In the 1980s, Belgium and Ireland accumulated debt with such alarming speed and persistence that Italy’s problems paled in comparison. Belgium was the most indebted sovereign of the time and its debt stock was surging faster than that of any other developed nation, while Ireland followed as a close second. Reeling from the economic shocks of the 1970s, neither country could regain control over the alarming growth of its debt. Although both countries adopted sizeable fiscal adjustment packages as early as 1982, the adjustments proved to be vastly insufficient in the face of ballooning interest costs and only succeeded in slowing, but not reversing debt growth in both countries. In the late 1980s, however, the debt trajectories of the two countries diverged. Belgium’s debt continued to snowball alarmingly in the absence of radical new adjustment due to ever-more onerous interest payments. It reached 135 percent of the GDP by the time the precipitous fall in European interest rates finally started to ease the interest burden in the mid-1990s. Ireland, on the other hand, adopted a second major adjustment package in 1987, which rapidly reduced the country’s indebtedness long before interest and growth rates changed for the better in the mid-1990s. Subsequently, the debt-to-GDP ratio decreased consistently in both countries until the global financial and economic crisis struck in the late 2000s and pushed the debt-to-GDP ratios over 100 percent again in both countries (see Figure 4.1).
This chapter compares and contrasts the politics of debt accumulation in the two countries in order to explore the effect of fiscal polarization in two similarly open economies. It argues that the relatively fast reaction to fiscal imbalances in both countries was motivated by their intense exposure to international economic competition. It explains how the severe negative effects of high inflation on trade, employment, and profits created the necessary political conditions for stringent deflationary policies, underpinned by radical fiscal tightening in both countries in 1982. At the same time, the chapter emphasizes that Belgian and Irish governments had very different room for maneuver in raising taxes and cutting spending due to different levels of fiscal polarization. In Belgium, the polarizing architecture of social security generated intense conflicts between business and labor. These conflicts were temporarily suppressed at the height of the economic emergency in the early 1980s, but they immediately resurfaced once the first adjustment package had brought inflation under control and they made it impossible to increase taxes or to retrench entitlements. As a result, fiscal effort was constrained to cuts in public investment and collective consumption for the rest of the decade, which proved insufficient to stop the snowballing of debt as the interest-burden grew, despite an astonishing reduction in these expenditures. Thus, Belgium remained on a path of incessant debt growth until the steep fall in interest rates finally freed the country from the chokehold of debt in the mid-1990s.

In contrast, policymakers had much greater latitude in adjusting various spending and taxation items in Ireland because the encompassing nature of existing policies ensured that any adjustment affected large parts of society fairly uniformly and, thus, limited the room for contention about who should bear the bur-
den of fiscal stabilization. In the two waves of adjustment, taxes were raised, welfare transfers were retrenched, and public investment and consumption were cut with minimal political resistance.

Focusing on international economic exposure and fiscal polarization helps to account for the two countries’ fiscal trajectories more comprehensively than alternative explanations do. The common claim that debt accumulation arises from fiscal indiscipline has little bearing on the Belgian and Irish experiences. In both countries, the vast fiscal imbalances were originally triggered by a series of exogenous economic and financial shocks, to which both Belgium and Ireland responded with resolute fiscal tightening from 1982. Notwithstanding the lack of effective political control mechanisms to ensure spending discipline under divided governments in both countries (Hallerberg 2004), both Belgium and Ireland achieved remarkable and sustained reduction in spending in this period, evidencing the commitment of successive coalition and minority governments to spending control. The trouble was that the improvement in the primary balance could not keep pace with the increase in the interest burden. The divergence in the two countries’ fiscal trajectories in the second half of the 1980s had to do with differences in policy makers’ ability to extend fiscal effort beyond the realm of discretionary expenditure. Belgium was unable to change course due to its failure to complement spending discipline with adjustments to entitlements and taxes, whereas Ireland’s turnaround was made possible by achieving both.

Other explanations shed light on important aspects of the politics of policy adjustment in the two countries but fail to explain all significant similarities and differences. It has been noted that the ability of governments to enlist the support of the social partners was crucial in enabling the stabilization package of 1982 in Belgium (Jones 2008; Kuipers 2005; Hemerijk and Visser 2000) and the reforms of 1987 in Ireland (Baccaro and Lim 2007; Baccaro and Simoni 2008; Culpepper 2008). It remains to be explained, however, why further compromise proved elusive in Belgium since 1982 or how Ireland could already put into place a major adjustment package in 1982 without a social pact. Similarly, the ideational shift from Keynesianism to a neoliberal policy paradigm in the 1980s (McNamara 1998) helps to better understand the ideational background of the decisive deflationary turn in 1982 in both countries, but it does not explain why Belgium failed to step up its fiscal efforts the same way Ireland did when the first stabilization package proved insufficient to stem debt accumulation.

By analyzing the interplay of economic pressures and redistributive conflict in the two countries, this chapter fills in these gaps in our understanding
of the politics of debt accumulation and fiscal stabilization in Belgium and Ireland. It explains why divided governments could exercise surprisingly strong spending control in both countries, under what conditions governments could count on the support of social partners, and why the neoliberal policy paradigm was more fully embraced in Ireland than in Belgium. The first half of the chapter discusses how the economic pressures on Belgium’s open economy created the preconditions for a rightward shift in the government coalition and for a compromise between employers and part of the labor movement, which made it possible to embrace a new, stability-oriented policy paradigm and to put into place the drastic fiscal adjustment package of 1982. Then, it demonstrates how conflicts between business and labor about the social security system undermined the government coalition that had launched the first wave of stabilization and reignited hostility between social partners once the worst economic side effects of fiscal problems had been neutralized. The second half of the chapter discusses Ireland’s success in adjusting its fiscal policies in the face of alarming debt growth. It shows that political conditions were conducive to fiscal adjustment practically irrespective of the composition or strength of the government in power or the presence or absence of corporatist consultation, because intense exposure to international economic forces made stabilization urgent while the encompassing nature of existing fiscal policies implied that no political actor could spare any major social group from fiscal pain. (For an overview of the alternative explanations for the pattern of similarity and divergence between Belgium and Ireland in the 1980s, see Table 4.1.)

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The next section analyzes Belgium’s fiscal policies in the 1980s and early 1990s in detail to show that drastic fiscal effort in public investment and consumption was coupled with practically complete inaction in the field of revenues and entitlements. The third section explores the societal bases of this lopsided fiscal effort. It discusses the conflicts between business and labor over the social security system and the shared interests of the two classes in macroeconomic stability in the economically more dynamic and internationally more exposed Flemish region of the country. Then, it discusses the political and policy manifestations of these conflicts and commonalities of societal interests. The fourth section reflects on the longer term implications of the foregoing analysis for Belgian politics. The fifth section turns to the Irish case. It briefly discusses the fiscal policies of the period and goes on to explain why fiscal effort could encompass the entirety of public finances. It analyzes the structure of societal interests and how they were represented in the political sphere. The sixth section argues that Ireland’s effectiveness in dealing with its recent fiscal problems is still rooted in the same socio-political structure that allowed the country to overcome its debt problems in the 1980s. The concluding section draws the main lessons of the chapter.

Fiscal Rigor and Recklessness in Belgium since the 1980s

Belgium’s serious fiscal troubles began with the oil crises. The country had previously been on a favorable fiscal path. Although it inherited a large debt stock from the time of the war, the debt-to-GDP ratio dwindled swiftly in the postwar decades due to robust economic growth and moderate deficits (Reinhart 2010, 23). In the second half of the 1970s, however, the budget was thrown out of balance by the effects of the major economic downturn triggered by the two oil crises and by a jump in the costs of outstanding debt. Expenditure was set on an explosive trajectory, growing from 45 to 64 percent of the GDP within ten years after the first oil shock. Social expenditure grew by 8 percentage points as the welfare system was flooded with unemployed and early retirees in the wake of the economic downturn (Hemerijk and Visser 2000). Non-social security expenditure also increased by 5 percentage points as successive governments tried to remove excess workforce from the job market by boosting public employment (Hemerijk and Visser 2000). The increase in primary expenditure was compounded by a jump in the interest burden around the turn of the decade—from 4 to 10 percent of the GDP—due partly to increased borrowing but, more impor-
tantly, also to a two-thirds increase in the interest rates charged on Belgian sovereign debt (Barro and Sala-i-Martin 1990). Initially, the expenditure explosion was partially counterbalanced by a surge of revenues, because double-digit inflation generated extra tax income via fiscal drag (Blöndal 1986, 117). However, when Belgium joined the fixed exchange rate regime of the European Monetary System in 1979, it became crucial to rein in inflation to maintain parity with low-inflation Germany. As inflation was brought down, revenues leveled and the full scale of the fiscal damage of the economic and financial shocks became visible. By the beginning of the 1980s, it was also clear that the damage would last beyond the immediate crisis years.

By 1982, the debt-to-GDP ratio had grown close to 100 percent, and annual borrowing was above 10 percent of the GDP. Fiscal imbalances had started to cause problems with maintaining a fixed exchange rate within the EMS due to high inflation and balance of payments issues. Belgium was forced to devalue the franc in the wake of several currency crises, but other member states only consented to such realignment on the condition that austerity measures were taken (Hemerijck et al. 2000, 236; McNamara 1998, 142). In view of the direness of the situation, a radical austerity package was adopted.

Spending on public consumption and investment was cut back via the introduction of the rule that expenditure cannot grow in real terms and that additional cuts would be made whenever this was necessary to ensure that the nominal value of the deficit does not increase (European Economy 1993). As a result, such expenses shrunk 11 percentage points to 20 percent of the GDP, a fifth lower than their pre-crisis level in the early 1970s. Investments were cut by two-thirds; subsidies to firms were halved, and the compensation of employees decreased by a fifth. In these years, Belgium moved from spending on public consumption and investment on par with countries of similar levels of development to spending the least on public consumption and by far the least on public investment (IMF 1998, 17).

Adjustments to social security, on the other hand, were much smaller, especially in view of the enormous shock to the sector around the turn of the decade. The austerity package of 1982 included some tightening of the unemployment benefits and increases in contributions paid by employers (Hemerijck and Visser 2000); but beyond that, changes remained minimal, and Belgium continued to spend significantly more on social security than comparable countries (IMF 2004, 6). Outlays in this sector decreased slightly during the decade but only by 2 percentage points, which was a rather small improvement in light of their preceding surge. Importantly,
the reduction happened mostly endogenously: family allowances dwindled in the wake of a decrease in the number of births, while unemployment transfers decreased thanks to the relative improvement of the labor market situation in the second half of the 1980s (Festjens 1993, 236).

It was not for the lack of trying that adjustments failed to happen. The 1980s saw four attempts to retrench the social security sector. The 1981 Disaster Plan, which attempted to freeze pension expenses and tighten conditions on several social security benefits failed because coalition partners (Christian Democrats and Socialists) disagreed over how radical the retrenchment should be and the government fell over the issue. A proposal to reform the pensions of civil servants put forward in 1983 was withdrawn in the face of strikes. The St. Anna Plan of 1986—which included heavy cuts in the unemployment insurance and limited future pension entitlements—also stirred up fervent labor demonstrations and was left unexecuted after the government that proposed it had to resign. It was only in 1982 that cuts in social security were actually enacted and pension contributions increased, although they proved ultimately insufficient (Anderson et al. 2007, 321–23; Marier 2008, 88). The deficit of the social security sector shrank somewhat during the decade—from 11 percent of GDP in 1980 to under 8 percent by 1990—but the gap was still sizeable and started to widen again.

In contrast, there was almost no attempt to involve the revenue side in the consolidation effort. On the contrary: after a prolonged period of growth, revenues declined from the mid-1980s onward due to two personal income tax reforms—the Grootjans tax-reform of 1985 and the Maystadt tax-reform of 1988—which led to a significant decline in direct tax revenues (European Economy 1993), while the so-called “Maribel operation” of 1981 granted employers of manual workers exemption from contribution to social security. Indirect taxes were left untouched throughout the decade to avoid detrimental impacts on inflation. The only revenue increases came from the raising of pension contributions and the creation of new levies in 1982, but these were more than offset by the decrease in other sources of revenue. (Anderson et al. 2007, 322).

As a result of the sustained campaign of austerity, the primary balance climbed to a surplus of 5 percent in 1990, 13 percentage points higher than at the beginning of the decade. Nevertheless, net borrowing still amounted to 7 percent of the GDP because the interest burden had kept steadily growing throughout the decade to 12 percent of the GDP by 1990. The steady growth of the debt-to-GDP ratio was only paused for a single year, on the peak of an economic boom in 1989, but it was rising to new heights.
again in 1990, and it surpassed 130 percent in 1993. It was in this disheartening situation that the decision about creating a common European currency arrived and Belgium looked very far from being able to fulfill the fiscal criteria for accessing the monetary union.

In 1993, the government embarked on a renewed consolidation effort. First, it announced a “Global Pact on Employment, Competitiveness, and Social Security,” which included plans to reform and significantly retrench social security, especially in the field of unemployment benefits (Kuipers 2005, chap. 5; Marier 2008, 89). When this pact failed in the face of fierce opposition from the social partners, the government put forward a new “Global Plan” to save the day through limited cuts in pensions (a reduction of the highest pensions and a 1 percent solidarity tax on the highest early retirement benefits), a mix of minor tax increases (raising VAT by a percentage point; increasing excise rates on alcohol, tobacco, and energy; and introducing a new real estate tax) and one-off measures like the sale of the central bank’s gold reserves and privatization (IMF 2005; Kuipers 2005, chap. 5; Marier 2008, 89–90). While these measures managed to further improve the primary balance by the late 1990s, they—once again—achieved little in terms of closing the gaping deficit of the social security sector. In the following year, plans were discussed to increase the financial viability of the pension system through an increase of the retirement age, higher taxes on the highest pensions, and a decrease in civil servants’ pensions, but when the unions expressed their disapproval, the plan was dropped (Anderson et al. 2007, 331; Marier 2008, 90–124). This 1994 attempt to rebalance the social security sector proved to be the last one ever since.3

Nevertheless, the headline deficit figures improved significantly in the second half of the 1990s as the external financial environment dramatically changed for the better. Interest rates sharply dropped across Europe, and the interest burden on the budget melted away from its peak at 12 percent of the GDP in 1990 to under 7 percent in 2000 and further to around 3 percent in 2010. The fiscal efforts of the 1980s and 1990s finally bore fruit: high primary surpluses translated into a balanced budget and Belgium’s debt-to-GDP ratio started to rapidly decrease without further fiscal adjustments. By the late 2000s, just before the global financial and economic crisis struck, the debt-to-GDP ratio was back at 87 percent. Thanks to its steadfastness in controlling its public consumption and investment expenses and to the fortuitous change in interest rates, Belgium was saved—and managed to enter the monetary union with the first group
of countries—despite its inability to tackle the enormous problems of its social security sector.

The next section investigates the political background of policy making in this period to explain this curious, lopsided fiscal effort, which combined the greatest rigor with remarkable lack of progress on the issue of consolidating the social security sector either through significant retrenchment or through revenue increases. This policy mix inflicted considerable fiscal pain on the country while it simultaneously jeopardized fiscal stability through relentless debt accumulation. Belgium escaped acute trouble as conditions on global financial markets turned better just in time to avoid crisis and to meet the requirements for euro-accession. However, its travails are intriguing from the perspective of understanding the political bases of the country’s ability or inability to deal with the problem of sustained excessive debt accumulation.

The Societal Bases of Rigor and Recklessness

Belgium’s prolonged battle with debt provides a glaring example of the limits of governmental power in resolving acute redistributive conflicts and, thus, in solving budgetary problems. This section demonstrates that successive Belgian governments’ maneuvering room in making adjustments to the budget were circumscribed by the preferences of business and different labor groups. Heightened conflict between business and labor about social security excluded the possibility of revenue increases and entitlement cuts, except at times when acute economic troubles forced the two sides to compromise. In 1982, labor groups in the economically more dynamic Flanders, which suffered heavily from the rapid decline in foreign competitiveness, defected from the united labor front defending generous entitlements. They showed themselves to be ready to compromise with business, which was itself in great distress due to the macroeconomic problems Belgium’s open economy experienced. This made limited retrenchment and increases in employers’ contribution possible. This “reform-coalition” between business and Flemish labor also enabled the government to launch the wave of deflationary reforms that included cuts to collective consumption and investment spending as well as measures insulating monetary matters from fiscal problems.

However, this coalition was short-lived. The first wave of reforms averted the most acute danger to foreign competitiveness, and fiscal prob-
lems ceased to directly bear on the welfare of labor or business. As a result, the unified labor front was restored in its rejection to retrenchment to social contributions, while business was more concerned with the size of social contributions than with the deficit of the social security sector. In this situation, all that successive governments could do was to step up their efforts in cutting expenditures that had less direct impact on the interests of well-delineable social groups. The resultant dramatic shrinking of funds available for public consumption and investment contributed greatly to the heightening of regional conflict between Flanders and Wallonia over the distribution of such funds, but it had no bearing on the conflict between labor and business and, thus, on the social security issue, which proved to be impossible to solve ever since.

Conflicts and Commonalities of Interests and Social Coalitions

Social security was the focal point of political wrangling over fiscal stabilization in Belgium not only because the fiscal imbalances of the sector were massive—they amounted to more than a tenth of the GDP in the early 1980s—but because its architecture strongly polarized the interests of contributors and beneficiaries. As in all Bismarckian welfare states, the social security system in Belgium was designed to provide generous, contribution-based entitlements to workers from funds generated by payroll taxes that directly increase the costs of labor (Hemerijk and Visser 2000). Unlike in arrangements where general tax revenues dissipate some of the welfare costs across society and allow for more undifferentiated burden-sharing in consolidation efforts, losses from benefit reductions or revenue increases in this contribution-based setup fall squarely on one group, creating incentives for each side to demand solutions that place the entire burden of consolidation on the other side.

Yet, in 1982, both cuts and revenue-increasing measures were successfully enacted under the Special Powers Act. When sacrifices hurt most—at the peak of unemployment and in the midst of a wave of bankruptcies—they were made. It was later in the decade, when growth and profitability picked up, unemployment somewhat subsided and the opposing sides could have better afforded to thrash out a compromise that front lines hardened and further reform proved elusive. Successive governments put forward proposals that favored business interest by seeking to rebalance the system exclusively through entitlement cuts. These invariably failed in the face of fierce union opposition.

At first sight, this pattern of discord and compromise simply confirms
the importance of “crisis” in fostering compromise noted by several experts of Belgian politics (Pochet 2004, Kuipers 2005). The compromises of 1982 were achieved in the context of economic emergency. High inflation had fueled serious problems with international competitiveness from the time Belgium joined the fixed exchange rate system of the EMS in 1979, causing a catastrophic rise in unemployment and a wave of bankruptcies. In 1982, problems culminated in a currency crisis. Taming inflation—to restore international competitiveness and to strengthen the credibility of the fixed exchange rate—required immediate macroeconomic stabilization, especially the consolidation of public finances.

However, the crisis narrative conceals the fact that different sections of Belgian society had different incentives to compromise their fiscal interests in the economic emergency of 1982, depending on how much their welfare depended on the country’s international competitiveness. Macroeconomic stabilization was very urgent for businesses and workers in the economically more dynamic Flanders because they could reasonably hope that sales, profits, and employment would rebound if the inflationary pressures subsided. Rapidly declining Wallonia, on the other hand, had such profound long-term problems due to its outdated industrial structure that macroeconomic consolidation in itself was unlikely to improve the Walloon economy enough to compensate for fiscal sacrifices. It was the shared interests of Flemish labor and business in international economic competitiveness that gave rise to a powerful social coalition in support of the stabilization package of 1982. The acquiescence of Flemish workers in moderate welfare cuts was particularly important in enabling the compromise on social security because strikes by Walloon workers only had no chance of successfully blocking reform.

The Flemish competitiveness coalition did not last. After the first wave of stabilization had improved macroeconomic conditions and businesses and employment somewhat recovered in the second half of the 1980s, the incentives for further compromise evaporated. The front lines hardened again as Flemish labor reverted to its alliance with Walloon labor and business started demanding cuts to labor-cost increasing contributions. Despite ever more alarming debt accumulation, significant reform to the social security sector was unfeasible because the debt problem ceased to have direct bearing on economic conditions. Inflation had been brought under control, and it was insulated from fiscal problems through institutional changes that ensured the independence of the central bank. Even the announcement of plans for a monetary union and the adoption of the Maastricht criteria for membership failed to change this situation, despite
the importance of accession for business and labor in the more dynamic export-oriented regions. The previous decade had shown that the government could effectively improve the primary balance by cutting collective consumption and investment expenditure whenever reforms to social security failed, weakening the urgency for compromise on this divisive redistributive issue.

In sum, the politics of consolidation were governed by developments along two dimensions. Class conflict over the issue was particularly acute due to the polarizing nature of the social security architecture. However, regional divisions—especially within the ranks of labor—modulated class conflict depending on the extent to which fiscal problems bore on economic performance. Workers in economically healthy Flanders had a strong incentive to compromise for the sake of eliminating the negative economic side effects of debt. These incentives induced them to defect from their alliance with labor in persistently declining Wallonia whenever their employment prospects were endangered by macroeconomic imbalances. A coalition between business and Flemish labor was strong enough to trump opposition not only from Walloon workers, who were especially strongly wedded to the welfare safety net due to the hopeless state of the Walloon economy, but also from any other interest group that might have had a stake in blocking cuts to collective consumption or investment expenditure. However, the reforms launched by this temporary coalition in 1982 eliminated the link between fiscal and macroeconomic problems, making it possible for class conflict to dominate the strategic context of consolidation for the rest of the 1980s and 1990s.

The Observable Manifestations of Evolving Coalitions: The Behavior of Parties, Unions, and Employers’ Organizations

This analysis of conflicts and commonalities of interest across groups in society and their effect on the formation of social coalitions is consistent with the behavior of different political actors in this period. Clusters of labor and business interests were represented by an intricate web of institutional actors in the partisan and the corporatist sphere, which allowed the commonalities and conflicts of interests between the different clusters play out in a complicated arrangement within the political scene. Yet, patterns of government coalitions and trade union behavior in the 1980s and early 1990s clearly reflect the détente between business and some labor groups at the height of economic troubles, the role of Flemish labor in making this compromise possible, and the renewed straining of class relations after
the most pressing economic problems were addressed and Flemish labor restored the unity of the labor front. Showing this requires a brief introduction of the Belgian political system first.

The Belgian party system had been historically structured around three sets of cleavages—religious issues, acute class conflict and regional-linguistic differences—and thus came to be dominated by Christian-Democratic, Liberal, and Socialist parties with a Flemish-speaking and a francophone party in each ideological family⁴ (Deschouwer 2009). For most of the 1980s, the Christian Democrats dominated elections due to their overwhelming electoral strength in Flanders, drawing on a mixed constituency of labor, business, and the self-employed in the economically more dynamic areas (De Winter 1996, Claeys 1996). Socialists were not far behind—in fact, they pulled ahead of the Christian Democrats in the 1987 elections—enjoying solid support in the declining heavy industrial areas of Wallonia and pockets of heavy industry in Flanders around Antwerp and Ghent (Delwit 1996). Liberals were firmly in third place throughout the decade, relying on the steady electoral support of relatively younger, better educated, white-collar employees, managers, and self-employed from the economically most dynamic areas of Flanders, Wallonia, and the Brussels area alike (Fitzmaurice 1996).⁵

The trade union movement was also divided along ideological lines, but all three unions—Christian, Socialist, and Liberal—retained their national unity, despite different linguistic proportions within their memberships. The Christian union was the largest of the three, and its membership was biased towards Flemish speakers. The Socialist was a close second, with a balanced membership across the two linguistic communities. Liberal unions were rather insignificant (Claeys 1996; Marier 2008). On the employers’ side, a single national organization participated in the system of social partnership, representing enterprises on both sides of the linguistic divide, but this organization was in competition with an alternative Flemish organization for the support of Flemish business. The social partners wielded policy influence in their institutionalized roles in administering the social security funds and participating in the National Labor Council or in the Central Economic Council. More importantly, however, they achieved power through cultivating strong ties with the political parties, achieving synergies from the mobilization capacity and the electoral power of their membership.

In this setup, the Christian Democrats (especially the successful Flemish party) and the Christian union represented the pivot in the conflict between different labor groups and business over the social security issue.
The standpoints of Liberals and Socialists were clear on each end of the spectrum. Liberal parties and the employers’ organization pushed for the retrenchment of social security on behalf of business. Socialist parties and the Socialist trade unions fought tooth and nail for keeping entitlements to protect the interests of pensioners as well as workers in declining areas stricken by long-term unemployment. In contrast, the Flemish Christian Democratic parties and the Christian union faced hard dilemmas. The Flemish Christian Democrats were confronted with contradicting demands from their varied constituencies: businesses clamored for lower social security contributions, whereas labor was wedded to entitlements. To make things more complicated, businesses themselves worried that a too aggressive stand on retrenchment might trigger large-scale labor unrest at a time they were barely coping (Jones 2008, 170). These contradicting demands were directly represented in the party’s decision-making as the different Christian Democratic constituencies (usually referred to as *standen*) exerted influence on the party’s policy choices not only via electoral channels but also through their representatives within the party. The Christian union was ambivalent between compromising with employers for the sake of better employment opportunities, which would have benefited its Flemish majority, and the defense of social entitlements, which was in the interest of all of its members, but was especially crucial to the Walloon minority. The political balance of power and the fate of social security hinged on the behavior of these pivotal actors not only because they represented something of a middle ground in the conflict but also because they represented such powerful forces in the partisan and corporatist spheres.

The stance of these actors evolved with the changes in the economic environment. At the beginning of the 1980s, Christian Democrats had been governing with the Socialists for a decade. With the deepening of the economic, monetary, and fiscal crisis, the government came under increasing pressure to adjust policies, but intragovernmental disagreements about policy reform caused cabinets to fall in rapid succession. In 1981, the government was about to put into place a “Disaster Plan” to restore macroeconomic stability, but it foundered on Socialist resistance to pension cuts. It was in this situation that Christian unions started to signal their readiness to support painful reforms for the sake of economic recovery. In secret negotiations with the Flemish Christian Democratic leadership, they consented to breaking up the Christian-Democratic-Socialists coalition and to forming a new government with the Liberals. This secret consent given by trade union leaders only became known to the wider public in 1991 (Jones 2008, 188). In an economic recovery plan, the Christian
unions also laid out some welfare sacrifices they would be willing to accept to ensure the success of this new coalition in putting forward a stabilization package (Jones 2008, 170–71). The new Christian-Democratic and Liberal coalition passed the Special Powers Act in 1982, which represented a compromise as cuts to social security were balanced by increased social contributions. Socialist parties protested and Socialist unions organized strikes, but the Christian unions kept their promise and refrained from striking, rendering Socialist protest ineffectual. Importantly, the reforms met with the approval of the constituencies of the political actors involved, despite the secrecy surrounding the initial negotiations about political and policy changes. Christian union leaders faced no backlash for not joining the Socialist strikes in opposition to welfare cuts; Christian Democrats got more votes in the next elections, while the Liberals maintained their vote share. The new political alliance between these actors was supported by a social coalition between business and Flemish labor.

This social coalition did not survive for long, though. Although the Christian Democratic and Liberal government coalition lived on after the 1985 elections and continued to push for further consolidation, the tacit alliance with the Christian unions disintegrated and further reforms to social security proved elusive. Christian unions had much weaker incentives to consent to further sacrifices on behalf of their members after the threat to international competitiveness had been successfully averted, growth gradually picked up, and unemployment started to decline in Flanders (Jones 2008, 52). Liberals and business constituencies of the Christian Democrats were also less willing to tolerate high social security contributions. The coalition adopted the so-called St. Anna Plan in 1986, which included heavy cuts in the unemployment insurance, limited the accumulation of benefits, and decreased the level of future pensions, with no corresponding sacrifices from businesses’ side. Christian unions strongly objected and this time they did join the Socialist unions in the mobilization for strikes. The government had to resign not long afterwards due to pressure from the Christian workers movement on the leadership of the Christian Democratic Party to break with the Liberals (Marier 2008, 88). The St. Anna Plan remained unexecuted (Anderson et al. 2007, 325).

The new elections in 1987 only reinforced the significance of class conflict in structuring the political scene. The Christian Democrats lost votes to the Socialists in Wallonia, who now wielded the strongest electoral force in the country, and to the Liberals in Flanders, who continued to siphon off Flemish Christian Democratic voters from then on (Fitzmaurice 1996). The Socialists and the Christian Democrats were in government together
again. The Socialists made sure that cuts to the social security system were off the agenda for the rest of the decade. In fact, they even achieved some corrections in entitlements that had not been indexed under the previous governments. The Flemish Christian Democrats could not confront them without alienating their labor section. At the same time, they were sorely conscious of losing business support to the Liberals and, thus, (successfully) sought to decrease the fiscal pressure on businesses. The Christian-Democratic and Socialist coalition survived until 1999.

In 1993, while in coalition with the Socialists, the Flemish Christian Democrats seized upon the emergency generated by the combination of monetary integration, a disastrous fiscal situation, and a recession to try to broker a “historic compromise” between labor and business. The Global Pact on Employment, Competitiveness and Social Security was to solve the persistent imbalances of social security, decrease the cost of labor, and help make sure that fiscal problems would be resolved in time for the euro deadline. Unsurprisingly, it also promised to resolve the conflict that was breaking the Flemish Christian Democrats’ constituency apart. The odds of a breakthrough seemed better than ever because of the major challenges the country was facing. First, joining the euro with the first group of countries was of immense importance to the Flemish economy, which was so dependent on competitiveness in the European markets. Second, the recession had increased unemployment—although mostly in Wallonia, less significantly in Flanders—and created problems for business. Third, debt reached truly alarming proportions and borrowing was still high.

In the event, the “Global Pact” failed spectacularly, proving the crisis discourse of the government and the reference to the country’s problems ineffectual in the absence of direct incentives for labor and business to make painful sacrifices. Euro accession had real urgency, but it was far from clear that better fiscal figures could only come from social security reform, given the decade-long experience with successive governments finding ever-newer savings through cuts in public consumption and investment. In Flanders, the slump in employment and growth was much less serious than the economic troubles of the late 1970s and early 1980s, while Wallonia was much harder hit (Dejemeppe-Saks 2002). Moreover, in the low-inflation environment of the early 1990s, it was much less clear that fiscal consolidation would be a remedy to economic problems than in the early 1980s when the link between exchange rate troubles, inflation, and fiscal policy was much more obvious. Finally, in the absence of any indication of a looming debt crisis, debt was not of immediate concern to either business or labor.
This lack of pressing motivation for compromise is evident both in the design of the “Global Pact” that was put forward by the government and in the response by unions. Presumably as a result of the desperation of the Flemish Christian Democrats to win back the business support they had been losing to the Liberals, the proposal presented to the public was tailored entirely to business’ liking and offered little to labor by way of a compromise. The unions had been involved in preliminary bargaining, but their demands were left out of the final draft (Kuipers 2005, chap. 5; Marier 2008, 89). The proposal contained plans to reform the structure and administration of the social security system, to make it more selective, to limit expenditures, and, thus, to restore the system’s financial balance. It was especially in the field of unemployment benefits that substantial retrenchment of entitlements was to take place. Simultaneously, the plan proposed to decrease social security contributions on specific types of employment in order to decrease the costs of labor for business. If the Flemish Democrats were hoping that they would be able to strike a similar deal with the Christian unions as in the early 1980s, they seriously miscalculated. Even if Christian union leaders had been inclined to further negotiate about the pact, they had no other choice than to reject this unbalanced pact under immense pressure across the board from the rank and file for strikes (Kuipers 2005 p97). In the face of united labor opposition, the pact could not survive.

The Enduring Problems of a Fiscally Polarized Polity

Remarkably, the “Global Pact” of 1993 has been the last attempt to rebalance social security despite persistent (and, in the recent years, further widening) deficits of the sector. The precipitous fall of interest rates since the 1990s stopped and reversed the snowballing of debt, reducing the urgency of the issue and allowing it to be shelved. Nothing demonstrates better that social security ceased to be a sore point of Belgian politics than the fact that Liberals and Socialists were able to form a coalition in 1999—ejecting the Christian Democrats from government for the first time since the Second World War—and they successfully governed together through 2007.

As class conflict cooled, interregional differences took center stage. Party competition has revolved ever more intensely around the protection of the regional interests, especially in Flanders, where increasing attention has been directed to the unequal contributions to and benefits received from the public purse across regions. The Flemish political discourse first
started to focus on the unequal fiscal capacities between regions after a
number of studies showed that Flanders was paying the bills of high unem-
ployment and disproportionately high health costs in Wallonia in the sec-
ond half of the 1980s (Kuipers 2006; Marier 2008; Beland and Lecours
2008). The issue then increasingly gained ethnic overtones as structural
unemployment plaguing Wallonia and the inability to control health care
costs started to be traced back to factors like “bad life habits” or a “cul-
ture of dependency” (Beland and Lecours 2005). As the growing successes
of separatist parties like Volksunie and Vlaams Blok/Belang highlighted
the electoral appeal of Flemish nationalism, Flemish Liberals rebranded
their party as protectors of Flemish interest (Jones 2008, 205). Christian
Democrats followed suit and entered into electoral cooperation with the
openly separatist New Flemish Alliance (Jones 2008, 218). By 2010, the
New Flemish Alliance was winning the elections on its own.

The dramatic shrinking of funds for public consumption and invest-
ment in the 1980s surely contributed to the intensifying of this conflict.
Tension between the two linguistic communities and, thus, the two regions
had been an important factor in Belgian political life in the postwar period,8
but the divisions had not gained economic-redistributive relevance before
the 1980s (Beland and Lecours 2008, 153). The intensification of cross-
regional tensions led to a series of constitutional reforms that separated
the financing of collective consumption and investment expenditures between
the regions and devolved decision-making to the regional level.9 It also led
to increasingly insistent calls from Flemish political actors for the regional
splitting of social security. Unsurprisingly, the Walloon side has used its
constitutional veto to stop further devolution, as no political actor in Wal-
lonia can agree to reforms that reduce interregional transfers that increase
the per capita disposable income of an average Walloon household by more
than 8 percent (Caruso et al. 2002).

This had grave consequences for the country’s political stability. The
question of state reform is threatening to break up the country, and it has
dramatically increased political uncertainty, best exemplified by how aston-
ishingly long coalition formation takes after each election (nine months in
2007 and 541 days after the 2010 elections.). At the same time, the shift to
regionally motivated politics also has serious implications for the issue of
social security reform. Political attention is no longer centered on how the
imbalance of the redistributive system can be resolved but whose problem
they should be. Flanders could operate a balanced system (without having
to ask business to pay more in or labor to take less out). Wallonia would
be bankrupt because it is unlikely to be able to borrow the necessary funds
to finance the enormous discrepancy between contributions generated and entitlements drawn by its population. In a sense, this would resolve the issue, but at the price of possibly breaking up the country and bankrupting half of it.

The immense political turmoil of the past years—in the midst of years of serious financial and economic crisis—reveals the costs of the persistent failure of Belgian society to renegotiate existing terms of redistribution in the past four decades. Although favorable changes in interest rates freed the country from the chokehold of debt in the 1990s and decreased the price of the conflict in fiscal terms, the political costs remain. Decades of class strife—in which labor and business were able to insulate themselves from the negative side-effects of debt and dig in their heels in protecting their polarized interests—are now followed by intense regional conflict in another negative sum game. In view of the veto that constitutional arrangements guarantee to the two communities, this conflict is unlikely to be resolved as long as the Kingdom of Belgium exists, but its intensity does not seem to subside. It fuels continuous political uncertainty. During the global financial and economic crisis, strong control over collective consumption spending and the continuation of low interest rates limited the damage to public finances. The debt-to-GDP ratio grew by only 20 percentage points in the past eight years to 107 percent. However, unfavorable changes in interest rates could easily plunge the country into similar fiscal troubles as in the early 1980s. With politics paralyzed by the issue of state reform, the country would be ill-prepared to deal with such an emergency or, in fact, with the economic hardships and emerging problems of population aging that are already on the horizon.

Ireland and the Benefits of TINA

The Irish case provides an interesting contrast—and a useful shadow case—to the Belgian one. Ireland was hit by similar fiscal and economic shocks as Belgium in the late 1970s and early 1980s, but it dealt with them much more effectively. Just like Belgium, it adopted a sizeable deflationary and fiscal adjustment package in 1982, which proved to be similarly insufficient in the face of ballooning interest costs and only succeeded in slowing, but not reversing, debt growth. Unlike Belgium, however, Ireland soon responded to this situation by renewed efforts, which affected many of those areas of the budget that the previous consolidation package had not and set the debt-to-GDP ratio on a steep downward path well before
the fall of interest rates, and the famous growth spurt of the Celtic Tiger helped further lighten the debt burden.

This section explains that Ireland was better able to adjust its fiscal policies because economic pressures made fiscal stabilization equally urgent, but there was much more limited room for wrangling over the distribution of fiscal sacrifices due to the structure of conflicts and commonalities of interest within society. It shows that successive governments were able to make a wide range of adjustments to spending and taxes that affected households across society because the large majority of society had a crucial economic stake in swift stabilization, but could not hope to be spared of the sacrifices necessary to make it happen. Policy makers could convincingly use the “there is no alternative” argument. This section also briefly reflects on the way Ireland has been dealing with the debt problem that it encountered in recent years as a result of its banking crisis to demonstrate that enduring patterns of societal interests give rise to similar pathways of fiscal stabilization today as in the 1980s.

Just like in Belgium, the fiscal troubles of the 1980s were ushered in by the oil crises in Ireland, too. Having amassed a considerable debt stock in the 1950s and 1960s, Ireland had been successfully decreasing its debt-to-GDP ratio for a decade when things turned sour in the mid-1970s. As growth slowed and unemployment increased, the government experimented with fiscal stimulus in vain (Honohan 1999). As a result, debt surged. By 1980, the debt-to-GDP ratio had grown to 67 percent from a low of 40 percent in 1973. When interest rates shot up in the early 1980s, the debt started to snowball at alarming speed. Within two years, the debt-to-GDP ratio was over 80 percent.

In 1982, Ireland embarked on stabilization. It broke with Keynesian stimulus and embraced austerity. VAT and personal income taxes were increased, while public investments and food subsidies were radically reduced (Alesina and Perotti 1996; Honohan 1992 and 1999). This achieved a 6-percentage point improvement in the structurally adjusted primary balance. However, this was not enough to counterbalance the growth of the interest burden and, therefore, only succeeded in significantly slowing, but not reversing, the accumulation of debt (Honohan 1992; IMF 1998). By 1987, the debt-to-GDP ratio was at 109 percent. Consequently, a renewed effort was made. The government wage bill was significantly squeezed via a hiring freeze and below-inflation wage increases, transfers were cut, and spending on infrastructure investments were further reduced (Alesina and Perotti 1996; Honohan 1992 and 1999). This tightening in spending was complemented by a tax reform in 1988 that widened the tax base.
but decreased marginal tax rates both on corporate and personal incomes and by a one-off increase in revenues due to a tax amnesty (Giavazzi and Pagano 1990; Alesina and Perotti 1996). These measures succeeded in setting the debt-to-GDP ratio on a firm downward path for the longer term. Within the next five years, the debt-to-GDP ratio decreased by 20 percentage points to 88 percent in 1992. Then, with the drop in interest rates and the high growth of the Celtic Tiger years, it fell precipitously, plunging to 36 percent in 2000 and to 24 percent in 2007, the last year before the banking crisis.

Biting the Bullet: The Societal Bases of Resolute Stabilization

The steadfastness of the stabilization efforts is understandable in light of the large corollary harm that fiscal problems were inflicting on Ireland’s open economy and on Irish society. Budgetary imbalances fueled inflation, which had a devastating effect on the competitiveness of Irish firms after 1979 when Ireland fixed its exchange rates to those of its lower-inflation European trading partners in the framework of the European Monetary System. Unemployment climbed from 7.8 percent in 1979 to a high of 16.8 percent by 1985, average growth in the 1980s was a third lower than in the preceding decade. Problems with competitiveness directly affected firms and workers in exporting and import-competing sectors but also had indirect repercussions for the sheltered sectors through the decline of domestic demand. Inflation also hurt sections of society whose livelihood was not directly dependent on the health of the economy. Public sector workers repeatedly ran into the problem of wrestling nominal wage increases from the government only to end up with lower take-home pay due to the joint effect of high inflation and fiscal drag (Baccaro and Lim 2007). People dependent on transfers saw the real value of those transfers melt away. No parts of the Irish economy and society were fully immune to the problems generated by inflation, which explains the resolute commitment to deflationary policies throughout the decade.

What bears more explanation, however, is how uncontentious the actual austerity measures were. They placed the entire burden on households while completely sparing business, and yet there was almost no protest from those who were asked to bear the pain. Neither of the packages attempted to increase the fiscal pressure on business. The tax reform that accompanied the stabilization package of 1987 even cut corporate tax rates from 47 to 43 percent (Alesina and Perotti 1996). Measures affecting the income of households, on the other hand, were bold and comprehensive.
Austerity encompassed VAT and personal tax increases, cuts in food subsidies, large reductions in social transfers, and a rollback of public employment and wages. Apart from the tax reform of 1988, which put a stop to the constant increase of tax pressure on households, all the adjustments of the decade required newer and newer painful sacrifices from large swaths of society. Yet, none triggered major social upheaval and few encountered major political resistance.

The exemption of business from fiscal sacrifices can be explained with the dependence of the Irish economy on foreign firms. From the late 1950s, Ireland had increasingly opened up to foreign direct investment and sought to lure investors with tax advantages, for example the Export Profits Tax Relief of 1956, which exempted export profits from half and then all of corporate taxation, or the setting of a uniform low, 10-percent tax rate on profits earned in manufacturing in 1978 (Barry 1999). By 1973, foreign firms accounted for a third of manufacturing employment and their share continued to grow to 50 percent by the 2000s (Kirby 2010). Increasing corporate taxation would have risked reversing the favorable trend in foreign direct investment inflows, causing employment to drop even further at a time of surging unemployment. Therefore, it was not in labor’s interest to push for greater burden sharing by business.

With businesses spared, households had to bear the fiscal pain, and they had little incentive to delay the inevitable by arguing about how that pain should be distributed among them. The majority of Irish society could not realistically hope to avoid making sacrifices and therefore had no stake in resisting any austerity package when another was likely to hit it in similar fashion. Rebalancing the budget required very large adjustments and was thus bound to involve significant cuts to some or all of the largest expenditures items (like transfers and public employment) and/or large, across-the-board tax increases. Most of these measures would affect much of the population fairly uniformly. Irish society was bound to choose “solidaristic” solutions because it was not possible to design austerity packages that would shield large sections of society and still successfully close the fiscal gap.

The reason for this lies in the relative homogeneity of society and the pattern of existing policies, which did not generate large differences in vested interests. Limited income dispersion was an important aspect of social homogeneity. Although income inequality within the Irish population was large in comparison with the rest of Europe, this was caused mostly by a “long thin tail” of the distribution towards higher incomes, but the overwhelming majority of society was concentrated at the low-end
of the income scale (McDonough and Dundon 2010). Because of this, tax increases and cuts in food subsidies had similar effect on the bulk of the population. Small income dispersion and the architecture of the welfare system also led to fairly uniform interests concerning social security across the majority of society. In the Irish Beveridge-style system, fairly meager contribution-based insurance benefits were matched by tax-financed assistance benefits for those who did not qualify for insurance, with the entire system centrally operated by the government (Callan and Nolan 2000; McCashin and O’Shea 2009). This precluded insider-outsider conflicts between those who earned eligibility and those who did not. Furthermore, due to the historical origins of the system, agrarian groups and the urban working class enjoyed many of the same benefits (McCashin and O’Shea 2009). Thus, the large majority of society was affected by cuts in social transfers fairly uniformly.

Public servants were the only larger group that had interests distinct from the rest of society. They did try to claim immunity from cuts to their income: even as late as 1986, a teachers’ strike still averted a public sector pay freeze. Eventually, their resistance was relaxed, though, and they agreed to a hiring and wage stop in 1987. While it is questionable how long they would have been able to hold their own in the face of large sacrifices demanded from the large majority of the population, public sector workers also had an important material reason to acquiesce in bearing part of the pain of austerity. By 1987, they had repeatedly experienced that continuing inflation and fiscal drag counteracted the effect of any nominal wage increases they achieved in negotiations with the government and left them with ever-lower purchasing power (Baccaro and Lim 2007). Under these circumstances, they were better off with a deal that froze public sector pay but implied lower inflation and involved a tax reform. Thus, by 1987, there was no significant area of public finances outside of corporate taxation that had not been adjusted for the sake of stopping debt growth.

**Parties, Unions, and Austerity**

These societal foundations of Ireland’s experience with fiscal stabilization were clearly mirrored in the stance of the most important political actors: the two major parties, Fianna Fail and Fine Gael, and the labor movement, encompassing the Labor Party and the unions. Given the untouchability of business due to the dependence of the country on foreign investors, no political actor could single out a group to pay for stabilization outside of its supporter base. At the same time, the economic emergency generated
by the decline in competitiveness made stabilization equally urgent for the supporters of every significant political player. Therefore, all political actors embraced austerity after some posturing and took turns in putting into place the painful measures that affected the majority of society.

The two major parties relied on the support of almost identical cross-class constituencies (Donaghey and Tegue 2007). Fianna Fail and Fine Gael—who between them shared more than 80 percent of the vote in the 1970s and 1980s—drew support from all corners of society, and their voter bases exhibited negligible regional or socio-economic differences (McAlister and O’Connell 1984; Farrell 1999). The Labor Party remained a very distant third, small and overshadowed by Fianna Fail both in getting the working class vote and in nurturing links with trade unions (Sinnott 1984; Mair 1990). Given the lack of differentiation of their voters, the two large parties never focused their strategies on kindling (re)distributive conflicts. Their programs had been virtually indistinguishable on economic and social issues in the decades preceding the 1980s (Sinnott 1976; Laver and Hunt 1992). In the face of mounting fiscal troubles in the 1980s, neither party could credibly promise to large groups of voters to find a solution that would shield them from fiscal pain. This strengthened their hands because delay would only increase the magnitude of the problem and force them to inflict even greater pain on their supporters. Moreover, neither large party needed to fear long-term negative electoral repercussions, as it was clear that no alternative strategy was available to either their main rival or to potential political entrepreneurs seeking to enter the political market.

After a brief period of wrangling, Fine Gael launched the first wave of stabilization in coalition with the Labor Party. They had already presented parliament with an austerity budget that contained large tax increases in 1981, but that package famously foundered on the resistance of independent members of parliament to the symbolic issue of taxing children’s shoes, bringing the government down (Honohan 1999; Hallerberg 2004). After new elections, Fianna Fail took over the government and proposed a budget with significant spending cuts, but it lacked the necessary external support to have it passed. After yet another round of elections in 1982, the new Fine Gael and Labor coalition was strong enough to pass a budget with significant tax increases and some spending cuts (Alesina and Perotti 1996; Honohan 1999).

Fianna Fail was to launch the second wave of fiscal tightening in 1987. Although it had campaigned for an end to austerity in the 1987 election, it initiated major cuts to the public wage bill, transfers, and investments
as soon as it formed a (minority) government (Giavazzi and Pagano 1990; Alesina and Perotti 1996). This second round of stabilization took place in an atmosphere of remarkable partisan consensus as the main opposition party, Fine Gael, decided to externally support it in parliamentary voting.\footnote{11}

Political consensus behind fiscal stabilization also manifested itself in the emergence of an important social pact: the Program for National Recovery in 1987. Endorsement by the unions lent further legitimacy to the austerity measures and guaranteed the commitment of public sector workers to wage restraint (Marsh and Mitchell 1999; Culpepper 2008). The consent of the labor movement to an essentially neoliberal stabilization package revealed union leaders’ conviction that such sacrifices were inevitable. They had learned from their inability to achieve real welfare improvements for their members throughout the 1980s that insisting on higher nominal wages in a high-inflation environment was a self-defeating strategy. They contented themselves with tax cuts in return for losses in transfers and for wage restraint, accepting that this was the most they could accomplish for workers in the given situation (Dellapiane and Hardiman 2012).\footnote{12}

The various political actors calculated well in embracing austerity. Voting data shows that the eagerness of the major parties to inflict fiscal pain did not alienate their supporters. Vote shares stayed mostly stable in the 1980s. There was only one exception: Fine Gael’s vote did plunge in 1987, the first election after the first round of fiscal tightening started in 1982. However, this is unlikely to be a punishment for the party’s espousal of austerity. Rather, it reflects a disappointment with its failure to definitively address the debt problem because the votes lost by Fine Gael went to the newly formed Progressive Democrats who embraced fiscal rectitude more openly than any of the old parties (Mair 1990). Voters condoned austerity. Unions also benefited from cooperating in the second round of tightening as their membership started to increase again after a long period of decline. Irish society did not seem to resent its political class for fiscal pain even though the rise of the Celtic Tiger and the spectacular dividends of fiscal stabilization could not be foreseen at the time.

Enduring Foundations of Effective Stabilization

Two decades after the breakthrough that helped Ireland reassert control over its debt, the country faces immense fiscal problems once again in the
wake of a severe economic and financial crisis. From a low of 24 percent in 2007, debt surged to a high of 120 percent in 2012 as a result of a catastrophic bank bailout scheme, the collapse of tax revenues, and surging expenditures. The policy response was remarkably similar to the one given to similar problems in the 1980s, both in its resoluteness and in its composition. As soon as the first imbalances appeared, a first austerity package was put into place in 2008, and it was progressively reinforced with successive measures when the proportions of fiscal problems fully revealed themselves. Stabilization affected large swathes of society without much differentiation, while mostly shielding the corporate sector. Welfare spending and public wage expenditures were substantially cut and income taxes, as well as VAT, increased (Dellapiane and Hardiman 2012). The debt-to-GDP ratio subsided under 100 percent in 2015 and is forecast to decline further in the coming years (Ameco).

Just like in the 1980s, adjustment has gone practically unchallenged across the political spectrum. The austerity program launched in 2008 by the Fianna Fail government was continued without hesitation by the coalition of Fine Gael and the Socialists after Fianna Fail was thrown out of government in the 2011 elections. Although unions failed to play the central coordinating and legitimizing role they performed in 1987—in fact, the Fianna Fail government deliberately chose to act unilaterally in 2008 and 2009, ignoring the practices of social partnership it had created in the late 1980s—this seemed to make little political difference or to undermine the political legitimacy of painful cuts and tax increases (Culpepper and Regan 2014).

Although the Celtic Tiger years brought impressive prosperity and economic development to Ireland, the underlying social structure and policy arrangements stayed stable enough since the 1980s to still rule out much wrangling in times of fiscal emergency. Overwhelming dependence on foreign investment still precludes increasing the fiscal pressure on businesses, while the interests of households are not polarized enough to make fighting about the design of stabilization worthwhile. The growth of income inequality of the past decades has been limited and was mostly manifested in the upper incomes pulling further away from the rest with middle and lower incomes growing roughly in sync (Nolan and Maitre 2000). The structure of welfare policies stayed roughly the same as before. Consequently, it would still be hard to come up with stabilization packages that place the burden on some groups while spare others, which allows Ireland to be resolute in its austerity efforts.
Conclusion

The Belgian and Irish cases of sustained and substantial debt accumulation in the 1980s demonstrate how important it is for fiscal stabilization that a large portion of society is sensitive to fiscal problems. In both cases, sensitivity to negative side effects arose from exposure to foreign competition. Both the Belgian and the Irish economy are significantly more open than the Italian. With budgetary imbalances fueling inflation, both countries were under considerable pressure to resolve their fiscal issues, which impinged heavily on their ability to compete internationally. This is reflected in the determination with which both countries embarked on fiscal stabilization in the early 1980s—a decade ahead of Italy’s first stabilization efforts—drastically improving their primary balances.

At the same time, the comparison of the Belgian and Irish stories also highlighted the role of fiscal polarization in determining the chances for effective and timely fiscal stabilization. In Belgium, the polarizing architecture of social security pitted labor and capital squarely against each other and precluded adjustments to a significant part of the budget. The two sides would cooperate as much as was necessary to keep international competitiveness insulated from fiscal troubles but would not come to a compromise over the gaping hole in social security, which had played such a central role in triggering and fueling Belgium’s fiscal problems in the past decades. This prevented Belgium from fully resolving its problems and left it exposed to developments in the financial markets (primarily, changes in interest rates). In contrast, the lack of polarizing fiscal conflicts within the Irish society allowed Ireland to effectively adjust any part of the budget—except for corporate taxation—and to pull itself up by its bootstraps.

The comparison of the two cases also sheds light on the role of institutional structures of policy making in influencing fiscal stabilization. From an institutional perspective, Ireland was worse placed to take decisive action or to engineer the compromises across society needed to make painful changes in the budget. It was ruled by divided coalition or minority governments, and it was lacking effective corporatist mechanisms to handle class conflict. In Belgium, coalition governments were the norm, but a time-honored system of corporatist consultation provided an important centralized forum for engineering compromise. Yet, it was Ireland that managed to effectively make the adjustments to its policies needed to fully regain control over borrowing, while Belgium was mired in debt until exogenous conditions changed. Some of Ireland’s successful adjust-
ment efforts involved corporatist consultation, namely the second round of stabilization in 1987, but at other times, like in 1982, they did not, and the last instance of austerity since 2008 took place via an explicit rejection of the system of social partnership. These patterns suggest that it is of lesser importance how the policy-making process is organized than what conflicts of interest need to be reconciled within it.

Finally, comparison of the Irish and Belgian cases also demonstrates the role of policy legacies and path dependence in shaping the underlying conflicts of interests that drive policy making. While the two countries looked back onto different economic histories and had developed very different economic structures, policies inherited from the past also had crucial importance for polarizing preferences towards fiscal stabilization in Belgium and allowing conflicts of interest to remain limited in Ireland. In Belgium, the architecture of social security strongly reinforced class conflict over a very large share of the budget because it provided generous benefits to labor from contributions that bore on business profits. In Ireland, the costs of welfare provision fell on the same social groups that enjoyed the benefits due to the combined effect of limited income dispersion and the complementation of social insurance with tax financed welfare benefits. This meant that any adjustment to the system was bound to affect the same group, reducing the possibility of conflict over this substantial part of public finances.

This chapter, along with the previous one, reviewed the effects of differences in structural variables—exposure to the negative side effects of debt and fiscal polarization—on countries’ ability to stabilize their public finances and regain control over excessive debt accumulation. The next chapter approaches the issue from a different angle, to demonstrate the deleterious consequences for sustained large-scale debt accumulation of high levels of distributive polarization and considerable insulation from the negative economic side effects in dramatically different economic, social, and political contexts in Greece and Japan.