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Austria: stable society and crisis-exposed banks

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Abstract:

Austria passed through recent crises relatively unscathed, although its banking sector remains vulnerable to shocks. Austria is the wealthiest EU country, with some of the highest living standards and lowest unemployment. As in many past crises, its unique system of a social partnership coordinating its economic and social policies served it well, despite increasing internal and external tensions that put it under pressure. During the two decades of its EU membership, Austria was more exposed to external shocks as its economy in general and banking sector in particular became more open. Austrian authorities managed to reduce the destabilizing effects of financial contagion and contributed to coordinated international responses to the financial crises. At the same time, the crisis experience undermined public support for European integration, as is indicated by the 20 per cent of votes for the populist right in the recent national and European elections. Nonetheless, the government remains broadly pro-European and support for EU policies and reforms is above the EU and Euro area averages.

Contents

INTRODUCTION

The impact of recent crises on the political discourse, as well as economic indicators, is clearly discernible in Austria, although it is one of the least affected countries within the European Union (EU). The country recently returned to the top of the list of wealthiest European nations, with high living standards and low unemployment (Eurostat 2014a). As in numerous past crises, its unique system of social partnership served it well. At the same time, there are signs of growing strains that put the long established patterns of cooperation under pressure. During the last two decades of its EU membership, Austria became ever more closely integrated with neighboring countries and the global economy. It is one of the largest beneficiaries of the single market, which allowed its firms to expand and succeed especially in the post-communist member states that joined the Union after 2004 (Breuss 2013, Petersen et al. 2014). However, the integration also created potential for cross-border contagion as shocks from other economies and financial sectors propagated towards Austria. Similarly, although the free movement of workers has benefited the Austrian society and economy, it has also created tensions that manifest themselves in support for anti-immigration policies (Dolezal and Zeglovits 2014, Aichholzer et al 2014).

Austrian authorities managed the recent crises rather well, proving their reputation of pragmatism and cooperation. The unique system of social partnership that manages internal conflicts, coordinates social and economic policies, and maintains external competitiveness of Austria, proved to be well adapted to the Euro Area circumstances. It allowed the country to reap the benefits of the single currency while avoiding the risks that plagued many of the Southern members. At the same time, the Euro crisis and migration pressures undermined public support for traditional political parties that form one of the key pillars of the social partnership system. The 2013 elections might be the last instance where the traditional parties of the 'grand coalition' achieve a majority. This trend was also borne out by the 2014 European elections that confirmed support for smaller parties, including the populist right.

In 2015, Austria celebrates twenty years in the European Union, where it quickly attained a place among the core countries. Its political stability, robust economic performance as well as policy-making capacity enabled it to shed its newcomer status, despite occasional setbacks such as the informal sanctions imposed by other EU members in 2000 after the right-wing populist party entered the government (Falkner 2001). In the EU, Austria is particularly active in environmental policy, financial crisis management as well as in matters related to enlargement and neighborhood policies.

This paper is structured according to the outline summarized in the introductory chapter of this volume (Pirro and Zeff 2015). The first two sections briefly summarize the influence of the EU on Austria and vice versa. The third section reviews Austrian responses to the recent crises, with particular emphasis on the banking sector, which proved to be the most important source of instability. The fourth section outlines the consequences of the crisis experience for the perceived practicality of federal and confederal models of European integration as outlined in Pirro and Zeff (2015). The final section summarizes the key conclusions.

THE EU INFLUENCE ON AUSTRIA

Austria has developed a unique system of governance that relies on a strong public sector, extensive social partnership and consensual policy-making (Traxler 1998). This system was at the core of Austria's transformation from a poor country during the inter-war period to one of the richest European countries today (Nowotny 1993). It facilitated its adaptation to the EU and Euro area membership and enabled it to take advantage of EU membership opportunities while also managing related risks. At the same time, globalization and Europeanization as well as change in Austrian politics has put the system under increasing pressure.

The social partnership is the core institution of 'democratic corporatism' (Katzenstein 1985), which provides formal institutional representation for workers, employers, farmers and other unions through chambers with compulsory membership. All positions in each chamber are filled through democratic elections (OECD 2013:94). Their primary task is wage bargaining, but negotiations cover issues of cooperation on technical innovations, education and vocational training (Crouch and Traxler 1995), as well as management of public services, administration of the social security system, pensions and family policies. The law then requires the government to consult with social partners on all economic and financial issues before it presents any legislative proposals (OECD 2013:94). Consultations are highly regularized; hence, actors can rely on informality and confidentiality, which increases the chances of arriving at a consensual solution likely to be accepted by respective social partners and in the parliament.

The social partnership is also instrumental for the management of the public sector that is one of the largest in the EU - 47 percent of annual GDP (OECD 2013:91). It offers comparatively generous social transfers, a complex network of public services as well as a comprehensive regulatory framework covering many aspects of life. A dense, multi-level system of federally, Länder and locally funded organizations dominate all segments of public services from education, health care and kindergartens to collective housing, public transportation and environmental protection. The public sector is a key contributor to the high standards of living (OECD 2013:94). Despite growing concerns about its inefficiencies (Fischer et al. 2011) and related corruption scandals (Dolezal and Zeglovits 2014), the arrangement continues to be endorsed by society (OECD 2013:95).

Wage bargaining is at the heart of the social partnership. It guarantees modest minimum standards but provides considerable upward flexibility, which is reflected by large wage differences between sectors, enterprises and job types (OECD 2013:94). It traditionally follows the lead of the metalworking industry that sets a benchmark for other sectors, regions and enterprises. Since this sector is exposed to German and global competition, it keeps the benchmark wages aligned with productivity and prevents unit labor costs from deteriorating to uncompetitive levels (Scharpf 1987). The close integration with German and other EU economies and participation in the European Economic Area that transferred most of the EU's economic aquis prior to 1995 membership, explains the ease of economic adaptation to the single market. The necessary reforms focused on modernization of the public administration and upgrading personnel skills necessary for functioning within the EU's multi-level governance (Falkner and Hunt 2006).

Austrian EU membership coincided with the onset of the Eastern enlargement process that brought eleven post-communist countries - many of them immediate neighbors of Austria - to the EU. This presented Austrian firms with new competition, but also enormous opportunities. They became one of the most active participants in the privatization and restructuring process in the post-communist countries. Many medium-sized firms became regional multinationals when they took control of major firms in manufacturing, retail distribution, telecommunications, utilities and banks across Central and Eastern Europe (CEE). This expansion also prevented foreign takeover of Austrian firms, which tend to be small by global standards, by larger multinationals. More importantly, it allowed them to extend production and supply chains to countries with substantively lower labor costs, which was instrumental for their sustained global competitiveness.

The entry of low-wage and low-tax CEE economies into the EU induced some internal reforms as well. Social partners agreed to reduce corporate taxation and the overall tax burden (OECD 2013:96), while ensuring that the combination of competitive advantages - such as political stability, efficient administration and the good quality of education and vocational training - motivated domestic firms to keep the high value-added operations in Austria and limit outsourcing to the labor-intensive, lower-value added parts of the production process.

Maintaining these advantages remains high on the agenda, as illustrated by the increase in research and development funding at the onset of the financial crisis (EUI 2011).

At the same time, evolving EU rules continue to erode some traditional competitive advantages. In 2014, after sustained pressure from Germany and other EU countries, Austria - together with Luxembourg - finally agreed to stop vetoing the EU tax transparency scheme. This will undermine the bank secrecy rules that allowed foreign bank customers to keep untaxed funds in Austrian bank accounts. Similarly, many utility industries that were sheltered from competition before Austria's EU membership are increasingly liberalized and exposed to competition within the EU and globally.

The single currency is the third most important source of EU influence on Austria after the acquis communautaire and enlargement. The country was well prepared due to historical links with Germany with which it formed a de facto monetary union because the Austrian Schilling had been pegged to the Deutschmark since the 1980s (Traxler 1998:258). Austria complied with the Maastricht criteria and joined the single currency in the first wave. The central bankers, managers, entrepreneurs and trade union leaders were all used to operating within the confines of hard currency policy and low inflation. The social partnership system is traditionally benchmarked to German policies, which keeps the wage raises broadly in line with productivity increases. Hence, it prevented any buildup of macroeconomic imbalances and competitive disadvantages that recently undermined the Southern Euro area economies.

Overall, the economy was well positioned to deal with the challenges of EU membership, Eastern enlargement and the Euro. Austria entered the Union as the country with the highest standards of living, to be outperformed by Ireland, Denmark and Netherlands during the pre-crisis decade (Eurostat 2014a). However, since all other EU economies suffered more during recent crises, Austria returned to the top in 2012 (Eurostat 2014a). Similarly, throughout its EU membership, Austria was always among the 5 EU countries with the lowest unemployment. Since 2010, it has the lowest unemployment in the EU and, along with Germany, the lowest youth unemployment. At the same time, even the lowest figures in the EU represent the highest rate of unemployment that Austria has experienced since 1960s (Eurostat 2014a).

However, maintaining the high living standards and low unemployment coincided with persistent public finance deficits and growing indebtedness. Ever since Austria entered the EU its government finances were always in deficit and in five separate years exceeded the 3 percent Maastricht limit. The public debt grew from around 68 to 75 percent of GDP, although just before the crisis it almost reached the 60 percent Maastricht limit - 60.2 percent of GDP in 2007 (Eurostat 2014a). The public finance data indicate a need for fiscal consolidation, which will present a renewed challenge for the social partnership. This will come on top of the increasing strain within the society, which has already been manifested in recent election results.

The unique system of social partnership was traditionally supported by a stable party system, dominated by the center-left social democrats (SPÖ) and the center-right People's party (ÖVP). During the post-WWII decades, these two parties typically governed together in a 'grand coalition' with a large majority (Rose 2000). However, in the 1999 parliamentary elections, the SPÖ suffered a heavy defeat, to which the ÖVP responded by forming a coalition government with the populist right-wing Freedom Party (FPÖ). This led not only to the imposition of informal sanctions on the Austrian government by the remaining EU members, but also to the undermined effectiveness of the traditional social partnership (OECD 2013:96). The sanctions faded quickly, although the uneasy coalition lingered for nearly seven years (Falkner 2001). The restoration of the 'grand coalition' after 2006 elections stabilized the traditional arrangement again.

However, long-term challenges to the social partnership persist. As the shift of competences from the national level to the EU level intensifies in response to the Euro crisis and other developments, it leaves the social partners in Vienna with a decreasing number of policy options (Scharpf 2010, Fernandes and Maslauskaite 2013). Moreover, the increasing diversity of the Austrian economy and society makes it more difficult to capture and reflect interests of important social groups within the traditional institutions of the social partnership. An increasing proportion of voters, including those with a migration background, feel underrepresented and excluded from the system, which often motivates their voting against established parties. Moreover, there is a growing concern about corruption among political elites (Dolezal and Zeglovits 2014).

In the past, groups such as the liberal professions, civil servants or bankers were able to free-ride on the moderation policies of social partnership (Nowotny 1993:14, Mayer et al. 2001). They could increase their nominal income above average while profiting from the low inflation secured by the system as long as they remained small enough. Disproportional wage increases of some groups undermine the solidarity among the traditional social partners, which is necessary for wage moderation and sustained competitiveness. Moreover, free-riding groups in important sectors - such as banking - may impose additional costs on firms in important export sectors, thus harming their productivity and competitiveness as well as eroding the purchasing power of households (OECD 2013:96). Hence, it is crucial to maintain and extend the inclusiveness of the chambers and parties, to prevent accumulation of benefits to politicians and privileged groups. The most recent elections suggest that nearly half of the electorate seems to think that the established elites are failing at this task.

The 2013 parliamentary elections resulted in an all-time low vote for the parties of the grand coalition - the SPÖ and ÖVP. They defended their combined majority by a margin of 0.8 percent, while a quarter of the vote went to the populist anti-establishment parties with an anti-immigration and anti-EU agenda. The election campaign was dominated by the issues of economy, welfare and corruption (Dolezal and Zeglovits 2014). The SPÖ and ÖVP focused on above average economic performance during the crisis, while the opposition parties emphasized primarily the corruption combined with an environmental agenda (Greens) or welfare issues that implicitly referred to an anti-immigration agenda (FPÖ). The new parties added a liberalization agenda (NEOS) and euroscepticism (Team Stronach) (Krizinger 2014). In the end, neither corruption nor euroscepticism became the most prominent issues as voters stuck to the traditional party competence ascriptions (Dolezal and Zeglovits 2014, Aichholzer et al. 2014). However, the lowest ever turnout (74.9 percent), the smallest ever vote - especially among the younger generations of voters - for the two dominant parties and two new parties in the parliament suggest that the next elections may reshape the traditional party politics that underpins the social partnership.

Overall, the EU influence on Austria over the last two decades was channeled by successive adaptations to the EU membership, enlargement, the Euro and recent crises. The central political and economic institutions were well equipped to steer these adaptations in such a way that enabled Austria to become one of the largest beneficiaries of the single market and single currency, while successfully containing many related problems (Breuss 2013, Petersen et al. 2014, Mattern et al. 2014). At the same time, changes in the external environment related to globalization and the EU, as well as internal factors stemming from increasing diversity, undermine the social, political and economic basis of the social partnership system. The perceived gaps in its legitimacy and effectiveness combined with future fiscal challenge, may force drastic changes as early as in the next parliamentary elections.

AUSTRIAN INFLUENCE ON EU

Almost an entire generation of voters, politicians and decision-makers have been directly participating in the day-to-day operations of the EU since 1995. As a result, Austria advanced from the newcomer status and achieved a standing comparable to some of the smaller founding members, despite occasional setbacks such as the 2000 informal sanctions. The country has successfully chaired two EU presidencies in 1998 and 2006, and its representatives are fully integrated within the EU and Euro area decision-making structures. Although there were only 19 Austrian MEPs in the European Parliament, Othmar Karas was elected a vice-president of the EP and Hannes Swoboda became the president of the important Socialists and Democrats Group in 2012.

Unlike most EU countries, Austria is not a member of NATO, but remains committed to the neutrality principle, which - despite its roots in Cold War agreements - became part of the national identity. It allows Austria to position itself as a neutral player and offer a convenient location for mediation in international conflicts, which is often an active contribution to a broader EU foreign policy. Recent examples include mediation events regarding Russia and Ukraine (2014), Iranian nuclear program (2014) or the US-Russia spy exchange (2010). At the same time, Austrian foreign policy - especially during the 1980s Kreisky era - used to be even more pronounced than today, when it is closely aligned with the EU.

The Austrian concept of neutrality does not prevent participation of its armed forces in the peace-keeping missions sanctioned by the UN Security Council. Hence, Austria keeps participating in international initiatives such as with NATO-led forces in Afghanistan and UN peace-keeping operations. It also participates in the EU security missions, such as policing in Kosovo.

Austria became a core participant in the environmental coalition of EU member states. It consistently supports initiatives to increase environmental standards, and leverages its leadership in renewable energy generation within the EU. At the same time, it strongly opposes nuclear energy - banned by law in Austria - as well as any fracking initiatives. This creates tensions with some of the neighboring new member states such as the Czech Republic, Slovakia or Poland that are generally more supportive of both fracking and nuclear energy. Austria is also a staunch opponent of genetically modified foodstuffs and the EU leader in organic farming.

Austrian authorities supported the EU enlargement policy, although the consequent issue of increased migration remains politically sensitive. Austria supported the 2004, 2007 and 2014 Eastern enlargements that created extensive economic opportunities and stabilized neighbor countries. It continues to support EU enlargement in the Western Balkans and neighborhood policy in Eastern Europe, although it remains firmly opposed to EU membership for Turkey.

At the same time, Austria utilized to the maximum the temporary measures protecting its labor market from the influx of workers from the post-communist EU member states. Free movement of workers remains an important political issue due to concerns about possible exploitation of the social welfare system, competition in the labor market and integration of migrant populations. The high levels of support for the anti-immigration rhetoric of the FPÖ induces the government to align closer with EU countries such as the UK or France that occasionally question existing EU rules on freedom of movement. However, the Austrian social system is better protected against so called 'benefit tourism' because it is based primarily not on residency, but contributions, and - unlike in other countries such as Germany -migrants in practice receive less social benefits than native recipients (Huber and Oberdabernig 2014). Similarly, labor migrants concentrate in sectors such as elderly care, construction, tourism or agriculture that could hardly operate without them, which limits their impact on labor market competition and employment. Nonetheless, like many other EU countries, Austria struggles to integrate its - especially non-EU - migrant populations into its education system and labor market, which keeps the issue on the policy agenda (Commission 2014a:7, Eurostat 2014b:2).

The political divisiveness of the migration issues is also clearly observable in the results of the 2014 elections to the European Parliament. The FPÖ anti-migration and anti-Euro ticket gained a fifth of the total vote and 4 MEPs out of 18. That is two more than in 2009, but at the same time, much less than some earlier polls predicted (Kritzinger 2014). The ÖVP and SPÖ coalition managed to achieve 51.1 percent majority, while the Greens got 3 MEPs and the new liberal party NEOS one. Overall, the Austrian contribution to the far-right rise in the EP remained sizeable but contained (Treib 2014).

In summary, after two decades in the EU, Austria is fully integrated within the EU governance structures and makes strong contributions especially in foreign, environmental and enlargement policies. It benefits from the economic side of European integration, but struggles with the integration of migrants, which fuels the Eurosceptic vote in national and European elections. The recent crises also aggravated this scepticism towards European integration.

AUSTRIA IN THE MIDST OF RECENT CRISES

The impact of the global financial crisis on Austria was relatively modest in comparison with other EU countries, but by no means negligible. The economy avoided excessive macroeconomic imbalances that deepened the crisis on the EU's Southern and Eastern periphery. However, it was highly exposed to financial contagion through its banking sector which was the main source of troubles during the financial and Euro crises and which may be exacerbated further by the Ukrainian crisis and sanctions imposed by the EU on Russia.

In 2009, Austrian authorities responded to the financial crisis by stimulating the economy through increased spending. The government introduced a series of social measures including abolishing university student fees, introducing a 13th month of family allowances, increasing social care subsidies, providing payment for some nursery school fees, and halting or postponing several price increases. It also stimulated demand in labor-intensive industries, such as construction by accelerated investment into infrastructure and by offering subsidies for renovation and thermal insulation of buildings. In line with the focus on competitiveness, the government also sustained funding for universities and increased the budget for the promotion of research and development (EIU 2011:11).

The labor market measures included a kurzarbeit scheme providing subsidies for up to two years encouraging firms to employ people for shorter working hours rather than dismiss them during the downturn (Bock-Schappelwein et al. 2014). The opportunities of job training for the unemployed were also increased. Furthermore, the government also provided special loan guarantees of up to € 300 million in order to facilitate lending to companies that form the core of the Austrian economy and are collectively the largest employers. The stimuli helped the economy to rebound from the recession of a 3.9 percent decrease in GDP in 2009 to surprisingly strong growth of 2 percent in 2010 (Eurostat 2014a). The quick return of growth reduced the social benefit outlays and boosted tax revenue, which helped to contain the government deficit and debt. Austria also remained in the small group of stable Euro area countries that retained high credit ratings and could provide credible guarantees for stabilization schemes such as the European Financial Stability Facility and later the European Stability Mechanism. However, the return of recession after 2011 pushed Austria towards fiscal consolidation.

The government passed a consolidation package in 2012 in order to meet the commitments under the Stability Programme submitted to the European Commission. The aim was to balance the budget by 2016, by a combination of tax increases and budget cuts. The package introduced tax on the sale of property, a "solidarity surcharge" on high earners and the closure of several tax loopholes. However, most of the savings were to come from austerity measures such as pay and hiring freezes in the public sector, cuts to pension increases and reduced eligibility for early or disability retirements (EIU 2011). At the same time, the government remained committed to the support for research and development, thermal insulation subsidies and large infrastructure investments, particularly into railways. The new government that came to power in 2013 is likely to introduce further austerity measures due to the escalating costs of the banking failures and increasing public indebtedness.

Maintaining the financial stability of banks throughout recent crises proved to be the most serious challenge for Austrian authorities. Internal stagnation and external expansion made the banking sector dangerously exposed to shocks, just before it suffered from the global financial crisis, Euro crisis and the Ukrainian/Russian turmoil. So far, the Austrian banks and authorities have managed these crises well, while also making a distinctive contribution to the stabilization within the EU and in its South-Eastern neighborhood.

Austria was 'overbanked' by the time of its EU entry in 1995. There were too many small banks, ill-prepared to take advantage of the single market and technological innovations (Mayer et al. 2001). They would be likely targets for acquisitions by larger European financial groups. However, banks responded to the new circumstances by domestic consolidation and expansion to the post-communist countries (OeNB 2004:23). They developed a unique business model of the 'second-home market' by forming a closely linked network of locally incorporated banks, rather than relying on cross-border services or a mere branch network (Epstein 2014). This novel business model was crucial for understanding the Austrian response to the financial and economic crisis on the Eastern periphery of the EU.

The Eastern expansion was very successful and profitable before the crisis, but left Austria exposed to the economies of Hungary, Romania, Serbia or Ukraine that fell into deep recession in 2009. Over € 200 billion, equivalent to about 70 percent of GDP, was at risk in these countries, which came on the top of the risk exposure to the domestic economy that shrank by 6 percent in 2009. The Austrian authorities responded quickly by providing potential funding of up to € 100 billion in October 2008 for capital and funding guarantees to the banking sector. The guarantee calmed market fears, the large banks sustained access to borrowing from international investors, and after a brief spike the interest rates normalized. In the end, only 2.4 percent of the money allocated for bank support was used (EIU 2011).

However, the potential for disaster was much greater, both for Austria and the CEE countries. International markets nearly panicked on October 2008, after economist and New York Times columnist Paul Krugman published a blog headlined: 'Eastern Europe 2008 = Southeast Asia 1997', drawing attention to eastern Europe's foreign currency loan exposure that could turn to crushing losses for Austrian banks. These fears were exaggerated because global financiers lacked understanding of both Austrian banks and CEE countries, some of which - such as Poland, the Czech Republic or Slovakia - remained stable and their banks profitable throughout the crisis. Nonetheless, there was a potential for extremely damaging panic, and authorities had to address it.

In February 2009, Austria's minister of finance proposed an EU-level rescue fund of €150 billion and Hungary's prime minister lobbied for an even larger package of €240 billion at the subsequent extraordinary summit of EU leaders (Epstein 2014). These efforts were rejected by the large EU countries that saw it as a specific problem of a few member states that did not require an EU-level response. However, Austrian and other Western banks with a strong presence in CEE countries faced sustained pressure as nervous international investors were reluctant to do business with them. Moreover, as some of the EU member states' governments bailed out their banks, they initially included provisions that limited financing of their subsidiaries in other EU and CEE countries (Epstein 2014:853). There was a risk that some of these banks would 'cut and run' from their foreign markets, which would hurt not only these host economies, but also other transnational banks present in CEE markets, including those from Austria (Kudrna and Gabor 2013:553). Austrian banks and authorities responded to this threat by a successful private-public initiative that partially substituted for the yet-to-emerge banking union.

The scheme, formally titled the European Bank Coordination Initiative, is better known as the 'Vienna Initiative' and bears an imprint of Austrian capacity for cooperation and mediation of competing interests. In November 2008, the three largest banks, which were also most exposed to CEE, got together and wrote a letter the European Commission asking for assistance in preventing the spread of banking nationalism that could induce the bank withdrawals from other EU countries (Epstein 2014). The letter, supported by Austrian Central Bank and supervisory authorities, was also sent to international organizations active in CEE countries. These joined in and helped to develop a series of agreements for Latvia, Hungary, Romania, Serbia and Bosnia-Herzegovina. Transnational banks agreed to continue financing their CEE subsidiaries, while the CEE governments reiterated their compliance with reform requirements imposed by the International Monetary Fund (IMF). In addition, the Commission clarified that bailout clauses that restrict financing of bank subsidiaries and branches in other EU countries are illegal under single market law (Commission 2008). The IMF, EBRD and European Investment Bank contributed with a €33 billion loan package to support foreign banks lending in CEE countries (EBRD et al. 2011).

The Vienna initiative tamed the panic on financial markets in the CEE region and averted further escalation of instability. In the end, only two minor banks had withdrawn completely from the CEE countries, while all large banks from Austria, France, Germany, the Netherlands, Belgium and even crisis-stricken Greece stood behind their subsidiaries (EBRD et al. 2011). However, it did not change the underlying problem of large exposure to potential bank instability between home countries of transnational banks such as Austria and the host countries in CEE, whose banks remained dependent on capital from their foreign parent bank. Authorities in Vienna tried to limit this exposure with several new rules, including limits on new lending to foreign subsidiaries set only to 110 percent of its local deposits (EBRD 2013:54). This new rule was not compatible with the aim of the Vienna initiative and it triggered the protests of host countries. This eventually induced the Commission ruling that such measures were incompatible with the single market and Austrian authorities demoted its status to mere recommendation. Nonetheless, the episode illustrated the contradictory motivations of member states' authorities that on one hand try to find a cooperative response to the crisis, but on the other hand need to protect their national interest (Kudrna 2012:289).

Government guarantees and the Vienna initiative successfully stabilized the banking sector as a whole. Yet three smaller banks became insolvent and had to be nationalized during 2009. The most serious case was the Hypo Alpe Adria, the sixth largest bank that expanded aggressively into Balkan countries and employed questionable business practices that included involvement in several corruption scandals in Croatia. Its expansion was supported by a state guarantee provided by the government of the Austrian province of Carinthia, which was dominated at the time by the populist FPÖ politicians. However, the province was never in a position to pay billions of Euro if the guarantee was called upon. Hence, when the bank failed, Austrian federal authorities had to step in and take over losses created by irresponsible decisions of the provincial government. This doubled the public deficit from 1.5 to 3 percent in 2014 alone and pushed the state debt of Austria towards 80 percent of GDP.

The government imposed the "solidarity tax" on bank balance sheets and imposed other fees on the financial sector in an effort to recoup some of the costs of bank restructuring (KPMG 2012). It also supported the initiative of eleven EU countries that considered implementation of the financial transaction tax, which is a controversial initiative with uncertain prospects of being adopted (Schneider 2014). However, these initiatives have increased the tax burden on banks beyond the levels of Germany and other neighboring countries, which may undermine Vienna's status of the regional financial center. The Hypo Alpe Adria scandal and high taxes are illustrative of the increasingly ambivalent relationship to banking, which was a boon during the pre-crisis decade but became a major burden after the crisis erupted. Moreover, there are further losses to come if the Ukrainian crisis and EU-Russian conflict escalates.

Ukraine was a source of losses ever since the onset of the financial crisis, but Russia accounted for nearly a half of the net profit of Austrian banks in 2013. Austria also remains more exposed to Ukraine and Russia than any other banking sector in the EU (Ficenec 2014). A protracted conflict in the Ukraine will deepen losses, but escalating EU sanctions on Russia are a real threat, especially if they result in some forced exit or even some form of expropriation. Moreover, all other CEE economies are likely to suffer from the loss of Russian and Ukrainian export markets, therefore export-oriented firms might not be able to repay loans to local subsidiaries of Austrian banks. In short, after six years of fending off one threat after another, there is no sign of relief for Austrian banks and financial authorities.

AUSTRIAN SUPPORT FOR FEDERALIZING REFORMS

While the series of recent crises had a relatively modest impact on social and macroeconomic stability in Austria, the banking sector was persistently a source of major concerns and losses. At the same time, Austria has benefited enormously from the expansion of its firms and banks throughout the enlarged EU and beyond. This makes the country a firm supporter of EU and Euro area reforms such as the banking union, which preserves the economic benefits of international cooperation while containing its potential risks and costs (Kudrna 2014:14-18). However, these reforms tend to centralize macroeconomic and financial policies on the EU level, thus pushing the EU past the confederal model as outlined in the introduction to this volume.

The EU model that emerges from the post-crises reforms is better characterized as contingent federalism or federalism by exception (Enderlein et al. 2012). The so called 'six- and two-pack' reforms of macroeconomic oversight as well as the banking union have centralized oversight and decision-making on economic affairs, which brought the EU closer to federal-like arrangements. However, no reforms so far introduced any automatic stabilizing mechanism, such as common unemployment insurance or some kind of cyclical adjustment mechanism, which are a hallmark of fiscal federalism. The European Stability Mechanism or the Single Resolution Fund can provide temporary fiscal support to participating EU countries stricken by financial or economic crisis. However, any such support is always contingent on identification of the source of the problem and commitment to reforms that would prevent its reoccurrence. Hence, all the new federal-like aspects of the reformed EU governance framework can only be used in exceptional circumstances and include no automatic fiscal transfers.

Austria, as all other EU member states, is likely to support further centralization in those areas where it seems in its national interests. At the same time, it will argue for more flexibility – a more confederal approach - in all those areas where it prefers to protect national specifics. The outcome in each policy domain depends on complex bargains within the EU decision-making system. Nonetheless, it is fair to conclude that in response to recent crises, Austria supported federalizing reforms that moved the EU, and in particular the Euro area, further from any confederal model of governance.

Conclusion

Throughout the recent crises Austria remained exceptionally stable. As in the past, its unique institutional framework of social partnership served it well. Before the crisis, it helped to prevent an accumulation of any macroeconomic imbalances that could undermine Austrian competitiveness and make the economy excessively vulnerable to external shocks. During the crisis, the social partnership underpinned the economic stimulus in 2009, followed by very gradual fiscal consolidation during the subsequent years. As a result, Austria was able to preserve its high living standards and low unemployment.

The banking sector proved to be the single most important threat to economic stability. Austrian banks expanded to other EU and non-EU countries in Central and Eastern Europe very successfully and profitably during the decade before the crisis. However, this exposure was a source of major uncertainty among international creditors, who initially failed to differentiate among the stable and ailing CEE countries and to understand Austrian banks' long-term commitment to these economies. The risk of panic was contained by the Vienna Initiative masterminded by Austrian actors and supported by the Commission and international financial organizations. The Initiative proved to be a useful contribution to the stabilization of the Eastern periphery and the neighborhood of the EU. At the same time, the domestic bank supporting measures could not prevent failure of three smaller banks, of which the case of Hypo Alpe Adria generated lasting economic and political consequences.

Nonetheless, Austria required no external support as did a number of EU countries on the Southern and Eastern periphery. To the contrary, its fiscal strength enabled it to make a contribution to the credibility of the European Stabilization Mechanism and other crisis management measures that the EU created to assist in the stabilization of crisis-stricken banks and countries. At the same time, Austria is also set to benefit from recent EU reforms. The banking union, and especially the emerging single resolution mechanism, provides an additional layer of potential support for its large international banking sector. Hence, the financial panic regarding Austrian exposure to other economies is less likely to repeat itself, even if the Ukrainian and Russian crises continue to escalate.

Recent crises have dented the trust and support of the EU and the Euro within the electorate (Eurobarometer 2013:2). The traditional parties of the grand coalition narrowly defended an overall majority in the 2013 elections and a fifth of the votes in the 2014 European elections went to Eurosceptic parties. Over time, these trends may challenge the traditional social partnership arrangements as well as Austrian cooperation on the EU level. However, there is currently no serious discussion of a major change of policy towards European integration, and Austria remains committed to the Euro and the EU.

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