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Good and Bad Banking on Europe's Periphery: Pathways to Catching Up and Falling Behind

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Pathways to Catching Up and Falling Behind

Rachel Epstein and Martin Rhodes

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Rachel Epstein and Martin Rhodes

Abstract

In this paper we seek to explain why bank performance has varied so dramatically during and after the financial crisis on Europe's periphery, both across states and within them. Our dependent variable is bank performance defined in terms of credit provision and banks' contribution to financial stability. Our independent variable is the particular mix at play between political/social purpose and what we call 'market authority' - the importance of market incentives, signals and pricing within a particular financial 'ecosystem'. "Economic nationalism" or the politicization of local and regional banks has often imbued banks with social and political goals, serving the economy at different levels, and is one major source of political/social purpose. But the latter must be constrained by market authority. We argue that for optimal bank performance, economic nationalism or political/social purpose must be constrained by market authority, otherwise a political logic (e.g. cronyism, a lack of professionalism, and deficits in banking expertise) can easily subvert or distort credit provision and undermine financial stability.

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1. Introduction

Banks have been both blessings and curses for states. Banks can lay the foundations for economic power. But they can also cause economic catastrophe. The organization of finance, starting with banks, has always been central to catching up in the global economy. Equally important to states that have approached the pinnacle of economic power has been staying there. In this regard, banks have also been critical to economic adjustment, maintaining or regaining competitiveness, and therewith states' international power positions.

To say that banks have often been instrumental to state formation, economic development, and even the prosecution of war is not to claim that banks, in the service of states, have always been effective in such undertakings. Indeed, there is enormous variation in the degree to which banking systems have provided adequate credit to an economy, funded innovation, ensured financial stability, insulated countries against external economic shocks, or provided countercyclical lending in downturns.

Equally, there are also variations in the extent to which the mobilization of the financial system by the state (both national and subnational) behind political or social objectives (which we call political or social purpose) is good for the banks themselves. The bank-state relationship can be fraught with difficulty. In the banking sector, as in other sectors of national economies, market failure and state-induced failure both occur. The banking sectors' fragilities in both respects were clearly on display during the post-2008 financial crisis and after. And nowhere was variation along both dimensions – market behavior and politically or socially-oriented banking – more evident than on Europe's periphery, East and South.

The research question here is two-fold. We seek to explain why bank performance has varied so dramatically during and after the financial crisis on Europe's periphery, both across states and also at times within them. Our dependent variable is bank performance in terms of credit provision and banks' contribution to financial stability. Our independent variable is the particular mix at play between political/social purpose (the various forms of which we detail below) and what we call "market authority," which refers to the importance of market incentives, signals, and pricing within a particular financial "ecosystem." Our second, related research question is why bank behavior contributes to catching up and adjustment in some countries, but sets other states back.

2. The Argument

We argue that banks performance – measured in terms of credit provision (their ability to fund the growth of firms, household needs, and governments) and financial stability (their propensity to support or undermine the financial system via their lending and borrowing practices) – depends on the particular mix of social/political purpose and market authority underpinning banks' behavior. Against this background, what is often referred to as "economic nationalism" imbues banks with social and political goals, serving the national economy. Economic nationalism is therefore one major source of political and social purpose. Embeddedness in local or regional political networks is another. But we also argue that for optimal bank performance, economic nationalism or political and social purpose must both be constrained by market authority.

Our use of the concept “economic nationalism,” under which we subsume political or social purpose, needs further definition. Its connection with banking and finance has been construed by Eliassen et al. (2001) largely in terms of the protection of national markets (in this instance European ones) from external EU competition rules or from foreign takeovers, using: i) special rules governing the financial sector; ii) the exercise of discretionary power by regulatory or supervisory authorities when applying EU rules; iii) open political intervention; and iv) state subsidies and public ownership systems that distort competition. But this list of protectionist measures does not exhaust the ways in which political authority affects the behavior and performance of banks. Véron (2013) adds under the heading of “banking nationalism”: i) bailouts and guarantees in the crisis to prevent the failure of non-systemic banks and protect all shareholders; ii) supervisory forbearance, of which the most common form is propensity of national supervisors to refrain from forcing public disclosure of losses by their banks; iii) regulatory laxity, whereby regulatory requirements, such as capital standards and disclosure requirements, are watered down to allow weak banks to avoid recapitalization or restructuring; and iv) ring-fencing, which refers to the practice of states using “moral suasion” to nudge locally operating banks to prioritize the nation in their internal capital and funding allocation decisions.

We would also add to this broad set of definitions the tradition in many European countries of regional or local banks, as, for example, in the case of the German Länder (regional) banks and local Sparkassen, as well as the Spanish cajas de ahorras and Italian banche popolari (mutual or cooperative banks), which are often critical for local credit provision and are often also embedded in local political networks. Analysis of such banks reveals different mixes of political purpose and market authority. In some cases, there has been a balance between the two; in others, political purpose has overwhelmed economic logic and contributed to poor bank performance and failure.

When market authority is in productive tension with social purpose (and the political authority that lies behind it), it prevents banks from engaging in excesses of two kinds. The first is related-party lending and the politicization of banking management such that profit goals are subverted, weakening the prudential standards of the bank and exposing it to high credit risk because of the dominance of social or political goals over market-pricing. The second is excessive risk assumption – via intemperate external borrowing and lending into a market in which risk is also mispriced by herd behavior and the distorted incentives of market bubbles. Both phenomena can be found in particular cases. When sufficiently widespread – and that is more likely when the liberalization and deregulation of national or local financial markets is not accompanied by a commensurate upgrading of bank risk management or prudential supervision – such behavior introduces systemic risk.

But what kind of institutional context constrains such behavior? We find that countries or regions/localities with elements of bank-related political purpose in combination with robust political competition, political party turnover, and a strict delineation between political/social purpose and politicization are most likely to have domestically-controlled banks that both provide sufficient credit and guard against financial instability. The importance of political competition for the nature of political purpose is that when political competition is robust, political purpose remains free from political cronyism in the state-bank relationship, whether that relationship is found at the country-level (as in much of our analysis of Central East European cases) or at the local and regional level where many of our Southern European cases are located. When political purpose degenerates into political cronyism and corruption, which is frequent when a political context is marked by party political influence and control in the absence of competition, market authority is also typically negated. We also find, however, that achieving this optimal mix of social purpose and market authority had by 2016 become increasingly challenging for Europe's peripheral states, and therefore rare.

3. The Outcome of Interest: Variable Bank Performance in East-Central and Southern Europe

Most of the East Central European New Member States (NMS) of the European Union (EU) differ from their southern European counterparts in at least one critical way when it comes to banking. With the exception of Slovenia, all of the post-communist NMS have very high levels of foreign bank ownership (including by large Southern European banks). By contrast, Italy, Spain, Portugal, and Greece (like most other West European States; see Eliassen et al. 2001) have protected preponderant domestic control over their banking sectors – regardless of EU legislation implemented since the 1990s designed to open them up.

Table 1: The Eastern Periphery EU Member States

Country	**Percentage of Foreign-Owned Banks Assets:**	
	2008	**2013**
Bulgaria	84	70
Croatia	91	90
Czech Republic*	84	85
Estonia	98	97
Hungary	84	84
Latvia	66	65
Lithuania	92	93
Poland	77	68
Romania	88	89
Slovakia	99	85
Slovenia	31	34

Source: EBRD 2009 and EBRD Banking Survey for 2013. *Source for Czech Republic is from Claessens/van Horen 2016 because the country had exited EBRD programs before this data was collected.

Table 2: The Southern Periphery EU Member States

Country	Percentage of Foreign-Owned Banks Assets:	
	2008	**2013**
Greece	14	0
Italy	6	6
Portugal	24	23
Spain	2	2

Source: Claessens/van Horen 2015.

Foreign domination in finance in East Central Europe (ECE) allows some broad generalizations to be made about bank performance and variation both within and across the countries of the region. Large-scale foreign bank ownership in ECE stemmed from a combination of post-communist banking crises, EU enlargement, and international institutional pressure (Epstein 2008, 2007; Bonin et al. 2014; Medve-Bálint 2014; Grittersová 2016). Foreign-owned banks increased the availability of credit to East Central European economies overall, where for the first time rich countries largely financed development in a substantial set of poorer ones (EBRD 2009). That credit has been channeled mostly to foreign direct investment (FDI), consumer credit, and mortgage finance, however, with ambiguous consequences for East European convergence and catching-up prospects (Nölke/Vliegenthart 2009; Bohle 2014; Jacoby 2014; Bonin et al. 2014; Epstein 2014a, 2017).

We also know that foreign-owned banks were no more likely to contribute to financial instability than their domestically-controlled counterparts in the NMS (Bonin 2010; Bonin/Louie 2015; Epstein 2013, 2014b, 2017). The largest West European banking groups that invested in ECE, covering 65 percent of banking assets there, did not “cut and run” during the recent US and European debt and currency crises. In other words, they did not repatriate resources (as many had expected) to their home markets to the detriment of eastern markets.

In addition to the foreign-versus-domestic-bank distinction in ECE, there was also significant variation across countries, most notably among the few remaining but large domestically-controlled banks. Among domestic banks, PKO BP in Poland, which was controlled by the state throughout the period under consideration, is the outstanding case of strong credit provision, including through the US financial crisis. The bank has also contributed to Poland’s financial stability over the last decade. Hungary’s OTP bank comes closest to Poland’s PKO in terms of credit and stability. But domestic banks in Latvia, Bulgaria, and Slovenia, as counter-examples, were considerably worse for their national economies, having taken on too much risk, either before, during, or after the US and Eurozone crises. It is precisely this kind of variation among the remaining domestically-controlled banks in ECE that we seek to explain in this paper.

In southern Europe, by comparison, there is much less variation along the foreign-owned-versus domestically-owned-bank dimension because foreign entrants into southern European markets have been few. But there is more variation in bank performance over time in southern Europe compared to eastern Europe given the longer history of state influence over banks under capitalism in that region. And, as in the NMS, we also find variation in bank performance across and within countries. The key distinction within the financial systems of southern Europe has revolved around whether banks were internationally-oriented multinational banking groups with increasingly arms-length relationships to home political and regulatory authorities, or whether they were locally-oriented instead, and susceptible to political purpose and in many cases political interference too.

A notable difference between East and South has been the purposeful deployment of banks in the service of economic catching up and power aggrandizement in southern Europe (via domestic consolidation and outward expansion) – a strategy largely precluded in eastern Europe by international institutional pressure in the context of EU enlargement. In southern Europe, a number of scholars have chronicled how bank liberalization and reform were actually meant to preserve oligopolies, restrict competition, protect banking markets from foreign incursions, and create the conditions for banks' outward expansion (Pérez 1997; Guillén/Tschoegl 2008; De Cecco 2009; Deeg 2013). Sewing up domestic banking markets was perceived as especially important in advance of the single market's completion in the early 1990s – to fortify national banking sectors against intensifying European competition (Dermine 2006). Domestic bank consolidation, followed by international expansion, particularly to the post-communist world, led to a significant internationalization of European banking sectors, including those on Europe's southern periphery (Grossman/Woll 2014). Greek banks moved into the Balkans, while banks from Italy, Spain, and Portugal also developed major markets in ECE and locations further East.

By 2016, however, southern peripheral countries were less concerned about how to boost state power through bank internationalization and profitability than about how to resolve problems in their domestically-oriented banking sectors (or the domestic debt holdings of their otherwise internationalized banks) that ranged from being just ongoing political irritants to existential crises. On the existential side of the spectrum was Italy, whose banking sector was saddled with more than €350 billion worth of non-performing loans and where the failure of Monte dei Paschi di Siena had revealed corporate governance problems that applied across the savings bank sector. Greece's banking sector was also on the European Central Bank (ECB) life support, having suffered ongoing deposit runs over many years of economic crisis and contraction. In Portugal and Spain, the problems were more concentrated (in the regional savings banks, or *cajas* in Spain) and both countries in 2012-17 were dealing with the fallout from bank failures and restructurings – Banco Espírito Santo in Portugal's case and Bankia (built from failing *cajas* in Spain). In both instances, but for different reasons, investors had been hit. In both cases too, problems with these specific banks and difficulties and delays in their post-crisis privatizations were dragging down their respective banking sectors as a whole. Across southern Europe, there was also the ongoing problem of banks' sovereign debt exposures and the threat from the European Banking Union (EBU) that such exposures would be curbed by the ECB and the Single Supervisory Board (SRB) over time.

The uniformly grim depiction above masks important variation across countries and within them, however. There is a case to be made, for example, that the countries in greatest difficulty by 2016/17 – Italy and Greece – had relatively healthy and well-governed banking sectors before 2008 and that it was the US financial shock and its after-effects in the European debt and currency crisis that were the sources of banks' difficulties. Regulatory negligence toward domestically-oriented savings banks in Spain and similar regulatory failures in Portugal by contrast were, according to some observers, the key problems in those two countries. We argue, however, that this binary characterization of better versus worse bank regulation paints an unrealistically simple picture of the causes of variable bank performance. Banks as different in performance as Monte dei Paschi di Siena and Intesa Sanpaolo, for example, both stemmed from the same Italian regulatory milieu. The same could be said of the failed saving banks (*cajas*) in Spain on the one hand versus larger Spanish banks such as La Caixa and Santander on the other. We argue that variable bank performance, which we find both within and across countries, is best explained by the particular constellation of market authority and political/social purpose (and the degree to which cronyism and lack of political competition characterized the latter) underpinning different banks' behavior. In the following section, we theorize what conditions contribute to the productive tension between bank embeddedness on the one hand and market sensitivity on the other.

4. Theorizing the Drivers of Bank Behavior: The Role of Embedded Discipline

Figure 1 counterposes social and political purpose on one dimension against market authority on the other, and we use the spectrum from low to high on each dimension to specify a set of trade-offs. We then locate the banks that we study empirically below in this two-dimensional space so as to characterize particular banks and their behavior and to establish a degree of causality between our independent and dependent variables.

As noted in the previous section, it is the relationship between market authority and social/political purpose insofar as it pertains to *particular* banks that is important here. Thus, a national financial system can differ internally as to the optimality or sub-optimality of the market-social/political purpose mix. This will arise because a certain type of bank is differentially regulated from another; because the national or subnational state attributes a certain kind of political or social purpose to some banks but not others; or because some banks (e.g. those with international reach) are more distant from political authority than those that are territorially limited in scope.

Figure 1: Social/Political Purpose versus Market Authority in National Financial Systems

Market Authority

Low ⟷ **High**

Social/Political Purpose

High ⟷ **Low**

I – Embedded/Low Discipline	**II – Embedded/High Discipline**
Pre-1988 cajas (Spain)	**PKO (Poland)**
State-owned Slovenian banks	**La Caixa (Spain)**
Monte dei Paschi (Italy)	**OTP (Hungary)**
III – Low Embeddness/Low Discipline	**IV – Low Embeddedness/High Discipline**
Parex (Latvia)	**Intesa & Unicredit (Italian)**
CCB (Bulgaria)	**Santander & BBVA (Spain)**
Post-1998 cajas (Spain), e.g. CatalunyaCaixa, Novagalicia, CajaMadrid etc.	
Banco Espirito Santo (Portugal)	

Source: Authors.

We therefore hypothesize the following kinds of causality:

In *quadrant I*, there is a suboptimal mix of social/political purpose and market authority (in which the former prevails over the latter) such that banks will be politicized and/or caught in a web of related-party lending (political excess); political cronyism will characterize the relationship with the state (local, regional, or national), subverting market authority.

In *quadrant II*, there is an optimal mix of social/political purpose and market authority (both are high; one constrains the other) and we refer to this "sweet spot" as "embedded discipline";

In *quadrant III*, weak regulation (which may be purposeful on the part of political authorities – see below) permits or incentivizes market indiscipline (unconstrained borrowing and lending by banks), the mispricing of risk (market excess), and in some cases corruption. These banks' behavior is also undermined by the absence of social purpose – the absence of constructive nationalism, or the absence of nationalism at all;

In *quadrant IV*, there is the possibility of well-regulated open market banking (light-touch state intervention alongside high market authority), in which the potential for risk mispricing or herd behavior is contained.

To elaborate further on bank behavior under these four different sets of circumstances, we start with the notion of "embedded discipline" (quadrant II) to refer to banks that are disciplined in responding to market signals but that are also socially embedded in their political order. "Embedded" in this instance refers to Ruggie's interpretation of Polanyi, in which social purpose dominates market rationality (Polanyi 1944; Ruggie 1982). Whereas discipline prevents a bank from accumulating excessive risk, embeddedness connotes a sensitivity to national or subnational social, political, and economic goals. Banks characterized by "embedded discipline" pay attention to market conditions, but they are not enslaved by them.

The embeddedness of a bank will allow it, under certain circumstances, to buck market trends. When other lenders are holding back, an embedded bank will engage in countercyclical lending, including in a financial crisis, to significant borrowers whose survival is important to the national economy. Being able to act counter-cyclically in a crisis, however, depends on a prior period of relative conservatism. Thus, banks marked by embedded discipline are likely to appear outliers in normal times as well. While other banks are moving into risky assets and activities, banks with embedded discipline appear relatively restrained. While a rigorous and transparent regulatory and supervisory framework provides support to the disciplinary side of the equation, the institutional set-up of bank oversight alone does not explain this outcome of interest in its entirety: alertness to market signals and restrained risk-taking on the one hand paired with bank business activities that advance national or subnational social and political goals on the other.

With respect to "discipline," banks on Europe's periphery varied greatly in risk-taking prior to the financial crisis. Measures of risk accumulation include loan-to-deposit ratios, wholesale borrowing for the purposes of lending (including across borders), and foreign exchange lending. Turning to quadrant II's polar opposite, quadrant III (i.e., weak discipline in open market banking and limited social purpose), if loans exceed a bank's liquidity in deposits, it means a bank is borrowing funds from another source to support lending. Wholesale borrowing could lead to vulnerability in a crisis if that funding cannot be rolled over. Maturity mismatches also increase risk. Foreign exchange lending can introduce currency mismatches, whereby fluctuations in relative values, and particularly currency devaluation in the borrowing country, increases the overall debt load and payments required. This is effectively what happened to the Spanish savings banks, or *cajas*.

In Central and Eastern Europe (CEE), the embedded discipline of domestic banks was more likely to emerge where economic nationalism during bank privatization was centered around preserving some policy discretion as a means for strengthening the country's power position within the EU and international system. Such discretion has amounted, when employed, to credit expansion and restriction and channeling finance to politically favored firms.

Abdelal (2001) has theorized nationalisms with varying social purpose. It turns out that nationalist striving for relative autonomy (as in Poland) was better for domestic bank behavior than economic nationalism geared almost exclusively toward high levels of European integration (as in Latvia) or the absence of any truly nationalist program – where narrow interests prevailed at the expense of the collective enterprise (as in Bulgaria). At the same time, political competition was important for discipline – to restrain nationalist impulses from dominating.

The five CEE countries included here – Poland, Hungary, Slovenia, Bulgaria, and Latvia – are all post-communist accessors to the EU since 2004; they are all striving to catch-up with Western Europe in economic terms; and they all have mixed banking market structures, with four of the five cases, however, having majority foreign ownership. Their banks vary on the independent variables, including social purpose in economic nationalism during bank privatization in the 1990s and early 2000s, political competition, as well as on the development of "embedded discipline" in their domestic banks. Domestic banks in Poland and Hungary served their economies very well or relatively well through the crisis, while in Latvia, Bulgaria, and even Slovenia they did outright damage to their economies. The four southern European cases – Italy, Spain, Portugal, and Greece – reveal similar variance across but also within countries. The case selection is representative of the two respective peripheries and also helps us assess competing explanations for bank behavior – based on the regulatory environment alone, formal institutions in ownership structure, or relative market share of foreign versus domestic banks.

The central research question in this paper, about why some banks serve their economies better than others, should provide further insight into why banks either do or do not assist their states in catching up in the global economy, or for those already approaching the pinnacle of economic power, in staying there. We acknowledge that crisis performance is not the same as developmentalism. Nevertheless, how banks conducted themselves in the run-up to the US catastrophe and after reveals cooperative capacity between states and finance. It also shows the extent to which collective, as opposed to narrow, interests helped fashion the response. We conclude that some states in ECE would likely benefit from more domestic control over finance, while West European states would likely benefit from more foreign bank ownership. But not every country is equally well-poised institutionally or ideationally to use its banks for catching up or for preserving competitiveness.

5. Bank Behavior in East Central and Southern Europe

5.1. Embedded Discipline (Quadrant II)

PKO Bank Polski: The Strongest Case of Embedded Discipline

In terms of the outcome of interest, we categorize majority state-owned Powszechna Kasa Oszczędności Bank Polski (PKO BP) as having contained risk in the run-up to the US financial crisis and as having acted counter-cyclically and in support of the Polish economy since. Expanded lending distinguished PKO BP from most banks operating in the Polish market, particularly foreign-owned ones. By 2011, PKO BP had overtaken Pekao SA, owned by Italy's UniCredit, as Poland's largest bank, measured in terms of loans, deposits, and market capitalization. PKO PB also embarked on its own international strategy, purchasing Sweden's Nordea holdings in Poland for PLN 2.81 billion in 2014, and expanding to serve its corporate clients in other European countries, including Germany, France, Czech Republic, and the UK.

We argue that PKO BP was strongly characterized by embedded discipline and a constructive performance vis-à-vis the Polish economy for the following reasons:

PKO BP's embedded discipline is rooted in Poland's economic nationalism, which, since the transition began, has revolved around preserving some degree of economic self-sufficiency, despite demands by international organizations and the EU that Poland (like other post-communist countries) relinquish policy autonomy in favor of international interdependence and market openness (Epstein 2008). Poland is famous for liberal "shock therapy" in the Balcerowicz Plan from 1990, but that was never the end of the story. Bohle and Greskovits (2007; 2012) refer to Poland as an "embedded neoliberal" state and point to the long-standing debate in the country about the appropriate role of the government in economic management – including through select ownership of strategic assets.

PKO PB was a direct outgrowth of Polish desire to maintain a degree of economic self-sufficiency, *but banking nationalism has been tempered by political competition*. Because political parties were continually debating the appropriate role of the state in backstopping the bank, bank managers kept the bank ready for imminent sale and adopted a more disciplined and conservative strategy than some of their counterparts elsewhere in Poland and in ECE. The principle behind the state's controlling ownership stake was that Poland needed its own major financial player. So, in addition to discipline, national economic and political goals were also a concern.

PKO PB thus maintained a loan-to-deposit ratio below 100 percent – against a sectoral average of 120 percent by mid-2011 – which meant its deposits, not foreign or domestic wholesale borrowing, funded lending. By contrast, Parex Bank in Latvia or the state-run banks in Slovenia were heavily dependent on cross-border borrowing. PKO BP also engaged in considerably less foreign exchange lending than many banks elsewhere in Poland or ECE. And it provided credit or guarantees to economically-important enterprises, namely to the state-owned Social Insurance Institution (ZUS) in 2009 and, with the help of the government and UniCredit's Pekao SA, to Polimex-Mostostal (a construction and engineering firm engaged to upgrade and expand Polish power plants) in 2012.

Poland's "national champion" strategy has been viewed at times as hostile and unfair. But its protectionism is much milder than that of some of its West European counterparts (Epstein 2014a), and there is little doubt that the Polish economy had access to more credit, was less vulnerable to withdrawal of foreign capital flows, and enjoyed stronger growth as a consequence of PKO BP's activities than would have been possible without them.

Hungary's OTP: Highly Embedded but More Weakly Disciplined than PKO

Hungary's OTP (Országos Takarékpénztár és Kereskedelmi Bank Nyrt), the country's biggest bank by market share, has also proven highly embedded in carrying out the state's economic and political goals, retaining domestic depositors and supporting government policies – even those directed against all banks indiscriminately. But it has had a much higher risk profile than PKO BP, which is surprising because OTP, though domestically-managed, is mostly privately- and majority foreign-owned – but through dispersed shareholdings. In theory, it should have been more disciplined by the market than state-owned PKO BP, but was not.

Thus, while OTP contributed to Hungary's vulnerability along some dimensions (it engaged in foreign exchange lending and benefited from mortgage schemes favorable to banks at great cost to Hungarian taxpayers), it also tried to prevent some of the worst excesses. Overall, OTP would seem to be a second case in which a domestic bank is more insulated from an international crisis than foreign banks. OTP had a lower loan-to-deposit ratio than the sectoral average, which allowed it to sustain lending in the crisis counter-cyclically. And while it engaged foreign exchange lending, it was more constrained in doing so than many of its competitors.

More controversially, OTP has helped, or at least not obstructed, the Fidesz government's efforts to limit the role of foreign actors in the economy (Johnson/Barnes 2015). Victor Orbán's government has implemented Europe's biggest bank tax, as well as a financial transactions levy. OTP pays these fees like every other bank, but it has been quiescent – at least publicly. While foreign-owned banks have taken their grievances to the EU, Hungarian, and IMF authorities, OTP has been noticeably absent from these efforts.

We explain OTP's embeddedness and relative banking conservatism as follows:

First, OTP's strategic caution was driven in part by the fact that it did not have a foreign parent bank's funding upon which to draw. OTP's relative insulation from the crisis, which required an IMF bail-out for Hungary in 2008, was further evidenced by the fact that OTP did not join the coalition of banks that requested the ECB and EU to extend crisis management measures beyond the Eurozone. OTP's balance sheet grew by .8 percent between 2007 and 2009, but client loans declined by only one percent. The bank's superior position was also reflected in robust profit growth: its after-tax profits increased by 28.4 percent in 2007-9 when almost every other bank lost money (Várhegyi 2010: 843).

But second, and most critically, like PKO BP, OTP's embedded discipline is rooted in economic nationalism. As in Poland, segments of Hungary's political class have been concerned about maintaining relative autonomy for banks. The first conservative democratic government in Hungary was even more intent than Polish nationalist and leftist elements to maintain a high degree of domestic bank control, via state ownership and private Hungarian owners. While agreeing with the EU and IFIs that some foreign competition would benefit banks, the center-right MDF (the Hungarian Democratic Forum) government (1990-94) privileged domestic owners. It was only after negative reporting in the international financial press in mid-1993 that the government agreed to a recapitalization and privatization plan with the World Bank that involved foreign buyers for two banks, MKB and Budapest Bank. OTP's privatization began in 1995 (under the socialist MSzP), but foreign strategic investors were barred from buying a controlling stake, allowing it to maintain a Hungarian identity and ties to the Hungarian state, even though majority foreign-owned through dispersed shares. *Importantly, it was political competition in Hungary, in addition to political party turnover, that constrained nationalist impulses, without eradicating them entirely*.

Spain's La Caixa – Socially Embedded, Effective Market Engagement

The Barcelona-based Caixabank – a bank controlled by minority shareholdings rather than dispersed ownership – has been one of the most active entities in terms of acquisitions from among the plethora of failed smaller *cajas*. The entity, currently presided over by Isidro Fainé, started off with acquiring two small entities in 2010 (La Caixa and Cajasol). In 2011, it moved on to larger acquisitions when it took over Banca Civica, the first IPS created in Spain (composed of Caja Navarra, Caja Burgos, and Caja Canarias with a later incorporation of Cajasol) and in 2013 merged with Banco de Valencia (Cardenas 2013). The question is, what differentiated La Caixa from Spain's other *cajas*, which, as argued further below, became both disembedded and undisciplined with the deregulation and liberalization of the sector from the late 1980s onwards, with typically disastrous consequences in the crisis after 2008?

La Caixa – now Spain's largest domestic bank after the mergers of recent years – was the only large bank to emerge from Spain's banking crisis unscathed. There seem to be several factors behind its superior performance. First, its long-term management by CEO Isidro Fainé (who became the most important force for banking reform in the sector after he was appointed president of the Spanish Confederation of Cajas de Ahorros in 2010), his commitment to skills and competence in La Caixa, its prudential lending practices in the run up to the crisis, its ongoing commitment to its social role through its charitable foundation, as well as to deep, long-term relational lending, explain a great deal. But the fact that it has kept its distance from politicians – in part because it has been large enough to escape their influence – has been critical and helped to protect it from lending excess or imprudent borrowing.

The bank's governance structure has in fact been carefully designed to minimize political influence and to maintain its commercial probity. Those holding public offices by political appointment of public authorities are forbidden from holding office in the bank's General Assembly and on the Board of Directors and Control Committee. Further, there is an indirect election of delegates representing deposit holders to the General Assembly. They are drawn by lots and elected by General Assembly members from delegates in each electoral district to avoid interference by political parties (Caixabank 2009). To this list of factors should be added the importance of price signals related to its broad portfolio of investments, which has allowed La Caixa to eschew borrowing and building debt obligations on the international wholesale market. Market strength is also derived from La Caixa's broad deposit base and its high income from large-scale equity investments both in Spain (ranging from oil and gas group Repsol to energy provider Gas Natural and mobile phone giant Telefónica) and abroad (telecoms in Brazil, oilfields in Canada, and power stations in Mexico) (Buck 2015).

La Caixa's simultaneous preservation of its original social mission as a *caja de ahorros* demonstrates that an optimal mix of market discipline and social/political purpose is far from impossible in a liberalized and deregulated financial system. La Caixa retains some €500 million every year for investment in extensive social activities (in health, education, science, and international development) through its charitable foundation, which, it argues, is the third largest in the world (Buck 2015).

5.2. Embedded/Low Discipline (Quadrant I)

State-Owned Slovenian Banks – Pro-cyclical Borrowing and Lending

Slovenia had precisely the kind of nationalism in the 1990s and early 2000s that produced highly embedded banks. *But without significant political competition in the transition, economic nationalist impulses* *and embeddedness went unchecked*. Slovenian banks therefore lacked market discipline, becoming highly reliant on cross-border borrowing with maturity mismatches for their operations. When interbank markets froze in September 2008, Slovenian banks were vulnerable. The country then suffered the biggest output decline – an 8 percent contraction in 2009 – of any post-communist EU member, excluding the Baltics, and borrowing costs spiked dramatically at the height of the Eurozone crisis because of bank weakness and the perceived interconnectedness of bank-state finance. The banking sector has been a major source of Slovenia's economic malaise, which has thrown its convergence process into reverse (Epstein 2014b).

Nationalist striving in Slovenia achieved a strong degree of economic autonomy and self-sufficiency – its two largest banks, Nova Ljubljanska Banka (NLB) and Nova Kreditna Banka Maribor (NKBM) were majority state-owned and accounted for nearly half the Slovenian market before the US financial crisis (EBRD 2010: 144) – and while profitability at these two banks and a third state-owned one, Abanka Vipa, was a concern, "managers also had an implicit mandate to provide affordable credit to Slovenian citizens and businesses" (Spendzharova 2014: 50), which led to a toleration for a less profitable banking sector (IMF 2007b). But these banks were also highly pro-cyclical before and during the crisis, and by mid-2011, non-performing loan ratios at the two largest banks were estimated at 15 percent. Using bonds to bail out its banks helped push the government deficit to 5.5 percent of GDP in 2009, which was in violation of the Stability and Growth Pact and prompted the Eurozone's "excessive deficit procedure."Although both NKBM and NLB passed the European Banking Authority's stress tests in the summer of 2011, NLB did so only by a slim margin. That bank was required to raise more capital by the spring of 2012. But again, at the end of 2013, with NPL's in the sector equaling over 20 percent of GDP, the Slovenian state was providing an additional €4.78 billion to eight of the country's banks. In a reversal of previous Slovenian strategy, in 2015 NKBM – one of 15 state-owned firms slated for sale as part of the recovery plan – was fully privatized to the European Bank for Reconstruction and Development (EBRD) and the American investment firm Apollo Global Management.

Italy's Monte dei Paschi di Siena

The story of Italy's Monte dei Paschi – the world's oldest bank, founded 545 years ago – reveals many similarities to that of the post-1988 Spanish *cajas* discussed below, except that it remained locally embedded in a strongly politicized local network of control – which effectively eliminated political competition with regard to banking control and objectives. Like the *cajas*, Monte dei Paschi had been a locally embedded lender, in Siena, Tuscany, with a foundation that funded local social and economic initiatives (the Sienese called the bank their "Bancomat", or "ATM") and has always had close relations with the dominant party in the local political system, until the 1990s the Italian Communist Party, and subsequently with its successor the Italian Democratic party. But again, unlike the Spanish *cajas*, it remained located within this system – which ultimately led to its degradation under inexperienced and incompetent politically-appointed leadership – until its collapse in 2012-14.

Initially created as Monte Pio in 1472 to help the poor and indigent after the plague wiped out half of the city-state of Siena's population, the organization grew into bank lending to local farmers. Renamed in 1624 when Siena was absorbed into the Grand Duchy of Tuscany under the Medici, Monte dei Paschi became a corporation controlled by local politicians in 1936, with profits used to support civic activities, including the world-famous Palio horse race. In 1995, the bank became a joint-stock company and was split into a bank, the Banca Monte dei Paschi di Siena SpA (MPS), and a non-profit foundation, the Fondazione Monte dei Paschi di Siena. The latter organization, whose Board is composed mainly of local political appointees, has been the majority shareholder of Monte dei Paschi (Jassaud 2014).

Monte dei Paschi's big problems began in 2006, when banking inexperience and incompetence collided with the new world of high finance in which greed conspired with politics to produce spectacularly imprudent borrowing and expansion. Giuseppe Mussari – a local lawyer with extensive political connections but no banking experience – was appointed chief executive in 2006. In an example par excellence of political cronyism, Pierluigi Piccini, the mayor of Siena from 1990 to 2001, made his friend Mussari a member of Monte dei Paschi foundation in 2001. With 60 percent of MPS shares, the foundation controlled the bank. Shortly thereafter Mussari became the foundation's director, and in 2006 was appointed by the foundation to the position of MPS CEO. In 2007, Mussari led the financially disastrous acquisition of the Padua-based Banca Antonveneta S.p.A. from the Spanish Santander Bank Group for €9 billion, when Santander itself had valued the bank at only €5.6 billion just months before. Apparently, Mussari neither negotiated nor checked Antonveneta's books to ascertain its real value – or compatibility as a merger prospect for MPS. To finance the Antonveneta deal, MPS sold €2 billion worth of 10-year subordinated upper tier two bonds to retail investors in 2008, and used undisclosed derivatives contracts – with Deutsche Bank and the Japanese Nomura – to cover losses. The latter were to be the bank's, and Mussari's, undoing (Sanderson 2013).

Between 2011 and 2015 Monte dei Paschi lost €14 billion – including €10 billion under the leadership of Fabrizio Viola who replaced Mussari in January 2012 with the aim of rescuing the bank (Sanderson 2016). In October 2014, Giuseppe Mussari, along with former chief executive Antonio Vigni and ex-finance boss Gianluca Baldassarri, was sentenced to three years and six months in jail for misleading regulators in relation to the undisclosed derivatives trades. MPS failed the European Banking Authorities stress test in July 2016. In the third week of December 2016, MPS was effectively nationalized with a government recapitalization after a private-sector based recapitalization failed.

Finally, there was a serious regulatory problem in the supervision of MPS – and other Italian banks in which politically-constituted foundations had a controlling or influential stake. While the Bank of Italy – Italy's most respected institution – appears to have carried out its supervisory responsibilities of the MPS bank to the letter, the MPS foundation fell under the responsibility of the Italian Treasury, whose surveillance of the foundation's conduct appears to have been much weaker and more accommodating of its behavior (Boeri 2013).

5.3. Low Embeddedness/Low Discipline (Quadrant III)

Latvia's Parex Bank

While Poland and Hungary balanced European integration alongside some self-sufficiency, Baltic nationalism and economic policies that followed were not so much predicated on striving for relative autonomy, but rather on re-orienting economic and political relationships westward to the EU and NATO. This included trade, currency, and monetary policy, principally as a means of escaping Russian influence. As for banking, Latvia generally followed the bank privatization policies of other ECE countries, selling most state assets to foreign capital. However, its biggest domestic bank, Parex Bank, did not emerge from state socialism but was founded in 1988 by two private entrepreneurs: Viktors Krasovickis and Valerijs Kargins – the first people (in 1990) to get a private license in the Soviet Union to trade in hard currency (Bohle/Greskovits 2012: 130).

Parex Bank "was one of the early, highly entrepreneurial post-Soviet banks, complete with all the baggage" (Åslund/Dombrovskis 2011: 39f). Not only was Latvian economic nationalism focused on maximizing integration with wider Europe, but in its founding, Parex was divorced from any notion of social purpose. Moreover, the bank proved to be pro-cyclical and destabilizing. Parex was Latvia's second largest bank before the crisis, with three competitive rivals in the Latvian market, all from Sweden (Nordea, Swedbank, and SEB), together comprising 75 percent of the market (EBRD 2008: 146). None of these banks had a robust local deposit base in Latvia. If the Swedish banks mostly financed lending there through borrowing from parent banks, Parex relied on European wholesale markets. If Parex Bank attracted depositors, they were often from abroad – both East and West.

Parex Bank's reliance on foreign funding, both deposits and wholesale, explains why, following Lehman's collapse in September 2008, Parex was on the brink of disaster (EBRD 2009: 184). The bank lost 25 percent of its deposits as early August-November 2008. And just as the US financial crisis was going global and interbank funding markets froze in early 2009, €975 million worth of Parex Bank's syndicated loans came due. This was the equivalent of 4.6 percent of Latvian GDP (Åslund/Dombrovskis 2011: 43). It was therefore Parex Bank's imminent collapse that led Latvia to call in the IMF for an international rescue. The bank had contributed much to Latvia's extreme economic vulnerability.

Bulgaria's Corporate and Commercial Bank (CCB)

If Latvia is a good case for showing that domestic bank ownership per se does not ensure limited risk-taking, counter-cyclicality, or social lending to counter a downturn, the Bulgarian case is useful for showing the limits of even a strong regulatory and supervisory context.

If Polish and Hungarian economic nationalism had been defined in part by striving for some economic self-sufficiency and Latvian nationalism, though highly contested, was geared toward escaping Russian influence through intense westward economic integration, Bulgarian nationalism was notable for its lack of an economic program. As Spendzharova (2014: 34) argues, Bulgarian privatization and regulatory reform in the post-communist transition were characterized by a "grabbing hand strategy […] where governing elites created intransparent markets and fueled corruption."

After the banking crisis of the late 1990s, however, Bulgaria created a currency board and a highly independent central bank that ultimately engaged in strong prudential supervision. Most banks were sold to foreign owners. Thus, the institutional set-up boded well for rigorous and independent bank oversight. But while it effectively supervised foreign banks (see especially Spendzharova 2014), *political connections meant that domestic Bulgarian banks were apparently given a free ride and were able to grow as a consequence*.

This mattered by 2014 when two domestic banks had grown in market share to become the third and fourth largest lenders in the country. One of those banks, Corporate and Commercial Bank (CCB), experienced devastating deposit runs starting in June 2014. The bank was closed in June and its license was revoked in November. By the end of 2014, its liquidation was being planned. Although the origins of the deposit runs are still disputed, personal rivalry between CCB's majority shareholder, Tzvetan Vassilev, and a major borrower at the bank, Delian Peevski, was at the center of events that sparked the panic-creating deposit withdrawals in mid-June. There were other family members, media empire,s and multiple cross-shareholdings involved in the crisis, but the allegation that Vassilev attempted Peevski's murder through a hit squad was at its core.

The original bank runs also put enormous liquidity pressure on Bulgaria's First Investment Bank, which required a government bail-out (Raiffeisen 2015: 40). FiBank was also long suspected of illegal activity, including money laundering on behalf of Bulgarian and foreign criminals, in addition to its legitimate retail business. It is therefore the absence of any economic nationalist program with social purpose at its core and the subversion by powerful (often criminal) interests of bank oversight that explain the rise of undisciplined and disembedded domestic banks in Bulgaria.

Spain's Cajas (CatalunyaCaixa, Novagalicia, Caja Madris etc. – and Bankia)

Many of Spain's most problematic savings banks, or *cajas de ahorros*, became crisis-ridden as a result of a series of factors not too dissimilar to those found in the Latvian and Bulgarian cases. Once locally embedded regional banks, linked to charities, and with important social and cultural functions, following the deregulation and liberalization of Spain's financial sector, they either engaged in banking activities beyond their localities and in areas where they had little competence and/or were undermined by political corruption (Cardenas 2013; IMF 2006). Often incompetence, corruption, and undisciplined borrowing were apparent in the same institution: research shows that *cajas* led by CEOs with no previous banking experience, no graduate education, and who were politically connected did much worse than others in the run up to the crisis (Cuñat/Garicano 2010). The costs – social and economic – of the failure of a great many *cajas* in the crisis have been huge. Just three of the most problematic *cajas* – Bankia, CatalunyaCaixa, and Novagalicia – had capital deficits (to be covered partly or fully by the taxpayer) of €54 billion – over five percent of Spanish GDP (Garicano 2012).

The *cajas* had always had quite different corporate governance structures from commercial banks; indeed, many board members have been directly appointed by local and regional governments, and politicians have often exerted a powerful influence over their operations. Originally, these were highly embedded banks in the sense that they were imbued with social purpose and their activities limited to particular communities, but over time, following financial reforms, they quickly extended their business to other parts of their region. After liberalization in 1988, all restrictions on location were lifted, and the process of *caja* branch expansion and reach began, which accelerated from the early 1990s until the crash in 2009. In terms of our diagram, the *cajas* moved from quadrant I (market discipline was low, but this mattered little when they were limited to lending from deposits to solvent clients) to quadrant III. In the process, their role in constructive local relational banking was destroyed – even if many also continued with their charitable social welfare work.

Many *cajas* also either invested in or lent heavily to real estate developers in the absence of reliable risk analysis. Extensive corruption emerged from the nexus of *cajas*, real estate developers and regional politicians, with particularly blatant examples at Caja Madrid (where subprime lending was a big problem) and Valencia's Caja de Ahorros del Mediterráneo (CAM), which engaged in dubious loans to developers *and the regional Popular Party government* (Cardenas 2013). These and other problematic *cajas* were busy reclassifying, refinancing, and extending loans to cover up their losses in the years running up to their collapse. Which raises the question of why the Bank of Spain (an otherwise solid and highly professional institution) failed to fulfill its supervisory mandate and tackle the root problems with an audit of the sector early on.

Part of the explanation comes from standard issues of regulatory failure: the career concerns of regulators, an unwillingness to expose problems that should have been detected earlier, and the lack of an adequate bank resolution fund. The unintended consequences of the adoption of dynamic provisioning – a tool endorsed by Basel III in December 2010 – have also been mentioned as a factor encouraging imprudent lending and borrowing (Garicano 2012). By forcing banks to increase provisions without reference to any specific loan, dynamic provisioning may actually have helped conceal for a certain amount of time the extent of the *caja*'s liabilities. But as in the case of Bulgaria's central bank, political connections seem to have constrained the Bank of Spain from intervening effectively in the sector. As Garicano (2012) argues, "the supervisor, confronted with powerful and well connected ex-politicians decided to look the other way in the face of obvious building trouble." But political considerations also determined the less-than-effective solutions ultimately put in place, as in the merger of sick *cajas* in Catalonia and Galicia (as well as the Bank of Spain's approval of Bankia), which were implemented in accordance with a political rather than economic logic.

The worst such case – the result of Spanish Popular Party's influence and control of savings banks, in addition to the inability of the Bank of Spain to fight them – involved the merger of a number of failed *cajas* including Bancaja from Valencia and Caja Madrid in the same undercapitalized entity, Bankia BFA. Both Bancaja and Caja Madrid were responsible for bad party-related lending, while Caja Madrid also bought City National Bank of Florida in 2008 for an estimated US $1.7 billion – a price equal to three times its book value – leading to losses totaling €500 million (Cardenas 2013). The merged entity Bankia also suffered from incompetent management, poor supervision, and political meddling by the Spanish Socialist government led by Luis Rodríguez Zapatero. Zapatero backed an IPO of Bankia – which was floated on the basis of unaudited accounts (see Mallet/Johnson 2012) – and convinced Spanish banks and corporations to take on shares "in the national interest" when international investors showed insufficient interest. The rest of the shares were sold to some 400,000 individual savers. Two years after Bankia's 2011 IPO, its stock was trading at around 90 percent below its listing price. By late 2012, its shares were worthless and it had received €22 billion of taxpayers' money in a series of bailouts.

Portugal's Banco Espirito Santo

In August 2014, Portugal's Banco Espirito Santo was also rescued by the state, after reporting €3.6 billion in losses, but whose shareholders had lost some €10 billion by the time the bank collapsed. In this case, the problem lay with a family-based controlling structure via various financial vehicles, which allowed the family patriarch Ricardo Espirito Santo Salgado to finance the family's own companies from the bank and to build up high levels of debt, especially after the financial crisis hit Portugal in 2010. Under the terms of Portugal's 2011 international bailout, Portuguese banks, including Banco Espirito Santo, were no longer allowed to pay dividends to their shareholders, including the Espirito Santo family – which had adverse consequences for the family's various companies.

Poor and incestuous management practices combined again with a bifurcated and dysfunctional supervisory system: The Espirito Santo's family companies were mostly registered in Luxembourg, while their main asset – Banco Espirito Santo – was in Lisbon. Little information, apparently, was shared between the two countries' regulators, and allowed the perilous state of the companies' finances to remain hidden (Goncalves et al. 2014).

5.4. Low Embeddedness/High Discipline (Quadrant IV)

Southern Europe's Multinational Banks

Southern Europe's increasingly multinational banks – notably two Italian banks, Unicredit and Intesa San Paolo, and two Spanish banks, Santander and BBVA (all but Intesa have dispersed ownership), – have transitioned, to use Richard Deeg's felicitous phrase, from "zeros to heroes" over the span of the last three decades (Deeg 2012). From relatively small domestic retail banks, these banks have become disembedded from their domestic markets (and the political milieu of their erstwhile local counterparts) and created powerful international empires that emerged relatively unscathed from the international financial crisis – although Santander did better in this respect than Unicredit which, as Deeg (2012: 24) writes, "was less efficient, held lower reserves, and was badly hurt by the general financial crisis of 2008-09 which was especially acute in much of CEE."

The story of this success, although closely connected to cautious and prudent management while under an expansionist phase reveals a high level of market discipline on these banks' operations, there is clearly a political dimension as well – but one that is quite different from the cozy cronyism of the smaller and politically embedded Italian and Spanish local banks. As financial investors in multiple foreign markets – mainly Latin American in the two Spanish cases (though Santander also has extensive European operations and took over the British Abbey National in 2005) and Central and East European in the two Italian cases – these banks managed first to escape the political machination of their system's politicians, but only after they went through a phase of national financial "developmentalism," during which political support for domestic consolidation was provided to make these banks too large to be taken over. This financial "national champion" strategy – part and parcel, however, of domestic banking liberalization and deregulation, combining internal consolidation and external expansion – was politically inspired but created transnational entities that were no longer beholden to domestic political impulses. Banking developmental nationalism in these cases, including restricting the entry of foreign banks, created the domestic conditions for outward expansion. The international profile that these banks ultimately assumed led them to repudiate their national embeddedness and national regulation and has made them powerful supporters of the EU's shift since 2012 to European banking supervision under the European Central Bank.

In the cases of both Unicredit and Santander, strong leadership, astute market positioning, and unusual (for Europe) carefully considered cross-border acquisitions (with Abbey National for Santander, and the German HVB Bank for Unicredit) all combined to create a strong contrast with banks such as Monte dei Paschi. While the latter remained mired in opaque structures of control, Santander and Unicredit both shifted their corporate governance systems towards an Anglo-American style shareholder-value philosophy and operation. National regulation by the Spanish and Italian Central Banks also worked much more effectively at home for Santander and Unicredit than for their smaller, more politically embedded domestic peers. Low embeddedness and market discipline therefore paid off for these new transnational financial groups.

6. Conclusion

In Central-Eastern Europe we have two cases of nationalist striving for some economic autonomy with political competition (Poland and Hungary), one case of integrationist nationalism (Latvia), one case of weak or even non-existent economic nationalism (Bulgaria), and a fifth case of highly embedded banks with little market discipline because of weak political competition (Slovenia). All five East Central European cases confirm the importance of embedded discipline: where states were driven by the perceived need for some self-sufficiency and domestic banks were carved out of state-socialist monobanks for that purpose, they have tended to be risk-averse, counter-cyclical stabilizers – but only if political competition also constrained nationalist impulses. Where economic nationalism was either geared toward integration or was absent, domestic banks offered no political or economic upside to the state and even did damage to their national economies.

In Southern Europe, we have greater variation both within and between systems. Both Italy and Spain have their problem banks who begin to engender systemic instability during the financial crisis. The only example of a southern European bank in our "embedded discipline" sweet spot (quadrant II) is the Spanish La Caixa, also the only large bank to emerge from Spain's banking crisis unscathed. Our other southern cases all lacked market discipline whether politically or social embedded or not. Yet both countries have also produced a number of highly successful transnational banks, which emerged from the processes of deregulation and liberalization of banking markets in the 1990s and whose domestic consolidation via bank mergers created a platform for subsequent international expansion.

In both Southern and Central Eastern Europe the critical variable seems to be market discipline. Even socially and politically embedded banks like Spain's La Caixa, the Polish OTP, or Hungarian PKO can do well if run according to a cautious and prudential financial logic. And banks that have transcended their domestic systems and national embeddedness can also flourish when, as in the cases of Santander and Unicredit, they are run in line with the same principles. The weakly embedded Portuguese Banco Santo Espirito failed because those principles were ignored in a context of regulatory dysfunctionality. Embeddedness, absent market discipline however, led to the spectacular failure of the Italian Monte dei Paschi and contribution of the state-owned Slovenian banks to the decline of Slovenia's economy. That so few banks can be found in our "embedded discipline" sweet spot (quadrant II) suggests that nationalism and banking very rarely make happy bedfellows.

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