One in and one outside the EU

Austria and Switzerland take different paths

BY *BARBARA BECK*

Austria and Switzerland have much in common. Both are democracies with federal governments; both are small, with populations of about eight million and seven million, respectively; both inhabit a sometimes hostile Alpine geography in the middle of Europe; and they share a border. But their histories have been very different, and in recent decades each has reached its own accommodation with its European neighbours. For Austria, that has meant membership in the European Union, while for Switzerland, it has led to an emphatic independence and a number of carefully negotiated compromises to enable it to do business with the EU.

Austria was a relative latecomer to the EU, arriving long after the six founding members (Belgium, France, Italy, Luxembourg, the Netherlands and West Germany) signed the Treaty of Rome establishing the European Economic Community (EEC) in 1957. Under Austria's 1955 state treaty that restored its independence after the Second World War, it was required not only to remain strictly neutral, but also to abstain from any direct or indirect political or economic union with Germany. In 1960, it became one of the founding members of the European Free Trade Association (EFTA) that grouped together Britain, Denmark, Norway, Portugal, Sweden and Switzerland. This provided a framework for dismantling trade barriers without the political obligations involved in EEC membership.

Austria in the "other economic union"

The arrangement proved satisfactory until 1986, when the European Community (EC, its new name after 1965) embarked on a plan for closer integration. Under the Single European Act, it aimed to establish a single internal market within the EC that would allow the free movement of people, goods, services and capital among all its members. The EFTA countries, meanwhile, started negotiations to set up a European Economic Area in the hope of sharing some of the benefits of the single market. But Austria was disappointed by the terms that were offered and decided to pull out.

– AP Photo: Donald Stampfli

A woman holds 50 euro banknotes and 100 Swiss francs. Both can be withdrawn from automatic teller machines in Geneva, Switzerland.

Thanks to the political changes taking place in Central and Eastern Europe, Austria in 1989 felt able to submit an application to join the EC. Following successful negotiations, more than 66 per cent of its people voted for entry in a referendum in April 1994, and at the beginning of 1995, it became a full member. It embraced the European Monetary Union in 1999 and adopted euro notes and coins in 2002.

For a country that depended on the European Union for about 70 per cent of its trade it seemed to make sense to seek membership. This not only meant that Austria was able to take full advantage of the single European market, but also that it would be able to influence any future developments from the inside. Admittedly, a country with eight million people might not carry much clout in a union whose member countries have a population of 450 million (and more to come), but it will have more influence than an outsider.

Barbara Beck *is the Surveys Editor of* The Economist. *She is based in London. She is the author of E-trends: what the future holds in the e-world (2002, Economist Books), and of* The Economist's *2004 special survey, "Is Switzerland still a special case?*

EU expansion to the East affects Austria

Austria arrived in time to get involved in the negotiations for the EU's enlargement to the east, a subject close to its heart. It had mixed feelings about such expansion. On the plus side, the entry of eight eastern European countries in 2004 meant that, for the first time, Austria was entirely surrounded by other EU countries, so it no longer had to police a huge border with non-members. The entry of all those new members also opened up new business opportunities and created jobs at home. On the minus side, the much lower wages and standards of living in the accession countries were seen as bringing more competition and an influx of foreign workers who undercut the domestic labour force.

Austria's doubts about enlargement showed up in a marked decline in the EU's popularity after its accession. Matters were made worse by tight fiscal policies adopted by the government to comply with EU rules and Austrian job losses caused by foreign takeovers. But what caused particular anger in Austria was the EU's collective response to its 1999 elections. These brought big gains for the right-wing, anti-immigration Freedom Party, which was invited into a coalition led by the centre-right People's Party. Fearing that Austria might slide toward right-wing extremism, all other EU countries suspended bilateral contacts in early 2000. This prompted the resignation of the party's colourful leader, Jörg Haider, though the party remained in the coalition. The other EU states eventually resumed normal relations. But the Austrians felt offended by what they saw as interference in their internal affairs. The recent Austrian elections in October gave the Social Democrats a two-seat edge over the conservative People's Party, with whom they were negotiating a coalition in mid-October. The new government coalition is likely to exclude the Freedom Party, removing this particular bone of contention.

In any case, relations with the EU have become somewhat more cordial recently. In spring 2005, Austria ratified the proposed new EU constitution (although its rejection by the French and the Dutch soon afterward in effect killed it off). In the first half of 2006, Austria held the rotating presidency of the EU, which was generally seen as a success and improved both Austria's image in the EU and the EU's image among Austrians. But Austrians still grumble that as EU members they have to go along with everything that is decided in Brussels, whereas Switzerland next door avoids the obligations of membership while still gaining many of the advantages. And other problems might lie ahead. For example, Austria has made it clear it is opposed to Turkish accession to the EU, and might hold a referendum if the EU approves it. If the Austrian people say no, that would create a tricky situation.

Switzerland's special case

But even if Austria's enthusiasm has waxed and waned, the country has at least worked within the EU. Switzerland has preferred to go it alone, instead. That should come as no surprise: the country has always been wary of joining international organizations. Even so, in 1992, having successfully completed negotiations for joining the European Economic Area, it actually filed an application for EU membership. But in a referendum later that year, the Swiss people turned down the carefully negotiated EEA agreement by the narrowest of margins. That obliged the Swiss government to put its EU application on ice, where it is likely to remain for the foreseeable future.


– Photo: Austrian Chancellor's Office

Austrian Chancellor Wolfgang Schüssel (left) opening the exhibition "Austria in Europe". – Austrian Chancellor's Office

Yet Switzerland still had to find a way of doing business with the EU, with which its economy is highly integrated. For many years, it had been in the habit of aligning its legislation in areas such as banking, insurance, competition and product liability with that of its EU neighbours to speed the flow of goods and services. But more co-ordination was needed, and in 1994 Switzerland opened negotiations with the EU on a number of sectoral dossiers dubbed "Bilaterals I." Five years later, agreement was reached in seven areas: the free movement of people; air and land transport; agriculture; technical barriers to trade; public procurement; and research. In 2000, the results were approved by the Swiss people by a two-thirds majority in a referendum.

Swiss sign Bilaterals II with EU

However, it soon became clear that a further round of negotiations was needed ("Bilaterals II"), partly because not all the issues from the first round had been resolved, but more importantly because new ones had emerged. This time, the agenda included Swiss participation in the EU's arrangements for fighting crime and for asylum policy, known as Schengen-Dublin, as well as combating fraud and the taxation of savings. This last item proved particularly contentious because the Swiss felt it would threaten their banking secrecy, an important competitive advantage in their financial services industry. A compromise was eventually reached and the Bilaterals II agreements have now also been signed and ratified. The cantons took part in negotiating Bilaterals II because Switzerland's major constitutional revision of 1999 gave the cantons the right to participate in the making of foreign policy, in particular in international negotiations pertaining to their exclusive powers. This development was intended to offset the gradual loss of cantonal selfrule due to the pressures of increased international co-operation in bodies such as the EU.

The problem for Switzerland is that the EU is constantly evolving, so the agreements will have to keep being updated, opening up the prospect of never-ending negotiations. Over time, the EU might become less willing to enter into such negotiations and less prepared to make concessions. Meanwhile, Switzerland has no input into the decisions made in Brussels.

Many Swiss argue that despite these drawbacks, Switzerland is actually better off outside the EU. As a member, it would have to pay a hefty annual membership fee (although even as an outsider, it makes a financial contribution in return for access to the EU market). If Switzerland were to join the euro zone, it would also have to abandon its cherished Swiss franc, which might push up interest rates by a percentage point or two. The country's banking secrecy would become increasingly difficult to maintain, and its system of value-added tax would have to be adapted. Even its farmers would be less mollycoddled.

On the other hand, Switzerland would clearly gain from automatic access to a huge market on its doorstep, and from the opportunity to help shape EU policies from the inside. Swiss Europhiles also believe that EU entry would administer a positive shock to their country, rousing it from its complacency, increasing competition and reducing its egregiously high price levels. In recent decades, economic growth in Switzerland has been far slower than in its European neighbours, including Austria, so the Swiss are no longer much richer than everyone else around. But there are many reasons for that, only some of them related to keeping out of the EU. Indeed, many analysts agree that in economic terms, the advantages and disadvantages of Swiss membership are fairly evenly balanced. In the end, the decision will be a political one. The recent electoral gains of the anti-EU Swiss People's Party have made EU entry in the foreseeable future that much less likely.

But the main reason why Switzerland is likely to stay out for quite some time is its system of federalism and direct democracy. Were it to join, it would have to accept the entire body of legislation on which the existing Union is based — the *acquis communautaire* — without being able to pick and choose. And once in, it would have to fall in with the EU's policies, whether it liked them or not. That would be hard to swallow for a country that invariably consults its people about almost every major decision at every level of government. The Swiss government has commissioned a study, due out this year, to look at the options for its future relations with the EU, but no one is expecting quick results.

The two Alpine republics have found different ways of living with the EU, in one case on the inside, in the other on the outside. Each has made the choice that best suits its political system. Both choices carry risks. But given that both countries remain rich and successful, it would be hard to argue that one is better than the other.