How durable is the impact of the European debt crisis on attitudes on national and EU democracy and governance? A closing gap.

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Abstract

Studies find that the European debt crisis and the austerity policies forced upon deficit countries by the EU and the IMF affected citizens' attitudes on democracy and governance. The conditionality imposed upon peripheral Eurozone countries (Portugal, Italy, Ireland, Cyprus, Greece and Spain) reduced institutional trust at both the national and EU levels, creating a trust gap between conditionality and no-conditionality countries. This letter uses a difference-in-difference event study design to investigate whether this gap is permanent or whether it fades away over time. Findings suggest that attitudes on national and EU democracy and governance worsened in 2010 after the European debt crisis in conditionality countries as opposed to other EU countries. However, this gap started to reduce in 2014, and was eventually closed in 2017.

Keywords: Institutional trust; democracy, governance; European debt crisis; conditionality; event study

Introduction

There is abundant evidence on the effects of economic crises on citizens' support for democratic institutions. When people are discontented about economic performance, as is the case during recessions, institutional trust declines (Dustmann et al. 2017; Funke et al. 2016; Stevenson and Wolfers 2011). In the context of the European debt crisis, several studies provide evidence that when the Troika (the European Commission, the European Central Bank, and the International Monetary Fund - IMF) pressured national governments to deviate from the policy demands of voters, it eroded trust in the political establishment and increased support for populist outsiders (Armingeon and Guthmann 2014; Armingeon et al. 2016; Magistro et al. 2021), especially so among less economically well-off individuals (Dotti Sani and Magistro 2016). However, there is less work on how persistent these declines in trust are. Are these falls in trust permanent or do they fade away? After the onset of the European debt crisis in 2009, the deficit countries of the Eurozone periphery[1], which I call the "conditionality group", experienced a steep loss of confidence in democratic national and European institutions as a result of the external adjustment programs imposed on them by the European Union (EU) and the IMF, compared to countries in the EU that did not undergo such external pressure. This finding has been considered a cause of serious concern and a big threat to democracy (Armingeon et al. 2016; Dotti Sani and Magistro 2016). This is especially relevant since we know that economic grievances can encourage populist vote choice when established political parties are unresponsive to citizens' policy demands, especially for those groups with the largest grievances (Dustmann et al. 2017; Hobolt and Tilley 2016; Magistro et al. 2021).

In this short article I use a difference-in-difference event study design to evaluate the heterogeneous treatment effect of EU/IMF conditionality by year, and to establish whether and when the treatment effect fades away. Findings suggest that indeed, in the aftermath of the European debt crisis, attitudes towards national and EU democracy and governance worsened more significantly in countries under EU/IMF conditionality. However, starting in 2013, the effect of the economic adjustment programs started to reduce slightly, only to fade away around 2017, as the gap between no-conditionality and conditionality EU countries disappeared.

Attitudes on National and EU Democracy and Governance in the Aftermath of the European Debt Crisis

Starting in late 2009 the European Union was hit by a sovereign debt crisis, which was the result of a mix of factors, including a credit-fueled boom, competitiveness differences, and fiscal misbehavior. The periphery of the Eurozone (Portugal, Italy, Ireland, Cyprus, Greece, and Spain), which I define as the "conditionality group", was hit particularly hard, and its governments had to enter formal or informal agreements with the EU and the IMF to pass austerity measures and structural reforms in exchange for bailouts[2]. Regardless of which governments were in power in these countries or the promises they were elected on, these agreements severely limited their policy options. Conversely, Eurozone countries with more competitive economies had more autonomy on which fiscal measures to adopt, while those outside of the Eurozone bloc had access to more macroeconomic policy instruments to respond

[1] Namely Portugal, Italy, Ireland, Greece, Cyprus, and Spain.
[2] While Italy never entered into an official agreement with the Troika, see Sacchi (2015) on the implicit conditionality that Spain and Italy were subject to in 2011.

to the crisis. For this reason, as opposed to people in no-conditionality countries, citizens of conditionality countries are more likely to blame both EU institutions, for imposing economic adjustment programs on them with weak democratic legitimacy, as well as national institutions, for ceding their sovereignty to supranational institutions (Armingeon et al 2016). While it has been well-documented that countries in the periphery of the Eurozone experienced steeper declines in institutional trust (Armingeon et al 2016; Armingeon and Guthmann 2014; Dotti Sani and Magistro, 2016), it is not clear how durable this fall in trust is, and whether the gap in trust between conditionality and no-conditionality countries eventually closes.

Data

The guiding question of this article is: how durable are the effects of the European debt crisis and the austerity policies forced upon deficit countries by the EU and the IMF towards attitudes on national and EU democracy and governance? I use the 36 waves of the Standard Eurobarometer survey– biannually from 2002 to 2019 – and include 28 European Union countries, consisting of a total of 737,442 observations. Furthermore, to validate my findings, in the online appendix I provide the results of the same models ran using a different dataset, the European Social Survey, consisting of 9 waves - from 2002 to 2018 – and including 24 European Union countries, for a total of 332,315 observations.

In order to measure attitudes on democracy and governance at the national and EU levels, I use a series of variables that have been available biannually since 2002 from the Standard Eurobarometer survey and that tap into citizens' perceptions of democratic institutions. The first concept I intend to measure is attitudes on national democracy and governance. The three variables available in all waves that come closest to measuring this concept are trust in the national government, trust in the national parliament, and satisfaction with the way democracy works in one's country. To tap into attitudes towards EU democracy and governance I use trust in the EU and satisfaction with the way democracy works in the EU. Trust in the national government and parliament and trust in the EU are binary variables taking value 0 if the person tends not to trust the institution in question and 1 if they tend to trust it. Satisfaction with national and EU democracy are ordinal variables taking discrete values from 1 – very satisfied, to 4 – not at all satisfied. I transform them into binary variables for ease of analysis with the trust variables. This means that they take value 1 for people who are either very or fairly satisfied with democracy and 0 otherwise. Finally, to conduct the analyses, I build two distinct indexes. The first index, measuring attitudes to national democracy and governance, takes the average of the individual answers to the questions on trust in the national parliament, trust in the national government and satisfaction with the way democracy works in one's country. The second index, measuring attitudes to EU democracy and governance, takes the average of the individual answers to the questions on trust in the EU and satisfaction with the way democracy works in the EU. The composite indices also range from 0 to 1, with 1 signifying a higher support for institutions.

The treatment variable, the conditionality group, includes countries that underwent EU/IMF conditionality as a result of the European debt crisis starting in late 2009, namely Portugal, Italy, Ireland, Cyprus, Greece, and Spain. The countries that never experienced Troika conditionality as a result of the crisis exist as a control (no-conditionality group)[3].

[3] To be clear, austerity policies were also passed in many countries outside of the Eurozone, however, the clear difference here is choice: those countries were not forced into economic adjustment programs by external actors

I also include some socio-demographic control variables: education (age at which the individual finished education), female (1 for female and 0 for male), and age. Since I am concerned that the European debt crisis and the response to it affected economic variables such as employment status, GDP growth, and one individual's subjective economic situation, I do not control for these variables, as this would likely lead to post-treatment bias (Gelman and Hill 2007, p.188-192). Finally, I apply post-stratification weights in all of the models and I cluster all of my standard errors by country.

Model

I use a difference-in-difference (DID) event study design to evaluate the treatment effect of EU/IMF conditionality. I use a dynamic specification, which allows for non-parametric changes in the treatment effect over time (Cunningham 2021; Sun and Abraham 2020). Since I am particularly interested in seeing heterogenous treatment effects by year, and whether and when the treatment effect fades away, I include leads and lags of the treatment variable, instead of using a single binary indicator variable.

The model follows this form:

$$Y_{ist} = \alpha_s + \alpha_t + \beta_1 Treat_s \times Years\ to\ Treat_{st} + \beta_2 X_{ist} + \varepsilon_{ist}$$

I fit a model based on the above equation for individual i in country group s, in year t. Y_{ist} is the outcome variable - attitudes on democracy and governance - α_s and α_t are unit (a dummy for conditionality country group) and year fixed effects, X_{ist} is a vector of controls. $Treat_s$ is a dummy variable that indicates whether a country is ever treated with EU/IMF conditionality, and $Years\ to\ Treat_{st}$ is a set of dummy indicators of the number of years until (or since) the country underwent EU/IMF conditionality (from period – 7 to 10, where the -1 time lag is used as the dropped reference, and period 0, when the treatment starts, is 2009). Full regression tables and figures of the predicted values of attitudes on national and EU democracy and governance are provided in the online appendix. In the next section I discuss the estimates of the DID event study model, as shown in Figures 1 and 2.

Findings

The estimates in Figure 1 (β_1 from equation 1) represent the marginal effect of being in a country that has undergone (or will have undergone) EU/IMF conditionality in a given year, relative to a year prior to the European debt crisis started – 2008 - the last year for which conditionality should have no effect on attitudes towards democracy and governance, if the parallel trends assumption holds. Figure 1 shows that the control and treated groups are statistically the same before treatment: prior to the debt crisis and to the conditionality that ensued, there is a zero effect of the crisis and conditionality. This supports the parallel trend assumption in DID estimation. Substantively, this means that before the European debt crisis and the EU-IMF conditionality that ensued, attitudes on national democracy and governance were similar between conditionality and no-conditionality countries. However, after the crisis started

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(Armingeon et al. 2016). Furthermore, they had other policy instruments available, including currency devaluation/depreciation.

in late 2009 a gap in institutional trust emerged. This gap started to slightly reduce in 2014, but only disappeared in 2017 (although barely so – as the coefficient is very close to conventional statistical significance), 8 years after the onset of the European debt crisis. Figure 2 shows a similar story for attitudes on EU democracy and governance, with one key difference. Trust in the EU and satisfaction with EU democracy were actually higher in conditionality countries than in no-conditionality countries before the European debt crisis. Then after the crisis, a gap between the two emerged, as attitudes on EU democracy and governance worsened significantly more for conditionality countries. In a similar way as for national institutions, this gap started to close in 2014, only to disappear in 2017. As of 2019, there was no sign of this gap to start widening again, although we yet have to see whether COVID-19 may change this.

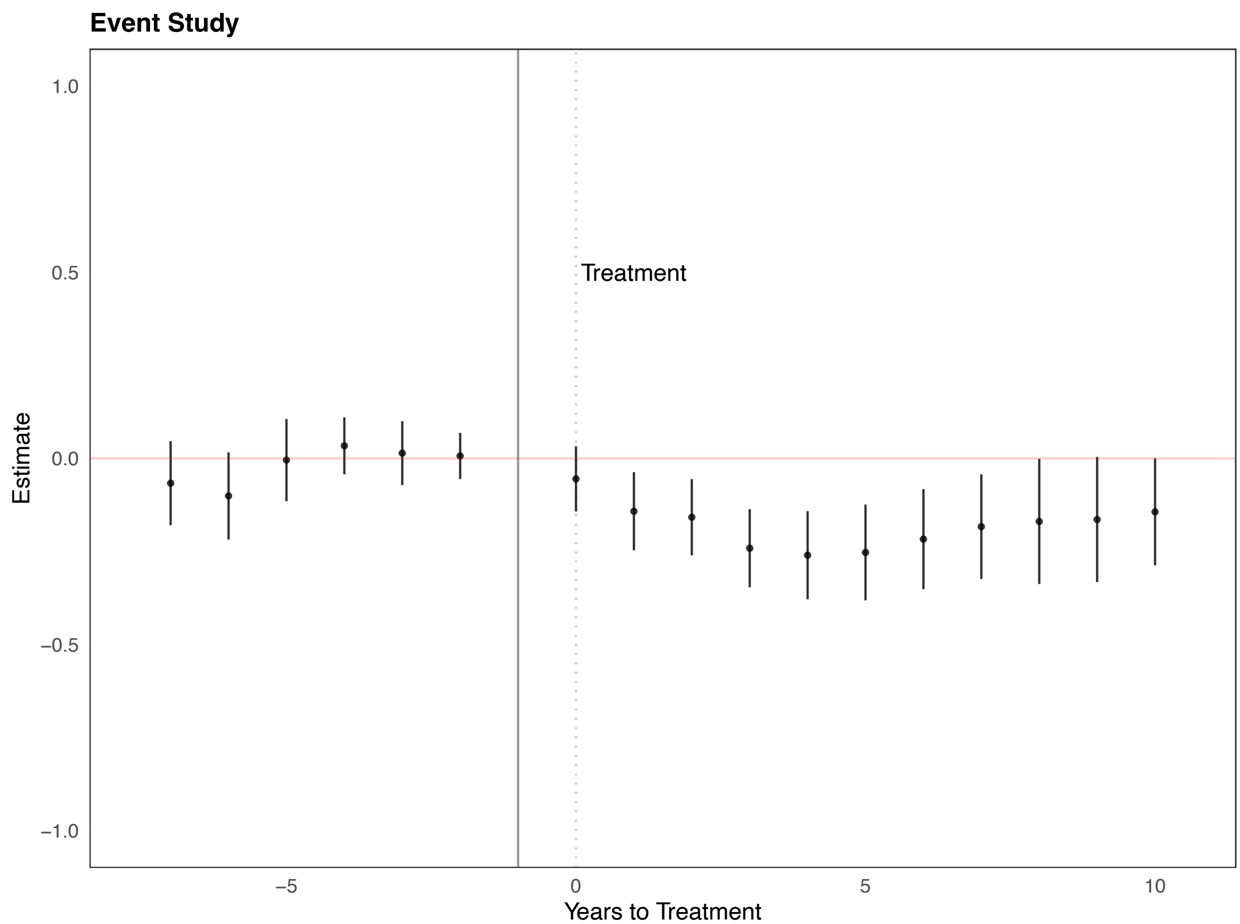

Figure 1: Estimates of EU/IMF conditionality on attitudes towards national democracy and governance for conditionality countries, using leads and lags in an event study model. The black line represents the last pre-treatment time period. The dotted line represents the start of the treatment.

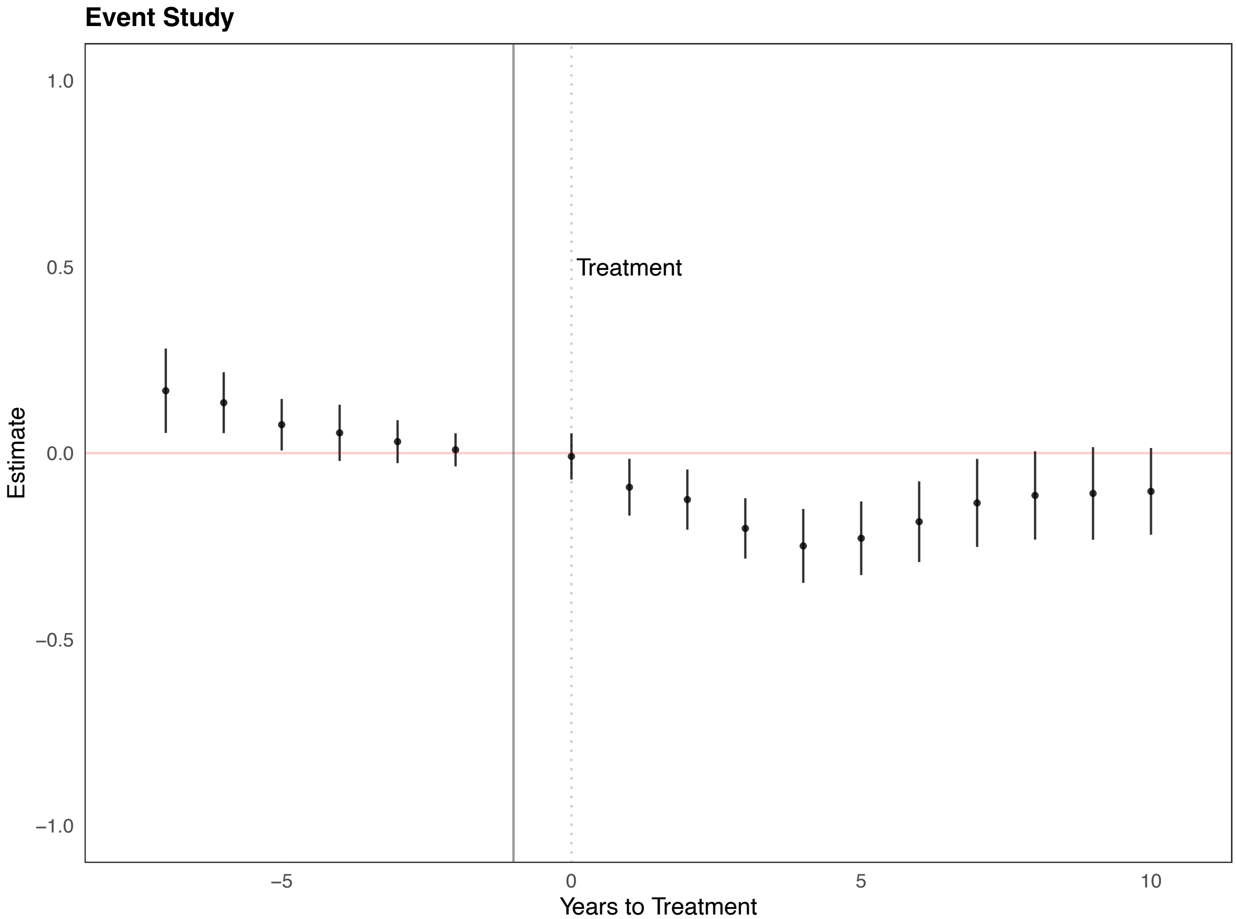

Figure 2: Estimates of EU/IMF conditionality on attitudes towards EU democracy and governance for conditionality countries, using leads and lags in an event study model. The black line represents the last pre-treatment time period. The dotted line represents the start of the treatment.

Conclusion

Several studies have found that economic adjustment programs during the Euro-crisis had negative consequences for the attitudes of citizens towards their democratic political system (Armingeon and Guthmann 2014; Armingeon et al. 2016; Magistro et al. 2021). In this short article I investigated how durable this decline in trust has been across countries.

Findings suggest that indeed conditionality countries experienced a steeper decline in both EU and national institutional trust compared to no-conditionality countries after the onset of the European debt crisis in 2009. This gap in trust, although it started to reduce slightly around 2014, only disappeared in 2017. While many consider the end of the European debt crisis the end of 2012, growth for the peripheral countries only began to resume between 2013 and 2015. In that time period, they have saw unemployment decline, although it remained painfully high in some countries, such as Greece and Spain. However, it wasn't until 2017 that the gap in trust with the control group closed. This seems to indicate that while in the aftermath of the debt crisis trust went down dramatically rapidly in conditionality countries, the economic recovery did not lead to an equally fast resurgence in trust. Instead, it took years to revert back.

A question that remains open is how durable this increase in trust for conditionality countries will be. According to some, the divide between conditionality and no-conditionality countries is a structural feature of the European Monetary Union, which cuts off the Eurozone's periphery from the rest of the continent in terms of democratic legitimacy and permanently pits surplus nations against deficit nations (Armingeon et al. 2016). If this reading is correct, other crises will soon widen this gap again, endangering the functioning of these democracies as a whole. COVID-19 is a case in point. While initially it looked like populist parties in many countries were suffering from rally around the flag effects that boosted support for government incumbents, it is unclear what the ultimate scope of the COVID-19 crisis will be, especially since the burden of this crisis seems to again fall heavier on the peripheral countries. Investigating how COVID-19 impacted institutional trust between these two groups of countries remains a question for future research.

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