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# FISCAL SOVEREIGNTY UNDER EU CRISIS MANAGEMENT: A COMPARISON OF GREECE AND HUNGARY

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This article concerns the changing conditions of fiscal sovereignty within the Eurozone in the context of the evolution of the EU's institutional crisis-management framework during the recent financial crisis. It begins with a method-of-difference approach to compare the dynamics and outcomes of the crisis in the Greek and Hungarian economies, on the basis of their similarly troubled fiscal positions and domestic political environments. On this basis, an argument is made that the outcomes in Greece (i.e. a breakdown in national fiscal sovereignty and severe economic losses) were not an inevitable product of the economic fundamentals, but at least partially attributable to uncertainty about the extent and expedience of financial assistance through the Eurozone's crises management institutions. The European Central Bank's (ECB) 2012 declaration of "unlimited support" for Eurozone governments has done much to calm markets, but has also created an institution with an ambiguous and self-imposed "dual-mandate". This article concludes that the precedent established by the last crisis has created a fraught situation, leaving the Eurozone without viable options that are both economically efficacious and politically legitimate. Relying on either the ECB or the European Stability Mechanism to manage any future crisis could well provoke a backlash among the Eurozone member states as national fiscal sovereignty is eclipsed by ever-deeper ad hoc financial commitments on the part of the institutions of crisis management.

**Keywords**: sovereignty, fiscal sovereignty, European Central Bank, European Stability Mechanism, IMF, crisis management, Hungary, Greece

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## INTRODUCTION

Debt crises have a long history of catalysing major transfers of sovereignty. As Sargent (2012) noted in his Nobel Prize lecture, it was the debt crisis among the American state governments of the 1780s that caused the United States to abandon its original confederative structure for the Constitution and federalism, effectively transferring most aspects of sovereignty in the United States from the state to the national level. Today, the European Union (EU) is still grappling with the lingering effects of its own first major wave of sovereign debt crises. While it has not led to a fundamental restructuring of the polity comparable to the federalization of the United States, this article's hypothesis is that it has nonetheless had significant consequences for the *de facto* distribution of fiscal sovereignty between the Eurozone national governments and the EU-level institutions. Furthermore, the crisis leaves in its wake a complex dilemma for the EU-institutional crisis management in the event of another crisis along similar lines, which remains a distinct possibility given the fiscal positions of several Eurozone governments. The study concludes that the outcome in the Greek case was suboptimal (a breakdown in fiscal sovereignty *and* staggering economic losses in Greece and the whole EU), yet will constitute a precedent guiding future institutional crisis management efforts in the absence of a coherent alternative institutional framework being delineated and endorsed prior to another crisis.

The EU country subject to the most attention during the post-2008 crisis management efforts has been Greece, having experienced severe economic turmoil and still undergoing a long-term structural economic adjustment program. Greece has been the recipient of an absolute majority of external financial assistance provided across eight EU member states receiving funding since the outbreak of the financial crisis in 2008 (EC 2018c). The so-called "Troika", consisting of the European Central Bank (ECB), the International Monetary Fund (IMF) and the European Commission (EC) has exercised significant external authority in managing the Greek economy. These institutions have negotiated conditional structural adjustment programs in connection with the disbursal of financial assistance, programs which have had substantial effects on the country's tax system, provision of pensions and other government benefits and public services, as well as legal conditions surrounding wages and collective bargaining rights (IMF 2010; Matsaganis 2011; Schulten – Müller 2013; Featherstone 2015).

Regardless of the desirability of the economic outcomes there, this being the first major test of the Eurozone institutional crisis management means that the efforts in Greece and the institutional developments they entailed constitute an important precedent. For better or worse, the precedent set by the crisis will likely shape the EU's response to its next crisis in the absence of a substantial institutional reform before that time.

This article will rely on comparative case studies of crisis management efforts in Greece and Hungary following a 'method of difference' logic. The aim is to illustrate the specific details of the institutional precedent and to test the hypothesis that the outcomes in Greece were not purely a function of its economic or fiscal fundamentals, but at least partly attributable to the institutional conditions of crisis management in the Eurozone themselves. This is followed by an effort to disentangle the complexity of institutional conditions through analysis of the design and roles of different crisis management institutions and the specific implications of their activities for fiscal sovereignty. Beginning with an argument for the relevance of the Greece – Hungary comparison, the article then examines the nuances of the condition of national sovereignty within the EU through a conceptual framework developed by Krasner (2001). The specific concept of fiscal sovereignty along with its status in the pre-crisis EU is explored in further detail, followed by an argument that fiscal sovereignty was demonstrably and substantially intact at the national level both inside and outside the Eurozone prior to the crisis. The case studies of Greece and Hungary are then presented and compared in order to illustrate the substantially different outcomes in these fiscally similar economies. The structure and role of the various crisis management institutions is then analysed in more detail and the architecture they form is juxtaposed in terms of its relationship with national fiscal sovereignty in the Eurozone.

The article concludes with the argument that despite the ECB's declaration that it will do "whatever it takes to preserve the Euro" (ECB 2012b), substantial ambiguities persist about the future of the relationship between crisis management and national fiscal sovereignty, particularly how and *how quickly* the EU institutions will act to contain and override national control over fiscal policy in the members at risk of insolvency in the event of a second crisis. The goal of this study is not to produce a narrative on how powerful international financial institutions can capriciously act to undermine small countries' sovereignty (e.g. Plank 1993; Hall 2003), or an effort to assign blame for the economic fallout in Greece (Skiadis et al. 2013; Hussain 2013). It is, rather, to show that certain ambiguities and tensions continue to surround the institutional crisis management tools available within the Eurozone that will quite possibly make it difficult or impossible to avoid the primary outcomes of the Greek case (severe EU-wide economic losses *and* a breakdown in national fiscal sovereignty) in the event of another major crisis. Without a renewed effort at debate, consensus-building and reform, in a second crisis the Greek case may unfortunately serve more as a guide to the outcomes one should expect, rather than to those that might be hoped to be avoided.

## 1. CASE SELECTION AND METHODOLOGY

This article relies on a 'method of difference' comparative case study approach in order to test the hypothesis that the breakdown of fiscal sovereignty between 2008 and 2012 in Greece was necessitated by its economic fundamentals and fiscal profligacy by comparing crisis management in Greece and Hungary. The specific area of interest in this comparison is the variation in the degree to which the two national governments retained control over fiscal decision-making, i.e. their national fiscal sovereignty, within their respective institutional crisis management frameworks. The Greek case is then further analyzed in terms of what the precedent set by the relevant crisis management institutions implies for the status of national fiscal sovereignty in the Eurozone. The study finds that the Greek case constitutes a breakdown in fiscal sovereignty within the EU institutional setting, with the Hungarian case serving to illustrate the difference in crisis management tools and fiscal sovereignty outcomes for an otherwise similar economy located within the EU but outside of the Eurozone, thereby highlighting the effects particular to the membership in the monetary union. The study then goes on to argue that fiscal sovereignty across the Eurozone has been placed in an ambiguous position, potentially undermined by both supranational actions by the ECB and intergovernmental processes within the European Financial Stability Mechanism (EFSM). This dilemma will make the resolution of any future crisis especially difficult and divisive within the existing institutional setting. The specific conclusions about the Greek case are not automatically generalizable to the cases of the other Eurozone countries at present, but do illustrate the precedent established within the existing institutional framework for extreme cases like that of Greece in the event of future crises.

There are a number of factors complicating the comparison between Greece and Hungary. Greece joined the EU in 1981, first among the former dictatorships of Southern Europe. By the 1990s, it was on a steady course of catching-up with the EU averages in terms of income and development, and after joining the Eurozone saw a major convergence of sovereign interest rates with the German bund, with 10-year debt trading at near parity with Germany's from 2002–2007 (Federal Reserve 2019). Hungary was a post-socialist transition economy that joined the EU much later, in the Eastern Expansion of 2004. Like most of Europe, Hungary enjoyed a period of steady growth between 2000 and 2006, but did not experience a convergence in interest rates comparable to that of Greece or the Eurozone members, with interest rates both more volatile and consistently higher than those in Greece. Furthermore, while both economies went through recessions in the wake of the global economic upheaval beginning in 2008, their respective recessions were primarily driven by different types of crisis and at different times; the Hungarian economy was strained by a banking and financial crisis between 2008 and 2010, while Greece was caught in a sovereign debt crisis beginning in 2010. Nonetheless, the comparison of Greece and Hungary is grounded in a *most similar systems* approach, on the basis of key economic similarities, particularly with respect to their persistently problematic fiscal positions in the run-up to their respective economic crises, but they differ with respect to the key independent and dependent variables of this study, Eurozone membership (and by extension of institutional crisis-management frameworks) and the status of national fiscal sovereignty.

Greece and Hungary are quite similar across a variety of criteria relevant to their roles in the global economy and their domestic fiscal situations. They have similarly-sized populations and economies, and their pre-crisis business cycles were roughly equally correlated with those of the core Eurozone economies, suggesting similar levels of economic integration/peripherality in relation to the core EU economies (Suppel 2004). Most importantly, both countries maintained similarly large state sectors and welfare budgets in the years leading up to the crisis (both unusually large for their income level) and were consistently unable to meet the EC's criteria for budgetary discipline. Indeed, Greece and Hungary ran the two largest deficits in the EU every year between 2003 and 2008 (OECD 2019). Political economists have argued in both cases that this was due in large part to their domestic political environments, in which politicians were consistently constrained by particularly strong public demands for maintaining high levels of government spending (Alt et al. 2014; Benczes 2016). They were further characterized by broadly similar internal political developments around the time of the beginning of their respective crises, namely with respect to changes in national governing parties (Benczes 2016; Visvizi 2012). Of the seven other EU members to receive emergency external financing during the crisis period (Cyprus, Hungary, Ireland, Latvia, Portugal, Romania and Spain), Hungary was the most broadly similar to Greece in terms of the countries' size and role within the broader European economy, as well as their structural fiscal positions, historic relationships with the EU's fiscal discipline monitors, and domestic political constraints. They are thus the pair that are best able to satisfy Fritz Scharpf's methodological criteria that in case selection for comparative studies, "[the cases] capacity to empirically identify the causal effect of differing institutional conditions on policy outcomes depends on a restrictive case selection that would need to hold constant the influence of two other sets of contingent factors – the policy challenges actually faced and the preferences and perceptions of the actors involved" (Scharpf 2000: 762). Both countries struggled with fiscal discipline, evinced a clear preference for running large budgets and deficits, and were faced with similar internal political dynamics and similarly strained relations with EU fiscal monitors.

The institutional focus of the study is on the IMF, the ECB, and the EFSM. This is far from an exhaustive list of all the institutional actors involved in crisis management, but does include the most critical institutions in terms of autonomy of decision-making and access to financial resources and/ or other means of assistance. The EC is given some attention because of its significant role in crisis management in both Greece (Bauer – Becker 2014) and Hungary (Piroska 2017) and, in general, as an inter-institutional agenda-setter and coordinator, but is not considered a key actor in the closing analysis of the relationship between fiscal sovereignty and institutional crisis management because of its lack of final authority over resource allocation[1].

## 2. SOVEREIGNTY AND FISCAL SOVEREIGNTY IN THE EU

Sovereignty is a broad and perennially contested concept and it is thus necessary to clarify its definition for the purposes of this study. An in-depth review of the different schools of thought on the matter would occupy far too much space, and instead it seems necessary to establish the merits and relevance of one broad and broadly accepted definition of the term. The multi-faceted conception of sovereignty developed by Krasner (2001) is useful for understanding what sovereignty means within the EU and will serve as the framework for this study.

Krasner's sovereignty perception relies on three overlapping concepts: international legal sovereignty, which is the recognition by other states of a state's capacity to conduct international relations and commit to agreements; domestic sovereignty, involving the actual capacity of a state to govern and exercise its authority within its territory; and Westphalian sovereignty, meaning the absence of any authority other than the domestic one being substantively exercised on the state (Krasner 2001).[2] The nature of the different forms creates an inescapable tension; states often cede some of their authority over domestic matters to external structures like international organizations, sacrificing aspects of Westphalian sovereignty under the assumption that the domestic government's capacity to achieve its ends will be enhanced. Restriction of national authority under international financial arrangements in general and monetary union in particular are both examples of using international legal sovereignty to legitimate the par-

[1] Except the limited b.o.p. Assistance system, and even then, the European Council must co-approve funding requests.

[2] A fourth form, Krasner's interdependence sovereignty (involving state capacity to regulate flows of people, goods, and ideas across its borders) is not considered here because of its virtual irrelevance within the EU, given the Single European Act/Four Freedoms.

tial cession of Westphalian sovereignty in order to achieve enhanced economic outcomes and by extension the furtherance of the domestic sovereign's ends, and thus, are not theoretically incompatible with the preservation of national sovereignty, constituting only a rearrangement of its various components. Indeed, even if an international arrangement fails to improve conditions of domestic sovereignty (or achieve any other particular aim), it is nonetheless legitimated by the state's exercise of international legal agreement and on these grounds cannot be said to be an infringement on national sovereignty.

The EU has been described as an example of a "shared sovereignty" system, which involves "the engagement of external actors in some of the domestic authority structures of the target state for an indefinite period of time" (Krasner 2009). But shared sovereignty has a critical precondition: the upholding of international legal sovereignty and a voluntary national agreement to the shared sovereignty system (Krasner 2003). While, in principle, the EU institutions all enjoy legitimacy as they were endorsed by elected governments of the various member states, the degree of authority that has accrued to them over time has produced a great deal of debate around the general condition of national sovereignty in the modern EU. To the extent that it has been retained, national sovereignty within the EU can be broadly conceptualized as an interlocking balance of the exercise of domestic, Westphalian and international legal sovereignty. Member state national governments have retained wide-ranging competencies, among them control over fiscal matters. It is within this balance that the concept of fiscal sovereignty is best understood, a subcategory of domestic sovereignty substantially retained even in those countries opting to join the monetary union, though one precariously situated in the delicate balance between national governments, the EU monetary and legal institutions, and forces emanating from the global economy at large.

*Fiscal sovereignty* amounts to national control over the raising and distribution of government revenues and other funds, including decisions to take on and whether or not to repay sovereign debts (Rodden 2004). Fiscal sovereignty is a "right which has been carefully guarded by sovereign states and protected in international law over hundreds of years" (Biswas 2002), and as the German Federal Constitutional Court has noted, "the decision on public revenue and public expenditure is a fundamental part of the ability of a constitutional state to democratically shape itself" (Bundesverfassungsgericht 2014). Fiscal sovereignty does not imply that governments are immune to the consequences of profligate fiscal policy or defaulting on sovereign debts, but rather that governments retain the ultimate capacity to make such decisions in the first place. It is not a negligible part of a state's aggregate national sovereignty.

In agreeing to join the Eurozone, EU members necessarily and unambiguously give up national control over *monetary policy*. But in a legal sense fiscal policy remains an essentially national competence for both the Eurozone and non-Eurozone member states alike (Schuknecht 2004; Chilarez – Ene 2012). This is confirmed by the wide variety of fiscal structures found across the Eurozone member states as well as consistent treatment of nearly all fiscal matters as national competencies in the various EU treaties (Chilarez – Ene 2012). Given the foundational EU principle of subsidiarity, fiscal sovereignty cannot be assumed to passively devolve to the supranational level alongside the explicitly agreed to control over monetary policy in the absence of any additional explicit agreement to that effect (Bureau – Champsaur 1992). While the European Council members have agreed to certain fiscal criteria through the Stability and Growth Pact (to be discussed in more detail in the next section), these remain soft-law agreements with limited EU-level enforcement; in effect homogenization of fiscal policy remains very limited and substantially determined by national rather than EU-level political will (Hermann – Dornacher 2017). There has been some discussion of a fully-fledged EU fiscal union, which would necessarily entail the end of national fiscal sovereignty (e.g. Bordo et al. 2013). But under the existing EU law, for both the Eurozone and non-Eurozone member states alike, fiscal sovereignty remains intact at the national level. However, in the Eurozone member states it is situated at the nexus of an even more precarious balance of institutional and market forces given the potential conflicts between national fiscal prerogatives and the exigencies of maintaining a currency union.

In his paper on the relationship between fiscal sovereignty and fiscal discipline, Kopits (2012) found that the best way for governments to maintain their fiscal sovereignty over the long-term is to bind themselves within a permanent rules-based fiscal framework and show commitment to it through transparency and consistency. Governments reliant on external financing that are not bound by clear and consistent rules are likely to see their fiscal sovereignty weakened over time as creditors become suspicious of the sovereign's creditworthiness, eventually forcing the state to appeal for emergency funding with externally imposed fiscal conditions attached (i.e. a breakdown in the state's capacity to determine its own budget, its fiscal sovereignty). Kopits identified four cases where states have lost their fiscal sovereignty altogether:

1) the Ottoman Empire's financial collapse in the early 1900s,
2) the League of Nations loan to Hungary in 1924,
3) the Indonesia IMF standby agreement in 1998, and
4) the EU-IMF bailouts of Greece in 2010 and 2012.

With reference to the Greek case, he emphasized the growing role of "disciplinarian" international bond markets in the modern era, in which bond prices respond almost in real time to fiscal policy decisions. However, it should be noted that this “disciplinarian” view of highly reactive modern international financial markets leaves essentially no room for discussion of market actors motivated by non-fundamental financial factors, including irrational “panic” effects and, more importantly for this study, uncertain institutional conditions. These effects may lead to a substantial upheaval in sovereign debt markets not directly stemming from changes in a country’s balance sheet or “commitment to a rules-based framework”, particularly during periods of crisis. Nonetheless, this short list of modern cases, in which national fiscal sovereignty fully broke down, supports three arguments about the nature of fiscal sovereignty: firstly, that instances of fully compromised fiscal sovereignty are fairly rare; secondly, that modern fiscal sovereignty exists largely at the mercy of international bond markets (regardless of any assumptions about market rationality); and thirdly, that a certain degree of national fiscal sovereignty is indeed held to have been generally preserved within the framework of the EU/Eurozone; the list does not include cases involving the EU members beyond that of Greece. This lack of effective control over national fiscal matters is reflected in the fact that, despite the EU’s introduction of a fiscal regulatory framework and enforcement mechanism in 1997 (EC 2018b), the EU lacked the authority to prevent several member states from sliding into unsustainable fiscal positions over the next decade, with Greece and several other Eurozone countries eventually falling into sovereign debt crisis.

The Stability and Growth Pact (SGP) came into full force in the EU in 1999 among all member states (and was agreed by countries that joined the Union thereafter), with the goal of preserving both general EU-wide economic stability and the Eurozone monetary union by establishing fiscal criteria for government debt-to-GDP ratios and deficit levels as a percentage of GDP, which were to be kept below 60% and 3%, respectively (EC 2017c). The SGP provided for the monitoring of national fiscal performance by both the European Commission and the Council and implemented a formal mechanism called the Excessive Deficit Procedure (EDP) for warning and, if necessary, eventually sanctioning repeated transgressors. However, in practice the SGP proved inadequate for keeping fiscal indicators within the intended parameters; member states might have agreed to its rules in principle but the Pact’s enforcement mechanisms were not enough to compel them to consistently abide by them (Buti et al. 2003).

Greece and Hungary ran the two highest deficits in the EU in 5 of the 10 years from 1999 to 2008; Hungary managed a 3.0% deficit in 2000 and debt below 60% of GDP in 2001 and 2002, but otherwise both countries exceeded both the SGP criteria every year. Greece maintained average sovereign debt around 110% of its GDP, with only Italy holding higher average debt over this period. Hungary’s average debt was substantially lower (65%); however, this was the highest level of debt observed among any of the new member states in every

*Table 1*

| Observation of SGP criteria, 1999–2008 (Expansion states counted prior to membership) | | | | | | |
|---|---|---|---|---|---|---|
| Year | Number of member states with deficit over 3% of GDP | Number of member states with debt over 60% of GDP | Greek deficit | Greek debt | Hungarian deficit | Hungarian debt |
| | | | as a % of GDP | | | |
| 1999 | 6 | 11 | 5.8 | 96.6 | 5.1 | 66.3 |
| 2000 | 6 | 9 | 4.1 | 111.1 | 3.0 | 60.5 |
| 2001 | 10 | 8 | 5.5 | 114.0 | 4.1 | 58.5 |
| 2002 | 9 | 8 | 6.0 | 114.5 | 8.8 | 59.5 |
| 2003 | 9 | 8 | 7.8 | 106.9 | 7.1 | 60.2 |
| 2004 | 9 | 9 | 8.8 | 111.4 | 6.5 | 63.6 |
| 2005 | 8 | 9 | 6.2 | 115.1 | 7.8 | 66.7 |
| 2006 | 6 | 8 | 6.0 | 115.2 | 9.3 | 70.3 |
| 2007 | 2 | 8 | 6.7 | 112.7 | 5.0 | 70.9 |
| 2008 | 10 | 10 | 10.2 | 117.4 | 3.7 | 74.5 |

*Source:* OECD.

single year. But roughly one-third of the EU members in violation of the SGP criteria at any given point over this period were not at all small relative to peripheral economies like Greece and Hungary; both criteria were violated by Germany and France in five out of nine years and by Italy in seven of them (OECD 2019). But, instead of being compelled to bring their budgets in line with the Pact, France and Germany agreed to place the SGP in abeyance in 2003, sidestepping their obligations to observe it. As a 2004 IMF report noted, in practice, "neither the preventive [i.e. surveillance] nor dissuasive (i.e. Excessive Deficit Procedure) procedures of the SGP proved enforceable" (IMF 2004: 83). In 2005, reforms were introduced in the European Council in hopes of improving coordination and speeding up implementation of EDP (EC 2005). While some progress was made on reducing deficits between 2005 and 2007, the same did not hold true with respect to sovereign debt, and all progress on either front was immediately erased with the beginning of the economic downturn in 2008. Under the SGP, the member states declared themselves to be bound by a set of "rules" *a la* Kopits, but, in practice, were largely able to manage their budgets as they saw fit. In other words, states both in- and outside of the Eurozone retained *de facto* exercise of national fiscal sovereignty, with a number of them theoretically jeopardizing it by risking exposure to "disciplinarian" forces on international bond markets.

And yet market discipline was slow in coming. While interest rates varied among the Eurozone members, the broad trend was toward Eurozone-wide convergence around low rates (Federal Reserve 2019). Likewise, rating agencies granted high credit ratings to the Eurozone member states, even to those economies like Greece with questionable underlying fiscal fundamentals. Howarth – Quaglia (2015) read this as evidence that markets were not fully convinced of the inviolability of the "*no-bailout clause*" and were in fact expecting a full bailout by the ECB should any of the Eurozone economies become insolvent. Any such assumptions were put to the test in the European sovereign debt crises beginning in 2009, most strongly so by the Greek case.

### 2.1. Case study – Greece

Despite the frequent conflation of the Greek sovereign debt crisis with the broader financial crisis beginning in 2008, Greece actually had minimal exposure to the toxic assets that were responsible for turmoil elsewhere. While the banking and liquidity crises in the global economy did play a role in the Greek descent into debt crisis, it was more directly attributable to weaknesses in the fundamentals of the Greek economy, and, especially, to fiscal imbalances than was the case in other countries, including Ireland and Spain (Mabbett – Schelkle 2015). The government violated the terms of SGP every year from 1999–2008, with deficits rising from four per cent of GDP in 1999 to peak at 10 per cent in 2008 and debt levels well in excess of the SGP limits (OECD 2019; World Bank 2019). The EU opened an Excessive Deficit Procedure against Greece in 2004 and then again in 2009, but failed to compel the government to cut its spending (EC 2017a). Greek debt grew rapidly after 2008, and by 2010 the government had virtually lost all access to funds in the sovereign debt market, with yields climbing above 20%. Greece's credit rating fell to junk status and speculation about a potential default spread to the rest of the Eurozone (de Santis et al. 2013).

Political turmoil also drove speculation about potential insolvency. The center-left PASOK party came to power in October 2009 amidst the deteriorating economic circumstances and revealed that the budget deficit in 2009 was higher than what the previous center-right New Democracy government had claimed. Though the real figure was seen by some as common knowledge before the new government took power, PASOK's efforts to blatantly discredit the previous government brought about an abrupt negative reaction on financial markets and on the part of other Eurozone governments (Visvizi 2012). The Greek government initially responded with calls for increased financial regulation to stop speculation rather than committing to address its structural fiscal problems. The economic reforms in the Greek Ministry of Finance's updated Hellenic Stability and Growth Program (SP10) involved reduction of the deficit to 3% by 2012 and a general reduction in government debt. In other words, it was little more than a redoubled commitment to observe the terms of the SGP. The move left markets and rating agencies unconvinced. Speculation about the effects of a possible default arguably grew beyond what was merited by economic fundamentals. Greece appeared to become trapped in the bad equilibrium described by Buiter – Rahbari (2012), in which high interest rates constrain a country's access to sovereign debt markets, making it all the more difficult for the country to finance its obligations and increasing the perceived risk of sovereign default, which in turn further drives up interest rates in a vicious circle. Greece became the subject of global media attention and criticism of its policy record. It also faced the Union's most serious speculation about a possible sovereign default and even full exit from the Eurozone, and as the government was rapidly shut out of the sovereign debt market it became clear that Greece would be forced to ask for external assistance if there was to be any chance of avoiding a default.

The European Council discussion of a rescue plan for Greece began in April of 2010, with Germany insisting that any funding would be contingent on Greece accepting conditional economic reforms. The Commission, acting as broker between Greece and the creditor governments, also insisted on fiscal reform through austerity measures (Bauer – Becker 2014). After some resistance to these conditions, the Greek government accepted them and in May the EC, ECB, and IMF accepted a €110 billion rescue package, with €30 billion coming from the IMF in the form of a standby agreement and the rest from a pool of funds collected from the other Eurozone states[3]. In accordance with the conditions of the agreement, fiscal consolidation involved increased VAT, real estate and luxury taxes, new taxes on fuel, cigarettes and alcohol, and levies placed on the remaining profitable firms (IMF 2010). Immediately effective cuts to public spending came in the forms of:

- pension reductions,
- cuts to bonuses, and
- a general sharp decrease in public investment (Matsaganis 2011).

Long-term commitments to broader structural adjustments involved:

- public administration reforms,
- labour market and wages reform[4],
- pension system reform,

[3] Except Slovakia.

[4] These reform packages included cuts to the minimum wage and measures reducing employers' costs associated with dismissing employees (Kentikelenis et al. 2016).

- health care system reform,
- business environment reform,
- reforms aimed at promoting investment and exports, as well as
- reforms aimed at increasing the levels of absorption of [EU-allotted] structural and cohesion funds (Visvizi 2012).

The agreement sparked popular unrest across Greece and left many citizens deeply sceptical of austerity, particularly given an increase in unemployment and the continued declines in wages, production and investment. The agreement clearly called for deep changes to Greek fiscal policy, but despite its scope and severity, investors were largely unconvinced that the agreed-upon funding and assurances of reform would be enough to stabilize the country. As bond yields continued to increase on secondary markets, the IMF assumption that Greece would be able to finance its own debt by 2012 became wholly untenable (Visvizi 2012). Germany and France applied strong pressure to the Greek government to demonstrate the country's commitment to prolonged economic austerity, and thereby curb speculation. As a result, new elections were held, replacing PASOK with a pro-austerity national unity government. The idea of a national referendum on Eurozone membership was dropped, and Greece reiterated its commitment to remaining in the currency union and to further economic restructuring (Schimmelfennig 2015).

In July of 2011, the IMF admitted that the initial adjustment program had failed to achieve several of its aims, citing the need for "refining the Fund's lending policy and framework to better accommodate the circumstances of monetary unions" and the unexpected depth of the Eurozone crisis, but defended its conditions and described the recession as unavoidable (IMF 2013: 2). The Fund found particular difficulty in translating "promises of conditional assistance from partner countries into formal program agreements" (IMF 2013: 2). In other words, the ambiguity of the commitments from other states proved a hurdle that slowed down the process of crisis management. These delays occurred very much at the expense of the Greek economy, which was embroiled in the effects of negative speculation about its fate for the duration of this process.

A new round of funding was eventually agreed in 2012, totalling €130 billion with an IMF contribution of €28 billion (BBC 2012). A new set of reforms was attached to the funding, with an emphasis on privatization and the sale of government assets rather than the more controversial areas of wage and benefit cuts. The second bailout package was also contingent on the acceptance of a partial sovereign default for holders of the Greek government debt. The vast majority (95.7%) of bondholders accepted the restructuring, reducing the debt obligations of the Greek state by approximately €100 billion in the *largest sovereign default* *in history* (Porzecanski 2013). Initially, the political turmoil within Greece led many observers to believe that their exit from the Eurozone was imminent, and as a result, markets remained tumultuous in the wake of the default, but by the end of 2012 (i.e. after the ECB declared its commitment to unlimited assistance) bond yields had fallen significantly (Zettelmeyer et al. 2013) and fears about a possible "Grexit" subsided.[5]

The fragile post-default equilibrium was tested with parliamentary elections and a national referendum on austerity in 2015, the results of which suggested widespread public dissatisfaction with Greece's ongoing structural adjustment program. The elections brought a coalition of left-wing Syriza and junior partner right-wing ANEL to power (Ministry of Interior 2015), both populist parties campaigning on anti-austerity platforms (Aslanidis – Kaltwasser 2016). The new government called a referendum polling the Greek electorate on whether it approved of the conditional bailout agreement. The referendum was condemned by the EC for jeopardizing European stability and cooperation, with EC President Jean-Claude Juncker openly and strongly encouraging Greeks to vote "Yes" to ensure that they remained in the EU (EC 2015). Regardless, the Greek electorate roundly expressed disapproval of the agreement; with the "No" vote winning a majority in every region of the country (Daly 2015). The results renewed fears of another Greek default and/or exit from the Eurozone, and 10-year bond yields spiked to 15% immediately after the referendum, their highest point since late 2012 (Bloomberg 2019). However, in the days following the referendum EU leaders were able to agree to the terms of a third bailout with the Syriza government through the European Council, effectively committing Greece to structural adjustment and continued membership in the Eurozone (Aslanidis – Kaltwasser 2016). As of early 2019, Greece retained debt close to 180% of GDP and saw GDP growth of 1.5% for 2017 and 1.9% for 2018. Bond yields have stabilized near 4.5%. However, aggregate Greek GDP in 2018 was just slightly over half of its peak in 2008, and recovery to pre-crisis levels of output at current growth rates would take decades (World Bank 2019b). In 2018, the Greek government agreed with the IMF to maintain an annual budget surplus of 3.5% through 2022 in exchange for an extension of repayment deadlines (Kahn – Brunsden 2018).

[5] *Editor's note*: "Grexit", a congenial portmanteau combining the English words "Greek" and "exit" was coined in February 2012. When the term was born, it was meant to convey the conclusion of cold-blooded market analysts who then put the chances of Greece leaving the eurozone at 50 per cent over the following 18 months (for more details, see *Financial Times*, 23 December 2012). In December 2016, this journal published a Special Issue under the title *Grexit-Brexit – The Future of European Integration*. From this collection of 9 papers on the Greek economy, see Mihalyi (2016), Csaba (2016) and Rosefield (2016).

**2.2. Case study – Hungary**

Like Greece, Hungary had long been at odds with the EU over its public finances prior to the sovereign debt crisis. It is unusual among the newer EU member states (NMS) for its very large state sector and high social spending (Benczes 2016), as well as its high level of sovereign debt. On the cusp of the crisis in 2007, it held public debt equivalent to 71.6% of GDP, less than Greece but well above the SGP criterion, and the highest among the NMS by a substantial margin (OECD 2019). Benczes attributed Hungary's weak fiscal position to strong public expectations of compensation for its economic losers after its transition from a planned economy (2011), and strong public support for maintaining the elements of the welfare system of the socialist era (2016). These factors made structural reform effectively impossible from a political standpoint in the years preceding its accession to the EU. Similar to the case in Greece, Hungary provoked the corrective arm of the SGP and spent 9 years (2004–2013) under the Excessive Deficit Procedure (EC 2017b), while failing to improve its fiscal position in the run-up to the financial crisis.

Hungary saw yields and debt levels spike after 2008, leading to the further deterioration of its already strained public finances. This was partly fuelled by speculation about a potential default, but was exacerbated by Hungary's position as a small, open economy dependent on foreign financing and markets (Nölke – Vliegenthart 2009**)**, making it highly vulnerable to turmoil in the Eurozone and the global economy (Johnson – Barnes 2015). In its report on the necessity of IMF intervention, the Fund noted that "with the decline in global liquidity and increase in risk aversion, financial markets in Hungary came under intense pressure, given Hungary's high debt levels and significant balance sheet mismatches. Several government bond auctions failed, liquidity in the secondary bond market dried up, and bond yields rose sharply" (IMF 2011: 2). The Hungarian forint was subject to speculative attacks and lost substantial value against the Euro, worsening Hungary's financial position (Csaba 2013a). The government was left nearly bankrupt and was forced to seek assistance.

In November of 2008, the Hungarian government negotiated a loan with the IMF of €12.3 billion, in combination with €6.5 billion in EU funding through the Balance of Payments Assistance fund and a further €1 billion from the World Bank (IMF 2008). The IMF took the lead in the Troika because of its experience with conditionality and ability to work much faster than the EU institutions (Bod 2010), though Hungarian policymakers were forced to respond simultaneously to the conflicting imperatives from all three institutions, a situation that inhibited the overall crisis management process. The ECB largely ignored the mounting crises in the countries outside of the Eurozone, in spite of the fact that Hungary was dominated by Eurozone-based banks, meaning a crisis there could have severe consequences within the currency union as well (Piroska 2017). The primary goals of the IMF were to push Hungary towards fast and substantial consolidation of its fiscal position to restore market confidence and liquidity support and recapitalization of its banks to prevent internal bankruptcy during the crisis. Much like Greece's initial bailout package, the IMF program envisioned a structural fiscal adjustment amounting to 2.5% of GDP, with broad reduction of government expenditure through a general scaling back of the large state sector and social transfers. The program also emphasized adherence to the EU's existing fiscal framework to ensure long-term commitment to a reduction in government spending (Kopits 2012). The EC focused on eliciting a commitment to austerity policy in order to improve the Hungarian fiscal position (Piroska 2017). Markets reacted positively to the news at first, but as it became clear that 2009 would be a year of much sharper economic contraction than initially expected both in Hungary and the broader global economy, Hungary was forced to ask the IMF for a waiver on its deficit commitments (IMF 2011).

Like Greece, Hungary was undergoing a period of internal turmoil, with the Socialist Party (MSZP) government of Prime Minister Ferenc Gyurcsány resigning in April 2009, and the Fidesz party coming to power in May 2010, partly on a campaign of criticism of the previous government's fiscal profligacy. After the Fidesz takeover, the fiscal framework agreed to "agreed in the previous year" the year prior was largely ignored. Hence, Hungary sent mixed signals to global markets as to its budgetary discipline. It scrapped previously considered structural reform measures but imposed new taxes, though ultimately the government deficit remained at 4.5% of GDP for 2010, the same value as the previous year. Bond yields increased and the government's debt was downgraded (Kopits 2012). In its review of the loan's effectiveness, the IMF noted that "although the program was able to deliver a considerable fiscal adjustment, much of the structural fiscal adjustment has since been reversed" (IMF 2011: 3). Hungarian prime minister Viktor Orbán's government was openly critical of the IMF and its programs and employed a mix of unorthodox fiscal policies, including taxes targeting foreign banks, that have been characterized as "financial nationalism" (Johnson – Barnes 2015). In June of 2010, the Fidesz government "expelled" the IMF from Hungary and suspended the consultations on the Stand-By Agreement, with Prime Minister Orbán justifying the decision as a matter of preserving national sovereignty (Szakács –Than 2010).

With the withdrawal of external support and the deterioration of the Greek situation, speculation about weaknesses on the European periphery mounted and Hungary saw its position worsen as a result of capital flight and currency devaluation. The government agreed to new negotiations with the IMF in November of 2011, calming investors despite the lack of a coherent stabilization strategy. The negotiations were delayed until summer of 2012 due to disputes about the government's respect for central bank independence, and no further funds were ever actually transferred to Hungary through this program (EC 2018a). Over the next several months this became somewhat irrelevant, as Hungarian bond yields dropped significantly, trading at yields below those of many Eurozone countries (Csaba 2013a), meaning that (*after* the replenishment of the central bank's reserves with the IMF and EU money) Hungary was once again able to finance itself without external assistance.

This outcome contradicted the market-discipline hypothesis, as Hungary was able to sell bonds at relatively low interest rates despite its inconsistent and unorthodox policy measures during the crisis period (Howarth – Quaglia 2015). With a series of successful bond sales, the incentive to seek emergency financing diminished, and the IMF withdrew from negotiations in July of 2012, with Hungary capable of fulfilling its own needs despite continued breakdowns elsewhere in the EU. After 2012, HUF began to recover from the devaluation it had undergone beginning in 2008 (Mabbett – Schelkle 2015). The Hungarian balance sheets continued to improve, with debt-to-GDP and deficit levels falling below the EU averages. In 2013, the EU withdrew its Excessive Debt Procedure against Hungary (EC 2014b) and the government repaid its remaining debt to the IMF (Johnson – Barnes 2015). Initially economic growth was modest but fairly consistent, with GDP recovering to 100% of the pre-crisis level. Despite the ECB's pledge of unlimited support for the Eurozone, as of early 2019 Hungarian bonds continued to trade below their Greek counterparts. The alienation of investors, foreign banks, and the IMF itself stemming from the government's unorthodox approach to crisis management may well incur significant costs to the Hungarian economy in the years and decades ahead, but for the time being the economic outlook in Hungary remains decidedly brighter than that in Greece.

While the core fiscal problems precipitating crisis in Greece and Hungary (debt, deficits, overdue structural reforms) differed only by a limited degree, and both countries were experiencing similar dynamics in their domestic politics, the crisis management processes had dramatically different results. Greece ultimately agreed to external demands for commitment to a long-term program of conditional funding, undeniably giving up its fiscal sovereignty in the process. Hungary managed to retain its fiscal sovereignty, operating with relative disregard for the IMF's conditions and employing unorthodox fiscal policy. Part of the success of the Hungarian package and failure of the initial Greek one was the relative speed and efficiency with which an IMF-led program could operate in comparison to an EU-led one. Hungary has essentially re-stabilized despite receiving only a fraction of the funding Greece did, while it remains unclear in Athens how and when Greece will ever regain its economic vitality. This is generally consistent with Mabbett – Schelkle's finding in their own comparison of the crises in Greece and Hungary (along with Latvia's): "... being out of the Euro did not prevent economic decline, but it did allow countries to recover" (2015: 512). The costs to the Hungarian economy and its business environment associated with its unorthodox approach, such as they may be, will only be fully realized over the long-term. The next section turns to different institutional mechanisms responsible for how the crises were managed.

## 3. KEY CRISIS MANAGEMENT INSTITUTIONS

### 3.1. European stability mechanism

In October 2012, the treaty establishing the European Stability Mechanism (ESM) was ratified by 17 states of the Eurozone, creating a "permanent crisis resolution mechanism", with a lending capacity of €500 billion (ESM 2017). The Mechanism is governed by international rather than EU law. It is authorized to perform the same loan and market operations as the earlier, temporary European Financial Stability Fund (EFSF), and was created to replace it. After the transfer of the EFSF's assets, the ESM managed over €750 billion (Csaba 2013b), and as of late 2018 had available capital of approximately €700 billion. The ESM is managed by a Board of Governors, consisting of the various Eurozone members' ministers of finance. Decisions are taken on the basis of qualified majority (an 80% threshold), with votes weighted according to the contributions of each Governor's member state. It has no direct accountability to other EU institutions or national bodies.

The ESM has faced criticism for both its operational structure and its relationship with national authority. Christova's analysis notes the lack of any automatic mechanism for partial waivers of debt obligations (2011). This implies that any sort of partial waiver of obligations (like the one seen in Greece in 2012) would have to be negotiated on a case-by-case basis, which of course risks a prolonged period of market turmoil drawing more countries into possible default. Moreover, the ESM is limited in its capacity to alleviate the core problem of massive debt burdens through extending further credit to insolvent states, and indeed risks creating a cycle of rising debt levels and deepening dependency on external assistance (ibid). It has also been noted that the institutional design of the ESM is essentially a product of undesirable path-dependent outcomes; while the EFSF proved itself a sub-optimal force for dealing with a debt crisis much worse than initially expected, its institutional design was essentially copied for the ESM because of the immense political costs of debating and gathering consensus for any alternative (Gocaj – Meunier 2013), costs which still hang over any effort at significant reform today. Lastly, the ESM's budget limit is about four times larger than the total annual operating budget of the EU (ESM 2017). This fact, combined with the right of the ESM to capitalize private banks, implies a massive transfer of financial authority from the national to the supranational level (Csaba 2013b). It should also be noted that the Mechanism has allowed the EC to substantially expand the scope of its influence over national fiscal policy by acting as a negotiator between creditor and debtor governments, a more significant role than the monitoring and limited sanctions capabilities it was vested with through the Stability and Growth Pact (Bauer – Becker 2014).

### 3.2. European Central Bank (ECB)

The other key EU crisis management institution is the ECB. Initially reluctant to make an official statement on the extent of its commitments to the Eurozone member states' solvency, but as the financial and fiscal situation across the monetary union deteriorated, the ECB eventually issued a declaration in September of 2012 that it would indeed provide the Eurozone states with (conditionally) unlimited support in the form of "Outright Monetary Transactions" (OMT), essentially purchases of government debt in secondary bond markets (ECB 2012a). This declaration has not been accompanied by any amendment to the Bank's Statute nor any relevant piece of the EU legislation, and in 2012 the German Constitutional Court challenged its legal basis, with the European Court of Justice eventually making a final 2015 ruling that the OMT program was, in fact, legal under EU law (Court of Justice 2015), and the German Constitutional Court finally accepted the program as legal under German constitutional law in 2016 (Payandeh 2017).

The ECB's declaration of unlimited support to the Eurozone without any accompanying push for legislation gradually calmed markets while avoiding some of the public debate likely to arise out of a formal legislative initiative, debate that might have stoked a new round of speculation at the time. The Bank's approach has nevertheless exposed it to criticism. The guarantee of support for the Euro effectively implies a second core mandate for the ECB, one which has the potential to directly conflict with its original, foundational mandate of price stability. Weber – Forschner see an acute need to clarify this ambiguity if institutional legitimacy is to be maintained in the Eurozone, arguing that "the ECB cannot simply expand its own mandate; this requires a stipulation by law through an amendment of the Treaty… otherwise, democratic legitimacy as a main trait of the 'European idea' is lost" (2014: 50). In the absence of a clear national endorsement of unlimited support across various Eurozone governments, the ECB is charting a new course while ignoring the commitment to credit it ultimately implies for every state in the currency union. It is clear that this is not only a threat to the democratic legitimacy of the EU, but also to the foundational premise that it is an order legitimated by international legal agreement among sovereign nations, a necessity in any coherent shared sovereignty regime. It is at this point ambiguous as to the extent the ECB would be able to actually rely on OMTs as a crisis management tool without fomenting a major clash over fiscal sovereignty and a general crisis of EU-institutional legitimacy.

### 3.3. The IMF and key differences among the institutions

The ECB is a central bank, and the IMF and ESM are international financial institutions, but to some extent their functions have overlapped in their efforts at resolving the European financial crises. While they are all potential agents of crisis management and can now all provide funds in some form to the troubled Eurozone governments lacking other sources of financing, they are working with different mandates and resources. Their differences help to reveal that it is the structure of the EU institutions and their tools rather than international sovereign debt financing in itself that have jeopardized national fiscal sovereignty.

Firstly, the IMF works from a defined pool of assets. It cannot lend more than it collects from its members and cannot collect funds beyond the contribution quotas that every state agrees to upon joining the Fund. Like the IMF, the ESM is able to issue loans to troubled governments, though it can also directly buy bonds in primary and secondary markets (ESM 2017). And like the IMF, the ESM also works from a defined pool of assets and is thereby limited in its potential for action by the will of national governments. On the other hand, as a central bank the ECB can issue Euros and is now also ostensibly committed to unlimited support for troubled Eurozone members, meaning it can potentially take steps towards maintaining the currency union that may undermine its original mandate of maintaining low inflation. The change in its status that this commitment implies constitutes both a significant deepening of Eurozone economic integration and a substantial transfer of power and competencies from the national to the supranational level. Unlike the other two entities, the ECB's pool of resources does not have a clearly-defined limit. Obviously, the ECB is practically limited by inflation risk, but this does not create absolute boundaries within which it can operate.

The second key difference between the institutions lies in how they are governed. The IMF relies on a cooperative model with proportional voting with the member states allowing votes based on contributions, and thus "cannot, in broad terms and over a sustained period, pursue policies which the members do not generally approve" (Mussa – Savastano 2000: 84); otherwise members will withdraw from the Fund's programs (as was the case in Hungary in 2011), or possibly withdraw from the Fund altogether. The ESM is structured around proportional financial contribution from the various EU members, but each country is nominally equally represented by their nationally-appointed seat on the Board of Governors, with "the granting of financial assistance; the terms and conditions of financial assistance; the lending capacity of the ESM; and changes to the menu of instruments" all proceeding on the basis of "mutual agreement" (ESM 2011). But it has been noted that the ESM has tended towards domination by a few large member states, particularly Germany, with small states having little say in the direction of policy and no practical possibility of withdrawing from the Mechanism (Schimmelfennig 2015). Nonetheless, both of these institutions do retain a certain connection to the national governments of their constituent member states and operate in an intergovernmental setting. On the other hand, the ECB is at its core a self-governing supranational institution. The European Council elects the six-member Executive Board, but the Eurozone member states are not proportionately represented nor are representatives expected to pursue their own nation's particular interests.

Lastly, there is a difference in the nature of the foundational agreements underlying the various entities in terms of their implications for sovereignty within Krasner's framework. The IMF is based on international legal sovereignty; by accepting its Articles of Agreement and paying in their quota, a state presumes it will enhance its economic wellbeing and by extension capacity for exercising domestic sovereignty. Likewise, when a state enters into a program with the Fund, it negotiates the terms of the agreement and rejects them if it is unsatisfied without withdrawing from the Fund altogether. In both cases, sovereignty is exercised *via* international agreement. Fiscal policy may be substantially shaped by IMF conditionality, but only when an agreement has been reached in the first place. The ESM is also grounded in international agreement among representatives of the contributing states and was approved by their national parliaments. However, the lack of further accountability to elected parliaments, domination by a few large countries and severe, unpredictable costs associated with withdrawing from the Mechanism mean that there is significant leeway for the ESM to effectively ignore member states, including small states' national fiscal sovereignty. This is especially true given the absence of any kind of guiding, legitimating intergovernmental agreement on the ESM's expanded role. Despite the intergovernmental character of its origins, it is ultimately an institution run by insulated and nationally unaccountable executives, with the unilateral right to further expand its own lending capacity, in addition to making decisions about to whom and under what conditions making loans. Its massive balance sheet constitutes a major shift in the effective distribution of financial authority from the national to the EU-level. The EU member state governments potentially risk their own solvency, and thus, fiscal sovereignty through loans, the terms of which they may have little or no effective control over.

Finally, the unequivocally supranational ECB has moved away from the role envisioned in the Maastricht treaty and substantially expanded its mandate without any legitimating agreement. The fact that the ECB has committed itself to buying sovereign debt in secondary markets to bring down interest rates for the troubled governments, taken over as supervisor for the Eurozone's core banks, and given a guarantee to provide potentially unlimited support to governments to preserve the currency union have led to serious doubts about whether it can still be called an independent institution (Weber – Forschner 2014), specifically that aspect of institutional independence associated with having distinct preferences from those of its principles (*i.e*. the member states) and a position of neutrality with respect to the interests of other political actors (Haftel – Thompson 2006). The new ECB mandate of unlimited support is difficult to reconcile with the original one of price stability, and it is unclear which mandate will receive priority should they come into conflict and what exactly conditionally unlimited support will mean for troubled economies in the future. The ECB and its operations potentially risk losing much of the legitimating force of international legal agreement that an institution like the IMF has. Shared sovereignty cannot be extended to situations in which the legitimacy of the international agreement is in question. While all Eurozone members did agree to the founding of the Bank in the Maastricht Treaty, it is becoming unclear how much more change, if any, the Bank can make before these agreements are essentially rendered irrelevant. The ECB has empowered itself in such a way that potentially alters the fundamental nature of fiscal authority for countries across the Eurozone.

The Hungarian case in this study serves to illustrate that there are real differences in crisis management conditions inside and outside of the Eurozone with respect to fiscal sovereignty, and that fiscal sovereignty is not rigidly bounded by market reactions as implied by Kopits' "disciplinary market" framework. It also shows that the IMF is still very much constrained by the necessity of international legal agreements. It cannot force its conditions on debtor states unable or unwilling to meet them. While Hungary agreed to structural reforms and austerity early on, the unexpected severity of the crisis meant that the IMF had to remain flexible in its expectations for 2009, allowing the Hungarian deficit to expand without seeking countermeasures. After the Fidesz government came to power in 2010, the agreed fiscal framework was largely ignored. This did produce short-term negative consequences in terms of Hungary's bond yields, credit rating and the exchange rate, but the government was not institutionally constrained from exercising its authority. The "disciplinary" force of global markets did not result in a major policy reversal nor was the government ultimately compelled to seek further external emergency funding. After some time, Hungary has managed to move towards what is for now a more sustainable fiscal position through its own measures, independent of the IMF, and has furthermore been more compliant with the EU SGP-criteria than in the years prior to the crisis. Significant economic costs may be incurred over the long-term as a result of these unorthodox policy measures, but it is clear that, on the basis of this case study, it cannot be argued that there is an inherent compromise of national fiscal sovereignty bound up with membership in or agreements with the IMF. Furthermore, the case illustrates that even a sustained program of fiscal actions evincing the lack of a "rules-based framework" is not necessarily met with a breakdown in fiscal sovereignty. Whereas fiscal sovereignty did break down in the Greek case, it appears that it was not the mechanism of emergency conditional agreements with external creditors in themselves that led to the eventual stripping of fiscal authority from the Greek national government, but rather the prolonged ambiguity about the institutional management of the situation and the EU's authority to override the Greek domestic political preferences. The final section of the study discusses the tensions between the EU institutional crisis management framework and national fiscal sovereignty in the Eurozone.

## 4. FISCAL SOVEREIGNTY UNDER CRISIS MANAGEMENT AND THE DILEMMA OF A SECOND CRISIS

"Economic governance" has been substantially expanded in the EU since 2008[6], and since then the Eurozone has been more compliant with deficit criteria than in the period leading up to 2008. Bond yields have both fallen and tended towards convergence with the German rates, and by 2017, even the troubled Greek economy had begun the gradual process of recovery. However, a second debt crisis remains a strong possibility for the Eurozone. Overall debt levels remain high across the Union and growth sufficient to meaningfully change this remains a distant prospect. Substantial differentials with the German bund persist in a number of member states as of early 2019, particularly in Greece, Portugal and, most significantly, Italy. These differentials indicate that default risk remains

[6] E.g. the 2011 "six-pack" reforms, the 2012 Treaty on Stability, Coordination and Governance, and the 2013 "two-pack" legislation.

unevenly distributed, suggesting investors do not view the ECB's commitment to "unlimited support" as a definitive guarantee of solvency. If investors again become panicked about a potential default in a Eurozone country and external financial assistance becomes necessary, the EU will be placed in a difficult position. The IMF alone may not be able to provide enough resources to overcome a debt crisis comparable to the last one (particularly if it involves a larger economy than Greece), meaning that the ECB and ESM will have to either coordinate a response or act alone to stabilize the economy. The ECB could rely on OMTs to relieve debt markets, and/or the ESM could be used to provide liquidity and capital support. Both crisis management tools have powerful implications for national fiscal sovereignty in the currency union.

Action by the ECB in the form of OMTs could manage to prevent another protracted debt crisis if markets reacted well. As an independent institution, the ECB could potentially act fairly quickly to suppress an impending crisis in one country before it spread to others. Assuming whatever conditions the Bank expected of the beneficiary state could be negotiated expediently, OMTs might prove a far more effective tool for preventing full-scale crisis than inter-governmentally negotiated structural adjustment programs. However, the very essence of the ECB's potential capacity to act expediently to head off a potential crisis lies in its insulated, supranational character, and specifically its capacity to act without first reaching a consensus among the Eurozone members. While many of them might agree in principle to the idea of empowering a technocratic and efficient institution in order to resolve crises rapidly, another protracted crisis with the ECB at its center, buying up debt from multiple Eurozone members with varying degrees of historical commitment to the EU's fiscal framework, has the potential to substantially reshape the position of fiscal sovereignty across the Eurozone, not to mention to provoke a major backlash on the part of national governments**.** Without the backing of a new EU Treaty to legitimize the ECB's commitments and to at least give some voice to national perspectives on how adherence to the EU fiscal criteria will factor into the OMT program, the newly empowered, dual-mandate ECB cannot be said to be based on a coherent international agreement, and is thus totally incompatible with Krasner's shared sovereignty framework.

Alternatively, the EU could follow the precedent of the Greek case and rely on intergovernmental negotiations for external funding through the ESM, which is essentially structured like the European Council, satisfying the requirements for preserving international legal agreement. But as the Greek case makes clear, it is difficult or impossible for negotiations like this to proceed rapidly enough to effectively contain a crisis. The inability of the EU to reach a quick decision deepened market destabilization and meant that by the time the first package of funding was agreed to, it was totally insufficient to serve its purpose. It took two more years for a second package to be negotiated, by which point the Greek economy had deteriorated much further, necessitating an even deeper commitment to budget-tightening reform against strong national backlash and ultimately leading to a total breakdown in the country's fiscal sovereignty, as well as devastating economic losses in Greece and across the Union. Were an even larger economy than Greece to go through a similar, extreme scenario, the process of negotiating an adequate funding package would be more politically difficult and the aggregate economic losses stemming from a slow response even more severe. The Greek case illustrates the enormous potential downside to waiting to begin intergovernmental crisis management negotiations only after the need for external intervention had become fully apparent. Thus, the ESM seems caught between intergovernmental negotiation but operating far too slowly to be an effective crisis management tool, or working on the basis of a "mutual agreement" in only a nominal sense and being effectively dominated by one or at most a few large countries in the name of expediency. The incentives for avoiding the former are obvious given the outcomes in Greece, but the consequences of the latter quite incompatible with maintaining an intergovernmental, legitimate institution, as well as the long-term preservation of national fiscal sovereignty in the EU.

Some might consider it useful to have the threat of a fate similar to Greece's hanging over would-be profligate Eurozone members; the unenviable situation there has perhaps done more to "bind" the other economies in "rules-based frameworks" than any piece of formal legislation. But this hardly serves as a guarantee that the Eurozone has permanently insulated itself from the possibility of another crisis along the lines of the previous one. While the EU would have some new tools with which to confront it, the results of this institutional analysis suggest that in the event of another major crisis the Eurozone will face an inevitable dilemma for national fiscal sovereignty. Either the ECB must step outside of its original role and be relied on to calm markets despite lacking a clear political mandate to do so from national governments, or an intergovernmental solution must be reached through the ESM, most likely either too slowly to effectively stabilize the troubled economy or too quickly to allow for a genuinely intergovernmental process. The first scenario appears politically unacceptable and the second economically perilous, and both potentially massively controversial and polarizing. Even a shrewd combination of ECB and ESM efforts would likely do little to avoid the basic dilemma. Without a clear agreement on the respective roles of OMTs and the ESM, national fiscal sovereignty will remain caught between two powerful but flawed institutions of crisis management, the use of either of which will have critical implications for the national authority of the currency union's member states as well as the future direction of their economies. The pact on which the EU rests, shared sovereignty legitimated by international agreement, would become an increasingly nominal one, as would fiscal sovereignty as a retained national competence.

## 5. CONCLUSION

The institutions of the EU derive their legitimacy from the international agreements that establish them. This is the essential basis of the EU's shared sovereignty arrangement with the national governments of the individual member states. While the Eurozone countries have unambiguously given up control over monetary policy in joining the currency union, in principle fiscal sovereignty remains an essentially national competence. The case studies in this article show that despite their similarly problematic fiscal positions and internal political dynamics, over the course of the financial crisis fiscal sovereignty was preserved in Hungary though it broke down in Greece. This study concludes that this was at least partly due to the prevailing crisis management institutional conditions within the Eurozone rather than being a pure function of Greece's economic fundamentals. Ambiguity about the extent, expedience and overall efficacy of the EU's response in Greece relative to the IMF-led efforts in Hungary led to a much more protracted crisis in the case of Greece and much more severe economic fallout. Furthermore, the Hungarian case suggests that fiscal sovereignty is not fundamentally incompatible with conditional external financial assistance where it is predicated on international legal agreement.

The ECB's 2012 commitment to "unlimited support" for the troubled Eurozone economies did much to calm markets and bring stability to Greece and the currency union as a whole, but current debt markets suggest that default risk remains unevenly distributed, and the prevalence of structural economic weaknesses and high levels of sovereign debt in many member states suggest that a second major financial crisis remains a significant risk for the Eurozone. Relying on either or both of the two major crisis management institutions creates a major dilemma for the condition of national fiscal sovereignty across the Eurozone, one that exposes the EU to backlash from national governments invoking their control over domestic fiscal policy. The ECB's new commitment to unlimited support lacks the legitimacy of intergovernmental endorsement and has clear potential to conflict with its foundational mandate of price stability. On the other hand, financial assistance packages negotiated through the ESM are likely to come too slowly to achieve their basic purpose if a genuinely intergovernmental consensus-based approach is taken, but allowing one or a few large countries to dominate the process risks forcing small countries to take on financial commitments without effective control over their terms, a clear jeopardization of their fiscal sovereignty, and more broadly, the political legitimacy of the ESM and the currency union. The outcomes of the Greek case, a breakdown in national fiscal sovereignty coupled with devastating economic losses, must ultimately serve as a case study in the crisis management outcome best avoided rather than as a guiding precedent for the handling of future crises.

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