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## Austria is fast becoming Europe's latest debt nightmare

A mini-Greece is about to go off in Europe's heartlands, and markets don't even know it



The hills are alive with the sound of bankruptcy Photo: Copyright (c) 1965 Rex Features



By **Jeremy Warner**

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Ah Austria, land of schnitzel, lederhosen, Mozart, alpine meadows and beer drinking. Less widely appreciated is its special place in the history of catastrophic banking crises.

It was the failure of Creditanstalt, a Viennese bank founded in 1855 by

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**Anselm von Rothschild**, that arguably sparked the Great Depression, setting off an unstoppable chain reaction of bankruptcies throughout Europe and America.

No-one would think that what happened **last week at Austria's failed Hypo Alpe-Adria Bank International** falls into quite the same category; we are meant to be in the recovery phase of the latest global banking crisis, so this is more about re-setting the system than again bringing it to its knees, right?

Well, make up your own mind. I suspect neither financial markets nor policymakers have yet caught onto the full significance of the latest turn of events.

In a nutshell, the Austrian government has had enough of funding the bank's losses, and announced plans to "bail-in" external creditors to the tune of €7.6bn instead.

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As such, this marks a test case of new European rules to make creditors pay for failing banks. About time too, you might say. What took them so long?

Only in this case, the bonds are notionally guaranteed by the Austrian state of Carinthia, which now theoretically becomes liable for the bail-in. It's an echo of the mess Ireland got itself into at the height of the banking crisis, when it foolishly attempted to stem the panic by underwriting all Irish banking liabilities; the move very nearly ended up bankrupting the entire country. Hypo will bankrupt Carinthia.

Essentially, what the Austrian

government is doing is cutting loose an entire region, rather in the way the federal authorities in the US allowed Detroit to go bust a number of years ago.

It's a mini-Greece going off in the heartlands of Europe.



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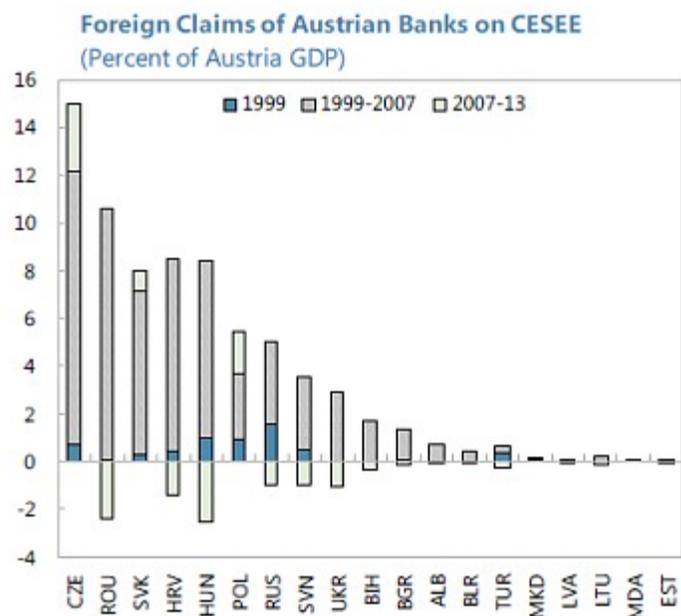


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In Hypo's case, the bail-in also threatens knock-on consequences for public bodies elsewhere, including Bayern Landesbank, a big holder of Hypo bonds which is owned by the German state of Bavaria, and the Munich based FMSW, which is again publicly underwritten.

All this is just the tip of the iceberg; Europe is awash with interlinked banking and public liabilities, many of which will never be repaid and basically need to be written off.

Massive creditor losses are in prospect. The European authorities had us all half convinced that Europe's debt crisis was over. In truth, it may have barely begun.



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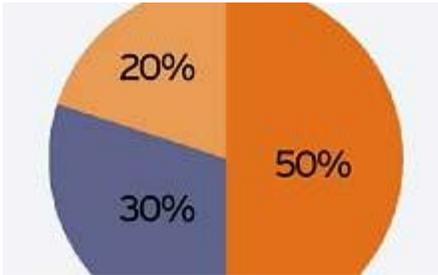
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