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Summary

Spain aims to use Brexit to change Gibraltar's 'unfair' economic model.
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Foreign Policy

Spain aims to use Brexit to change Gibraltar's 'unfair' economic model…

The government sees a chance in the Brexit negotiations to exert pressure on the UK overseas territory of Gibraltar, which voted 96% in favour of remaining in the EU, to change its low-tax model which it regards as a 'tax haven' that engages in 'unfair competition'.

Following the European Council's approval of the Brexit negotiation guidelines, which among other things condition any future relationship between Gibraltar and the EU to prior agreement between the UK and Spain, Spain's Foreign Ministry set out its position in a document sent to parliament.

Spain entered the EU in 1986, 13 years after the UK and along with it Gibraltar, and had to accept the Rock's special regime. But since then Gibraltar's position has allegedly 'led to a situation of unjust privilege'.

Madrid points out that Gibraltar enjoys the four EU freedoms (free movement of people, goods, services and capital), yet is not part of the customs union or subject to British law. As a result, 'it has developed its own regime that is extremely permissive on issues such as tax, customs and business creation, which, in practice, has turned it into a tax haven'.

The maximum rate on personal income is 25% and corporate tax is 10%, both much lower than in Spain but comparable to some other EU jurisdictions such as Luxembourg and Dublin. Gibraltar does not have to apply VAT, and there is no tax on capital gains, wealth and inheritance and no withholding tax. There are more companies registered in Gibraltar than the 11,400 households.

Gibraltar received a glowing review from the OECD of its record on exchange of tax information and transparency. Its overall rating was largely compliant, the same as the UK, Germany and the US.

Madrid refuses to sign bilateral tax information and double taxation agreements with Gibraltar as it views this as tantamount to recognising the Rock.

The Popular Party government says it will not use Brexit to resolve the age-old sovereignty dispute (Gibraltar was ceded to Great Britain under the 1713 Treaty of Utrecht), but it will push for a post-Brexit situation that 'prevents an economic situation of unfair competition'.

Gibraltar has rejected Madrid's offer of shared sovereignty as a way to remain part of the EU.

While the Spanish government is adopting a predictably hard stance towards Gibraltar, as it sees an opportunity to press its case, it would like a 'soft' Brexit because of the magnitude of the trade and investment relation with the UK and the large number of Britons living in Spain and Spaniards in the UK.

Madrid would like little change in the current legislation on the rights of European citizens already resident in the UK and British nationals in the EU. One proposal is for the rights of these nationals to be respected if they have lived in these countries for more than five years.

Government grants citizenship to Venezuelan critic

The government granted Spanish citizenship to Miguel Henrique Otero, the editor of *El Nacional*, the only remaining national newspaper in Venezuela still openly critical of President Nicolas Maduro's increasingly authoritarian government.

Otero fled Venezuela 'for fear of reprisals' after having received 'threats from the Venezuelan regime'. He runs the newspaper from Spain.

Relations between Madrid and Caracas have been tense for a decade. In the most publicised spat, King Juan Carlos told Maduro's predecessor, Hugo Chávez, to 'shut up' at the 2007 Ibero-American summit in Chile after he called José María Aznar, a former conservative Prime Minister, a 'fascist'.

In 2014, the Venezuelan government recalled its Ambassador after Aznar's successor, Prime Minister Mariano Rajoy voiced support for Leopoldo López, a jailed opposition leader. López was imprisoned in 2015 for 14 years for inciting violence during protests (a sentence upheld by the Supreme Court in February 2017).

José Luis Rodríguez Zapatero, a former Socialist Prime Minister, is attempting to mediate between the Venezuelan government and the opposition, but with no results so far.

Earlier this month Maduro accused Movistar, a subsidiary of Spain's Telefónica, which has been operating in Venezuela since 2005, of helping to orchestrate protests against his government. Movistar clients used their mobiles to send messages in support of protests.

Hyperinflation and an economy that contracted 10% last year and continues to shrink, coupled with a regime that has become a dictatorship, are driving Venezuelans to emigrate to Spain.

Domestic Scene

Popular Party rocked by yet more corruption scandals

The corruption scandals that have engulfed the ruling Popular Party (PP) seem to be never ending. In the latest one, Ignacio Gonzalez, a former regional Prime Minister of Madrid (2012-15), was arrested and imprisoned as part of a probe into the alleged misuse of public funds at a water company, while his predecessor, Esperanza Aguirre (2003-12) and then leader of the PP group in the city's parliament, resigned after admitting she had failed to properly oversee the actions of her protégé.

Dubbed Operation Lezo, the investigation has produced some high-profile arrests, including Javier López Madrid, the CEO of the big construction company OHL. His father-in-law, Juan Miguel Villar Mir, the controlling shareholder in OHL, and Eduardo Zaplana, a former Mayor of Benidorm and Spain's Labour Minister from 2002 to 2004 were named in a court list of 60 individuals targeted in the probe.

The publicly-owned water company, Canal de Isabel II, controlled at the time by the then PP-led Madrid government, is believed to have been involved in suspicious transactions, including the purchase of a company in Latin America at a price way above its market value.

The Civil Guard searched OHL's headquarters in Madrid and took away documents regarding the 2007 contract for building and operating a commuter train service and the alleged payment of a commission to González in his Swiss bank account.

In other ongoing cases of corruption, embezzlement and misappropriation of public funds, Francisco Granados, a former Madrid PP Secretary General, has been in prison since October 2014 awaiting trial. Last February judges handed down 11 convictions in the Gürtel bribes-for-contracts case (between 1999 and 2005) that is still in the courts.

Rajoy has been summoned to testify in the Gürtel case. He is not accused of any wrongdoing himself. Rajoy has always denied any knowledge of what went on.

Fourteen people who held senior political posts when Aguirre was Prime Minister of the Madrid regional government, including four mayors and five members of her cabinet, are under investigation.

The far-left party Podemos seized on the latest scandals and vowed to table a no-confidence vote in parliament against Prime Minister Mariano Rajoy, although it has no chance of succeeding as it does not have the support of the Socialists or the centrist Ciudadanos. The deeply divided Socialists are embroiled in a bruising process for choosing a new leader in a primary election to be held later this month with three candidates.

Ninety-six per cent of those surveyed by Metroscopia last month said they believed more corruption scandals would be unearthed.

In a separate development regarding the long-running investigation into the unexplained wealth of Jordi Pujol, a former regional Prime Minister of Catalonia (1980-2003), his wife and their seven children, police said the family had hidden more than €70 million in Andorra.

An unearthed document, dated 1995, showed Pujol's wife Marta giving coded instructions to her bank to move money (she addressed herself to 'Reverend *Mosén*' and called herself 'mother superior' of a Congregation). The Pujol family said the document was false.

Her eldest son, Jordi, was jailed without bail last month after a judge decided he was obstructing an investigation into alleged money laundering and tax fraud carried out by his family.

Population slips for fifth consecutive year…

Spain's registered population continued to fall in 2016, albeit by a marginal amount of 17,982 to 46.5 million (-726,295 since 2012), according to provisional figures by the National Statistics Institute (INE).

The fall, for the fifth straight year, was due to foreigners leaving the country (see Figure 1). The number of Spaniards rose by 50,741 to 41.98 million while foreigners dropped by 68,723 to 4.54 million (9.8% of the total population). The number of foreigners at 1 January 2017 was 1.3 million below the peak of 5.8 million in 2011.

The largest fall was in the number of Rumanians (-32,930 to 684,532), followed by Britons (-19,832 to 236,669), and the biggest rise in the Chinese (+7,446 to 207,593).

Figure 1. Registered foreign population by the top-10 countries of origin, 1/I/2017 and 1/I/2016

	2017 (1)	2016	Change
Morocco	747,872	755,459	-7,587
Rumania	684,532	717,462	-32,930
UK	236,669	256,501	-19,832
China	**207,593**	**200,147**	**+7,446**
Italy	189,005	182,269	+6,736
Colombia	145,055	140,527	+4,528
Ecuador	141,582	158,285	-16,703
Bulgaria	126,997	133,951	-6,954
Germany	110,378	119,820	-9,442
Ukraine	102,786	99,060	+3,726
Other	1,857,389	1,855,100	+2,289
Total	4,549,858	4,618,581	-68,723

(1) Provisional figures.

Source: INE.

While Rumanians are leaving the country because of the lack of employment prospects (the jobless rate among foreigners was 25.5% at the end of March compared with 17.8% for Spaniards), some Britons, particularly elderly ones, are returning home because of uncertainty over Brexit and whether they will lose their health rights when the UK stops being a member of the EU.

Also, fewer Britons are buying houses in Spain, due to the slump in sterling since last year's vote to leave the EU and uncertainty over the terms of Brexit. Britons are still the biggest foreign buyers, but having accounted for more than 21% of total purchases by foreigners in 2015, they made up 19% of 2016's total.

Spain's population increased every year from 2008 to 2012 when it began to fall as the country's recession deepened (see Figure 2).

Figure 2. The rise and fall of Spain's population (million) (1)

	2008	2010	2012	2014	2016	2017
Spaniards	**40.88**	**41.27**	**41.52**	**41.74**	**41.93**	**41.98**
Foreigners	5.26	5.74	5.73	5.02	4.61	4.54
EU-28	2.10	2.35	2.44	2.05	1.84	1.76
Non EU	3.16	3.39	3.29	2.96	2.77	2.78
Total	46.15	47.02	47.26	46.77	46.55	46.53
% foreigners	11.4	12.2	12.1	10.7	9.9	9.8

(1) At 1 January of each year and based on those registered in town halls.

Source: INE.

Earlier this year the government created a commission to find ways to encourage women to have more children. Spain's fertility rate of 1.3 children is one of the lowest in the world.

… More than 27,000 foreigners obtain 'golden visas' for investing in Spain

A total of 27,301 non-EU citizens have won permission to live and work in Spain since the government introduced a law in 2013 granting these rights in return for buying expensive property, investing in government securities or filling certain qualified jobs.

The so-called 'golden visas', which also exist in other EU countries, were introduced after the 2008 global downturn. In Spain's case, residency is automatically granted when purchasing a property for €500,000 or more or investing at least €2 million in public debt, among other conditions.

The launch of these visas had little impact until the government softened the requirements in 2015 and extended the law to include the wider family of those investing.

The largest number of property investors are the Chinese (702), followed by Russians (see Figure 3). In all, 2,236 people obtained 'golden visas' by this route.

Figure 3. Golden visas in return for buying property worth €500 million

Country of origin	Amount (€ million)	Number of investors
China	489.0	702
Russia	502.6	640
Ukraine	62.5	83
Egypt	36.4	59
Venezuela	49.6	54
Saudi Arabia	33.6	52
US	31.9	39

Source: Economy Ministry.

Parliament calls for Franco's remains to be moved from Valley of Fallen basilica

Lawmakers voted in favour of moving the tomb of General Francisco Franco, Spain's dictator (1939-75), from the Valley of Fallen civil war monument in the mountains near Madrid.

The 198-1 vote with 140 abstentions does not mean the minority conservative Popular Party (PP) government has to act on it as MPs voted on a non-binding motion, put forward by the Socialists, which the executive can ignore. However, the move does put the PP under some pressure.

The Socialists say the monument needs to be transformed 'so it ceases to be a place of Francoist and 'national-Catholic' memory and is remade as a space for the culture of reconciliation and collective democratic memory, where the victims of the civil war and the dictatorship are recognised and treated with dignity'.

The conservative PP rejected a similar motion in 2013 when it had an absolute majority, believing it would open old wounds. This time the party abstained, suggesting a softening. The Catalan Republican Left also abstained as it wanted the motion to be much bolder.

Labour from the losing Republican side of the 1936-39 Civil War was used to build over 19 years the Valley of the Fallen, which is crowned by the world's highest cross (150 metres). Some 34,000 people from both sides are buried there but 12,000 of them, mostly republicans, have never been identified.

The bitterly divisive monument has long been the target of groups that want to re-address the past and produce a narrative of the fratricidal conflict that can be accepted by all sides.

Parliament also called for the creation of a commission to investigate the whereabouts of the remains of an estimated 115,000 people killed by Nationalist forces during the conflict and by the Francoist state after it, a recommendation backed by the United Nations.

After taking office at the end of 2011, the PP closed the Civil War and Dictatorship Victims Office, which had been created by the previous Socialist government. One of its roles was to help victims search for their loved ones in mass graves from that period and the aftermath in the 1940s.

The setting up of the office followed the Socialists' 2007 Historical Memory Law, which the PP voted against and whose funding has been ceased.

Press freedom report reprimands government for its 'gag law'

Reporters Without Borders (RWB) takes the government to task in its annual report on the state of media freedom in the world for its 'gag law', which it says, restricts press freedom.

The Citizen Security Protection Law, commonly referred to as the 'gag law', was adopted in 2015 by the previous Popular Party (PP) government when it had an absolute majority in parliament.

It followed massive protests outside parliament and other public places against corruption and austerity measures, usually led by supporters of the anti-establishment Podemos, which went on to win 71 seats in parliament in last June's general election and led to a PP minority government.

The law tightens public security laws and imposes heavy fines for taking part in an 'unauthorised protest', using social media to call on people to protest and trying to stop an eviction taking place, among other restrictions.

Opposition parties are calling for the law to be repealed.

Spain improved its position in the RWB ranking from 34th to 29th place out of 180 countries, but this was due to worsening freedoms in other countries and not to any improvements in Spain (see Figure 4). The index is based on indicators of pluralism, media independence and respect for the safety and freedom of journalists.

Figure 4. 2017 World Press Freedom Index

Country ranking	Score
1. Norway	7.60
16. Germany	14.97
29. Spain	**18.69**
39. France	22.24
40. UK	22.26
43. US	23.88
52. Italy	26.26

Source: Reporters Without Borders.

The Economy

Government finally close to gaining support for 2017 budget

Just one member of parliament holds the approval of Spain's 2017 budget in his hands.

The conservative Popular Party, with 137 deputies in the 350-seat Congress, needs the support of 176 MPs and is one short. The centrist Ciudadanos was the first party to back the government's budget and the Basque Nationalist Party (PNV) recently came on board.

That leaves Pedro Quevedo, a little known MP for Nueva Canarias, a small party from the Canary Islands, who has yet to be won over. He is holding out for more money for the Canary Islands.

The PNV's support came at the cost of a reduction of €569 million in the contribution, known as the *cupo* (quota), that the Basque government makes to the central government in Madrid to cover areas not transferred to it, such as defence and foreign affairs.

The Basque Country enjoys considerable autonomy, dating from historic rights restored in 1979 after the end of the Franco dictatorship. It has its own special deal, which is regarded as particularly unfair by poorer regions such as Extremadura and Andalusia and also by the pro-independence camp in richer Catalonia.

The 2017 budget could not be approved last year because the country was 10 months without a functioning government as a result of two inconclusive elections. Last year's fiscal deficit (4.54% of GDP) came in, for the first time since 2008, within the EU imposed parameter (4.6%).

The deficit continues to narrow from a high of 11% of GDP in 2009 to an expected 3.1% this year (see Figure 5).

Figure 5. Outcome of 2016 general government balance and 2017 targets (% of GDP)

	2016 outcome	2017 targets
Central government	-2.52	-1.1
Regional governments	-0.82	-0.6
Local governments	+0.64	0.0
Social Security	-1.62	-1.4
Total fiscal balance	-4.33	-3.1

Source: Finance Ministry.

Failure to approve the budget would probably trigger a snap election which the PP would win, according to the latest poll by the state-funded CIS. The PP would capture 31.5% of votes compared to 19.9% for the Socialists.19.7% for the far left Unidos Podemos and 14.9% for Ciudadanos.

Unemployment slightly up at 18.8%, forecast at 11.2% in 2020

The jobless rate inched up in the first quarter, traditionally a weak period after the seasonal labour hired for Christmas, to 18.8%.

The number of unemployment stood at 4.25 million, down more than 500,000 over the last 12 months but slightly higher than at the end of 2016. Easter this year fell in April, not March.

With the economy projected to grow by close to 3%, job creation will pick up as the year advances. This summer looks like setting yet another tourism record.

April's figure for registered unemployment (based on those recorded every month in the government's employment centres as opposed to a quarterly household survey) showed a sharp fall on 129,281 in the number of jobless to 3.7 million.

While the job numbers are improving, the quality of employment is cause for concern. Around one-quarter of contracts signed last less than a week and 40% less than a month. There is a constant rotation of workers on short-term contracts. More than seven in 10 employees aged between 15 and 24 in Spain had a temporary contract in 2016 (see Figure 6).

Figure 6. Share of temporary employees aged 15-64 in EU countries, 2016 (%)

Country	%
Poland	27.5
Spain	**26.1**
France	16.1
EU	14.2
Italy	14.0
Germany	13.2
UK	6.0
Rumania	1.4

Source: Eurostat.

The number of workers who sign more than 10 contracts a year increased from 150,000 in 2012 to 270,000 last year, according to INE.

Prime Minister Mariano Rojo has promised to end the current legislature in 2020 (assuming an early election is not called) with a jobless rate of 11.2% and 20 million jobholders, thus returning to the pre-crisis number in 2008 before the property bubble burst and recession. At the end of March, 18.44 million people were in employment.

Even if this is achieved, the unemployment rate would still be higher than the 8% in 2008, but less than half the peak of 27% in 2013.

Most of the fall in the jobless rate is due to the creation of precarious, low-quality jobs. Some 95% of contracts signed since the government's labour reforms in 2012 are temporary or part-time. Many of these jobs are in cyclical industries such as tourism and construction and offer little or no security, in stark contrast to the lucky ones on permanent contracts including most public sector workers.

The government and trade unions reached an agreement in March to move 250,000 public sector workers, mostly in education and health, from short-term to permanent contracts over the next three years.

Three of Spain's regions were among the 10 regions in the EU with the highest unemployment rates in 2016, all of them well above Spain's national jobless rate: Andalucia (28.9%), Extremadura (27.5%) and the Canary Islands (26.1%).

Spain loses its first renewable energy case in international arbitrage court

The World Bank's International Centre for Settlement of Investment Disputes (ICSID) ruled partially in favour of the British-based Eiser Infrastructure and its affiliate Solar

Energy Luxembourg and ordered the Spanish state to pay €128 million plus interest in compensation for reducing subsidies to the renewable energy sector after they invested in three solar plants.
The decision was a setback as Spain faces 26 other cases filed by companies that invested in solar energy projects before the cutbacks, first by the Socialist government in 2010 and then by Popular Party administration in 2013.

Outward direct investment highest of EU countries in 2016

Spanish companies invested US$53.9 billion abroad last year, the highest amount among EU countries (see Figure 7).

Figure 7. Foreign direct investment outward flows, 2010-16 (US$ bn) (1)

	2010	2011	2012	2013	2014	2015	2016
France	48.1	51.5	35.4	20.4	48.0	37.5	52.3
Germany	125.4	78.0	62.2	36.7	84.9	81.1	39.9
Italy	32.6	53.7	8.0	25.1	26.3	22.3	22.7
Spain	**38.4**	**45.2**	**-2.5**	**27.5**	**45.0**	**57.9**	**53.9**
UK	48.0	95.6	20.8	40.5	-148.4	-82.1	-12.6

Note: figures rounded to nearest decimal.

Inward foreign direct investment (FDI) was the fourth-highest of EU countries at US$30.8, up from US$25.3 billion (see Figure 8).

Figure 8. Foreign direct investment inward flows, 2010-16 (US$ bn) (1)

	2010	2011	2012	2013	2014	2015	2016(p)
France	13.9	31.7	16.1	34.3	0.2	39.6	34.1
Germany	65.6	67.5	28.2	10.0	-10.7	21.1	14.9
Italy	9.1	34.3	0.09	24.3	23.2	19.3	28.9
Spain	**40.3**	**32.4**	**24.7**	**52.2**	**34.3**	**25.3**	**30.8**
UK	58.1	42.2	55.6	51.6	44.8	33.0	253.7

Note: figures rounded to nearest decimal. (1) Excluding special purpose entities which have little or no employment, physical presence, or operations in a country but do provide important services to multinational enterprises, such as holding assets and liabilities or raising capital. (P) Provisional.

Source: OECD and IMF.

The figures exclude special purpose entities and so is productive investment.[1]

Spain's stock of investment of outward investment stood at $461 billion at the end of 2015 (latest year available) and its inward position was $508.3 billion (see Figures x and 9).

Figure 9. FDI outward and inward stocks, 2013-15 (US$ mn)

	2013	2014	2015		2013	2014	2015
Outward				**Inward**			
France	1,325,443	1,245,091	1,198,805	France	761,383	680,946	660,175
Germany	1,448,431	1,378,657	1,376,809	Germany	955,168	848,139	795,175
Italy	533,039	490,650	467,314	Italy	365,004	352,482	337,093
Spain	**533,235**	**492,642**	**461,026**	**Spain**	**596,100**	**541,424**	**508,346**
UK	1,796,164	1,681,948	1,558,180	UK	1,512,648	1,628,573	1,408,294

Source: OECD and IMF.

Corporate scene

US Cordish resubmits mega casino and hotel project for Madrid

The Cordish companies, a US leisure group, submitted a new proposal to build a €2.2 billion casino and hotel complex on the outskirts of Madrid, following the rejection in March of its original plan.

If it is approved, it would be one of the biggest ever foreign investment projects in Spain and create much-needed jobs.

The new project has more leisure facilities including an artificial lagoon, a beach with free access and a 'World Soccer Hall of Fame Museum' (see Figure 10). Gaming would account for around 15% of the total area

[1] For an explanation of SPEs see https://www.oecd.org/daf/inv/How-MNEs-channel-investments.pdf.

Figure 10. Cordish's revised casino and leisure complex

The Madrid regional government said the initial project was not 'viable from an economic and organisational point of view'. It was particularly concerned about it having to invest at least €340 million in building roads and train connections to the site.

In its new proposal Cordish said it would 'assume the execution of the necessary public infrastructure'.

Court seeks trial of ex-IMF chief for Bankia listing…

The National Court recommended that Rodrigo Rato, a former IMF head (2010-12) and before that Economy Minister, and 31 others should go on trial for fraud and falsifying financial statements over the flotation in 2011 of Bankia, which later had to be bailed out.

Rato, Bankia's Chairman (2010-12), and 64 others were sentenced earlier this year in another case for misusing Bankia's corporate credit card.

… Banco Popular posts loss, denies looking to be sold

Banco Popular, the ailing and sixth-largest bank, made a loss of €137 million in the first quarter (profit of €93.6 million in the same period of 2016) and set aside €496 million (+70%) for its €37 billion of toxic real estate assets. The bank refuted speculation that it was seeking a rapid sale to save the bank.

Popular replaced its chairman earlier this year. The new Chairman, Emilio Saracho, a former JP Morgan banker, needs to raise more capital or sell the bank. The bank's shares have lost more than 90% of their value over the past five years, leaving its market value at around €2.9 billion, well below the €4 billion that analysts estimate Popular needs in fresh equity.

The non-performing loan ratio rose to 14.91% in March, up from 12.68% a year earlier.

Popular, which is due to inaugurate its new state-of-the-art 123,000 square-metre headquarters in the summer, is the weakest link in a banking system that has been largely cleaned up since Spain's real estate boom and bust as of 2008. The collapse of Bankia in 2012 triggered a €41 billion EU bail out of several banks in return for reforms. Spain exited that programme in January 2014.

The IMF's latest global financial stability report this month said 'the [Spanish] system is closer to putting most of the crisis legacies behind it'.

The taxpayer spent €56.77 billion on the banking system between 2008 and 2016 and will fork out another €1.1 billion this year, according to government figures. The net cost until 2016 was €48.22 billion (including dividends and interest on loans).

More than 81,500 bank jobs in Spain were shed between 2008 and 2016, 30% of the total, and the three largest banks, Santander, BBVA and Caixabank, got rid of another 992 in Spain in the first quarter of this year. The number of banks has been reduced from 55 to 14. Most of those that disappeared were *cajas* (local savings banks).

Iberdrola acquires stake in US offshore wind farm

Avangrid Renewables, a US subsidiary of Iberdrola, the world's largest wind farm producer, agreed to buy 50% of Vineyard Wind located off the coast of Massachusetts from Copenhage