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PREFERENCES, PREFERENCE FORMATION AND POSITION TAKING IN A EUROZONE OUT: LESSONS FROM THE UNITED KINGDOM

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Abstract: *In the literature on member state position taking in the eurozone crisis, the debate has mainly centred on whether national preferences are shaped exclusively within the domestic setting or influenced by shared EU-level norms or interaction within EU institutions. This article goes beyond this discussion. Drawing on original data collected by the authors, it uses the UK's experience to test the claims both of society-centred approaches, including liberal intergovernmentalism, and perspectives that emphasise the importance of shared EU norms or interaction. It argues that, while the first overlook the role of institutions as both actors and mediating variables in preference formation, the second rely have so far focused on the experience of eurozone members thereby raising the possibility of selection bias. Treating eurozone form as a series of processes rather than a single event, it contests the claim that preference formation is always driven by societal interests, highlights instances where government acts in the absence of or contrary to expressed societal interests, and reveals limitations of the shared norms critique of liberal intergovernmentalism. It shows that the UK government was driven by concern to protect the UK economy from financial contagion rather than solidarity with its European partners.*

The positions taken by governments in response to the eurozone crisis provide an important testing ground for competing theoretical approaches to preference formation. Although liberal intergovernmentalism (LI) remains the 'baseline theory' for many (Naurin 2018), critics highlight as problematic its assumption that the domestic arena is insular and emphasise the influence of the wider EU context and shared EU norms in shaping national preferences (Csehi and Puetter 2017, Hall 2012, Zimmerman 2014, Schirm 2016, 2018). Yet the role of top officeholders or institutions in deciding national responses to the eurozone crisis has not yet been fully explored.

This article sets out to assess the claims of both LI and its critics through an analysis of the UK's role during the eurozone crisis. We argue that although powerful economic interests (the City of London) were important, they did not always actively mobilise around the issue and the government frequently adopted preferences at odds with them. We offer two explanations for this. First, during the early phase of the sovereign debt crisis, UK government preferences were developed relatively autonomously by a small group of senior ministers and officials close to the Prime Minister and the Chancellor. Second, as the crisis unfolded, however, important political interests – namely, Parliament and the Bank of England – became central to the definition of UK preferences on eurozone reform. Importantly, the UK's preferences shifted over time, from a position of deliberately distancing the UK from the crisis, to trying to re-set relations with the EU. But we find little concern for EU norms or solidarity.

We make a threefold contribution to the existing literature. First, while LI emphasises a bottom-up view of preference formation in the eurozone crisis, this paper follows scholars who have highlighted the importance of political institutions and strategic calculation by governmental actors (Zimmerman 2014). Drawing on the 'old institutionalism' (Rhodes 2017), which highlights the role of political institutions as actors, it argues for the centrality of government agency and the importance of domestic institutional contexts in accounting for government positions. This top-down perspective stresses that at time governments have significant autonomy from organised societal interests.

Second, the paper challenges the 'new institutionalist critique' (NIC) (Van de Ven and Hargrave 2004: 260) of LI, which asserts from several theoretical perspectives that government preferences are increasingly shaped by EU institutional norms or orientations. The existing literature focuses on the experience of euro area members without investigating whether shared norms extend to eurozone 'outs'. Our evaluation of EU norms in the context of the UK therefore represents a 'tough case' for NIC. Finally, although 'big country' studies of France (Rothacher 2015), Germany (Bulmer 2014, Hall 2012,) and Italy (Bull 2018) exist, analysis of the UK's role during the eurozone crisis remain relatively sparse (Schelkle 2016 and Thompson 2017 are exceptions).

The article uses process tracing to examine the development of the UK's position in four areas, to provide a cross-section of policy cases: emergency measures for Greece, a permanent bailout facility for the eurozone, the fiscal compact, and Banking Union. Our rationale is that the eurozone crisis and eurozone reform need to be analysed as a *process* or processes, rather than an *event*. The analysis of public documents, industry reports and media coverage from this period is supported by eight anonymous interviews with UK politicians, civil servants, and financial institutions.

The discussion is organised into three parts. The first critically reviews LI and other bottom-up approaches, together with the NIC perspective, related to the eurozone crisis. The second section defines our empirical expectations to be tested in the paper. The third section undertakes a process tracing of UK preferences across each of the four cases, before summarising our main findings.

Theorising preferences, preference formation and position taking in the eurozone crisis: a critical overview

Three main theoretical perspectives have been applied to explain national responses to the eurozone crisis: liberal intergovernmentalism (LI) (Moravscik 1993, 1997, 1998); a societal approach (Schirm 2016, 2018); and a 'new institutionalist' critique (NIC) (Puetter 2014, Bickerton *et al* 2015). We review each in turn.

LI and preference formation

LI assumes that governments act purposively in the international arena, but emphasise the critical role of societal actors in defining government preferences (Moravcsik 1997: 516). Defining preferences as 'the fundamental *social* purposes underlying the strategic calculations of governments' (Moravcsik 1997: 513. Emphasis added), LI characterises national preferences as socially constructed and changeable, rather than as fixed and exogenous. Its explanation rests on classical pluralism. Preferences emerge through domestic political conflict: groups compete for influence by articulating their interests, and governments respond to these demands by aggregating them (Moravcsik 1993: 481-3). Hence, '[s]ocietal ideas, interests, and institutions influence state behaviour by shaping state preferences' (1997: 513). In intergovernmental negotiations, the government therefore 'represent[s] some subset of domestic society' (1998: 518).

LI's pluralist foundations have been widely critiqued. Although Moravcsik (1993: 488) suggests that sectoral issue interdependence creates incentives for groups to mobilise, little consideration is given to the conditions under which a government will balance these against other electoral, ideological, partisan or political considerations. Moreover, LI is largely silent on the causal significance of the particular political or institutional channels through which societal interests are transmitted to government. In other words, it downplays the mediating role played by institutions in privilege some societal interest over others (Schattschneider 1960, Tarrow 1996). It similarly overlooks how the powers of different branches of government influence outputs (Eckstein 1979), or how interests and ideas embodied in state institutions shape decision making (March and Olson 1989).

More broadly, LI lacks a coherent theory of the state: i.e. an account of the organisational structure, constitutional rules, established traditions, and accumulated history of the domestic polity. While Moravcsik makes reference to the 'executive', there is no account of how governments interact with legislatures, judiciaries, or state bureaucracies. The distinction between ideational, commercial and republican sub-variants of liberalism could be interpreted as an attempt to recognize and accommodate cross-national differences 'linking social preferences and state behaviour' (Moravcsik 1997: 515). But these categories are insufficiently fine grained to capture how macro-institutional variation in political systems (e.g. presidential vs. parliamentary, majoritarian vs. consensual) shape government preference formation.

Our critique of LI is rooted in 'old institutionalism' (Rhodes 2011) which emphasises the constitutional, political, administrative and symbolic resources available to the main branches of government. From this perspective, political institutions do not simply act as a conduit for societal groups, but are capable of acting autonomously in ways that can directly contradict powerful (economic) interests (Nordlinger 1981). It is our contention that cross-national differences in how power is distributed within national polities, electoral pressures rooted in inter- and intra-party competition, and the influence of well-resourced bureaucratic organisations are critical for explaining government preferences during the eurozone crisis (see Zimmerman 2014).

The societal approach

The 'societal approach' shares LI's emphasis on domestic societal interests, but also underlines the role of institutions and ideas (Schirm 2016, 2018). It defines institutions: 'as formal regulations, which structure domestic political and socio-economic coordination… [It] includes long-term complementarities resulting from domestic regulations that might shape governmental positions towards global governance'. Drawing on historical institutionalism and the 'varieties of capitalism' (VOC) literature (Hall 2014), Schirm (2016: 68) suggests that government positions are 'informed by their calculations of how international rules will affect their ability to sustain designs that are the foundation of economic groups' competitive advantages' (Schirm 2016: 68). Ideas, meanwhile, are defined 'as path-dependent and value-based collective expectations about

appropriate governmental policies'. Societal ideas can express themselves in 'practices', defined as the long-term behavioural expressions of ideational predispositions, which shape the construction of societal interests (Schirm 2016: 68).

Although the societal approach addresses important limitations of LI, there are other plausible conceptualisations. From the perspective of 'old institutionalism', for example, institutions are actors with political and legal resources, not regulations. Also, the institutions highlighted by the VOC literature may account for routine policymaking, but others may be more important at times of crisis (Hall 2014). At the very least, which institutions or institutional arenas are relevant is an empirical question that will vary depending on the political system of the country under consideration. Similarly, the definition of ideas is somewhat stipulative. Scholars have conceptualised the role of ideas in shaping policy in different ways, ranging from 'frames' to 'paradigms' (Hall 1992), or as focal points which enable decisions to be taken under conditions of uncertainty (Garrett 1993). In short, the societal approach fails to adequately explain why its definitions should be favoured over others.

The new institutionalist critique

The NIC perspective provides an important rebuttal to a number of the core claims of LI. The most important critique unifying scholars in this tradition is that shared norms, rooted in the EU as an institutional context, shaped the preferences of member governments during the eurozone crisis (Csehi and Puetter 2017). For example, Mitchell (2014) sees evidence of a powerful

European identity, while Laffan (2014) highlights a norm of responsibility to the collective, in shaping national preferences. Similarly, both new intergovernmentalism (Bickerton *et al* 2015) and deliberative intergovernmentalism (Puetter 2014) emphasise a commitment to consensus through ongoing dialogue between national governments. Equally, 'discursive institutionalism' underlines the importance of a shared policy discourse amongst EU member states (Schmidt 2013).

An important limitation, however, is that the analyses on which these arguments are based draw principally on the experiences of euro area members. Even though scholars report strong evidence of shared norms, selection bias remains a possibility. To address this shortcoming, the causal effect of shared EU norms, collective identity, or a sense of solidarity in the formation of government preferences needs to be applied to the case of non-eurozone members.

Theoretical expectations

This article assesses these theoretical claims by analysing the UK's role during the eurozone crisis. We select four cases to represent a cross-section of the crisis response over a three-year period: (1) emergency action (the Greek bailout in early 2010); (2) long-term measures to ensure the security of the Eurozone (the 2011 negotiations to create a permanent bailout facility for the Eurozone – the European Stability Mechanism (ESM)); (3) the commitment to greater fiscal discipline (the Fiscal Compact negotiated by European leaders in late 2011); and

(4) the move towards Banking Union (the proposal to centralise the supervision of eurozone banks in 2011-12).

With reference to the main theoretical perspectives outlined above, we specify the following empirical expectations:

(1) LI holds that preferences will be shaped by domestic societal interests, mobilised according to issue-specific functional interdependence. Producer interests are typically expected to prevail. Applied to the UK during the eurozone crisis, LI would expect that the interests of the financial sector would be most likely to mobilise and translate into state preferences defended by the UK in intergovernmental negotiation.

(2) The societal approach anticipates that governments adopt positions that are the foundation of economic groups' competitive advantages, but that these cost-benefit calculations can change rapidly, such as in response to economic crises (Schirm 2018: 65). It also predicts that government preferences will reflect path dependent and value-based collective expectations about 'appropriate' governmental policies. Applied to the UK, our expectation is that the government will seek to defend the position of the City of London; but that this will be circumscribed by long-standing beliefs – such as the primacy of the UK's national sovereignty, and the idea of EMU as a flawed political project.

(3) The NIC takes the view that member governments are subject to shared norms or interact in consensus-seeking institutional forums. Applied to the UK,

the expectation would be that the government would support measures that would safeguard the euro. The national interest would be superseded by, or identified in terms of, solidarity with eurozone members.

(4) Old institutionalism is an approach that emphasises the importance of formal political institutions and procedures, and the relative autonomy of state actors from societal interests. As a highly centralised polity, we would therefore expect preference formation in the UK to be shaped by a small group of key actors located within the 'core' executive, close to the Prime Minister (PM) and the Chancellor of the Exchequer.

We test these expectations by drawing on documentary sources, including the positions adopted by the main representatives of the finance sector: the Confederation of British Industry (CBI), CityUK and the British Banking Association, as well as original data from eight interviews conducted by the authors with UK politicians, senior civil servants, officials at the Bank of England, and institutions representing different sub-sectors of financial services. The civil servants interviewed were involved in the formation of UK government policy during key phases of the eurozone crisis. The interviews were semi-structured and included questions about the actors and processes involved in the formation of UK government policy.

The UK and the eurozone crisis

Before we turn to the four case studies, we make two important contextual points. The first concerns the wider economic and political context. The financial and economic crisis hit the UK early and severely, before the intensification of market pressure in the eurozone. The Labour Government, led by PM Gordon Brown and Chancellor Alistair Darling, had responded decisively to prevent the spread of financial contagion in 2008. However, the general election of 6 June 2010 produced a hung parliament. The Conservative Party and the Liberal Democrats immediately began talks to form a coalition government, but it was not until 10 June that Gordon Brown announced his resignation and on 11 June that the Conservative-Liberal Democrat coalition was formed, with David Cameron as PM.

The second relates to the UK's relationship with the EU. Although contestation of the European issue was a longstanding feature of British politics, opinion within Parliament became increasingly eurosceptic after 2010. The number of backbench Conservative MPs openly hostile to the EU increased significantly with the 2010 intake, and they became increasingly vocal with the emergence of the anti-EU UK Independence Party (UKIP) as a significant electoral force. As Conservative Party leader, Cameron had attempted to ignore the European issue but, after 2010, sought to neutralise the issue with the promise of a referendum 'lock' on any further delegation of power to Brussels. However, as Tory eurosceptics became more vociferous, and UKIP's electoral fortunes continued to

improve, he pledged in January 2013 to hold an in-out referendum on UK membership of the EU.

Case study 1: The Greek Bail-Out

In this first case, key decisions were made by a small circle of actors in a Labour government, motivated by concern for the wellbeing of the British economy and occasioned by EU and wider international pressure. UK preferences were not the result of mobilisation by societal interests, nor were they shaped by shared norms within a collective EU executive.

When signs of economic trouble in Greece were initially detected in Whitehall in summer 2009, the UK government was concerned about the likely impact on the UK economy and weakened domestic banking sector in the event of European-wide financial contagion (Darling 2011: 298). However, London did not think it should be financially liable for what it regarded as 'the eurozone's business' (interview 7). The government believed that the single currency was a flawed project for which it bore no responsibility, and conscious that the UK had successfully navigated its way through the financial and economic crisis (interview 6).

Although preoccupied with a domestic election and its own crisis response measures, the government recognised that periphery countries would need financial support to manage sovereign debt problems (interview 7). The key decisions were taken by the PM in consultation with the Chancellor and HM

Treasury, and to a lesser extent the Foreign and Commonwealth Office (FCO) (interviews 4, 7). The PM and HMT were firmly against providing direct assistance to Greece, but the FCO was keen to demonstrate that the UK could be 'good partners' and 'show solidarity' during the crisis (interview 6). Rather than provide financial assistance, it was therefore agreed that the UK should offer technical assistance to the Greek government – an offer, tellingly, that was never taken up (interview 5).

At an informal summit of euro area heads of state in February 2010, member states were divided (Hodson 2015). The UK, with Sweden – also outside the euro area – wanted financial support for Greece to be channelled through the International Monetary Fund (IMF), but was primarily concerned that the UK would not be financially liable for a bailout of Greece (interview 6). They were opposed by euro area member states, including France and Spain, who wanted a European response (Hodson 2015).

The UK government reiterated its position at an IMF Executive Board discussion in April 2010 (interview 4), but the IMF demanded EU participation (Pisani-Ferry et al. 2013).There was also a developing consensus among euro area member states that a community response to the crisis in Greece was necessary (interviews 4, 7). Ways of financing support for Greece were discussed by the Eurogroup in early May 2010, and it was agreed that, in the absence of dedicated mechanisms to deal with such circumstances, the euro area would provide support under G7+1 that would be administered by the European Commission. Although the UK government disliked the associated institutional arrangements

because they required an arrangement outside the treaties -- a so-called 'Bangladesh agreement', (interview 7) -- the UK joined the other member states in approving support to Greece and agreed to the Commission's role as an administrator of the bailout package.

The UK's concern that it should not be financially liable lay behind its opposition to the Commission's initial proposals for the creation of a European-level stabilisation fund with a lending capacity of around 500 billion euros (interview 5). While the UK considered the scale of resources appropriate to what might be needed to stop contagion spreading to Greece, Portugal and possibly Spain, it was unprepared to accept the Commission's proposal that the mechanism should be an EU budget facility. Appeals by the Commission for the UK to financially underwrite the currency through its own contributions were met with a strong rebuttal from the UK Chancellor (Darling 2011: 301). The UK also objected to use of Article 122(2) TFEU, allowing credit to be granted to a member state facing 'severe difficulties caused by natural disasters or exceptional occurrences beyond its control', to assist a country facing balance of payments difficulties (interview 7).

The EU, however, came under mounting pressure. The G7, and especially the US through Treasury Secretary, Timothy Geitner, insisted that the EU take immediate 'shock and awe' action to stem panic in European markets (Financial Times 2010). Following an acrimonious twelve-hour meeting of the ECOFIN Council on 9-10 May 2010, the UK reluctantly agreed to a loan agreement with Greece and the creation of a stabilisation fund composed of two elements

(interview 7). The EFSF was to be a fund of 440 billion euros guaranteed by the eurozone countries alone, but the UK was concerned that euro area countries would not be able to raise the guarantees they needed, which would leave the UK liable for a maximum of 6.6 billion euros under the EFSM (interview 6), a 60 billion euro facility guaranteed by the EU budget (Pisani-Ferry et al. 2013:17).

Despite the UK's strong reservations, there was an awareness in London that, since decisions under Article 122 (2) were taken by QMV, 'the UK could not block it' (interview 6). The decision also came at a difficult time for the UK. Since a new government had not yet been formed, the outgoing Labour Chancellor represented the UK in the negotiations (Darling 2011: 298). Although he had cleared the decision not to vote against with future Chancellor, George Osborne and a key figure in coalition talks, Vince Cable,[1] the precise terms of the conversation became controversial: first, when the new PM David Cameron criticized Darling and Labour on the grounds that the UK was potentially liable, and second when eurosceptic MPs John Redwood and Douglas Carswell, who strongly opposed any UK liability for problems in the eurozone, used it as political capital (House of Commons 2010).

Case study 2: The European Stabilisation Mechanism

In autumn 2010, the UK was becoming increasingly frustrated by the EU's failure to provide a lasting solution to break the 'doom loop' that had taken hold

[1] Cited from official note of the conversation (interview 5).

between banks and sovereigns in the eurozone: 'We were worried that fire from the burning house would spread to the UK', one senior official recalled (interview 7). The UK tried to persuade Chancellor Angela Merkel and the President of the European Central Bank (ECB), Jean-Claude Trichet, to allow member states to borrow at more attractive rates, but both were reluctant (interview 5). The US and China also made clear their views that the eurozone needed an enlarged bailout fund or commitment by the ECB that it would enable a 'lender of last resort' function (Reuters 2010).

Although Trichet rejected any idea that the ECB would become a lender of last resort, the Deauville compromise – a bilateral agreement negotiated by Chancellor Angela Merkel and President Nicolas Sarkozy in October 2010 – cleared the way to an enlarged ESM (Howarth and Quaglia 2016: 168). However, the UK government was concerned by Germany's insistence that an enlarged stabilisation fund would require amendment of the treaty (interview 7). Even though the simplified revision procedure under Article 136(3) would apply, Cameron would have to navigate the amendment through the House of Commons, where the 2010 intake of Conservative MPs was markedly more eurosceptic (House of Commons 2010: 4-6). Moreover, although the Conservatives had formed a coalition agreement with the Liberal Democrats, Cameron had tried to appease the eurosceptic wing of his party with a legislative commitment to hold a referendum in the event of any proposal to transfer further powers to the EU (Financial Times 2010). The appointment of veteran eurosceptic MP, Bill Cash, as chair of the EU select committee in the House of Commons, intensified scrutiny of the government.

On 28-29 October, the European Council (2010) agreed on the need to establish a 'permanent crisis mechanism to safeguard the financial stability of the euro area as a whole'. Cameron's focus was on securing a quid pro quo for the political risk he would be taking. However, attempts by the UK government to leverage a deal on the EU budget or to use an amendment of the treaty to return selected powers to the member states gained no traction (interview 6). Cameron managed eventually to secure an understanding that, once the ESM was in place, the EFSM would no longer be used for bailouts of eurozone member states (European Council 2010a). As one UK official noted: 'That was the big prize for us. To ensure that the ESM could come into play and stop the use of the EU budget' (Interview 6). Cameron was able to announce to Parliament that: 'Britain is not in the euro and we are not going to join the euro, and that is why we should not have any liability for bailing out the eurozone when the new permanent arrangements come into effect' (Gov.UK 2010).

The amendments won at the December 2010 European Council enabled Cameron to argue that he had fixed a problem inherited from his predecessors. He could also argue that the ESM was not a temporary guarantee, but an IMF-styled fund with increased financial firepower to safeguard stability – 'real cash which could be borrowed against' (interview 2). As the PM underlined, 'enabling eurozone countries to establish such a mechanism is in our interests' (Gov.uk 2010). Even if the negotiations on a permanent stabilisation fund had forced the UK government to risk bringing a treaty revision before parliament, the final agreement on the ESM solved the problems created by the EFSM.

In this second case, there was again no evidence of extensive lobbying by powerful societal interests, including the City of London. Financial industry lobby groups certainly produced several reports on the eurozone crisis and the implications of reform.[2] But, as a senior regulator noted, these carried little weight within government because 'they did not pay enough attention to what was politically realistic, or what the intentions of the key players were going to be' (interview 5). As a consequence, 'the City was quite weak in terms of its ability to influence the government's position' (interview 2).

There is also little evidence that the UK's position was shaped by shared norms: rather, the UK's main priority was to insulate its economy from eurozone contagion. The UK position was defined by a Conservative PM and Chancellor who enjoyed significant autonomy to shape EU policy during the twelve-month 'honeymoon period' of the Coalition Government (interview 2). This began to change in the second half of 2011 as it became clear that the sovereign debt crisis could not be contained in Greece. Although the government easily secured parliamentary approval for the ESM, it also triggered backbench opposition from a more Eurosceptic intake of MPs, hostile to any financial liability for bailing out eurozone members.

[2] For example, 'Balance of Competences Review – Economic and Monetary Policy', International Regulatory Strategy Group, 10 July 2014; 'Eurozone Caucusing: A challenge to the European single market?', British Bankers' Association, June 2014.

Case study 3. The Fiscal Compact

As economic conditions in the Eurozone deteriorated in 2011, London's attempts to remain detached from the crisis were increasingly thwarted. Neither Osborne nor Cameron wavered from the view they formed in May 2010 that the 'eurozone crisis is bad for us' (Interview 5). But fourteen months later, Osborne signalled a shift in UK strategy by endorsing the 'remorseless logic' of monetary union (Financial Times 2011). By accepting the need for fiscal union, Osborne's intervention reversed the UK's longstanding opposition to a two-speed Europe. This about-turn was prompted by a deepening frustration at the *ad hoc* responses of the eurozone countries to the crisis, and failure to address underlying deficiencies in the single currency's design (House of Commons 2013: 35-42). The speech was spearheaded by HMT and the PM, who regarded financial stability as the main priority, and believed that the UK could not legitimately try to shape further eurozone integration if it was not willing to participate (interview 4). It met some resistance from the FCO, concerned that official acceptance of a two-speed Europe would undermine UK diplomacy by no longer having a 'seat at the table' (interview 4).

In November 2011, the government secured support for a bailout to Ireland, even though it drew on the controversial EUR 60 billion facility agreed in May (Financial Times 2011). The government was also able to extend a bilateral loan of £7 billion as part of an international rescue package to the UK's nearest neighbour. To the surprise of some in Whitehall, the measure passed smoothly through Parliament (interview 4). To secure approval, however, Osborne had

pledged that the UK would not participate in any permanent bailout mechanism for euro area countries (Financial Times 2010).

The worsening crisis in 2011, and continuing lack of decisive action by eurozone states, reduced the UK government's room for manoeuvre by fuelling euroscepticism in Parliament and in the country (interview 7). The UK chose to remain largely on the sidelines. It was not involved in any of the Euro Summits in 2011, and was not a signatory to agreements strengthening economic governance, such as the Euro Plus Pact (Hodson 2012).

When Portugal requested assistance in spring 2011, however, the UK supported the use of the EFSM and briefly contemplated a bilateral loan (Gov.uk 2011). While a parliamentary vote was not necessary, the measure had to be presented to the European Scrutiny Committee in the House of Commons where it met significant opposition. In July 2011, as the crisis threatened to engulf Italy and Spain, Conservative eurosceptics joined with Labour MPs to vote against increased funding for the IMF on the grounds that British taxpayers' money would be used to bail out the euro and the UK would be complicit in imposing austerity on Greece (House of Lords 2012). The rebellion came as a shock to the government, which had assumed that there would be cross-party support on IMF involvement (interview 4). Shortly afterwards, in September 2011, around 100 Conservative MPs signed an Early Day Motion calling for a discussion on the eurozone crisis and a referendum on the Lisbon Treaty (Hodson 2012: 189-190).

Under increasing pressure from Parliament, Cameron sought to turn the eurozone crisis to his advantage by seeking to leverage the prospect of EU treaty reform to repatriate powers to member states (Thompson 2017). As announced by Foreign Secretary William Hague to Parliament in October 2011, the government's top priority would be to 'protect the rights' of countries outside the euro area, and to secure protections to 'prevent damage' to the financial services industry (House of Commons Debate 2011). The opportunity appeared much sooner than expected when Germany called for a treaty change to adopt measures that later became the Fiscal Compact.

Cameron met Chancellor Merkel to press his own demands for an amendment that would redefine the UK's relationship with the EU. Having been advised by the Legal Service of the Council that ratification by all 27 member states was required, Cameron believed the government had negotiating power (interview 5). When he was rebuffed, he tried at the December 2011 European Council to secure a veto over future EU financial regulation, but when this effort failed, the PM vetoed treaty reform, forcing EU leaders to agree the Fiscal Compact in the form of an intergovernmental treaty. Although welcomed enthusiastically by eurosceptics at home, the veto undermined the government's attempt to reset UK-EU relations (House of Commons 2013: 20-31).

The UK veto was widely interpreted at the time as a defence of the interests of the City of London. In reality, our interviewees argued that the preferences of the UK government were out of step with the financial industry. The City was not consulted on the 'wishlist' of special protections demanded by the government in

its name, and resented becoming a 'poster child for the December veto' (interview 2). Senior industry figures regarded Cameron's strategy as 'caustic', since it would damage London's standing as a financial centre, and told Treasury ministers that the UK's demands were 'misguided or unnecessary and liable to backfire' (Financial Times 2012). Leading figures argued that the UK needed to 'embrace' greater EU regulatory harmonisation to ensure London remained Europe's main financial centre (TheCityUK 2014).

Moreover, the City interpreted Cameron's demands for a UK veto over future EU regulation as an attempt to defend the autonomy of financial regulators, not the interests of the financial industry. According to an internal City report: 'The protocol would not have protected the City and appears rather to be an attempt to protect HMT's view of how the City should be regulated by national authorities with wide discretionary powers, unhindered by EU rules…If it were to be accepted by other member states it might actually damage the City' (TheCityUK 2014). Similarly, a senior Treasury official confirmed that the UK's priority was to defend taxpayers and the tougher prudential rules introduced in the wake of the banking crisis: 'We wanted to maintain as much control and supervision over the City as possible… which the City disliked since UK authorities may be stricter' (interview 2). This led City lobby groups to mobilise alongside their French and German counterparts *against* the UK government in support of the Commission's proposal for the maximum harmonisation of EU bank capital standards. It provoked Sharon Bowles, then Chair of the Economic and Monetary Affairs Committee in the European Parliament, to suggest that the

UK government was actually seeking ‘protection of taxpayers *from* the City’ (quoted in Schelkle 2016: 160).

In this third case, the mobilisation of societal interests was again largely absent as a driver of preferences. The City of London was not even consulted in advance of the December 2011 summit on the list of special protections that Cameron demanded on its behalf. Rather, the UK’s position was decided by the PM and the Chancellor, both of whom wanted a long-term solution to the eurozone crisis. The government’s room for manoeuvre was, however, increasingly limited by both Parliament and the Bank of England. Despite its policy reversal on the eurozone, which seemed to betoken a new solidarity with members of the euro area, the UK government continued to prioritise the defence of UK regulatory autonomy from potential encroachment from new eurozone institutions.

Case study 4: Banking Union

Banking Union highlights the interconnectedness of the EU single market and the eurozone. Although outside the euro area (Schelkle 2016; Thompson 2017), the UK was home to the largest financial centre in the EU and transacted the bulk of euro-denominated trading in derivatives. This made it difficult for the UK government to remain aloof.

Banking Union presented an opportunity for the Cameron government to play a more positive role, and thus repair some of the damage from the December 2011 summit. It ‘helped a bit with the feeling that we were trying to wreck the

[eurozone] project' (interview 7). The UK had long argued that the eurozone needed to do more to address the fragility of its banking system (Howarth and Quaglia 2016). Germany signalled willingness to consider using the ESM to recapitalise the banks, but also wanted stronger centralised supervision in the euro area. This presented the UK with a difficult choice. On the one hand, Banking Union risked fragmenting the single market, encouraging caucusing of 'ins' against 'outs', and creating powerful new agencies in Frankfurt that could come to dominate EU decision making on banking issues. On the other, opposition risked contributing to the crisis and forcing the EU into strengthening the European Banking Authority by converting it into a single supervisor for the entire EU – the UK included.

The UK eventually settled in favour of euro area Banking Union, reflecting the prevailing views of senior figures within the Treasury and Bank of England. From their perspective, the ECB should serve as the single supervisor because the largest under-capitalised banks were located predominantly within the euro area. Although full membership was ruled out, there was 'some consideration' in the Treasury about whether the UK could have some form of 'associate or cooperative membership'. But the Chancellor and the Bank Governor recognised that this 'just wasn't going to work' given the size of the UK financial sector and the terms of the domestic debate on Europe.

The City supported Banking Union as it would contribute to financial stability, and welcomed the UK government's determination to safeguard against future eurozone caucusing (BBA 2014). But this masked internal divisions over what

the UK's relationship with the new Banking Union should be. Large parts of the industry 'had a more relaxed view of shared sovereignty', feared the implications of a UK veto over a single European supervisor, and preferred the UK to be actively engaged in shaping eurozone integration 'from within' (Financial Times 2012). Some prominent UK banks went so far as to advocate full UK membership of Banking Union on the grounds that centralised supervision would reduce compliance costs, and might even be based on 'lower standards' (interview 5). But this position was firmly resisted by senior regulators: 'Some people in the City said, somewhat surprisingly, that the UK should be part of the Banking Union. But we were always very clear that we could not be in a position where we were handing supervision of our banks to an entity that we were not in control of. So that was a non-starter and became a defensive issue for us' (interview 2).

As in the previous three cases, financial industry lobbying had little impact in shaping the UK's position. A minister at the time commented that the City 'was backward in coming forward', reflecting the diversity of perspectives from different parts of the sector. Moreover, the City took its own importance 'for granted', assuming that financial industry preferences were shared by UK ministers (interview 6).

Despite the UK's decision not to join, an official closely involved in the negotiations revealed that 'behind the scenes', the UK 'played a very significant part in helping to think through how this could be designed' (interview, June 2018). In the negotiations, the UK secured a number of concessions, including

the principle of non-discrimination and the exclusion of Central Counterparty (CCP) supervision. But its key concern was to address the risk of future eurozone caucusing within the EBA, which could lead to the UK being permanently outvoted. The UK challenged the Commission's initial proposals for revising the EBA's voting procedures, and instead proposed the use of 'double majority decision making' to require a majority of both members and non-members of the Single Supervisory Mechanism. Although it secured an agreement along these lines in December 2012, it was a further twelve months before the Commission finally accepted the UK's proposal.

In this case, the UK government offered conditional support. Cameron insisted that Banking Union should be a eurozone-only entity, with bank supervision centralised under the ECB (rather than the EBA). The UK's position therefore reinforced the logic of variable geometry that Osborne's 'remorseless logic' speech had explicitly endorsed. Interests in the City were broadly sympathetic, although many of the largest financial firms would have preferred an even closer attachment. However, neither Conservative MPs, nor the Bank of England, were willing to countenance the prospect of the City being supervised from Brussels or Frankfurt. There is also little evidence that UK preferences were shaped by shared norms within an EU setting. Rather, the UK was first and foremost concerned to protect the UK economy by facilitating strengthened eurozone governance. Nonetheless, once the UK's conditions had been met, it was willing to play a more constructive role (albeit in private) by providing technical assistance to the Commission in designing Banking Union.

Findings and discussion

The UK's approach to the eurozone crisis challenges theoretical expectations on both sides of the debate. Contrary to LI, the positions adopted by the UK were not simply derived from long-standing preferences that were transmitted by powerful economic interests, then aggregated by government. The City was certainly important in shaping UK preferences during the eurozone crisis, but not in the way specified by the LI. We point to three findings. First, there is little evidence that the UK financial industry lobbied extensively around any of the four issues examined in the paper. Instead, City lobby groups made a conscious decision to remain on the sidelines. Second, while UK government preferences reflected the underlying interests of the financial sector with respect to the Greek bailout and the ESM, perversely this was from a position of economic vulnerability, not strength. In other words, the City's influence reflected its exposure to eurozone banks and as a potential transmission mechanism for contagion to the wider UK economy. Third, on the issue of further eurozone integration, the UK government's preferences either lacked support from the City (e.g. non-participation in Banking Union) or were heavily criticised (e.g. Cameron's demands for special protections for the City).

Our explanation of this is twofold. First, during the early phase of the eurozone crisis (2010-11), the Conservative-Liberal Democrat coalition was able to develop its preferences autonomously. UK preferences were developed within government by senior ministers and officials close to the Prime Minister and the Chancellor. Few other government ministers were involved, Parliament showed

little interest, and domestic interests had not mobilised (interviews 1, 2). However, as eurozone contagion spread and attention turned to more fundamental reform, such as the ESM, Fiscal Compact and Banking Union, the autonomy of this small group became circumscribed as new groups mobilised around the issue. In particular, the concerns of the financial industry were frequently 'crowded out' by more pressing demands from powerful political and institutional interests. Specifically, the role of backbench Conservative MPs, frequently allied with Labour MPs, was critical in constraining the government's capacity to agree to any further transfer of power or financial resources to the eurozone. Similarly, the influence of the Bank of England was felt in the Banking Union when it demanded special protections to ensure that UK regulators retained authority to regulate the City.

Moreover, the UK's position changed over time. The government continued to re-adjust its position in response to pressures from the EU level. During the early phase of the crisis, the UK government sought to distance itself. However, once it became clear that the UK would not be isolated from the effects of the crisis, it feared direct contagion. The UK government was also aware that the EU's failure to take decisive action was fuelling rising euroscepticism at home. This domestic vulnerability was an important driver of Osborne's attempt to recast UK-EU relations through his endorsement of the 'remorseless logic' of euro area integration.

This strategy was undermined, however, by the increasing activism of Parliament. In an effort to manage these political pressures, Cameron sought to

exploit the crisis by trying to extract, first, a treaty amendment to repatriate powers, and second, specific protections for a key UK economic sector. His failure to do so, which was exposed at the 2011 summit, undermined the UK's reputation with EU leaders by appearing to place the narrow interests of the financial sector above the survival of the eurozone. On Banking Union, it was in the UK's interests to play a positive role, given the exposure of the City to the fate of euro area banks. But, given an increasingly hostile political climate, this had to be done privately and away from parliamentary scrutiny. The goodwill generated helped the UK to secure a significant, if ultimately short-lived, victory over the EBA's voting procedures.

UK preference formation and position taking also contest the NIC contention that government responses to the Eurozone crisis can be explained in terms of a European preference, shared norms or values, or deliberative institutionalism. Although the UK expressed a desire that the EU take the necessary measures to ensure the stability of the eurozone, it did so primarily out of concern for the British economy. The UK was motivated more by economic self-interest and domestic political calculation than solidarity with its EU partners. Its support for EU action to safeguard the eurozone was strictly limited, especially in the early phases of the crisis when London's main concern was to limit UK liability: 'We did not want the eurozone to fail, but at the same time we did not want to pay for it' (interview 7).

Only to the extent that the UK sought to defend the rights of the single market as a whole, and the interests of the other euro-outs, could it claim to be acting on

the basis of solidarity. As the institutional architecture of the euro area was reformed and recast, the UK grew increasingly marginalized as a euro out. It became increasingly concerned about the spillover of fiscal, financial and banking matters into eurozone territory, especially when its insistence on a strict division of labour between the Eurogroup and ECOFIN proved difficult to sustain, not least because of its interests as a contributor to the programmes supporting Ireland and Portugal. Moreover, evidence of solidarity amongst euro-outs is hard to find. The UK did seek to strengthen ties with other 'outs', particularly Poland and Sweden, on the issue of Banking Union (interview 2), and Cameron spent considerable time trying to cultivate relations with Chancellor Merkel in Germany (interview 4). But the strategy ultimately failed. Although the UK wanted to safeguard its interests from euro caucusing, other non-members who regarded themselves as 'pre-ins', but also Denmark and Sweden, saw this as less of a problem. The decision by many 'outs' to join the EU's strengthened economic governance arrangements, including the Fiscal Compact and Banking Union, exposed the UK as an outlier.

Conclusion

The above examination of how the UK formulated its position to how the EU should respond to the eurozone crisis contributes to the debate on how national approaches are best theorised in three ways. First, it underlines the importance of understanding national responses not as a single event, but as multiple strands. By demonstrating that the same government can approach different

elements of eurozone reform very differently, it challenges the assumption that there is a single explanandum when examining national responses to the crisis.

Second, the UK case illustrates a shortcoming of LI that has not been reflected in recent literature on the eurozone crisis. Although there has been intense debate on the relative status of preferences and positions, the conceptualisation of preference formation as a society-led process has not so far been questioned. Since UK positions were often decided by a small circle of top politicians in the absence of significant interest group mobilisation, the UK case demonstrates that LI has limited explanatory purchase in countries where the state can act with greater autonomy from societal interests. The main constraints on the UK government were imposed by political (Parliament) and bureaucratic (UK regulators) interests, which is not foreseen by LI.

Taken together, these two findings support the argument made above that an account of preference formation needs to be sensitive to state-society relations, different models of interest intermediation, and the respective power and resources of domestic political institutions. These variables, which are core to the old institutionalism, are absent from LI. In the latter's pared-down conception of the domestic arena, which reflects the flawed premises of classic pluralism, the only actors are societal interests and the state executive. Such a limited conceptualisation of the domestic setting does not capture the factors that the UK case have shown to be important, nor does it provide a basis for understanding or explaining cross-national differences.

Third, the UK case provides a counter-example to the NIC of LI. Although critics have argued powerfully that member state preferences in regard to the eurozone crisis were shaped by shared norms and interaction within EU institutions, evidence has hitherto been drawn from euro area members. The UK case shows that membership of the eurozone area may be an important scope condition.

The article thereby advances the central aim of the special issue. As well as problematizing preferences and preference formation, it has contributed an additional country case study, and suggested new avenues for future theorising. We conclude that focusing on the 'old institutionalism' of formal institutions, procedures and power within polities can provide important added value when seeking to explain variation in national government responses to the eurozone crisis.

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