

THE SOCIAL SOURCES OF AUSTERITY

The Politics of Fiscal Consolidations in the UK and France, 1978-2014

by

Zbigniew Truchlewski

Submitted to

Central European University



*Doctoral School of Political Science,
Public Policy and International Relations*

In partial fulfillment of the requirements for the degree of
Doctor of Philosophy

Supervisor: **Assoc. Prof. Dr. Achim Kemmerling**

Budapest, Hungary

2016

Abstract

Why do countries implement austerity differently? Why do they follow different fiscal pathways? Why do some fiscal consolidations lead to social conflicts while others do not? This dissertation explains this variation by focusing on three key mechanisms - tax linkages, attrition and the evolution of social coalitions - in two most similar countries, the United Kingdom and France from 1978 to 2014.

I argue that where tax systems promote strong linkages between payments and benefits, social groups prefer tax hikes to spending cuts because they do not want to forgo benefits for which they have already paid. If those tax linkages are weak, social groups are more likely to resist tax hikes because of uncertainty. Second, attrition refers to the degree of infighting between social groups during austerity. It is measured as income inequality. Where social groups are equal, they are more likely to agree on higher taxes because of a fair additional tax burden: if incomes are equal, taxes are equal. Where inequality prevails, wars of attrition undermine consensus for tax hikes. These two mechanisms yield ideal-types embodied by the UK and France. Countries like the UK, where tax linkages are weak and inequality is high, are more likely to cut spending than to increase taxes. Conversely, countries like France, where tax linkages are strong and inequality is low, are more likely to increase taxes than to cut spending. These different configurations help explain the divergence of fiscal pathways during the age of austerity (1978-2014). Third, austerity can reshape social coalitions and influence future policy through these mechanisms. If inequality increases in a country with strong tax linkages, austerity provokes fiscal conflicts because social groups oppose spending cuts and tax hikes. Countries like Greece and Portugal as cases in point. I argue that France is coming closer to this configuration because inequality has been increasing in the last decade. In the UK, weak tax linkages and increased inequality levels since 1978 paved the way for deep expenditure cuts after 2010.

To be sure, many scholars have underlined the importance of social coalitions for the politics of policy-making. But these accounts ignore contextual preferences and the endogenous evolution of social coalitions. Therefore, the main contribution of this dissertation is to show how the interaction between in tax linkages and attrition levels yields a useful dynamic typology of the politics of austerity. Further, the dissertation has important theoretical implications. I show that traditional partisan or ideational explanations do not fully explain counter-intuitive fiscal pathways and the contested politics of austerity. I suggest that certain configurations of linkages and attrition favor certain parties and certain forms of fiscal governance. This dissertation also sheds light on the politics of austerity in the United States, the Eurozone and bailout countries. Finally, my argument also has important implications for the study of the Economic and Monetary Union, showing why some countries may find it more difficult to respect the Stability and Growth Pact than others.

Contents

Acknowledgments	ix
List of Tables	xiii
List of Figures	xv
Abbreviations	xvii
1 Introduction	1
2 Theories of Fiscal Consolidation	15
3 The Social Sources of Austerity	41
4 Linkages and Austerity	65
5 Attrition and Austerity	111
6 Coalitions and Austerity	155
7 Conclusion	215
References	232

List of Tables

4.1	Tax linkages in the UK and France	69
5.1	Counterfactual simulations of attrition and austerity	120
5.2	Preferences for taxes and spending in the UK, 1983-2014	131
5.3	Attrition and austerity after 2010, OLS regressions	152
5.4	Attrition and austerity after 2010, robust regressions	153
5.5	Summary statistics	154
6.1	Austerity as <i>Zwischenzug</i> and <i>Zugzwang</i>	160
6.2	<i>Zwischenzug</i> in the UK and <i>Zugzwang</i> in France	203
6.3	Summary statistics for panel data regressions	209
6.4	Partisan models of fiscal austerity, without LDV	210
6.5	Partisan models of fiscal austerity, with LDV	211
6.6	Partisan models of total austerity, with LDV and controls	212
6.7	Partisan models of tax hikes, with LDV and controls	213
6.8	Partisan models of spending cuts, with LDV and controls	214

List of Figures

1.1	Diverging austerity, 2010-14	4
1.2	Fiscal pathways, 1960-2010	5
1.3	The social sources of austerity and fiscal pathways	8
2.1	Fiscal governance in the UK and France	35
3.1	Visualizing the argument	49
3.2	Linkages and attrition in the OECD	50
3.3	Predicted probabilities of austerity	51
3.4	Hypothetical fiscal pathways in the age of austerity	57
3.5	British and French fiscal pathways	58
4.1	Income tax, social contributions and redistribution	72
4.2	Linkages and austerity	75
4.3	Tax Structures, 1965-2013	80
4.4	British tax linkages, 1965-2013	88
4.5	French tax linkages, 1965-2013	100
4.6	Tax reforms in the first decade of austerity	110
5.1	Inequality and austerity: Gini, Top 1% income share and polarization	117
5.2	Counterfactual simulations, austerity 2010-2014	121
5.3	Contour plots, austerity 2010-2014	122
5.4	Inequality, redistribution and austerity in the UK	126
5.5	UK structural break tests	127
5.6	Inequality, Redistribution and Austerity in France	138
5.7	Structural break tests, the UK and France	139
5.8	Recursive parameter estimates	151
5.9	Correlogram for cross-sectional regressions	154
6.1	Social coalitions, fiscal pathways and austerity bias	158
6.2	Partisan models of austerity	167
6.3	Behavior of $\hat{\beta}_{\text{Party}}$ over time	169
6.4	Political map of the UK, 1945-2010	176

6.5	UK partisan positions, 1945-2010	177
6.6	Political map of France, 1946-2012	192
6.7	French partisan positions, 1946-2012	193
7.1	Public support and fiscal outcomes, 2006-2014	224
7.2	Change in public support for spending cuts, 1985-2006	225
7.3	Social coalitions and political parties during austerity	227
7.4	Potential social bases for forms of fiscal governance	230