Fiscal Policy Learning from Crisis:

Comparative Analysis of the Baltic Countries

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Abstract: The experience of a major crisis is often expected to lead to policy learning but the empirical evidence about it is limited. The goal of the paper is to explore comparatively whether the crisis of 2008-2010 has led to fiscal policy learning by civil servants in the three Baltic countries. Despite some differences in the crisis experience, the finance ministry officials in all three countries have identified the same lesson from the crisis: fiscal policy should be counter-cyclical and help to stabilize the economy. The paper also discusses how various factors have influenced policy learning, including the acknowledgment of failure, blame shifting, and analytical tractability.

Key words: policy learning, fiscal policy, crisis, policy bureaucracy, comparative analysis

1. Introduction

Although the "crisis" in a broad sense is far from being over in Europe, it is worth taking a look back and asking: what have policy-makers learnt from the crisis experience (if anything) so far? While it is often argued that a crisis should lead to policy learning, we still have limited knowledge about whether and how it actually happens. Several authors writing on the topic of policy learning have lamented on the underdeveloped state of the literature (Dunlop and Radaelli 2015; Radaelli 2009; Howlett 2012). The same complaint could be voiced even more loudly about the more specific question of whether and how crisis influences policy learning by civil servants. Exploring policy learning by *civil servants* is warranted since they are considered to be among the most important learning actors in the policy learning literature (e.g. Heclo 1974; Radaelli 2008; Bennett and Howlett 1992; Hall 1993). As Heclo (1974, p. 303) has put it, "To officials has fallen the task of gathering, storing and interpreting policy experience." Given that the bureaucrats can influence the policy agenda and shape policy decisions (Christensen 2013; Page and Jenkins 2005; Hall 1993), inquiring into the kinds of lessons they have identified from a crisis can provide valuable insights about the dynamics of policy learning.

With our study, we seek to open up the "black box" of policy learning by civil servants at least a little bit. "Policy learning" refers to the updating of beliefs about key components of policy, based on experiences, analysis, or social interaction (Dunlop and Radaelli 2013, p. 599; Radaelli 2009, p. 1146; Zahariadis 2014). While policy learning may often lead to policy change and the occurrence of change is often viewed as evidence of learning (Hall 1993; May 1992; Bennet and Howlett 1992), it is useful – for the sake of conceptual accuracy – to keep policy *learning* and policy *change* analytically separate (Fenger and Quaglia 2015; van Nispen and Scholten 2015).[1] In this paper we focus on *policy learning* rather than on policy change. In other words, we seek to contribute to the scholarly discussion on whether and how a crisis can lead to the modification of policy beliefs that individual public officials have.[2]

We focus on the field of *fiscal policy* and the lessons that the officials of finance ministries have learnt from the recent crisis experience. Specifically, we look at the three Baltic countries to answer the following research questions: Have the fiscal policy officials learnt anything from the crisis of 2008-2010 and if yes, what? Have the civil servants in the Baltic countries drawn similar or different lessons from the crisis?

We concentrate on *fiscal policy* because the recent crisis in Europe has often been construed as a "fiscal" crisis (Schmidt 2014). Furthermore, given that the issues of fiscal policy have

[1] Indeed, even if policy actors have engaged in policy-learning, the modified beliefs themselves do not necessarily guarantee that policy change will ensue (Fenger and Quaglia 2015; Elliott and Macpherson 2010). Also, even if policy change occurs, it may take place for other reasons than learning (e.g. electoral considerations, external pressures, resource constraints) (Fenger and Quaglia 2015; May 1992).
[2] While several streams of literature related to policy learning (e.g. policy-transfer, policy diffusion, or lesson-drawing in public policy) focus on *actual* policy change, the focus of our paper is on ideational shifts rather than on whether the lessons are eventually translated into policy.

generated a lot of debates in the academic and policy communities since the Great Recession (see, e.g. Ban 2015; Vail 2014), it would be insightful to explore how fiscal policy beliefs have evolved among the civil servants after the crisis. While the policy learning framework has been used to examine fiscal policy learning at the EU level (Dunlop and Radaelli 2015) and at the member state level *during* the crisis (Zahariadis 2014), there are no studies that would explore fiscal policy learning in the EU *member states after the crisis*.

Bennett and Howlett (1992, p. 290) have suggested that advancing our knowledge of policy learning would be fruitful via "intensive examination of a few comparable cases". Such an approach allows us to explore qualitatively, first, whether and how policy officials have modified their policy beliefs, and, second, identify factors that have influenced their learning. The three Baltic countries were hit harder by the global financial crisis in 2008-2009 than other European countries (as witnessed by the largest output losses on record) but have also become regarded as "successful" examples of exiting from it via austerity measures (Staehr 2013). Thus, they can provide useful insights about policy learning from crisis.

The three Baltic countries can also be viewed as the "most similar" cases, because of their similar historical legacies and development trajectories. Despite their similarities, some small differences regarding the crisis experiences in the Baltic countries did occur (Kattel and Raudla 2013). The cumulative output losses in 2008-2010 were larger in Estonia (20.1%) and Latvia (21.7%) than in Lithuania (14.8%) (Eurostat). While the Estonian government managed to keep the deficit below 3% of GDP, Lithuania and Latvia recorded significant budget deficits in those years. Whereas Lithuania was able to borrow funds from international markets, Latvia had to turn to the IMF and the EU for financial support (Bakker and Klingen 2012; Kattel and Raudla 2013). Thus, it would be interesting to explore whether the differences in crisis experience influenced the lessons identified by the civil servants. While a number of studies have examined how the crisis was *managed* in the three Baltic countries (Kattel and Raudla 2013; Kuokštis 2013, 2015; Staehr 2013), there haven't been any studies so far that explicitly adopt a *policy learning* perspective and seek to identify what kind of lessons the public officials in these countries draw from the experience of the crisis. Our data come from semi-structured elite interviews with civil servants from the finance ministries in the three Baltic countries.

The paper is structured as follows. Section 2 outlines the theoretical predictions, followed by the empirical analysis in Section 3. Section 4 provides a concluding discussion.

2. Policy Learning from Crisis: Theoretical Discussion

In the existing literature, it is often argued that crises provide opportunities for learning (Brändstrom et al. 2004; Hall 1993; Hogan and Doyle 2007). Indeed, although learning *during* a crisis may be limited, due to the sense of urgency or analytical resource constraints (e.g. Boin et al. 2005; van Nispen and Scholten 2015; Zahariadis 2014), learning *from* the crisis, *after* the crisis, should be more likely, given the possibilities to reflect on what led to it and to evaluate crisis-time actions. Since a crisis is expected to "profoundly shake" those who are exposed to it first hand and hence to motivate them to prevent its recurrence (Brändstrom et al. 2004, p. 192), we would expect policy actors to take stock of the crisis experience. Crises can have a focusing effect by calling into question the existing policies and forcing policy actors to reconsider those policies (Brändstrom et al. 2004; Hogan and Feeney 2012; Hogan and Hara 2011), which should facilitate policy learning. Thus, our first theoretical expectation is:

E1: The experience of a crisis will lead to policy learning among civil servants.

While many studies do indeed argue that crises are conducive to policy learning, there are other studies that point to the necessity of adopting a more nuanced view, in the sense that crises *may* facilitate learning but it is not necessarily guaranteed (Fenger and Quaglia 2015; Heikkila and Gerlak 2013). Based on the existing literature, we can outline a number of theoretical expectations about factors that can influence whether the experience of a crisis leads to policy learning by civil servants.

First, the *nature of the policy area* is likely to influence whether and to what extent the experience of a crisis leads civil servants to draw lessons from it. In particular, the level of analytical tractability is likely to influence policy learning. The more "tractable" the policy problem, the easier it is to (quantitatively) measure performance indicators and to identify causal relationships between policy actions and their effects, and as a result, the easier it is for the policy bureaucracy to draw lessons from previous experiences (Jenkins-Smith 1985, 1988; Sabatier 1987; Dunlop and Radaelli 2015). Conversely, the more complex the causal relationships, the more ambiguous the policy experience and the more challenging it is to draw causal lessons (Sabatier 1987; Radaelli 2008). Thus, even if the experience of a crisis induces the civil servants to analyse more closely the causal relationships in their policy area – e.g. the factors leading to the crisis, the effects of policy actions undertaken in the midst of the crisis – the extremeness of the crisis and the uncertainties surrounding it may make the attribution of causality, and hence policy learning, more challenging than would be the case in "times of normalcy". Thus, the second theoretical expectation we will examine is:

E2: Policy learning is less likely to take place if the policy area is characterized by low tractability of problems.

Second, a crisis is more likely to lead to policy learning if the policy actors identify policy *failure*, meaning that they consider the policy in their area as being (at least partially) responsible for the crisis (Bovens and t'Hart 1995). Without the perception and identification of policy failure, there would be fewer incentives and pressures (if any) to challenge the existing policies and to identify lessons. Conversely, the perception of policy failure is likely to trigger the reconsideration of existing policies and a search for new ideas (May 1992; Zahariadis 2014). Thus, our third theoretical expectation is:

E3: A crisis is likely to lead to policy learning if the policy actors consider the crisis to have resulted from policy failure.

Although the acknowledgement of failure should foster learning, the former may be hindered by several factors. In order to maintain organizational stability, the officials may avoid evaluative efforts, in the fear that the findings might implicate them (May 1992). As Hood (2002, 2010) has emphasized, policy actors are often motivated to avoid blame. If civil servants engage in blame-games and seek to shift the burden of blame to others, the opportunities for learning from the crisis are likely to be more limited. Thus, our fourth theoretical expectation is:

E4: In order to avoid blame, officials would seek to avoid the identification of failure, which limits the opportunities to learn from crisis.

Another issue related to the perception of policy failure is whether the policy actors feel that they (or their organizations) could have done anything to *avoid* the failure. Here, again, existing theoretical discussions point to somewhat diverging predictions. On the one hand, based on the rationalistic approaches, we would expect that if the policy officials perceive that they could have contributed to preventing the occurrence of the crisis, they would be more motivated to draw lessons that would help them prevent similar crises in the future (Howlett 2012; May 1992). Hence, our fifth theoretical expectation is:

E5: Policy learning from crisis is more likely if civil servants feel that they could have taken steps to prevent the crisis.

On the other hand, if the civil servants concede that they could have done something to prevent or alleviate the crisis, they would assume a considerable burden of blame (Brändstrom and Kuipers 2003; Howlett 2012; Hood 2010) – and attempts to avoid such attribution of blame would undermine their efforts to draw lessons from the crisis.

Finally, policy learning from crisis by civil servants is likely to be influenced by external actors (especially organizations like the European Union, the IMF, the World Bank, and the OECD). Such actors can *facilitate policy learning* by providing new information, an outside view, or a more neutral analysis of the problems, and point to lessons that can be learnt from others who have experienced a similar crisis (Hogan and Hara 2011). Also, through interactions with the officials from external organizations, the "domestic" civil servants can be exposed to new interpretations of the experienced crisis and participate in the discussions that assess different policy alternatives (Radaelli 2008). Thus, our sixth theoretical expectation is that:

E6: Policy learning from crisis by civil servants is facilitated by external actors.

In the following, we will examine the plausibility of the theoretical expectations E1-E6 with the empirical analysis of the Baltic countries.

3. The Empirical Study

3.1. Background Information about the Crisis in the Baltic Countries

Since regaining independence in the early 1990s, the Baltic republics have stood out among the European transition countries as radical pro-market reformers. In the early 1990s, all three countries adopted a mix of policies advocated by the Washington consensus, including fixed exchange rates, liberalization of prices and trade, and wide-ranging privatization. The economic environments created as a result of such neo-liberal policy choices appeared to have put the Baltic republics on an impressive growth track, only interrupted by the Russian crisis at the end of the 1990s. After accession to the EU, all three economies witnessed an unprecedented boom. Between 2004 and 2007 the Baltic republics stood out among the EU countries for their high growth rates: the average annual growth rates for this period were 10.3% in Latvia, 8.5% in Estonia and 8.2% in Lithuania. These remarkable figures were, however, accompanied by signs of overheating, including double-digit inflation, a housing boom, appreciating real exchange rates, accelerating wage growth (that exceeded productivity growth), and a fast accumulation of net foreign liabilities and soaring current account deficits. One of the key features of Baltic economies has also been an overwhelming foreign ownership of banking assets. By the time the crisis hit, Estonia and Lithuania had over 90% of banking assets in foreign ownership, Latvia just above 60%. (Kattel and Raudla 2013)

The crisis hit all Baltic countries quickly and painfully. The domestic bubbles burst in early 2008, when the credit supply decelerated and banks started tightening credit conditions. The downturn was further exacerbated by negative developments in the external economic environment after the Lehman Brothers' bankruptcy. The cumulative GDP declines in 2008-2010 in the Baltics were among the largest in the world (Bakker and Klingen 2012; Staehr 2013) (see Table 1). In order to bail out the Parex bank, the Latvian government had to ask for international support from the IMF, the EU and Nordic countries in November 2008. In response to the crisis, all three Baltic republics implemented sizable fiscal consolidations in 2008–2010. The fiscal adjustment was the largest in Latvia, adding up to around 16.3% of GDP between 2008 and 2011, followed by Estonia (13.9% of GDP) and Lithuania (13.1% of GDP). (Kattel and Raudla 2013; Raudla and Kattel 2013) In all three countries, austerity measures were deemed necessary for maintaining their fixed exchange rate, achieving *internal* devaluation (rather than external) and restoring investor confidence (Kattel and Raudla 2013; Bakker and Klingen 2012; Staehr 2013). In addition, in Estonia, fiscal consolidation was also driven by the goal to join the Eurozone as fast as possible; in Latvia, by the requirements of the bailout package; and, in Lithuania, by the need to limit expensive borrowing to cover the budget deficit and to avoid sovereign default (Bakker and Klingen 2012; Raudla and Kattel 2011). Fiscal consolidation in all three countries entailed both expenditure cuts and tax increases, while larger weight was accorded to the expenditure side. The largest focus on expenditure measures could be observed in Lithuania (with 85% of the total consolidation between 2008 and 2011 made up on the expenditure side), followed by 70% in Estonia, and 60% in Latvia (Raudla and Kattel 2011). In 2010-2011, all three countries returned to a growth path. Estonia joined the Eurozone in 2011, Latvia in 2014 and Lithuania in 2015.

Table 1: Fiscal and economic indicators for Estonia and Latvia 2000-2015

Year	Budget deficit in Estonia (% of GDP)*	Budget deficit in Latvia (% of GDP)	Budget deficit in Lithuania (% of GDP)	Public debt in Estonia (% of GDP)	Public debt in Latvia (% of GDP)	Public debt in Lithuania (% of GDP)	Real GDP growth in Estonia	Real GDP growth in Latvia	Real GDP growth in Lithuania
2004	2.4	-1.0	-1.4	5.1	14.2	18.7	6.3	8.9	6.6
2005	1.1	-0.4	-0.3	4.5	11.7	17.6	9.4	10.7	7.7
2006	2.9	-0.6	-0.3	4.4	9.9	17.2	10.3	11.9	7.4
2007	2.5	-0.6	-0.8	3.7	8.4	15.9	7.7	10.0	11.1
2008	-2.7	-4.0	-3.1	4.5	18.6	14.6	-5.4	-3.6	2.6
2009	-2.2	-9.0	-9.1	7.0	36.4	29.0	-14.7	-14.3	-14.8
2010	0.2	-8.1	-6.9	6.5	46.8	36.2	2.5	-3.8	1.6
2011	1.2	-3.3	-8.9	6.0	42.7	37.2	7.6	6.2	6.0
2012	-0.2	-0.8	-3.1	9.7	40.9	39.8	5.2	4.0	3.8
2013	-0.2	-0.7	-2.6	10.0	38.2	38.8	1.6	3.0	3.5
2014	0.6	-1.4	-0.7	10.6	40.0	40.7	2.9	2.4	3.0

*Net lending (+) /net borrowing (-)
Source: Eurostat

3.2. The Crisis Experience and Policy Learning by Civil Servants

In this paper, we focus on the subjective understandings and interpretations of the civil servants in the three countries. In each country, we conducted interviews with five Ministry of Finance (MoF) officials. In selecting interviewees, we used purposive sampling: we identified officials who have been most closely involved in fiscal policy-making and also made sure that we interviewed civil servants from different levels of the organizational hierarchy in order to capture the potential diversity of viewpoints. The total number of MoF officials closely involved in fiscal policy-making in the Baltic countries is relatively small; hence, we felt that five interviews in each country should be sufficient to provide exploratory insights. The interviews were conducted between August 2014 and September 2015, and each lasted between 1.5 and 3 hours. The interviews were recorded, transcribed and also translated into English (in order to increase inter-coder validity by allowing all authors from the three different countries to read the transcripts). The authors read through all the interview transcripts independently, used open coding to identify the main themes, and then discussed the interpretations jointly in order to increase the validity of the findings. Given that we have defined "policy learning" as "the updating of beliefs about policy" by policy actors, we are primarily interested in their *subjective interpretations* rather than already implemented policy change. In order to capture the shifts in policy beliefs, the interviewees in all three countries were, on the one hand, asked directly about what policy lessons could be drawn about the crisis for fiscal policy, whether the crisis has triggered changes in fiscal policy and influenced their normative views on fiscal policy-making. These questions were worded as openly as possible, in order to allow the interviewees to focus on themes that they considered to be the most relevant. However, in order to identify the subtler changes that the interviewees might not have been able explicitly word as "lessons" from the crisis, they were also asked about the main causes of the crisis, whether the MoF could have done anything to prevent it, how they assess the actions undertaken during the crisis, and what role has been played by external actors in fiscal policy-making. These questions were also used for exploring the impacts of the various factors outlined in section 2.

3.2.1. Perceptions of the finance ministry officials about the causes of the crisis of 2008-2010 and its prevention

On the question about the causes of the recent crisis and whether external or internal factors were more important in contributing to the emergence of the crisis, most of the interviewees in the three countries pointed to a *combination* of internal and external factors, with greater weight attributed to *external* causes (global optimism, underestimation of risks, low interest rates) in Estonia and Latvia, and more weight to *internal* causes in Lithuania.

While several Lithuanian officials felt that the government could have, in principle, prevented the *real estate bubble* (e.g. via adopting macro-prudential regulation), the Estonian and Latvian officials felt that not much could have been done to prevent it. As one of the Estonian officials put it, “We did not have domestic banks we could regulate and tell them how many loans to give. ... We were in the EU and couldn’t use capital restrictions” (Interview Est1). In the words of a Latvian official: “The main objective cause of the overheating was us joining the European Union. .... It led to an increase in optimism and cheap interest rates and that, in turn, gave rise to the real estate bubble” (Interview Lat1).

When asked more specifically about whether the *ministry of finance* could and should have done something in the realm of *fiscal* policy to *prevent* the crisis, the overall assessment of the Estonian civil servants was that the MoF could *not* have done much (beyond what it already did). The overall narrative that came through in the interviews was that while the MoF had underestimated the size of the bubble and hence also the positive output gap – which resulted in pro-cyclical fiscal policy – “everyone else” (including the European Commission (EC) and the IMF) had done the same. All the officials noted that during the boom the Estonian government was already running surpluses (see also Table 1) and it would have been difficult to gain political support for having an even larger surplus. One of the officials also emphasized that lowering taxes, as the government had done, during the boom was clearly “bad timing” since it fuelled the boom, but this decision was “in the hands of the politicians” (Interview Est3).

Several Latvian interviewees conceded that running the deficits and stimulating the economy during the boom had magnified the bubble. They also argued that if the government had accumulated reserves, the bailout procedure could have been avoided and it would have been easier to “get through the crisis” (e.g., by using the reserves to save the Parex bank). At the same time, the MoF officials felt that their ministry could not have done much to prevent the crisis because fiscal policy decisions tend to be “in the hands of politicians” who can ignore the expert advice of the civil servants.

Most of the interviewees from Lithuania also argued that the government’s fiscal policy had been too loose during the boom and that this had resulted from politicians’ decisions. As one of the officials emphasized, “Increasing expenditures at a much faster rate than the GDP growth during the boom clearly was a complete nonsense” (Interview Lit5). Another interview noted, “The parliament still made those decisions despite experts saying that it would be bad” (Interview Lit4). Similarly to the Latvian officials, the Lithuanian interviewees felt that accumulating reserves during the boom would have made it easier to go through the crisis by using reserves to cover the deficits instead of having to borrow at high interest rates. Furthermore, the Lithuanian officials pointed to a range of specific measures that the MoF had proposed during the boom – including the adoption of a fiscal discipline law (requiring a surplus or balanced budget over a medium term), which had been suggested by the IMF mission in

Lithuania, the enactment of a comprehensive real estate tax, and a complete elimination of mortgage interest deductions for the income tax – but these were not supported by the parliament in their entirety.

3.2.2. The evaluation of crisis-time fiscal policy actions

When asked to evaluate the crisis-time fiscal policy actions, undertaken in 2008-2010, the Estonian officials' opinions were rather divided. One of the officials argued unequivocally that by opting for quick consolidation, the government did the "right thing" (Interview Est4). In contrast, another stated that "The austerity measures deepened the crisis" (Interview Est2). The others subscribed to more qualified assessments. They argued that, all in all, while the austerity policy may have been "a little bit harsh", the measures adopted "gave a positive push" by allowing Estonia to "exit the crisis" via joining the Eurozone. In their view, restoring credibility to the economy via Eurozone entrance had a more positive effect on the Estonian economy than expansionary fiscal policy would have resulted in. Curiously, while the official rhetoric of the Estonian government during the crisis period of 2008-2010 did not support a Keynesian approach (Raudla and Kattel 2011), the *ex post* interpretations of crisis-time actions by the officials refer to Keynesian arguments and most of the interviewees felt the need to justify the crisis-time actions with reference to a Keynesian prism. The interviewees argued, for example, "In reality, it cannot be said that we did not follow the Keynesian ideas in our fiscal policy." (Interview Est3) or "We have been criticized for not being Keynesian during the crisis, but in some ways we were. ... During the boom we collected reserves and then at the outset of the recession loosened the fiscal policy in a Keynesian way by running deficits." (Interview Est1) It was also noted that while some of the expenditure cuts (i.e. cuts to salaries, transfers, and investments) may have deepened the crisis, the government also tried to stimulate the economy by accelerating the use of the EU structural funds and trying to find consolidation measures that would not negatively affect aggregate demand (like taking out additional dividends from state-owned enterprises).

In Latvia, only one of the interviewed civil servants argued that the consolidation *cooled* the economy – but added that the government "had no choice" since the austerity measures were required by the IMF and the EC (Interview Lat3). The others argued that the fiscal consolidation had been *positive* for the economy. For example, "The crisis conditions have proven that cutting expenditures during an economic downfall does not always have a negative impact. Therefore, if we compare the theory that is taught in the university with what is going on in real life, the case of Latvia proves that we can restore growth with expenditure cuts" (Interview Lat1).

In Lithuania, all the interviewed officials argued that the government had acted correctly during the crisis. One of the officials did note though that the cutting of expenditures had been pro-cyclical ("we were cutting at an inappropriate time") but this was necessary given the circumstances (Interview Lit5). Another official even argued that it would have been inappropriate to pursue a Keynesian stimulus during the crisis since the economy was imbalanced and it was expensive to borrow (Interview Lit1). Furthermore, "The conditions for Keynesian policy were not present – the economy had to correct itself. ... One needs to take guidance from Keynes creatively and not follow the literal textbook approach. Keynes talked about the case of a large closed economy without a fixed exchange rate. ... But we were defending a currency board and had to restore investors' confidence." (Interview Lit1) Another official summed it up as follows: "If you have to borrow at 10%, you do everything you can to cut expenditures" (Interview Lit2).

In sum, the overall opinion of the interviewed MoF officials in *all* countries was that the governments in their country had acted *correctly* during the crisis, although there were some dissenting opinions among the interviewees in Estonia and Latvia. Interestingly, the use of Keynesian ideas in assessing the austerity measures undertaken during the crisis varied between the officials in the three countries. In Estonia, some of the officials even tried to argue that the government had tried to follow Keynesian principles in deciding on the austerity measures. In Latvia, the officials viewed the Latvian case as providing evidence of non-Keynesian effects of fiscal consolidation, whereas in Lithuania, it was argued that the conditions for Keynesian stimulus during the crisis were not present because of macroeconomic imbalances and lack of financing, while non-Keynesian effects of consolidation were also mentioned.

3.2.3. What has been learnt from the crisis for fiscal policy?

When asked about what they learned from the crisis, the MoF officials from all three countries pointed out that as a result of the crisis, fiscal policy has become much more important. As an Estonian official put it: “As a result of the crisis, the importance of fiscal policy is more clearly acknowledged and it is in the centre of attention” (Interview Est3). Also, several interviewees from Estonia and Latvia pointed out that the macroeconomic analytical capacities of the MoF officials improved as a result of the crisis. This seemed to be particularly pronounced in Latvia where – because of the bailout package – the IMF officials were more closely involved in consulting the MoF. In the words of one of the Latvian officials, “We learnt a lot from the IMF experts. I can really say that the entire crisis period was a good training – in terms of how to work, how to analyse, how to forecast. ... Now we go much deeper into details and analyse much more. ... Before the crisis, our models were relatively simple but during the crisis, in cooperation with the IMF officials, we improved our models.” (Interview Lat4)

Despite the fact that the crisis experience itself had been somewhat different in the three countries, the most important lesson in the eyes of the interviewed MoF officials is essentially the same. The interviewed officials from all countries *concurred* that the main lesson from the crisis is that "fiscal policy should be counter-cyclical and not pro-cyclical" and that "the budget should play a role in macro-economic balancing". The emergence of this "lesson" sounds somewhat paradoxical at first sight: all three countries implemented austerity measures during a major economic downturn in 2008-2010 – actions, which could be viewed as *pro*-cyclical – and, in all countries, most of the officials viewed the adoption of austerity measures as having been the "correct" course of action.

There appear to be two main reasons behind the emergence of this – at first sight counter-intuitive − lesson in the countries that have come to be regarded as the champions and positive examples of implementing austerity measures during a major recession. First, as mentioned in the previous subsection, with the benefit of hindsight, the officials in Latvia and Lithuania, but to some degree also in Estonia, view the pro-cyclical fiscal policy preceding the crisis as having contributed to the bubble. Running surpluses during a boom is also viewed as important for building up reserves – which, according to the interviewees from all three countries, helped Estonia to weather the crisis of 2008-2010 better, could have helped Latvia avoid the bailout programme, and allowed Lithuania to avoid expensive borrowing. Thus, in the eyes of most of the officials of all three countries, an important lesson of the crisis is that adopting a counter-cyclical fiscal policy during a boom should help avoid future crises, and, if they do occur, the accumulated reserves should help to overcome them. As the officials observed: "We did tighten the budget during the boom, but not enough. ... Accumulating reserves is important. Other countries now also say that this was the right thing to do. Those who had no reserves didn't manage the crisis so well" (Interview Est1). "The crisis has clearly proven that during the good years, if the government spends all the revenues and observes the nominal 3% [of GDP] deficit target, then during a downturn it objectively can't maintain it" (Interview Lat1). "The main lesson is that we should have had a more cautious fiscal policy before the crisis. ... We should have run a small surplus, like Estonia, not deficits." (Int Lat4) "We cannot avoid crises, especially since we are a small country, but we can prepare for them – the bigger the buffer the better. As the Estonian experience shows, if you have a reserve, the landing during the crisis is softer and you don't have to borrow at such high interest rates" (Interview Lit 3).

Second, a counter-cyclical role for fiscal policy is prescribed by the Fiscal Compact, which requires the members of the euro-zone to incorporate a structural deficit rule into the domestic legislation.[3] All three countries adopted a structural deficit (or balance) rule in 2013-2014, which now guides fiscal policy-making and forces the MoF to pay attention to the cyclical stance of the economy when preparing the budget.

Thus, our interviews indicate that, as a result of the combination of the evaluation of pre-crisis fiscal policies and the implementation of the Fiscal Compact, the officials from all three countries have adjusted their views on fiscal policy and have come to endorse the focus on structural balance in fiscal policy-making. This shift has been particularly pronounced in Estonia and Latvia. For example, the Estonian officials noted: "In fiscal policy, we used to focus on the nominal balance but now we strive to focus on the structural balance. ... At the moment, in our decisions, the structural balance has more weight than the nominal one. ... In order to ensure that fiscal policy is countercyclical, the structural balance indicator should be preferred over the nominal one." (Interview Est2) "Before the crisis, the focus of fiscal policy was on the nominal budget balance. ... Even if we had surpluses, these were often not planned. Now we take the economic cycle into account in planning the budget." (Interview Est1) The Latvian officials stated, for example: "Before the crisis, we didn't really have an objective in

[3] The structural position of the budget is calculated on the basis of a cyclically adjusted position, which is adjusted for one-off and temporary transactions. The cyclically adjusted budget position, in turn, is found by subtracting the cyclical component (or the output gap) from the nominal budget position (for a more detailed discussion, see, for example, Mourre et al. 2014).

fiscal policy-making but the structural deficit rule now provides us with a target" (Interview Lat4). "Without the structural rule we wouldn't know how much we can actually afford to spend during the good years." (Interview Lat1) In Lithuania, the interviewees mentioned there had been discussions about adopting a more counter-cyclical fiscal policy among the MoF officials already before the crisis – but the crisis experience and the Fiscal Compact helped to drive home the need for analysing the cyclical stance in fiscal policy making. "After the crisis, it was clear that nominal indicators are not enough: thus, structural indicators were introduced. ... These rules certainly contain more logic and rationality." (Lit 3)

At the same time, most of the interviewees from all three countries conceded that the calculation of the structural position is uncertain; thus, it is challenging to use the structural balance/deficit rule as a quantitative yardstick in fiscal policy in *real time* because the ex ante and ex post evaluations of the cyclical position of the economy can differ significantly. The interviewees also pointed to the fact that the domestic assessments of the structural position tend to diverge from the evaluations of the European Commission, which, in turn, increases uncertainty in fiscal policy-making.

Most of the interviewed officials stated that the new framework laws for budgeting, spurred by the Fiscal Compact, institutionalize the main lessons learnt from the crisis and constitute an important step forward in fiscal governance, but their assessment of the efficacy of the new rules varies somewhat from country to country. In Estonia, the overall opinion of the interviewees is that the new rules were not strictly necessary for Estonia, given its commitment to fiscal discipline, but the new law might provide some additional insurance for the future. The Latvian officials noted that while the MoF supports the new rules and acts as a watchdog, there is still a willingness among politicians to violate them, and that the *politicians* haven't really learnt from the crisis. The Lithuanian officials noted that the institutionalization of fiscal policy by creating sounder laws has been an important lesson from the crisis. Thus, while some manipulation might still be possible under the new rules – "implementing completely crazy fiscal policy, like increasing expenditure by 30% when the revenues grow 10%" (Interview Lit 5) – is now precluded. At the same time, it was also noted by Lithuanian officials that there might still be willingness by politicians to violate these rules: "The politicians still have the thinking that, ok, there are stricter rules now but other countries don't abide by them, so maybe we shouldn't either." (Interview Lit3)

4. Concluding Discussion

As the interviews indicate, fiscal policy learning from crisis has indeed taken place in all three countries, thus confirming our theoretical expectation E1. The main lesson identified by the finance ministry officials in all three countries is that fiscal policy should strive to be more counter-cyclical and avoid being pro-cyclical – which can be viewed as amounting to a change in policy goals.

As pointed out in the theoretical section, policy learning from crisis is more likely to take place if the policy actors acknowledge policy failure and consider their policy area as having contributed to the emergence of the crisis (e.g. Bovens and d'Hart 1995). Our empirical study indicates, however, that the links between the acknowledgement of failure and policy learning can be more complicated as no unambiguous support could be found for the theoretical expectation E3. In the Latvian and Lithuanian cases, indeed, the interviewed officials conceded that the MoF could have taken preventive steps in fiscal policy before the crisis, that the too loose fiscal policy during the boom had added fuel to the bubble, and hence the lesson for the future is that during a boom government should run surpluses in order to stabilize the economy. In Estonia, however, in the officials' view, for the most part, fiscal policy did *not* contribute to the emergence of the crisis. Still, the main lesson they identified from the crisis is *the same* as in the two other countries: during a boom fiscal policy should be more counter-cyclical. Thus, based on the Estonian case, it appears that policy learning is still feasible even if no clear policy failure is identified.

Our interviews also indicate that the links between the evaluations of *crisis-time actions* and policy learning are not necessarily straightforward – thus, our theoretical prediction E5 was not supported. In Estonia, at least some of the officials viewed the austerity policies as having cooled down the economy even further during the crisis, which, in turn, has driven home the principle that fiscal policy should be countercyclical. However, in the other two countries, the officials, for the most part, view the austerity measures as having been justified (despite their pro-cyclicality) but, still, for the future, consider it necessary for fiscal policy to be more *counter*-cyclical. While the interviews with the Estonian officials indicate that they even try to construe the crisis-time actions as having followed (at least some) Keynesian principles, the officials in the other two countries have subscribed more clearly to the notion of non-Keynesian effects of fiscal consolidation. It is also noteworthy that although Estonia did not make extensive use of the accumulated reserve in 2008-2010 (and opted for austerity measures instead), the officials in the other two countries have come to view having a fiscal reserve as an important instrument for being prepared for the next crisis.

How can we explain such non-linear linkages between the officials' evaluation of pre-crisis policies and crisis-time measures (described above) and the policy lessons they drew? On the one hand, it is plausible that the complexity of fiscal policy in general and the increasing intractability of the causal relations during a crisis in particular have played a role here. Given the difficulties involved in estimating the effects of fiscal policy on the economy (and also decreasing consensus in fiscal policy discussions internationally), drawing straightforward lessons from the pre- and crisis-time policies is challenging. Thus, we could see that the level of analytical tractability of the specific field we looked at *did* play a role in policy learning among the civil servants but it did *not* undermine it – implying that our theoretical expectation E2 could not be fully supported. On the other hand, all three countries have been subjected to similar policy pressures from the European Union – which has led to the emergence of the same policy lessons in all three countries, despite somewhat diverging crisis experiences and also different assessments of how fiscal policies contributed to the crisis and their effects during the crisis. Indeed, making fiscal policy more countercyclical via adopting structural balance as the main yardstick has been mandated by the European Union through the Fiscal Compact.

It was also argued in the theoretical discussion that the acknowledgment of mistakes and failure may be prevented by attempts to avoid blame (e.g. Hood 2010), which, in turn, would hinder policy learning. As our interviews indicate, however, the ability of the policy bureaucrats to *shift* blame – to other policy-makers (like politicians) – can in fact be conducive to policy learning, which goes against the theoretical expectation E4. Indeed, we can observe that most of the civil servants in these countries blamed the elected officials for undertaking faulty policies. The ability to *shift* the responsibility for problematic decisions to politicians (adopted before the crisis) appears to have allowed the civil servants in the finance ministries to engage in evaluative efforts and policy learning without having to cast themselves in a bad light.

Largely in line with our theoretical prediction E6, we can observe that external actors facilitated policy learning from crisis among the civil servants of the three Baltic countries. In all three cases, developments at the EU level provided a major impetus for policy learning among the MoF officials. The requirements of the Fiscal Compact provided a clear focal point to the officials for modifying their policy beliefs. Although the provisions of the Fiscal Compact were *mandatory* for the members of the Eurozone – and imposed top-down by the EU – our interviews indicate that their adoption has *not* been merely formal and symbolic (i.e. without a corresponding shift in policy beliefs of the local policy actors) but actual normative changes have taken place in the policy beliefs of the civil servants. Still, we can also conjecture that the EU-mandated rules may have, potentially, prevented more *country-specific* fiscal policy discussions and hence also more nuanced policy learning from taking place. In addition to the EU, the IMF contributed significantly to policy learning among the Latvian officials – especially by providing technical knowledge for fiscal policy modelling and forecasting.

In sum, we can see that the theoretical predictions outlined in the analytical framework of our paper do provide a useful starting point for exploring policy learning from crisis among civil servants. As our empirical analysis shows, however, not all of them are supported. This indicates that further theoretical (and also empirical) work is necessary to advance our understanding of whether and how policy learning from crisis takes place.

An important limitation of our study is that we focused only on policy learning by civil servants and not by elected officials, social partners, and think thanks. Given the increasing role of the MoF officials in fiscal policy-making – resulting from the crisis and the increasing technicality of fiscal policy owing to the structural deficit rule – providing insights about the shifts in their policy beliefs is valuable. Future studies could systematically compare policy learning from crisis among these different groups of policy actors. Further limitations of our study are that we have zoomed in on individual rather than on institutional (or collective) policy learning and have not examined to what extent the shifts in the policy beliefs of civil servants have been translated into actual policy change. Further studies would hence be needed to order to map the effects of the crisis on policy change over time.

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