more, there was no social dialogue at all.

Introduction

The Great Recession blew a huge hole in the public finances of EU Member States. In 2007 budget deficits in both the EU and EMU were almost in balance. By 2010 the combination of the automatic effect of the recession on both spending and revenues, the discretionary measures adopted by governments to stimulate recovery, and the funds they committed to rescue the banks, had pushed deficits to 6.8% in the EU and 6.3% in the euro area. Outstanding (gross) government debt is forecast by the EU Commission to rise to over 80% of GDP, more than 20 p.p. above the Maastricht debt limit.

In 2009 the ETUI produced a report, based on a survey of national experts, on the stimulus packages adopted by EU governments (Watt 2009). This follow-up report charts the reverse process: the austerity packages adopted by governments in an attempt to rein in their deficits and reduce their debt levels.

The turnaround from stimulus to austerity came suddenly in the Spring of 2010. The trigger was undoubtedly the Greek crisis (Watt 2010a). Greek debt had already been high prior to the crisis. Its taxation system was woefully inadequate as was the tax take. There were increasing doubts about the reliability of the statistics. Moreover, Greece, it was clear, would have to deflate its economy in order to reduce nominal wages and prices in order to regain lost competitiveness, implying an extended period of, at best, very sluggish nominal GDP growth. This was a poisonous combination.

All of a sudden, investors who had for the entire EMU period been happy to purchase Greek debt at more or less the same yield as that of Germany and other countries demanded substantially higher interest rates to hold Greek government bonds. Banks rushed to dump Greek assets, threatening the banking system, not only in Greece but also Europe-wide, with a renewed crash.

This led, on the one hand, to a bail-out and subsequently the establishment of the European Financial Stability Facility to protect other countries in a similar situation, with Ireland receiving a bail-out in October 2010. On the other hand, there was a huge incentive for countries to avoid being the next in line. Countries under pressure, such as Portugal, Ireland and Spain inside the euro area and the UK outside, announced tough austerity packages in an attempt to convince the markets that they were different cases entirely. At the same time, the provision of support packages also led, naturally enough, to the imposing of conditions on countries in receipt of support and, more generally, collective pressure to be seen to be tough on deficits.

Over time indeed, it seemed to be the case that governments increasingly purported to believe that fiscal deficits had caused the crisis, rather than the other way around.

The task of this report is to map out the outcomes and some of the implications of this austerity drive, to the extent that they were visible by the end of 2010.

We hope that this initiative will help provide feedback to national governments and other policymakers at both national and European level, not only on the effectiveness of their fiscal adjustment packages but also on their consequences for society. The report is based on a survey sent out to national experts who, in most cases, were members of the TURI network, a European network of national trade-union-related research institutes.[1] For a few countries, information was provided by research institutes that do not belong to TURI or by trade union experts. The ETUI is very grateful to all contributing colleagues for the information provided and their assessments. A list of all contributors is provided in an annex to this text. The authors are responsible for the evaluation drawn up on the basis of this information and set out in the following pages.

A number of other institutions have also examined the austerity packages (e.g. IMF, 2010). We have adopted both a comparative-national and a European perspective on the austerity packages and sought to extend our evaluation beyond their extent, composition, and the extent to which they are likely to be effective in consolidating public finances, in order to take in more qualitative characteristics. In particular, we have been interested in the austerity packages' potential effects on income distribution, in their impact on disadvantaged groups in society and on the objectives of the Europe 2020 strategy. We have also sought to identify the extent of involvement of the social partners at national level in devising these packages and the positions taken by the trade unions.

The report is structured as follows. Section 1 briefly describes some of the methodological issues involved in a survey-based report of this type. The second section paints the big picture of the size and timing of the packages for all those countries for which we have information. The remaining sections broaden out the analysis to more qualitative aspects. Section 3 looks at the split between revenue- and expenditure-side measures of different types, and considers the overall impact on income distribution. In Section 4, we consider the likely impact on specific groups of the population and this is followed, in Section 5, by an evaluation of the packages in the light of the priorities of the Europe 2020 strategy. Finally, we briefly report on our national experts' own assessments of their respective national packages (6) and, in the last section (7), on the role played by social dialogue and the evaluation by trade unions.

1. The authors would like to thank Mariya Nikolova, coordinator of the TURI network, for her assistance with the survey.

1. Methodological issues

We received completed questionnaires from seventeen of the twenty-seven EU member states, namely, from Austria, Bulgaria, Cyprus, Denmark, Germany, France, Greece, Hungary, Ireland, Italy, Latvia, Luxembourg, Poland, Portugal, Spain, Sweden and the United Kingdom. These countries represent 87 % of the GDP of the EU27. For the main macroeconomic indicators (size of packages and the distribution between spending and revenue side measures) we have extrapolated the figures based on these countries to the EU27 aggregate. The implicit assumption is that the outcomes for these main variables are broadly the same in the remaining countries. As they represent only 13% of GDP, small deviations will not matter greatly. The anecdotal sources available for some of the missing countries (e.g. Netherlands, Belgium) do not suggest that the approach adopted to fiscal consolidation differs in any systematic way from the figures presented here.

Moreover, the countries in our sample can be considered broadly representative of the EU as a whole, including as they do 'core' west European, 'peripheral' western and southern Europe and the range of central and eastern European countries. In the case of more detailed variables and breakdowns, where more qualitative assessments are necessary, not all questionnaire respondents were able to provide all the information requested and/or figures could not simply be aggregated. We, therefore, refrained from aggregation and extrapolation in such cases and discuss the national findings from a comparative perspective.

The information gathered relates to fiscal retrenchment packages that were adopted following the global financial crisis. The starting point is, in most cases, 2010. In some cases, such as Hungary and Latvia, where the crisis hit early, packages were adopted earlier than 2010, and these have also been included here. At the same time, we have sought, wherever possible, to distinguish those measures that were taken in response to the crisis from any fiscal rules or measures that were already in place before it hit . The general cut-off point for the data is November 2010, when the questionnaires began to be returned. In a number of cases, such as Ireland and Portugal, information that has become available since that date has been added.

Analysing government 'tax-and-spend' policies is fraught with difficulty. How should, for example, a spending freeze in a given area be evaluated? What is the basis for comparison? With the inflation-adjusted level? With previous fiscal plans? What about the non-renewal of time-limited measures? An additional problem is the knock-on effect of the fiscal contraction on GDP and thus on the denominator of deficit and debt-to-GDP ratios.

Inevitably, in attempting to compile findings from a large number of diverse countries, where data is in some cases rather patchy, compromises have to be made and some inaccuracies will have crept in. We have tried, wherever possible, through cross-checking with other sources and interaction with our national experts, to clarify major discrepancies. Still, the findings presented here should be taken as indicative of orders of magnitude. They represent a fairly simple adding-up of the expected size of announced packages and/or individual measures. Vague declarations of intent and measures that lack a quantitative basis are not included. In fact, in most member states for which we collected information, governments did not stick to 'cheap talk' in order to appease the markets, but have started enacting the majority of the planned measures that they announced. Having said that, of course even future already planned measures might not ultimately be implemented in full.

While these caveats obviously need to be borne in mind when interpreting the findings, the comparative approach taken here does have major advantages, for it enables the different policy options adopted by countries in frequently similar situations to be compared to one another. Moreover, the cumulative effects of fiscal consolidation across Europe can be better appreciated.

2. The objectives, overall size and timing of the austerity programmes

Overview

In the wake of the Greek sovereign debt crisis in the spring of 2010, fiscal austerity measures were announced in many EU member states in the course of that year. In most cases, the reason stated by governments for their adoption was to correct budget deficits that had been expanding rapidly in the wake of the crisis as spending shot up and tax revenues dried out, and governments launched discretionary fiscal counter-measures (Watt 2009). More specifically, the governments of member states also referred to the need to comply with the Stability and Growth Pact rules or, where appropriate, the Maastricht criteria for entry to EMU. In some countries an additional important constraint was to avoid suffering a Greek-style debt-financing crisis on the financial markets. A number of the member states worst hit by crisis, namely Latvia, Romania, and Hungary outside the euro area, and Greece and Ireland within it, received external support from the International Monetary Fund and – in various guises – the European Union; this support was conditional on their governments' announcing austerity programmes.

Table 1 below provides an aggregate picture of the size of the austerity packages in the EU as a whole (extrapolated from our sample as explained above) for a period that runs from 2007 to 2015. Austerity programmes differ from one another in terms of their time span. In some cases, governments have indicated a three- or four-year programme, but concrete quantitative estimates are available for only the first year or two. Moreover, we of course need to estimate nominal GDP in future years in order to estimate package sizes as a share of GDP: this has been done by extrapolation. For all these reasons, the reliability of the forecasts declines as we move further into the future. The main focus is on total size of currently announced austerity packages in Europe for 2011 and 2012, that is, the years during which the majority of austerity measures will be undertaken in the EU, and where reliability is reasonably assured. However, in many countries, these programmes are scheduled to run well beyond 2012 and, of course, additional contractionary packages may well be announced in coming months and years. It is important therefore to emphasise that the assessments here should be seen as a minimum (more on this below).

Table 1 **Austerity packages in the EU** (Based on 6-17 countries, depending on the indicator, representing approx. 55-87 % of EU27 GDP)

Austerity packages	From 2010 onwards*	Including measures prior to 2010*
Total (bn euros)	-487	-501
	2011 (% GDP) (12 countries)	2012 (% GDP) (6 countries)
Simple average	-0.9	-0.9
Weighted Average	-2.7	-3.6

Source: Own calculations based on our survey

* Extrapolated figures

The austerity packages currently in force or being planned will amount to a total of 487 billion euros for the next 3-5 years (see Table 2 below for more details on their duration by country), whereas if we added measures taken prior to 2010 in Hungary, Latvia and Ireland, the packages amounted to 501 billion euros. On average (weighted by GDP), these measures will correspond to 0.9 % of GDP per year in 2011 and 2012. It should be noted that the 2011 figure was calculated for 12 countries representing 69% of the EU GDP, whereas the 2012 figure was calculated for only 6 countries representing 55% of the EU GDP. As such, our figure for 2012 is probably less reliable than the one for 2011.

In passing, it is worth noting that the simple average of the national packages is substantially greater, indicating that packages are larger in smaller than in large countries (see below).

To put this number in context, the pre-crisis fiscal rules in the EU foresaw adjustments in the cyclically adjusted balance – which roughly corresponds to the discretionary measures considered here – of 0.5% a year. As such, the envisaged discretionary contraction now being implemented is clearly substantially greater. We could also compare with the historical record, but there are serious data constraints. Cyclically adjusted budget data are patchy up until the late 1990s and so aggregate figures are not available. In any case, the figures are only a rough guide to the size of discretionary measures and are subject to uncertainties about the rate of potential output growth. For what such comparisons are worth, the tightening in 2005 and 2006 was very mild by comparison, averaging less than 0.5% a year (data from AMECO). It is true that some individual countries have seen even stronger fiscal austerity packages in some years, again as suggested by the cyclically adjusted balances. The late 1990s saw a series of shifts in excess of 1% of GDP per year in the structural balances, in the UK, or in Belgium in the mid-1990s, for example. But these are *individual* cases, offset in their overall impact on the European economy by expansionary or at least neutral policies in other European countries.

What clearly emerges from these comparisons is that the size of the discretionary austerity measures *across the whole of Europe* planned for 2011, 2012 and (albeit with less quantitative certainty) subsequent years is certainly unprecedented.

The packages by country

The averages given above conceal large differences in the size of the austerity packages (see Table 2). The variance can be explained both by the different circumstances under which they have been adopted and by the views of the government in place. In 2011 the smallest reported retrenchment package is in Germany, which is not surprising given its very large current account surplus, unchallenged position as the issuer of benchmark European sovereign debt, and relatively fast recovery from the crisis. Similarly, a fiscal expansion of 0.4 % of GDP is planned in Sweden for 2011. More surprising are the comparatively low figures for Spain. By quite some margin, the highest figure is that for Greece, at more than 6% of GDP, followed by a number of central and eastern European countries and Ireland. Generally speaking, the ranking of countries is quite similar in 2011 and 2012, a notable exception being the UK which has 'backloaded' austerity to a considerable extent to 2012.

Member states, such as Hungary, Latvia, Greece and Ireland, that faced balance-of-payments or debt-financing crises and have sought external assistance from the EU and the IMF, have had to adopt far more severe measures, as measured by the size of the retrenchment as a share of GDP and the speed of adjustment (so-called 'frontloading'), than countries that did not. In this respect it should be noted, however, that the measures taken by the Hungarian centre-right government from 2010 onwards and reported in Table 2 were its own choice rather than attributable to any IMF conditionality.

Considering country cases in more detail, Portugal, which as this report went to press became the third country to seek financial assistance from the EU/IMF, has adopted an austerity package projecting an adjustment totalling 21.7 billion euros between 2010 and 2013. It should be noted that, under market pressures, the government had to start some of the measures already during 2010, and in September it had to take additional measures, as the Portuguese economy slowed down, in order to meet the set adjustment targets,.

Hungary and Latvia started pursuing fiscal retrenchment as early as 2006 – i.e. before the crisis – and 2008 respectively. In the former, the budget deficit had reached 9.4 % of GDP in 2006. Although this imbalance had been corrected by 2008 when the budget deficit was down to 3.8 % of GDP, the country faced turbulence in the international financial markets in that year, which led its government to seek assistance from the IMF and the EU; within this framework, it agreed to reduce the deficit by a further 2.4% of GDP that year. The combination of the measures taken in the context of conditionality and the international crisis resulted in falling short of public revenue targets to such an extent that further assistance and a third fiscal adjustment programme were necessary in March 2009.

In the case of Latvia, public finances deteriorated when the government took over the liabilities of the second largest bank in the country which was on the brink of collapse in 2008. To avoid a balance of payments crisis, Latvia applied for IMF assistance, the first part of which was received in December 2008. In early 2009, additional assistance was agreed and granted by the European

Union, the strict conditions of which were laid down in a Memorandum of Understanding. The declared objective of this international aid was to restore the country's fiscal stability. The severity of the measures in Latvia, coming on top of the bust in private-sector demand, was such that the country experienced a reduction in its real output of 18% between 2008 and 2009. This is a decline in output growth rate comparable to the traumatic transformation crisis experienced in the Latvian economy in the early 1990s.

Table 2 **Fiscal adjustment programmes by country**

	AT	BG [7]	CY	DE	DK	ES	FR	GR [8]	HU [9]	IE [10]	IT	LV [6]	LU	PL	PT [8]	SE	UK [4]
Planned end-year	2014	2011	2013	2014	2013	2012	2014	2013	2010	2014-2015	2012	2012	2014	2013	2013	2011	2015-2016
Overall size of austerity package (bn euros)	-13.6	-0.8	-0.3	-80	-3.3	-15.3	-83.2	-37.6	-9.4	-22.3	-37	-2.0	-0.7	-0.2	-21.7	1.4	-129
2010 (% GDP) [1]		-2.3				-0.5		-5.6	-4.4	-2.1	n/a	-4.0		-0.6	-1.2 [3]		-0.5
2011 (% GDP)	-0.8		-1.4	-0.4	Tba	-0.9	-1	-6.3	-3.8	-2.6	Tba	-2.2	-1.5	Tba	-4.9	0.4	-1.5
2012 (% GDP)	-0.3		Tba [2]	-0.3	Tba	Tba	-1	-2.4	-1.5	-3.8	Tba	Tba	Tba	Tba	-2.8		-1.6
2013 [5] (% GDP)	-0.1		Tba	-0.2	Tba	Tba	-1.1	-2		Tba			Tba	Tba	-3.6		-1.4
2014 (% GDP)	-0.2			-0.1			-0.9							Tba			-1.1

Sources: Responses to and own calculations based on our survey and supplementary research from government websites and other sources (see also footnotes)

(1) As far as possible, the figures reported per year refer to the value of new fiscal measures taken during that year as a percentage of GDP.

(2) To be announced. Refers to measures not yet announced even though the duration/total size of the package have been announced.

(3) Due to insufficient available information, this figure refers to only part of the retrenchment measures taken in Portugal for 2010 and it is, therefore, understating the amount of retrenchment for that year.

(4) The distribution of retrenchment measures over time is shown as a percentage of National Income for the UK (source: www.ifs.org.uk/publications/5311). The reported total amount of retrenchment was converted from pounds sterling to euros using the exchange rate of 25 February 2011 (source: www. Xe.com/ucc/)

(5) In all cases except the UK and Portugal, the share of fiscal adjustment over GDP in 2013 and 2014 was based on our own extrapolated GDP figures.

(6) The figures for Latvia are subject to much uncertainty as there are no official announcements about the overall size of the packages and the retrenchment programmes have been subject to regular revision. The size of the total package that is mentioned here refers only to announced measures for the years 2009-2011. It is likely that the total size of fiscal retrenchment in Latvia is under-reported.

(7) The figure of the total package for Bulgaria was converted into euros using the exchange rate of 25 February 2011 (source: www. Xe.com/ucc/)

(8) The total and annual figures used for the distribution of fiscal measures over the years in Greece and Portugal have been taken from the Stability and Growth Programmes devised by their governments in early 2010 and their subsequent updates in view of the escalating debt financing crisis, the memorandum of understanding that the Greek government signed with the EU and the IMF in May 2010, and the documents outlining the government budgets for 2011 in both countries. All these documents can be found at www.minfin.gr/portal/en (Greece) and www.min-financas.pt/english/default.asp (Portugal).

(9) The figures for Hungary refer to packages implemented in 2007, 2009 and 2010 respectively. The nationalization of the private pension schemes is not considered in this analysis.

(10) The annual figures for Ireland refer to the years 2009, 2010 and 2011 respectively. The total size of measures but not their annual distribution has been announced for 2012 and 2013.

Greece and most recently Ireland have had to seek, and have received, financial support from the EU and the IMF as the costs of financing their public debt rose to prohibitively high levels during 2010 (Clancy/McDonnell 2011). In the former case, a special rescue package was devised in May 2010 amid fears that the debt-financing crisis would spread to other members in the Eurozone periphery. Soon after the Greek package was announced, the European Financial Stability Facility was set up and Ireland was, last December, the first country to seek funding from the new facility. Both countries have had to sign memoranda of understanding with the funders setting out tough conditions, the fulfilment of which will be regularly reviewed for the funding of their borrowing needs to continue. In addition, the relatively high interest rates (above 5%) charged for such borrowing bind public revenues, leading to the need for even tougher austerity measures.

Countries such as France and the UK, both under right-of-centre governments or right-of-centre-dominated government coalitions, have also announced sizeable austerity packages to consolidate their public finances, although they are spread, in these two cases, over a longer time span. Given the large size of these economies, the adverse spill-over effects of such substantial packages in the aggregate EU economy are likely to be considerable.

France's gross debt-to-GDP ratio is expected to exceed 90% in 2010, while its government budget deficit has been relatively high, even by post-recession standards, at 8%. The government has already experienced a rise in its borrowing costs in the financial markets, although they still remain relatively low in comparison with those of other troubled Eurozone members.

The UK government saw its budget deficit shoot up in the aftermath of the crisis, reaching 10% in 2010, second only to that of Ireland. Its gross debt-to-GDP ratio was quite low before 2008 but is nevertheless projected to exceed 80% in 2011. The currently planned spending cuts are greater and more sustained than those inflicted by the governments of Margaret Thatcher in the early 1980s. These announced cuts are to take place, the government has reiterated, despite the fact that the UK economy shrank in the last quarter of 2010, with domestic demand remaining particularly weak.

Austria and Germany have also planned extensive packages for the period between 2011 and 2014, amounting to 13.6 and 80 billion euros respectively, even though in both countries the government budget deficits did not expand dramatically compared to the rest of the EU and they have very substantial current account surpluses (and thus an excess of savings taking the public and private sectors together). The pace of the retrenchment is due to accelerate in both countries as the programmes go along and to peak at 1.4 % of GDP in 2014 in Austria and 1.0% of GDP in 2014 in Germany.

Beyond 2012 and demand-side effects

There is considerable variation regarding the envisaged duration of the programmes. In several cases, such as Austria, Cyprus, France, Germany, Greece, Ireland, Luxembourg, Spain and the UK, the packages are due to run (well) beyond 2012 (see Table 2 above). In many of these countries for which we have precise information, the consolidation effort has been frontloaded, that is, the impact of the measures (as a share of GDP) is planned to be greater in the early years of the programme than in the later ones, regardless of whether or not these countries have already faced a debt crisis.

The currently planned time structure of the programmes does not, however, necessarily preclude the possibility that they will have to be prolonged, especially in cases like Greece and Ireland. The experiences of early starters like Latvia and Hungary are telling. Although we do not have data on planned measures beyond 2012, the fiscal austerity programme adopted by Latvia since 2009 has been frequently revised and extended over time to meet the targets set, as conditions for financial support – such as the assumptions of growth upon which they relied – were consistently undershot. This is primarily because of the contractionary effects that these measures have had on the real economy, which made meeting the targets of fiscal consolidation very difficult. The Greek government has already had to revise its own stabilisation programme for 2011, even though the consolidation efforts made by the government so far have been unprecedented. Portugal, as already mentioned, also had to step up its austerity measures last September in order to meet the targets.

Given the current EU forecasts for output growth in 2011, the employment losses suffered during the recession are unlikely to be recovered, while it cannot be ruled out that they will not increase further. According to the European Commission's latest forecasts (European Commission 2010: 27), output growth rates are projected to be 1.7 % in the EU27 and 1.5 % in the euro area in 2011 and 2.0% and 1.8% respectively in 2012. These forecasts are clearly subject to significant uncertainty due precisely to, among other things, the lack of consensus regarding the effects of fiscal consolidation and also the turbulence in the financial markets that so far does not seem to have subsided, as well as the likelihood of debt 'time bombs' in Europe's banks. However, even if these projections prove to be about right, they will not be sufficient to permit employment to expand at a rate that will significantly reduce unemployment, insofar as productivity and labour force growth alone are likely to suffice to sustain the forecast output growth. It is likely that this will merely exacerbate the weakness in demand, making the austerity packages even more counterproductive in pursuit of fiscal goals and increasing still further the likelihood that they will entail adverse effects on inequality.

The austerity packages are more likely to be more pro-cyclical in the countries most severely affected by the crisis and during the time when they are worst affected by depressed demand. Only in the case of the UK does there appear to be some backloading of the austerity measures, but here the total volume of the contraction is particularly severe. Backloading makes sense to the extent that it sends a credible signal to financial markets about serious longer-term consolidation while minimising negative demand effects until the economy is on a stronger footing. In all these cases, the current fiscal consolidation is due to take place against subdued growth conditions in the rest of the EU, unlike the situation that prevailed in the mid-to-late 1980s and the 1990s, while both Ireland and Greece lack any control over their monetary policy and their nominal exchange rate that could help ease the impact of fiscal consolidation and adjust their competitiveness relative to their main trading partners.

Policymakers' faith in the wisdom of austerity policies in the face of sluggish growth rests on the assumption that cuts will have a positive offsetting effect on private sector spending thanks to the 'confidence' that austerity policies induce in consumers and investors. Not only is the empirical evidence for such effects extremely limited, but a detailed study by the IMF (2010) clearly identified the conditions under which the normal 'Keynesian' contractionary impacts of fiscal consolidation are expected to be strongest. These are a) when monetary policy is not able to offset the fiscal contraction with more expansionary monetary policy; b) when countries are not able to devalue their currency to promote net exports, and, similarly, c) when external demand is weak, limiting export growth, for instance because trading partners are also engaging in austerity policies. All three of these conditions apply to the case of euro-area countries.

Ambitious public sector austerity packages like these imply corresponding adjustments in the savings and investment behaviour of the private sector and/ or net exports. If the public sector is to increase its saving as drastically as these austerity packages project, then either the private sector should reduce its own saving and increase investment or the country should increase its exports and reduce its imports, in other words improve its trade and current account balance, or a combination of both.

However, as we have shown in more detail elsewhere (ETUI 2011, ch. 2), under the current conditions of expected weak demand, deleveraging of the private sector, widespread uncertainty about employment prospects of households and the absence of a nominal exchange rate devaluation or indeed any willingness from countries with current account surpluses to reduce these, such adjustments in the private sector or current account balances are likely to occur through falling output (or at least below-forecast growth). This, in turn, would undermine further the efforts to reduce public budget deficits in the countries suffering from persistently high current account deficits.

At the same time, analyzing the figures in the light of the need to correct macroeconomic imbalances, the pattern of country adjustment can be evaluated as at least partly appropriate. Packages in Germany, Sweden and Austria, the three main surplus countries, are less severe, and backloaded to a greater extent, than those in deficit countries. Given the still fragile and weak nature of the recovery in Europe as a whole, however, and the need for faster demand growth and nominal price and wage increases in the surplus countries, they should have postponed austerity measures until 2012 at least, and should be committing to continued expansionary policies until then.

3. The composition of austerity packages: spending cuts or revenue hikes?

This section presents and discusses the composition of austerity packages in the EU with regard to their distribution between expenditure cuts and tax rises but with regard also to which particular areas of expenditure and which taxes have borne the larger burden of the adjustment. Table 3 below summarises the responses received from our questionnaire respondents regarding the distribution of measures between spending cuts and revenue hikes.

Conforming to the conventional economic policy recommendations (e.g. Alesina and Perotti 1995), the composition of the packages favours expenditure cuts rather than tax rises in most countries for which we have data. Exceptions in this respect are Cyprus and Greece but only for 2011, while Hungary's programme was balanced between the two sides in 2007. The imbalance between expenditure cuts and tax rises is particularly pronounced in Denmark, France, Hungary (2012), Ireland, Luxembourg and the UK, where expenditure cuts accounted for at least 70% of the measures. For 2012 the British government has in fact even scheduled tax *reductions* which will be offset by very severe spending cuts. The Portuguese programme provides for a two-thirds share in expenditure cuts and one-third share in revenue increases.

Table 3 **The distribution of measures between expenditure cuts and tax rises**

	AT	BG	CY	DE	DK	ES	FR	GR	HU	IE	IT	LV	LU	PL	PT	SE	UK
Revenue side (% of package)	47		65	35	40		27	43		33	40		26	100	33		27
2010								48	50	0.4							
2011	46		65	45			40	55	50	25 (1)		33 (2)			33		48
2012	49			38			30	44	30	33							-120
2013	52			31			20	0.1	90	33							
2014	48			27			20										
Expenditure side (% of package)	53		35	65	60		73	57		66	60		74	0	67		73
2010								52	50	99.6							
2011	54		35	55			60	45	50	75 (1)		66 (2)			67		52
2012	51			62			70	57	70	66							220
2013	48			69			80	99	10	66							
2014	52			63			80										

Source: Responses to and own calculations based on the Austerity Watch Questionnaire

(1) At the time when we received the survey response, these figures were still subject to some uncertainty in the Irish government Budget 2011

(2) Plans as announced in the Budget 2011.

Austria and Germany have a more balanced distribution between the two sides with spending cuts accounting for 51-52 % per year of the package in the former. In the latter, however, the balance shifts substantially over time from tax rises to cuts: from a position close to balance in 2011, expenditure cuts will account for 69% in 2013 and 2014.

In addition to this broad distribution of austerity measures, we also asked our respondents to assess the relative importance of measures affecting particular areas of spending and types of tax. Since we received only limited responses, the overview provided below is somewhat provisional, but the following general points can be made.

On the expenditure side, social protection and public administration are the two areas in which most national governments (for which we received detailed responses) are cutting or planning to cut expenditures from between 2010 and 2013, more often from the former. Expenditure cuts in social protection have been reported as the relatively most important measure in Austria, France and Germany throughout the period 2010-2013 and the second most important in Ireland between 2010 and 2012. Cuts in public administration were quoted as the most sweeping type of measure on the expenditure side in France and the second most important in Germany.

There are also some indications that expenditure cuts in the form of reductions in public investment are also relatively important, especially in Hungary, Ireland and Luxembourg but also in France and Austria. Environmental protection, research and development and education were, meanwhile, the areas least mentioned in the distribution of expenditure cuts and in those cases where they were mentioned they were always among the areas relatively less affected.

On the revenue side, indirect taxes are the type of revenue most frequently mentioned by national governments as being raised as part of an austerity package, across countries and over the years between 2010 and 2013. Moreover, among the revenue measures, raising indirect taxes is consistently among the top two most important in terms of quantitative impact.

Income distribution

Given this information, we have attempted to evaluate in a broad-brush sense whether the austerity packages can be considered ‘progressive’ or ‘regressive’ in terms of overall income distribution. Before proceeding with the analysis, it is worth making a few introductory remarks[2].

2. It can be argued that tax increases that are levied on the owners of specific ‘factors of production’ or specific products can be passed on to other groups in society through price increases, so that they are ultimately borne by others. We abstract from this point here. Such a process implies the need for a counter-factual which we do not possess. At the very least, in the short run the impact will be in the direction indicated, and even in the longer run the impact on prices will probably be less than complete, so some effect will remain.

On the revenue side, tax increases are generally likely to be regressive if they are concentrated heavily on indirect taxes, as the poor spend a greater proportion of their income on domestic goods than higher-income population groups (who save more and consume more abroad). This effect can be both mitigated and enhanced by the specific nature of the measures, in particular which product categories are affected. Raising value-added tax on food (for example where it is set at a lower-than-standard rate) will certainly be regressive, whereas higher taxes on luxury goods will be progressive. Energy/carbon taxes, taken by themselves, increase inequality: the poor spend relatively more on energy and have less scope to invest in energy-reducing technology.

Income taxes – the other main source of government revenue in most countries – are usually progressive in nature and, other things being equal, income tax hikes will increase the progressivity of the overall taxation system. However, depending on precisely which allowances, thresholds, ceilings and tax rates are changed, this need not be the case. Higher taxes on capital income, property/wealth, land, inheritances, and taxes on the financial sector can generally be considered conducive to reducing inequality, as the tax base is disproportionately held by the rich; even here, however, the devil may lie in the detail.

On the expenditure side, the issue is whether the impact of spending cuts disproportionately affects those on high or low incomes. This is not always easy to determine. Generally it can be assumed, though, that usage of most public services[3], which account for the bulk of public spending (Watt 2010b), declines as income rises (measured in terms of their importance in a household's overall consumption of goods and services). This is partly because the rich are more likely to make use of the greater choice and (sometimes) quality or convenience available on the market: I am more likely to borrow books from the public library if I am poor and buy books from the bookshop if I am rich. Moreover, access to many public services is subject to various forms of income conditionality ('means-testing').

Broadly the same considerations apply to government transfers. Some specific spending items may benefit owners of large corporations or middle and upper incomes generally, or specific high-income groups; cutting these would be progressive in distributional terms. A number of items (defence, infrastructure spending) are difficult or impossible to classify. Public sector pay cuts are hard to evaluate unless we have specific information on their distribution.

It is worth noting in this context that we are considering here only the direct impact of the austerity measures themselves. Knock-on effects of, notably, high unemployment, caused indirectly by the fiscal contraction on income distribution are not considered here. A related point is that, as a result of the economic situation generally, a falling wage share and rising poverty are to be expected in most European countries in the coming years.

3. Higher education is a likely exception.

Applying these considerations, and on the basis of the information from our survey, we have classified countries as follows:

Table 4 **The expected effects of the packages on income distribution**

Austerity package regressive	Main reasons for classification*
Poland	Focus on indirect tax hikes
Ireland	Cut in minimum wage and reduced income tax threshold at the bottom; indirect taxes
Cyprus	Indirect tax hikes and focus on supporting pensioners and large families
Germany	Welfare cuts and indirect tax hikes
Latvia	Indirect tax hikes and benefit cuts (pensions, unemployment)
Spain	Focus on social benefits and public services
Denmark	Changes in income taxes which do not make system more progressive; budget cuts that will affect the disposable income of the poorest 10% of population more than that of the richest 10%
Greece	Indirect tax hikes on wide consumer goods combined with (successful?) attempts to crack down on tax evasion among the better-off and 'horizontal' public wage and pension cuts
Austerity packages progressive	**Main reasons for classification***
France	Tax hikes focus on higher incomes
Luxembourg	Focus on income tax

Note: In the progressive and regressive categories, offsetting measures may exist but, given their relatively minor impact in quantitative terms, they are not listed here.

Overall, in our estimation, of the eleven countries for which we have a reasonably detailed qualitative assessment, the austerity packages in more than half (six) will, according to our assessment, have a direct regressive impact on income distribution. In all these countries revenue hikes are concentrated in the area of indirect taxation, while spending cuts focus on various government transfers and public services. This does not, of course, mean that there are no offsetting measures serving to mitigate the inequality effects, but we judge that such measures as do exist to this end fall far short of achieving their purpose.

Two countries – France and Luxembourg – appear to have introduced packages designed in such a way that the burden of fiscal consolidation is borne disproportionately by the broader shoulders of the relatively wealthy, or possibly the middle class. The main and most important tool by which this adjustment is achieved is progressive income tax.

This leaves three countries where we had some difficulty in reaching a conclusion: in Hungary, Austria and the UK key measures pull in opposing directions. A more sophisticated quantitative analysis would be required in these cases. The assessment of the UK may seem surprising, given the massive expenditure cuts dominating the news, but the situation is complicated: progressive measures (in particular a very substantial hike in the top rate of income tax) were introduced by the outgoing Labour government, and retained by the new Conservative-Liberal Democrat administration, whereas the new government's own measures have been, on the whole, regressive. According to a detailed analysis by the Institute for Fiscal Studies[4], the overall impact of the tax and benefit changes will be progressive over the period of consolidation (to 2014), but this does not allow for the very substantial public service cuts, by which it is, on balance, the needy who will be more hard-hit. In the case of Austria, considerable efforts were made to focus tax rises on upper income groups and capital; the spending cuts and indirect tax increases are probably smaller in magnitude but we leave this evaluation open.

4. http://www.ifs.org.uk/publications/5313/

4. The distribution of the effects of austerity measures across societal groups

In this section we are interested in the expected distribution of the effects of the austerity packages across different groups of the population. As discussed above, the aggregate analysis was based on responses from our national experts for 17 countries. A greater level of detail was required to provide information on more qualitative aspects and, moreover, in a few countries (such as Italy) the actual and definitive content of the packages – as opposed to vague declarations of intent – remains largely unclear. For these reasons, the response rate to our survey for those questions on which this section of the report is based is somewhat lower. Specifically, almost no data is available for Bulgaria, Italy and Sweden.

Regarding the impact on specific population groups, by far the most frequently mentioned were pensioners and those approaching retirement, and public sector workers. In a number of countries (notably in eastern Europe and Greece), pension levels have been cut (at least in nominal terms; this may be partially offset by falling prices); in others, access to early retirement has been restricted and/or the statutory retirement age has been increased.

In principle, changes in access to (state) pensions, such as raising retirement ages in the future, have the advantage from a cyclical point of view that they signal a longer-term commitment to fiscal consolidation without immediately depressing demand. Cuts in current state pension levels, however, unless targeted at those on higher incomes, will be regressive in distributional terms and have a substantial depressing effect on demand, as state pensions are more than proportionately important for those on low incomes.

Clearly public sector workers are bearing the brunt of the cuts in many countries (see also Glassner 2010 and Glassner/Watt 2009). A substantial number of countries (e.g. Ireland, France, Austria, Spain and Greece) have instituted – in some cases already prior to the crisis – longer-term plans to shrink the public sector by replacing only a proportion of those leaving through retirement. More immediately, job cuts, running into the thousands, have been announced or already implemented in many countries (Hungary, Ireland, Cyprus, Germany, Latvia, Spain and the UK). In many cases we have figures only for central/federal government, while numbers concerning cuts at the regional and local level are hazy. On top of this, public sector workers have suffered pay cuts, either directly or indirectly (in the form, notably, of higher contributions to pension schemes). In a number of cases, such wage cuts have been imposed unilaterally by the government, bypassing established collective bargaining processes.

A number of arguments have been made for this focus (Glassner/Watt 2010). There is the argument that public sector wage cuts are 'fair exchange' given the greater employment security in the public than the private sector. However, job cuts have also been substantial in the public sector. Depending on national legal framework, it may be easier and quicker to achieve spending cuts by attacking public sector workers than by cutting statutory benefits, making such measures attractive to governments seeking 'quick fixes'. In countries with large trade deficits but unable to devalue their currency (because they are members of the euro area or their currency is pegged to the euro), governments justify public sector wage cuts by the need to engage in an 'internal devaluation' of nominal wages and prices. Such cuts are seen as a lever to depress wages also in the private sector where government influence is only indirect. To the extent that prices have fallen (as in some Baltic countries and Ireland), nominal pay cuts must be interpreted differently from in countries such as Spain, where inflation remains comparatively high. However, cuts are also being implemented in surplus countries. Last but by no means least, many current incumbent governments in Europe and also the European Commission (e.g. EC 2010c: 22) consider for ideological reasons that the state sector is simply too big and/or that it is in the interests of longer-run efficiency or productivity to shrink the state.

Other population groups particularly affected in many countries are recipients of various welfare benefits. Although unemployment benefit regimes were made more generous in a number of countries in response to the crisis, a tightening is now taking place in a number of countries. In addition, minimum social benefits have been frozen in Spain and Portugal and a number of countries have reduced child allowances and other forms of family support; indeed, large families are reported as being amongst the main 'victims' of the cuts in Austria. In the UK child support has been cut, but only for wealthy families.

Little information emerged from our survey on gender-specific impacts of the austerity packages. It seems that detailed academic or official gender studies have not (yet) been undertaken. In most countries, public sector employment is predominantly female, so the focus on public sector cuts can be expected to affect women disproportionately. In France, for instance, the debate on pension reform has focused on gender issues (different retirement ages and life expectancy). To the extent that gendered roles in caring for elderly dependents, children, etc. make women on average more reliant on public services than men, a gender effect to the disadvantage of women may be expected in those countries where service cuts play an important role (e.g. Spain, Ireland, UK).

5. Assessing policy priorities within the packages with respect to the Europe 2020 strategy

The fiscal austerity packages are embedded in a broader and longer-term strategy for the European Union, the Europe 2020 strategy, which is supposed to put Europe on track for higher, but also smarter, more sustainable and also inclusive growth (Pochet 2010; Watt 2010c). It is therefore important to analyse whether the policies enacted and envisaged by member state governments as part of their fiscal consolidation packages are, or can be expected in coming years to be, in line with the priorities set out in the EU2020 strategy.

The European Commission's Annual Growth Survey (AGS)[5] is supposed to guide member states in setting their economic policies for the near term. The AGS calls for 'rigorous fiscal consolidation' while recommending that member states prioritise 'sustainable growth-friendly expenditure in areas such as research and innovation, education and energy'. The longer-term Europe 2020 strategy is designed around 10 so-called integrated policy guidelines[6]. Of relevance in this context, i.e. in interpreting changes in government spending and taxation, are, in particular, the guidelines calling for support for R&D and innovation (4), resource efficiency and emissions reduction (5), improving skills and training (8) and school and tertiary education (9), and, finally, combating poverty (10).

Our survey of national experts included questions that provide us with some information against which we can judge whether governments, in implementing their consolidation programmes, have taken such injunctions to heart, or, by contrast, the extent to which the practice of fiscal austerity is actually inimical to the pursuit of the goals of the Europe 2020 strategy. Responses were not, however, sufficiently consistent to allow aggregation.

Public investment[7]: In a number of countries substantial cuts in public investment have been implemented or are planned. In Hungary cuts, especially in motorway construction, began already in 2007. In the UK massive cuts in capital spending, averaging 29% in real terms to 2014/15, are planned, with education particularly hard hit. Substantial cuts in the investment budget are planned in Ireland, although the government claims that this reflects renegotiated, lower prices from contractors, so the real impact is hard to assess. In

---

5. http://ec.europa.eu/europe2020/pdf/en_final.pdf/
6. http://ec.europa.eu/eu2020/pdf/Brochure%20Integrated%20Guidelines.pdf/
7. In a number of countries, notably Germany and Spain, much public investment is determined at regional and local level and here information is currently lacking.

Luxembourg a significant reduction is foreseen in the amount allocated for investment (although in past years de facto spending was always lower than planned). In Spain billions of euros are being cut from the capital budget. In Austria the cuts (transport, school and university buildings) are set to rise over time (from around EUR 70-300 m p.a.) while these cuts do not offset the increase in public investment that was undertaken under the Economic Recovery package which is still running. In both Poland and Latvia, however, it is reported that EU funding is enabling investment in a number of major infrastructure projects to be maintained. Even so, at least in the case of Latvia, it has been reported that the co-financing of investment projects has been difficult, resulting in under-absorption of the money available from structural funds, which in any case has been relatively small compared to the planned amount of total investment.

Overall, the substantial cutbacks in public investment mark a repeat of the experience of the 1990s when the Maastricht convergence process led to a cut in capital spending by governments anxious to reduce deficits quickly. New investment projects are politically easier to cut than established rights and spending commitments. It is widely accepted, though, that much public capital spending has high multipliers, that is knock-on effects on aggregate demand, and in the longer run comes at a cost of lower potential output growth. In short, it is inimical to the EU2020 goals.

Education and training: In most cases where we have information, education and training budgets seem either to have either been cut in line with overall spending cuts or to have been, to some extent, spared. To this extent, some recognition of the priorities as set out in the Europe 2020 strategy seems to have occurred. However, in Spain massive cuts in pre-school and primary education are planned, whereas in Latvia the funding for education and science was reduced by half in 2009 and no plans for restoring it have been put forward in 2010 and 2011. As noted already, capital spending cuts in the UK have been particularly focused on education construction, which will have impacts, albeit in the longer term. Regarding training for the unemployed, it is important to see these developments in the context of the substantial rise in unemployment. Spending on active labour market policy *per unemployed* is set to fall precipitously. The appropriate response would have been a substantial increase in spending on active labour market policy, and notably on training and skills development, to help address any sectoral mismatch between areas of declining employment during the crisis and growing employment in the recovery.

Green growth and the environment: The evidence we have seems to suggest that, on the expenditure side, objectives such as promoting green growth are being shielded from austerity: spending cuts in environmental protection tend to be mentioned only rarely and to constitute a low share in the overall packages (of course, they do not constitute a big ticket item in public spending, either). At the same time, a number of countries have taken steps to combine the need for additional government revenue with ecological policy goals by raising or introducing various ecological taxes, as well as other measures.

Ireland is the only country to have introduced a carbon tax, although in some other countries (notably France) debates on the subject have made progress without any concrete action having been taken. Austria has raised transport fuel taxes, while several countries have altered vehicle registration tax systems (Ireland, Austria, Latvia). Both Austria and Germany will introduce a tax on airline tickets. As part of its offsetting 'offensive' programme, Austria has increased investment in retrofitting buildings. Lastly, environmentally harmful subsidies have been reduced. In the UK, energy and the environment spending will buck the trend to severe cuts, raising spending in real terms, while in Germany the total value of environmentally positive measures is estimated at around EUR 4bn annually. In Italy, however, not only were no positive measures envisaged, but plans for substantial investment cuts are reported.

In short, some positive elements can indeed be identified in this area. However, as was noted in the analysis of the stimulus packages (Watt 2009), the crisis must be seen as a major opportunity to reprioritise spending and taxation priorities and this opportunity is being taken to only a relatively limited extent.

R&D and innovation: We received too little information to evaluate this policy area.

Poverty: Referring back to the discussion in the previous section, we note the likely regressive impact of the packages in the majority of countries. In these cases, the austerity packages will make it harder for them to achieve the (relative) poverty-reduction goals under the Europe 2020 strategy. This comes on top of the impact of the crisis itself, notably high unemployment, which will work in the same direction. It is hard to see how substantial progress in reducing (relative) poverty can be made over the next few years in most EU countries under such conditions.

Overall, the findings cast serious doubt on the ability and/or willingness of member state governments to combine the fiscal austerity called for by the Europe 2020 strategy and Annual Growth Survey with the positive, longer-term measures required, according to those same documents, to raise Europe's potential to deliver 'smart, sustainable and inclusive' growth. And, to be fair, this is a 'big ask'. Arguably, the criticism should focus on the apparent cynicism of the AGS in calling for things which its authors know very well are not politically feasible given the simultaneous demand for fiscal austerity, rather than the lack of political will on the part of national governments (Watt 2011a). To put it simply: there is a major policy contradiction between the 'positive' goals of the Europe 2020 strategy and the imposition of draconian austerity requirements.

Having said that, some countries manage better than others to 'square the circle'. Particularly worrying are the cuts in public investment and also the – in some cases major – cutbacks in the area of education. At least some attempts are, however, being made to reap a double (fiscal and ecological) dividend through changes in ecological taxation and other environmental policies. In terms of inclusion, and anti-poverty goals, there is concern that the poverty and inequality-enhancing effects of the crisis (high unemployment, slow growth) will be further enhanced in many countries by the choice of fiscal austerity measures. A number of countries, though, have taken steps to shift the burden of fiscal adjustment on to the broader shoulders of the wealthy.

6. A political evaluation by national experts

The national experts were asked to evaluate their country's fiscal adjustment programme on the basis of several criteria. These were: 1. whether it was based on realistic assumptions about the macroeconomic conditions in the economy in the next few years; 2. whether the measures were fairly distributed across different social groups; 3. whether the tax system was to become more progressive following the measures; 4. whether the austerity measures are likely to undermine the longer-term goal of promoting green growth and a low-carbon economy; 5. whether the austerity measures are likely to undermine the longer-term goal of accelerating productivity growth; and 6. whether the austerity measures are likely to help avoid insolvency or relieve liquidity problems in the economy.

Experts were asked to indicate whether they agreed, disagreed or were neutral/didn't know. We have coded these as follows: 'agree' = 1; 'disagree'= -1; 'neutral/don't know'= 0. The scores are presented in Table 5. This assessment covers some of the issues already discussed above. It is important to emphasise that we are here reporting the judgments of our national experts, rather than our own assessment of their reports.

Table 5 **An evaluation of the packages by national experts**

AT	BG	CY	DE	DK	FR	ES	GR	IE	IT	LT	LU	PL	PT	SE	UK
The package is based on realistic assumptions about the macroeconomic conditions in the economy in the next few years															
1	-1	-1	0	1	-1	-1	-1	-1	-1	1	-1	1		-1	-1
The measures are fairly distributed across different social groups															
0	-1	-1	-1	-1	1	-1	-1	-1	-1	-1	-1	-1	-1	-1	-1
The tax system will become more progressive following the measures															
0	-1	-1	-1	-1	1	-1	-1	0	-1	-1	0	-1		-1	-1
The austerity measures are likely to undermine the longer term goal of promoting green growth and the low-carbon economy															
-1	0	1	-1		0	-1	1	-1	1	1	0	0		1	1
The austerity measures are likely to undermine the longer term goal of accelerating productivity growth															
0	0	1	1	1	0	-1	1	1	1	1	0	0	-1	1	1
The austerity measures are likely to help avoid insolvency or relieve liquidity problems in the economy															
0	-1	-1	-1	0	0	0	-1	-1	0	-1	-1	0		0	-1

Source: Responses to survey

The overall picture to emerge from this table is cause for pessimism. National experts have, for the most part, evaluated the austerity packages negatively from the perspective of both social considerations and the provision of solutions to the economic problems that they are meant to help resolve and the stated longer-term goals of policymakers for the EU economy.

Table 5 suggests that the austerity packages are evaluated most negatively with regard to the fair distribution of their measures across social groups and the extent to which they make the income tax system more progressive. All national experts disagreed that the austerity measures have been fairly distributed across different social groups, except in France, while it was suggested that in Austria the distribution was neutral.

In all countries except Austria, France, Ireland and Luxembourg, experts disagreed that the austerity packages are likely to make the income tax system of their country more progressive. The measures are likely to have this positive effect in France alone, while in the other three countries they are expected to be neutral.

Turning to the evaluation of the packages along the lines of whether or not they are likely to help resolve the economic problems in the EU and promote longer-term goals, the picture is again negative.

National experts have proved ambivalent as to whether the austerity packages will help avoid insolvency or help resolve liquidity problems for the countries that undertake them. This is coupled with a rather negative perception, especially among the countries with high public debt and ambitious consolidation programmes, of how realistic are the assumptions on which these programmes rest.

Going beyond the economic problems which the austerity packages are meant to solve, experts have been more pessimistic than optimistic and, overall, are divided on whether the measures will undermine or promote longer-term objectives such as accelerating productivity growth and promoting green growth and a low-carbon economy.

7. The role of social dialogue and political evaluation by national trade unions

We also asked our questionnaire respondents to provide us with information on the extent to which social dialogue processes enable the views of social partners and especially trade unions to be heard, on the position of national trade union organisations in their country on the government's measures, and, insofar as the trade unions have expressed such positions on the packages, what these positions have been. The replies are summarised in Table 6 below.

The first striking observation to emerge from our questionnaires is that Europe's austerity packages have, with only very few exceptions, gone ahead against the will of trade unions. In most countries for which we received responses, while social dialogue *did* take place prior to the announcement of the austerity packages, the unions' views were largely ignored in the final outcome. In several member states, there was no social dialogue at all.

It is no surprise then that in most countries trade unions have expressed political opposition to the measures decided by their governments. Exceptions to this trend are Austria, Italy and Slovakia. In Austria, although there has been no official social dialogue over the fiscal consolidation measures, trade union leaders have participated in informal discussions. The unions' stance in that country has been mixed. Italian trade unions have also been divided in their support, albeit for reasons that have less to do with fiscal policy *per se* than with domestic interest representation politics. Last but not least, in Slovakia unions have acknowledged the need for fiscal consolidation but have been opposed to the particular measures through which the government decided to pursue it.

The information we have on the alternative proposals made by unions suggests that they mostly suggest measures that would make the distribution of the adjustment burden 'fairer' in social terms, with those on higher incomes bearing more and those on lower incomes bearing less. In some cases, there have also been proposals to use, for purposes of adjustment, more public revenues (i.e. by raising taxes and introducing new taxes, such as on financial transactions) and less expenditure cuts (which tend to be regressive).

Table 6 **The role of social dialogue and the political evaluation of the packages by the trade unions**

	Social dialogue	No social dialogue	TUs supportive	TU positions
Austria	X		Mixed	Further increase in wealth taxes and less restrictive expenditure measures; targeted expansive measures in the fields of education, health, elder care and childcare as a supplement to consolidation
Bulgaria				
Cyprus	X – yet trade unions' positions barely taken into account			Measures to support those on low incomes, pensioners; measures to crack down on tax evasion and avoidance and the mismanagement of public funds by the government
Germany	X – yet trade unions' positions barely taken into account		No	More expansionary/less restrictive fiscal stance and/or tax increase for the rich
Denmark		X		Public deficit should be taken very seriously and fiscal tightening must take place; however, the recovery in the labour markets should not be jeopardised.
Spain		X	No	Favour measures that protect the most vulnerable; measures to change the country's production model; education policies to upskill the workforce; consider consolidation measures on the revenue side
France		X		Raise taxes on higher incomes, financial incomes and eliminate the income tax rate ceiling
Greece	X – trade unions' views largely ignored		No	In short term: more income redistribution, regulation of employment relations, reinforcement of welfare state, tackling of tax evasion and avoidance. In the longer term: implement a new growth plan
Hungary	X – yet trade unions' positions barely taken into account		No	
Ireland		X-Social dialogue collapsed during national level negotiations	No	Reduce budget deficit to 3% by 2017 instead of 2014; finance austerity measures worth 2bn euros by increasing capital spending, using funds from national pension reserve fund; negotiate with bondholders of banks which were bailed out
Italy		X	Divided	
Latvia	X		Yes for need for consolidation; No for speed and social consequences of several measures	Mostly requests to defend the welfare of population and prevent further economic stagnation and rise in inequality
Luxembourg	X-without agreement		No	Establish a ceiling on tax rates for high labour income; elimination of ceiling for health contributions.
Poland		X		
Portugal	X		Mixed/Divided	
Slovakia	X- though limited			
Sweden	X-at local level		No	
UK		X	No	

Source: Responses to survey

Conclusions

This paper has sought to evaluate from a European and national comparative perspective the austerity packages that the governments of EU member states have announced and implemented following the recent financial crisis and the Great Recession.

Difficulties inherent in an exercise such as this relate to the reference point or baseline scenarios against which any retrenchment measures should be evaluated, the presence of any knock-on effects of fiscal contraction of GDP, and even the comparability of data across countries. Still, the findings presented here can be used as indicative orders of magnitude and do allow at least some cross-country comparisons to be made and a sense of the overall European-level impact to be gained. New information is, of course, coming in all the time. The findings of this study offer a snap-shot of the information available around the end of 2010.

The study findings are summarised in the executive summary and will not be repeated here. Overall, the study raises serious doubts about the drive for austerity being embarked upon by EU countries. The simultaneous nature of the demand contraction, and the very limited offsetting impacts on demand via monetary policy and the exchange rate, mean that the output costs of the consolidation measures will be high. The risk is that this, in turn, will drag out the consolidation period, possibly condemning Europe to a 'lost decade'. Whether or not this will happen depends on some imponderables, notably the robustness of the recovery of the global economy, especially in emerging markets, but also the resilience of the private sector. At the time of writing (March 2011), food and especially energy prices have risen to worrying heights, putting a further drag on a recovery that in any case is expected to be far more sluggish than that from previous recessions. Even if the aggregate growth and employment figures prove more optimistic than in our assessment, the problem of the unbalanced nature of the European economy, especially that of the euro area, remains: the 'peripheral' economies almost certainly face a bleak medium-term outlook in the absence of major support efforts from better-placed countries and the provision of European-level solidarity. Even if a major crisis is avoided, the Europe 2020 goals are highly unlikely to be achievable in a context of persistently sluggish growth and regressive distributional tax-and-spend policies and cutbacks in areas such as public investment, education and active labour market policy.

This report has been concerned largely with painting a picture of political reality in Europe and not with making alternative policy recommendations. Yet it is clear from the path of the crisis, and implicit in our pessimistic assessment of the next few years given the policy path upon which Europe has embarked, that Europe's economic governance mechanisms need reform. One of the authors has elsewhere set out an alternative blueprint for a European economic governance architecture to promote growth, consolidation and economic convergence (Watt 2011b), and proposals will not be repeated here.

Europe's urgent need is for an investment offensive that creates jobs and demand in the short run and raises productivity and potential output in the longer run, equipping Europe with the tools it needs to master the difficult transition to a low-carbon economy. For now at least, there are no reasons to believe that this investment will be forthcoming to anything like the extent required from the private sector. With interest rates for solvent sovereign borrowers historically low, governments should be investing heavily in all the areas rightly identified as priorities in the Europe 2020 strategy: infrastructure, energy, education, R&D. The constraints on those governments currently unable to borrow at low rates need to be lifted by various means (European Investment Bank, support via the stability facility and a future permanent mechanism, mobilising European Social Fund resources). Once the recovery is assured and output increases, private sector firms, too, will raise investment.

It is widely believed in policymaking circles that austerity is necessary for consolidation, and consolidation necessary for growth and jobs. In contrast, we believe that Europe needs to grow out of its public-sector deficits and debts, which resulted from the spectacular failings of an unregulated private sector, especially in finance. To do that it needs to invest. And it should embark on that course without delay.

References

Alesina, A. and R. Perotti (1995) 'Fiscal expansions and adjustments in OECD countries', *Economic Policy* 10 (21), 205-248.

Clancy, P. and T. McDonnell (2011) 'From tiger to bailout: the Irish crisis', ETUI Policy Brief. European Economic and Employment Policy No 1/2011.

ETUI (2011) *Benchmarking Working Europe 2011,* Brussels: ETUI.

European Commission (2010a) 'European Economic Forecast – Autumn 2010', European Economy No 7/2010, Brussels.

European Commission (2010b) *Recommendation for a Council Recommendation of 27.4.2010 on broad guidelines for the economic policies of the Member States and of the Union*, Brussels.

Glassner, V. (2010) 'The public sector in the crisis', ETUI Working Paper No 2010.07, Brussels: ETUI.

Glassner, V. and A. Watt (2010) 'The current crisis reveals both: the importance and the limitations of the transnational coordination of collective bargaining policies', *Social Europe Journa*l. www.social-europe.eu/ [Accessed 26.04.2011]

IMF (2010) *Fiscal exit: from strategy to implementation*, Washington, DC: International Monetary Fund.

Pochet, P. (2010) 'EU2020 social impact of the new form of European governance', ETUI Policy Brief. European Social Policy No 5/2010.

Watt, A. (2009) 'A quantum of solace? An assessment of fiscal stimulus packages by EU Member States in response to the economic crisis', ETUI Working Paper No 2009.05, Brussels: ETUI.

Watt, A. (2010a) 'A Greek tragedy or a European farce? Time to re-write the script', *Social Europe Journal*. www.social-europe.eu/ [Accessed 26.04.2011]

Watt, A. (2010b) 'Spending cuts will hit the vulnerable hardest – so find another way!', *Social Europe Journ*al. www.social-europe.eu/ [Accessed 26.04.2011]

Watt, A. (2010c) 'European economic governance: what reforms are to be expected and what are needed?', *European Alternatives,* http://www.euroalter.com/wp-content/uploads/2010/11/Watt-ENG.pdf

Watt, A. (2011a) 'Commission to Member States: the crisis is over. Now take the AGS to the European Social Model!', *Social Europe Journal*. www.social-europe.eu/ [Accessed 26.04.2011]

Watt, A. (2011b) 'A blueprint for growth, consolidation and convergence in the Euro area', *Social Europe Journal*. www.social-europe.eu/ [Accessed 26.04.2011]

List of questionnaire respondents

Information was kindly provided by the following national experts or institutes:

Austria: Georg Feigl (AK Wien)
Bulgaria: Atanas Vladikov (University of Plovdiv)
Cyprus: Nikos Nikolaou and Christos Karydis (SEK)
Denmark: Erik Bjorsted (ECLM)
France: Catherine Mathieu (OFCE-SciencesPo)
Germany: Achim Truger (IMK)
Greece: Savvas Robolis (INE/GSEE), Sotiria Theodoropoulou (ETUI)
Hungary: Béla Galgóczi (ETUI)
Ireland: Rory O'Farrell (ETUI)
Italy: Mario Pianta (Sbilanciamoci)
Latvia: Raita Karnite (EPC-Latvia)
Luxembourg: Sandy Fournelle (SECEC)
Poland: Leon Podkaminer (WIIW)
Portugal: Antonieta Ministro (Ministry of Labour and Social Solidarity)
Sweden: Monika Arvidssson (LO)
United Kingdom: Lionel Fulton (Labour Research Department)

ETUI Working Papers

Jean-Claude Barbier
Changes in political discourse from the Lisbon Strategy to Europe 2020: tracing the fate of 'social policy'
WP 2011.01

Vera Glassner
The public sector in the crisis
WP 2010.07

Andranik S. Tangian
Not for bad weather: macroanalysis of flexicurity with regard to the crisis
WP 2010.06

Aída María Ponce Del Castillo
The EU approach to regulating nanotechnology
WP 2010.05 Janine Leschke and Andrew Watt
How do institutions affect the labour market adjustment to the economic crisis in different EU countries?
WP 2010.04

Rory O'Farrell
Wages in the crisis
WP 2010.03

Kurt Vandaele and Janine Leschke
Following the 'organising model' of British unions?
Organising non-standard workers in Germany and the Netherlands
WP 2010.02

Lars Magnusson
After Lisbon – Social Europe at the crossroads?
WP 2010.01

Igor Guardiancich and David Natali
The EU and supplementary pensions
Instruments for integration and the market for occupational pensions in Europe
WP 2009.11

David Natali
Public/private mix in pensions in Europe. The role of state, market and social partners in supplementary pensions
WP 2009.10

Vera Glassner
Government and trade union responses to the economic crisis in the financial sector
WP 2009.09

Igor Guardiancich
Institutional survival and return: Examples from the new pension orthodoxy
WP 2009.08

Alison Johnston
Wage policy in Austria and the Netherlands under EMU. A change in performance or the continuation of the status-quo?
WP 2009.07

Anna Maria Sansoni
Limits and potential of the use of vouchers for personal services. An evaluation of titres-services in Belgium and the CESU in France
WP 2009.06 (EN, FR)

Andrew Watt, with the collaboration of Mariya Nikolova
A quantum of solace? An assessment of fiscal stimulus packages by EU Member States in response to the economic crisis
WP 2009.05 (EN, FR)

Sigurt Vitols
European Works Councils: an assessment of their social welfare impact
WP 2009.04

Béla Galgóczi, Janine Leschke and Andrew Watt
Intra-EU labour migration: flows, effects and policy responses
WP 2009.03

Christophe Degryse and Philippe Pochet
Paradigm shift: social justice as a prerequisite for sustainable development
WP 2009.02 (EN, FR)

Vera Glassner and Béla Galgóczi
Plant-level responses to the economic crisis in Europe
WP 2009.01

These publications can be downloaded free of charge from our website.
Please visit: http://www.etui.org/research/publications

European
Trade Union Institute

Bd du Roi Albert II, 5
1210 Brussels
Belgium

Tel.: +32 (0)2 224 04 70
Fax: +32 (0)2 224 05 02
etui@etui.org
www.etui.org