Mastering the crisis but not the future: the Austrian model in the financial and economic crisis

Christoph Hermann and Jörg Flecker

1. Dynamics of the Austrian model

The Wall Street Journal, writing about Austria in 2006, noted that the once sleepy, corporatist economy had changed into one of Europe’s most competitive thanks to ‘free-market reform’ and tax cuts. Perhaps this is an exaggeration. Austria still has significant corporatist institutions and the liberalisation of markets has not gone as far as hoped for by the country’s economic elites, especially in the area of public services. However, there is no doubt that the Austrian model has undergone far-reaching changes since the mid-1980s, when an economic crisis put an end to the post-war system (Hermann and Flecker 2009).

While in the post-war decades Austria had a high share of public ownership in industries and banks and extensive market regulation that sheltered businesses from international competition, much of what has happened during the past three decades has been intended to create an environment that is attractive to foreign capital and to make native capital more competitive. Subsequent measures have included the liberalisation of trade and capital flows and the reduction of corporate taxes. Lower tax revenues, however, have aggravated budgetary problems and demands for budgetary austerity and cuts in the welfare system. As a result, economic and social policies have increasingly been subordinated to the overall objective of improving corporate profitability.

Many of the changes were facilitated through Austria’s accession to the EU in the mid-1990s, which in turn led to a further Europeanisation and internationalisation of the Austrian economy. While the liberalisation of the economy was accompanied by significant job losses in certain sectors – such as the electronics and chemical industries – due to the concentration and relocation strategies of international firms, Austrian
capital has profited immensely from the EU’s eastward enlargement. Austria has profited in particular from the introduction of the euro, which ultimately helped the country to move from a current account deficit to a surplus, with surpluses based mainly on gains in trade in services, including banking and retail activities. But while profitability and productivity soared along with internationalisation and the growing shareholder-value orientation, unemployment has remained high compared with the post-war decades (but low compared with other EU member states).

In terms of economic policy Austria has come much closer to what one might call the neoliberal mainstream. Two aspects of the Austrian reform process are particularly interesting: the transformation took place slowly, developing over several decades – the first ‘austerity package’ was introduced in 1987, while the last major welfare cuts took place in 2003. The changes were partly masked by institutional continuity (Hermann and Flecker 2009). Apart from a brief period of right-wing government (2000–2006) the social partners continued to play a substantial role in mitigating policy differences, even though the outcomes were generally more beneficial to capital than to labour. As a result, the changes took place without major resistance from organised labour. On the contrary, the trade union movement defended most of the austerity packages (except those adopted between 2000 and 2006) and Austria’s accession to the EU.

Another feature with regard to which Austria has shown remarkable stability is the ‘conservative welfare state’, with its high proportion of cash-based benefits. Despite some attempts to improve the situation of women, welfare institutions continue, in effect, to discriminate against women and other individuals with low incomes and discontinuous working careers. As a result, social inequalities have tended to increase despite a comparatively well developed welfare state and a stable and comprehensive collective bargaining system.

Inequalities are fuelled partly by the transformation of labour markets (Atzmüller 2009). Even though Austria has not experienced a direct attack on employment standards and security, atypical and sometimes precarious forms of employment have emerged alongside the standard employment relationship. By far the most important form of atypical employment is women working part-time hours. The employment rate of women has increased, but it is still far below that of the Nordic countries, especially if counted in full-time equivalents (Mairhuber 2010).
Three aspects of the transformation of the Austrian model have made the country particularly susceptible to the effects of the crisis: first of all, with economic liberalisation Austria has become more closely integrated in the European and world economies, while very moderate real wage growth and austerity policies have made it even more dependent on exports and hence on external demand. Secondly, privatisation spurred the transformation of the banking sector from a public utility into profit-maximising businesses, which are eager to take major risks if they promise extraordinary returns. EU enlargement into central and eastern Europe encouraged Austrian banks to turn themselves into international financial institutions with major branches in the new member states. The banking sector grew, with the effect that assets account for over three-and-a-half times of GDP (IMF 2013). For years these investments generated extraordinary returns but they have turned out to be a major liability during the crisis, which has hit countries such as Hungary, Bulgaria and Romania particular hard. Thirdly, low real wage growth and a persistent fall in the wage share (wages as a proportion of GDP) have not only limited internal demand but have also contributed to the trade imbalances within the European Union, aggravating the crisis for a number of peripheral member states and ultimately threatening the European integration project.

2. The crisis in Austria

The crisis hit Austria in the second half of 2008, ending a phase of accelerated growth that had started in 2003. GDP growth rates reached 3.5 per cent annually in 2006 and 2007, fuelling profits and inflation. After years of stagnation, workers also capitalised on the favourable economic climate and achieved significant real wage increases in 2006 and 2007. Growth also resulted in a fall in the unemployment rate below 4 per cent (Labour Force Survey) just before the crisis struck in 2008. GDP growth fell in the last quarter of 2008, but overall GDP still grew by 2 per cent in 2008 (Scheiblecker et al. 2010: 322). The situation changed in 2009. In the first quarter of 2009 the economy contracted by 2.2 per cent compared with the fourth quarter of 2008 and by 4.9 per cent compared with the first quarter of 2008. The economy continued to shrink until mid-2009 with the effect that GDP fell by 3.6 per cent annually. The last time the Austrian economy recorded such a decline in GDP was in 1949 (Scheiblecker et al. 2010: 323). Despite the massive blow the Austrian economy still performed better than many
other European economies, including Germany, where GDP fell by 5 per cent (ibid. 234).

The Austrian economy has always been highly dependent on exports, especially to its main trading partner, Germany. However, the internationalisation of the banking and other sectors has intensified relationships with other countries, including the new member states in central and eastern Europe (Hermann and Flecker 2009). The outbreak of the crisis and the following financial hysteria immediately affected the Austrian banking sector. The government quickly adopted a 100-billion-euro rescue package to calm investors and depositors. Nevertheless, total bank assets fell by 3.3 per cent in 2009 (Scheiblecker et al. 2010: 323).

Besides the banking sector the crisis has mainly affected exporters. Total exports fell by 20 per cent in 2009. Among the export sectors, manufacturing was hit particularly hard and within the manufacturing sector the main victims were producers of investment and durable consumption goods and related intermediate products. Output in manufacturing started to fall in the fourth quarter of 2008. Some manufacturers struggled with a 30 to 50 per cent decline in orders (Hermann 2011).

With some delay, the crisis also affected the construction sector. Even though Austria experienced a marked growth in construction in the years leading up to the crisis, the boom was not comparable to the situation in Spain or Ireland and was definitely not the cause of the crisis. Output decreased by 7.6 per cent in the first quarter of 2009 and by 2.3 per cent annually (Scheiblecker et al. 2009: 372). The decline in private demand was partly offset by public investments. These investments spurred growth in the construction sector in the fourth quarter of 2010 (ibid.).

The economic crisis quickly turned into a labour market crisis, but the reduction in employment was less severe than the contraction in GDP. While GDP fell by 3.6 per cent in 2009, unemployment increased by 1.4 per cent (Scheiblecker et al. 2010: 361). The number of unemployed persons increased by 57,000 from June 2008 to June 2009, while the number of participants in training programmes rose by almost 16,000 over the same period (Stiglbauer 2010: 28). Following the trajectory of the crisis, job losses first appeared in the manufacturing sector, with losses in February 2009 outstripping employment gains for the first time in six years. Over the course of 2009, employment in manufacturing fell by 6 per cent (Scheiblecker et al. 2009: 369).
Unemployment increased quickly and at an increasing pace until June 2009, when 33 per cent more unemployed persons were registered than in the preceding month. Overall, unemployment increased by 48,100 persons or 22.6 per cent from 2008 to 2009. In terms of registered unemployment, the unemployment rate increased from 5.8 per cent in 2008 to 7.2 per cent in 2009 (ibid. 366). If people in training and other labour market service measures are included, unemployment reached 9.6 per cent in 2009 (ibid. 368). According to Eurostat, unemployment accounted for 4.8 per cent in 2009 and was therefore significantly lower than in most other European countries (ibid. 366).

Among the first workers who lost their jobs were temporary agency workers. The number of agency workers increased significantly during the economic boom preceding the crisis, but declined by 15.9 per cent between July 2008 and July 2009; in manufacturing the reduction amounted to 32.8 per cent over the same period (ibid. 365). Employment cuts in manufacturing and in employment agencies combined were as big as in the rest of the economy put together (Stiglbauer 2010: 28). However, agency workers were not only the first to be laid off. They were also the first to be re-hired after growth started to pick up again in the second half of 2009 (Allinger 2011).

3. Responses to the crisis

3.1 Fiscal policy

In the face of the crisis, Austria, like many other countries in Europe and around the world, temporarily returned to Keynesian deficit-spending. As a first measure the government adopted a ‘generous’ rescue package for the Austrian banks. The government pledged to inject up to 100 billion euros into the banking system, if needed. The rescue package was extremely large relative to the size of the country and reflected the enhanced exposure of Austrian banks in central and eastern Europe. Rescue measures included the partial nationalisation of three major banks and financial support for others.¹ Up to the end of 2010 the government spent 5.874 billion euros on buying up the shares of troubled banks and took over banking-sector liabilities in the amount of 23.215 billion euros (Bundesrechnungshof 2012).

¹. Hypo-Alpe-Adria, Kommunalkredit and Volksbanken.
In addition to bailing out banks, the government also adopted two economic stimulus packages to help the struggling economy. The volume of the package was 12 billion euros, or 3.5 per cent of GDP (Breuss, Kaniovski and Schratzenstaller 2009; Berger et al. 2009). The main stimulus came from tax cuts for households and tax credits and subsidies for companies. A major tax reform which was initially planned for 2010 was brought forward and adopted in 2009. The tax giveaways accounted for 2.1 per cent of GDP, although they benefited mainly high earners. Households in the first four income deciles gained less than households in the tenth income decile (ibid. 36).

In terms of expenditure, stimulus money went mainly to the modernisation of railway infrastructure and road construction – not least to support the construction sector. Investments in social infrastructure included the introduction of a cost-free kindergarten year for children before they start school, but in sum they were fairly marginal. Instead, deficit-spending mainly followed the traditional spending path and barely promoted structural change, social innovation or ecological modernisation. On the contrary, the stimulus package also included a 22.5 million euro car scrappage premium to support the ailing auto (supplier) industry.

As a result of deficit-spending, the annual deficit increased from 0.9 per cent of GDP in 2008 to 4.1 per cent in 2009 and 4.6 per cent in 2010; the total deficit increased from 63.8 per cent of GDP in 2008 to 69.2 per cent in 2009 and 72.4 per cent in 2011. In order to tackle the growing deficit, the government adopted an austerity package in 2011, totalling 6.3 billion euros (Schratzenstaller 2011 and 2013). Except for a special tax levied on banks in exchange for the support they received during the crisis, the major part of the additional revenues came from consumer taxes. This means that lower income households contributed a significantly higher proportion of their income to the fiscal consolidation than high income households. Low income households also suffered from cuts in welfare spending, including cuts in care benefits and family allowances. Overall, the cuts mainly affected those who are most vulnerable and thus aggravated rather than alleviated social problems.

3.2 Labour market policy

The government adopted a number of measures to tackle rising unemployment, pooled in two labour market packages. The most popular
measure was the reform of short-time working. The reform was based on a social partner agreement, underlining the role of the social partners in mitigating the effects of the crisis. Short-time working existed before the crisis but played only a minor role. Among other things it was used to help companies affected by environmental disasters, such as floods. In October 2008, just before the outbreak of the crisis, 400 workers were registered as taking part in short-time working schemes (BMASK 2010: 300). From the social-partner perspective, short-time working is particularly attractive because it helps companies to retain qualified staff and avoid lay-offs, while most of the costs are covered by the government (Hermann 2011).

The reform was based on two amendments of the existing regulations. The main improvements concerned an extension of the short-time working period, first to 18 and then to 24 months. At the same time, the proportion of short-time working was extended to any number of hours between 10 and 90 per cent of regular working time (BMASK 2010: 293–94). The reform also introduced a rebate for employer social security contributions after six months of short-time working and special financial incentives for companies that combine short-time working with training or further education (ibid.). Further details of the introduction of short-time working were regulated in an inter-sectoral framework agreement negotiated between the Chamber of Economy and the Trade Union Federation (Allinger and Flecker 2010; Hermann 2011). Austrian companies also need a company agreement signed by a works council and a trade union representative if they want to switch to short-time working.

The two main unions representing workers in the industrial sector (PROGE and GPA-DJP) agreed that they would sign company agreements only if the affected workers receive 90 per cent of their regular wages, regardless of how many hours they were working. Because about 60 per cent of wages was covered by the Labour Market Service (the rate for unemployment benefit), the rest had to be paid by the companies concerned. Except in a number of small and medium-sized companies the unions were mostly successful in obtaining the 90 per cent replacement rate. While the social partner negotiations on the short-time working reform ran fairly smoothly, introduction on the company level occasionally sparked conflicts (Hermann 2011).

Short-time working is widely considered a success. It was used mainly in automobile production and by auto suppliers, as well as in engineering and the
metal sector more generally. At the peak of development in April 2009, more than 300 companies had introduced short-time working, affecting more than 37,000 workers (BMASK 2010: 300). The Federal Ministry of Employment, Social Affairs and Consumer Protection estimates that short-time working saved approximately 30,000 jobs (BMASK 2010: 304). Alfred Stiglbauer (2010: 35), however, estimates that the employment effect was only 6,800 jobs or 0.2 per cent of total employment.

While short-time working is considered a success, combining short-time working and further education was largely a failure. Only 20 per cent of workers on short-time working used the opportunity to improve their skills (ibid.). One reason may be that the additional incentives were targeted towards companies instead of workers worried that their jobs would still be there after the crisis. Another reason is that qualifications typically need long-term planning, whereas the crisis required ad hoc action (Bock-Schappelwein, Mahringer and Rückert 2011). In any case, while some workers were reluctant to combine short-time working with further training, many took the opportunity to go on training leave paid by the Labour Market Service for up to 12 months on 60 per cent of their wages. At the peak of the development, in November 2009, 6,900 workers took this opportunity and left work to study or improve their skills. This was six times more than in November 2007 (BMASK 2010: 302).

3.3 Wages and working hours

For a number of years real wages have increased only very moderately in Austria, clearly lagging behind productivity growth. Even at the height of the recent expansion in 2007 a nominal wage hike of 2.5 per cent turned into a real wage increase of 0.3 per cent. Interestingly, the crisis year became a major exception in this long-term development. In 2009, real wages soared by an astonishing 2.9 per cent, which was as much as in the preceding eight years put together. Of course, the main reason for the boost in real wages was the fall in inflation (from 3.2 per cent in 2008 to 0.5 per cent in 2009), but even in nominal terms wages increased more during the crisis year than during the preceding boom (Hermann 2011). In terms of both nominal and real wage growth Austria was among the leading countries in Europe, ranked above countries such as Sweden and Germany. In fact, 2009 was the only year for a long time when wage growth actually exceeded the combined growth in average prices and productivity (Schulten 2010: 198). The growth in real wages was
instrumental in sustaining demand during the crisis and, together with the tax cuts, compensated for the dramatic fall in exports.

However, with the exception of the public sector, where the government agreed to an exceptionally high wage increase to maintain purchasing power (3.55 per cent nominally and 3.5 per cent in real terms in 2009), the growth in (real) wages was not necessarily the result of social partner consent and a common strategy to confront the crisis (Hermann 2011). In several cases the negotiations were particularly tense and temporarily broke down, especially in the spring 2009 bargaining round. The unions repeatedly had to mobilise workers to increase pressure on employers to accept wage increases despite the accumulating economic difficulties (ibid.). While Austrian unions strongly rejected employer demands for wage moderation, the electronics industry agreement contained a provision that allowed companies in economic difficulties – that is, companies that suffered a 15 per cent or above decline in turnover in the first quarter of 2009 – to increase wages by 1.4 per cent instead of 2.2 per cent. However, the provision was fairly controversial in the union movement and remained an exception (ibid.).

Working hours fell significantly during the crisis due to short-time working, the clearing of overtime accounts and the shift from full-time to part-time hours. But at the same time many workers continued to work overtime. According to Labour Market Survey data, average weekly overtime hours decreased slightly from 8.5 hours in 2008 to 8.1 hours in 2010 (ibid.). Consequently, both employer and employee interest organisations took the crisis experience as a reason to demand a reform of the working time regulation. However, while the employers’ organisation pushed for further ‘flexibilisation’, including greater daily and weekly variation and the introduction of working time accounts, trade unions demanded a reduction of working time and the distribution of work among a larger number of workers (Allinger 2010; Hermann 2011). Both sides launched public campaigns to raise support for their position. However, as no side was prepared to make concessions the result was a stalemate and the continuation of existing regulations, which allow for comparatively long but collectively approved working hours.
After the contraction in 2009, the Austrian economy started to grow again in 2010. GDP grew by 2 per cent in 2010 and 2.7 per cent in 2011. The growth was driven by a strong recovery of export industry, fuelled mainly by the German upswing and sales to emerging economies, including China. However, growth slowed down again to 0.8 per cent of GDP in 2012, following a similar economic decline in Germany. Growth picked up again in the second half of 2013 and, according to preliminary figures, reached 2 per cent over the course of the year (0.3 per cent in real terms). According to economic forecasters, growth rates will remain slightly below 2 per cent in the coming years (Baumgartner, Kaniovski and Leibrecht 2014). Following the growth trajectory, registered unemployment fell to 6.7 per cent in 2011, but increased again to 7.0 per cent in 2012 (according to the Eurostat definition unemployment fell to 4.2 per cent in 2011 and increased to 4.2 per cent in 2013). Some sectors, such as the construction industry, continue to struggle with the effects of the crisis and a lack of new projects – even though the crisis has sparked investments in the housing market as an alternative to the stock market.

Recently, the economy has also suffered from a series of bankruptcies, including the liquidation of a major (Spanish-owned) construction firm with 4,600 employees and the insolvency of a major retail firm with 3,468 employees. Furthermore, while Austria still has one of the lowest unemployment rates in the EU, including low unemployment among young workers, many of whom are in vocational training programmes, a large part of the new jobs created since the crisis are part-time and not a few of them are short part-time. Hence the crisis has prolonged and accelerated the long-term trend of flexibilisation and precarisation, which has become an important feature of the Austrian labour market.

After exceptional real wage increases in 2009, collective bargaining also returned to the pre-crisis trajectory of moderate real wage gains. In addition, employers continued to step up pressure for the decentralisation of the existing bargaining system. As a result, the employers in the metalworking industry ended a 40-year long tradition of negotiating a uniform sector-wide agreement in 2012 and instead concluded separate agreements for the six sub-sectors. The subsectors are represented by distinct employer bodies, which are, however, all part of the Austrian Chamber of Economy. Initially, the new bargaining strategy sparked considerable conflict and led to a series of warning strikes. However, the
conflict was settled with the involvement of leading social partner repre-
sentatives from the employer and trade union camps. Furthermore,
in the end the differences between the six agreements turned out to be
fairly insignificant and the PROGE and GPA trade unions won a signifi-
cant wage increase (Allinger 2013).

Despite the austerity, the public deficit continued to rise in 2011 and 2012
and reached a high of 75.14 per cent in 2013, after which it is expected
to decline (Schratzenstaller 2013). Austria thus exceeded the Maastricht
cap of 3 per cent on new debt in 2009, 2010, and 2012 (ibid.). The gov-
ernment has subsequently increased efforts to cut spending without
adopting a new austerity package. However, the future of Austrian pub-
lic finances also depends on developments in the banking sector.

5. Continuing threats and unsolved problems

Austria has weathered the crisis relatively well. The recession was deep
but short. Social partnership played a major role in mastering the cri-
sis: trade unions and the employer organisations negotiated exception-
ally high wage increases during the crisis and successfully pressed for
a reform of short-time working which helped to maintain jobs during
the downturn. In some respect, the crisis led to a revitalisation of Aus-
trian social partnership. However, crisis corporatism quickly turned into
competitive corporatism when the social partners started to defend sub-
sequent austerity packages (see the contribution of Hans-Jürgen Urban
in this book). The austerity packages were criticised by the trade unions
but not challenged fundamentally. At the same time, wage agreements
fell back to the pre-crisis path of very moderate increases and in 2011
they were even negative in real terms.

The banks and their engagement in central and eastern Europe presents
a major threat to the public finances and future of the country. The li-
abilities of one bank alone (Hypo Alpe Adria), which was nationalised
in 2009 because of insolvency, could cost the country 11.7 billion euros
(approved by the European Commission as acceptable state support)
and according to some worst-case scenarios even up to 17 billion euros.2

derstandard.at/1378248815363/Hypo-Kapitalbedarf-im-schlimmsten-Fall-17-Milliarden-
Euro, accessed 12 September 2013.
Austria, furthermore, continues to be strongly dependent on the German market and the growth prospects of the German economy. In addition, growth prospects also depend on developments in Italy and central and eastern Europe, which are not only major trading partners but also closely interlinked through the banking sector (Italian investors own one of the largest Austrian banks).

Given the nature of the stimulus and austerity packages there is very little hope of a revitalisation and extension of the welfare state in order to counter the continuing de facto discrimination against women and low income earners built into the conservative welfare state model. New jobs continue to be frequently part-time and not a few are precarious. Hence female employment may continue to increase but at the cost of persisting gender inequality, especially with regard to male and female wages. The welfare cuts have aggravated rather than solved some of the most pressing social problems, including the organisation of long-term care or the labour market integration of disabled workers. Austerity and cuts in welfare benefits have further aggravated inequality.

As an OECD study (2013: 4) shows, despite the financial turmoil and stock market losses, the top 10 per cent of earners still increased their share more than the bottom 10 per cent between 2007 and 2010. Another study on the distribution of household wealth, published in 2013, showed that inequality in Austria is much larger than previously assumed: the wealthiest 5 per cent of Austrian households own almost half of gross wealth in the country, while the lower 50 per cent of households own a mere 4 per cent (Andreasch et al. 2012: 249). Despite growing inequality, the conservative forces in the ‘grand coalition’ government have blocked any attempts to increase taxes on capital and private wealth, for example on so-called private foundations that enjoy particularly low tax rates. Given the comparatively very low property taxes, even the OECD recommends a ‘review of capital taxation’ (OECD 2011: 26).

In sum, Austrian institutions have been helpful in rapidly developing and implementing anti-crisis measures. However, in doing so they have reinforced path dependencies, thereby blocking the adoption of more future-oriented strategies. As a result, the country seems to be in deadlock. On the surface Austria is doing comparatively well, managing to maintain growth and hold down unemployment. However, the alleged success story stands on shaky ground, such as growth in Germany and stabilisation of the situation in central and eastern Europe. Below the surface
the country faces a number of unsolved problems, including increasing labour market segmentation, growing social and gender inequality and a looming care crisis. In other words, while Austria seems to be able to hold on to existing achievements, it is not making the investments needed to cope with future challenges, including long overdue investments in public infrastructure and research, as well as in a profound social and ecological modernisation.

References


Allinger B. (2011) Temporary agency work on the rise with economic recovery, EIROnline.

Allinger, B. (2013) First strikes in 25 years mark start of pay round, EIROnline.


OECD (2013) Crisis squeezes income and puts pressure on inequality and poverty, Paris, OECD.