

## **Inside Spain 17**

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### **Foreign Policy**

#### *Growing support for Spain's 'alliance of civilisations' initiative*

The proposal of Prime Minister José Luis Rodríguez Zapatero for an 'alliance of civilisations' between the West and the Muslim world, launched a year ago, is attracting growing support. Co-sponsored by Turkey, it has won the backing of UN Secretary General Kofi Annan, who has established a high-level group of 18 personalities. It is also positively viewed by the UK, the current rotating EU president, which could provide some financing for it. Spain and the UK are the most active supporters of Turkey's bid to become a full EU member (see separate analysis).

The proposal, whose name counters Samuel Huntington's famous term 'clash of civilisations', includes anti-terrorism cooperation, correcting economic inequalities and cultural dialogue. It has so far received the backing of some 20 countries.

The UN has warned that the deepening divide between Western and Muslim societies is being exploited by extremists and constitutes 'a potential threat to world peace'.

The idea is one that cannot really be opposed, but there are serious doubts about whether it will get anywhere because of the difficulties in finding common ground. Indeed, there is not even agreement on what is meant by the term civilisation.

#### *Spain slips down the league of the US's closest allies*

More Americans view Spain as a close ally than they did in 2004, but in the overall ranking by Harris Interactive of the countries perceived to be the closest allies Spain declined from 9<sup>th</sup> to 11<sup>th</sup> position out of 25 countries (see Figure 1). Twenty two per cent of respondents said Spain was a close ally compared with 20% in 2004 and a high of 30% in 2003.

**Figure 1. How Americans View Other Countries (%)**

Country Ranking	Close Ally	Friendly, Not Close Ally	Not Friendly, Not Enemy	Unfriendly/ Enemy	Not Sure/ Refused	Rank in 2003	Rank in 2004
1. UK	74	18	3	1	4	1	1
2. Canada	48	37	10	2	3	2	2
3. Australia	44	36	9	–	11	3	3
4. Israel	41	31	13	6	9	4	4
5. Japan	30	37	22	5	6	=6	5
6. Mexico	27	47	16	4	7	5	6
7. Italy	26	43	17	4	10	=6	7
8. South Korea	25	31	20	14	10	9	8
9. Germany	24	46	22	2	5	=14	=10
10. Sweden	23	44	15	2	17	=12	=12
<b>11. Spain</b>	<b>22</b>	<b>43</b>	<b>19</b>	<b>1</b>	<b>14</b>	<b>8</b>	<b>9</b>

Source: Harris Interactive.

Germany and France, the countries towards which the Socialists have moved more closely since pulling Spain's troops out of Iraq in 2004, slipped down the league more than Spain. France, the country which was the most outspoken in its opposition to the Iraq war, fell from 8<sup>th</sup> place in 2002 to 16<sup>th</sup> this year while Germany dropped from 6<sup>th</sup> to 10<sup>th</sup>. Spain was in 12<sup>th</sup> place in 2002 and 8<sup>th</sup> in 2003 (it moved up because of the previous government's wholehearted support for the invasion of Iraq).

Meanwhile Spain's lukewarm feelings towards the United States remained the same in the latest annual poll by the German Marshall Fund of the US (see Figure 2). On a temperature scale of 0 to 100 Spain's thermometer reading of 42 was the second coolest among the 10 countries surveyed after Turkey. Eighty one per cent of Spaniards disapprove of the way George W. Bush is handling foreign policy, the third highest in the EU after France and Germany and well above the 72% average for the 10 nations.

**Figure 2. European Nations' Feelings Toward the United States**

Country	Thermometer Readings
UK	57° (62°)
Italy	57° (61°)
Poland	56° (56°)
Slovakia	55 (50°)
Netherlands	54° (55°)
Germany	51° (55°)
Portugal	51° (50°)
Europe 10	50° (55°)
France	50° (51°)
<b>Spain</b>	<b>42° (42°)</b>
Turkey	28° (28°)

Note: 2004 figures in brackets.

Source: German Marshall Fund of the US, Transatlantic Trends, 2005.

US nationals, however, show a notable sympathy towards Spain (63 degrees), much higher than for the French (53 degrees) and the Germans (60 degrees) and only surpassed by the affection they feel for the British (72 degrees).

The Socialists have made a big effort to get relations with Washington back on an even keel. The large contingent of Spanish peace-keeping troops in Afghanistan has helped to turn the page on Iraq, but Madrid will not go any further than this (see *Inside Spain*, Newsletter 16, 5 September 2005). Spain joined France and Germany in rejecting American calls for Nato allies to help fight insurgents in the country, insisting that they should limit themselves to a peacekeeping role and remain separate from the 20,000 strong US-led Operation Enduring Freedom. 'These missions must remain separate with separate chains of command. The only thing they have in common are that they are in

the same country', said José Bono, the defence minister. Britain supports the US plan, as one would expect.

The two main sticking points between Madrid and Washington are Cuba and Venezuela where the Socialists take a very different line.

#### *Parliament approves law on sending troops abroad*

The new National Defence Law requires parliament's approval for sending troops abroad and that these missions are backed by international organisations (the UN Security Council, the EU or Nato). The previous centre-right government of the Popular Party (PP) sent peace-keeping troops to Iraq in 2003 without seeking parliament's approval and without UN support. The PP voted against the law.

#### *Madrid to give new impetus to the Iberoamerican Community of Nations*

Spain will host the summit of the Iberoamerican Community of Nations on October 14-15 which will be attended by the heads of state and government of 22 countries including possibly Cuba's Fidel Castro.

The Community, founded in 1991, and which includes Spain and Portugal, has so far proved to be little more than a talking shop for the annual expression of good intentions. This summit is the first with a permanent general secretariat (SEGIB), headed by Enrique Iglesias, the former chairman of the Inter-American Development Bank (IBD) and a high profile personality. SEGIB is based in Madrid.

SEGIB was first mooted by the previous centre-right Popular Party (PP) government of José María Aznar and given shape by the Socialists who hope this will make the Community a more effective body. María Teresa Fernández de la Vega, the first deputy prime minister, recently visited Mexico, Costa Rica, Argentina, Brazil, Chile and Uruguay to drum up support for the summit.

Castro's decision whether to attend will be made at the last moment. There is a more than reasonable chance that he will attend as the Socialists reversed the PP's policy of isolating the Castro regime and played a leading role in getting the EU to re-establish normal diplomatic relations (see *Inside Spain*, Newsletter 9, 12 January 2005).

Representatives of 61 Cuban dissidents given long jail sentences in 2003 handed in a letter to Carlos Alonso Zaldívar, the Spanish ambassador in Cuba, addressed to José Luis Rodríguez Zapatero asking him to intervene personally for their release. Fourteen have so far been released including Raul Rivero, the best known. An improvement in Cuba's human rights is one of the conditions set by the EU for lifting its sanctions. Failure to achieve this could be particularly embarrassing for the Socialists.

### **Domestic Scene**

#### *Madrid court jails 18 al-Qaeda suspects over 9/11 attacks*

Spain became the first country in Europe to convict al-Qaeda suspects in connection with the 9/11 attacks. The heaviest sentence –27 years– went to Syrian-born Imad Yarkas for heading an al-Qaeda cell in Spain and helping to organise the 9/11 attacks. The other sentences ranged from six to 11 years.

Among those convicted was Taysir Alluni, a journalist for Arabic TV network al-Jazeera for collaborating with al-Qaeda.

Prosecutors had sought notional jail sentences of 74,337 years, representing 25-year terms for each of the 2,973 deaths in the 9/11 attacks. Six of the 24 defendants were acquitted.

The trial of people arrested in connection with the 11 March 2004 bombings in Madrid, which killed 191 people, is due to begin later this year.

#### *Parliament approves greater autonomy for Valencia*

Valencia became the first region to win more powers, following overwhelming approval of its new statute by the national parliament in Madrid. José Luis Rodríguez Zapatero, the prime minister, hailed the new deal as an example to be followed by other regions, but this was rejected by Basque and Catalan nationalists who are also pressing for greater autonomy.

In a rare move, the Socialists and the centre-right opposition Popular Party (PP) –which governs Valencia– joined forces to approve the new deal which, among other things, gives the region’s premier the power to dissolve the Valencian parliament and call elections and the right to create its own tax agency.

The PP, however, is adamantly against the nationalists’ aspirations in the Basque Country and Catalonia. José María Aznar, the former PP prime minister, says Spain ‘is at risk of being Balkanised’.

The Catalan coalition government, headed by the Socialists and which includes the pro-independence and anti-monarchist Catalan Republic Left (ERC), reached agreement with the nationalist CiU opposition party over a new autonomy statute. It was approved by the Catalan parliament and has to go to the national parliament in Madrid where it is expected to be watered down. Several of the reforms including calling Catalonia a ‘nation’ and not a ‘nationality’ (Valencia is now called an ‘historic community’) have been called unconstitutional. The terminology is not a question of semantics: becoming a ‘nation’ would open the door to independence. The Catalan government is also pushing for the right to levy its own taxes and to set its own limits on its contribution to the Spanish exchequer.

Zapatero is in a bind. The ERC’s support in the national parliament gives the minority Socialist government a majority in the legislative body, and opposition to this party’s aspirations could see it pulling the plug. And Zapatero said in the past that he would accept anything that came to Madrid with the support of the Catalan parliament, although he is trying to wriggle out of this promise by saying that this only applied to matters that did not impinge on the constitution or affected other regions.

Meanwhile the Basque government continues to press ahead with its demand for an ‘associated free state’ with Spain, which was rejected by the Madrid parliament earlier this year (see *Inside Spain*, Newsletter 10, 7 February 2005).

*Spain sends troops to enclaves of Melilla and Ceuta after hundreds of immigrants storm fences*

Spain moved troops into its North African enclaves of Melilla and Ceuta after several hundred immigrants armed with makeshift ladders succeeded in breaking through the border fences from Morocco. The assaults, which came at a time when the Spanish authorities are doubling the height of the fences, left eight people dead and scores injured.

The enclaves (see Figure 3) are increasingly targeted by sub-Saharan Africans as they are stepping stones to the European Union. Other immigrants try to make the treacherous sea crossing to mainland Spain, usually in rickety boats operated by mafia groups. The unlucky ones drown before they reach a beach.

**Figure 3. Ceuta and Melilla**



The Spanish civil guard regularly arrests more than 100 immigrants a week who make the crossing.

Rabat, which disputes Spain's sovereignty over the enclaves, and Madrid are cooperating much more closely than they did under the previous centre-right government, but Spanish officials suspect that Morocco is not doing enough to secure the borders.

Spain has received more than 4 million immigrants since the late 1990s, increasing the population by 10% to 44 million. No other European country has received such a large number, and it is beginning to strain the health and education systems (see item below on health).

*Spain slips in UN HDI index*

Spain was ranked 21<sup>st</sup> out of 177 countries in the latest UN Human Development Index (HDI), a small decline over its 20<sup>th</sup> position in the 2004 index, although because of periodic revisions of data or changes in methodology by international agencies, statistics presented in different editions of the Report may not be comparable.

The HDI is a composite index that measures the average achievements in a country in three basic dimensions of human development: (1) a long and healthy life, as measured by life expectancy at birth; (2) knowledge, as measured by the adult literacy rate and the combined gross enrolment ratio for primary, secondary and tertiary schools; and (3) a decent standard of living, as measured by GDP per capita in purchasing power parity (PPP) US dollars (see Figure 4).

**Figure 4. UN Human Development Index for Selected Countries**

<b>Ranking<sup>1</sup></b>	<b>Life Expectancy at Birth (2003)</b>	<b>Combined Primary, Secondary &amp; Tertiary Gross Enrolment Ratio (%) 2002-03</b>	<b>GDP per Capita (PPP US\$) 2003</b>
1. Norway	79.4	101	37,670
5. Canada	80.0	94	30,677
6. Sweden	80.2	114	26,750
10. United States	77.4	93	37,562
15. UK	78.4	93	27,147
16. France	79.5	92	27,677
18. Italy	80.1	87	27,119
20. Germany	78.7	89	27,756
<b>21. Spain</b>	<b>79.5</b>	<b>94</b>	<b>22,391</b>
27. Portugal	77.2	92.5	18,126
37. Chile	77.9	95.7	10,274
53. Mexico	75.1	90.3	9,168

(1) Out of 177 countries.

Source: United Nations Human Development Report, 2005.

### *Spain at the bottom of the league in upper secondary education*

One in three Spanish students do not complete their upper secondary education compared with one in every five for developed countries as a whole, according to the latest edition of the OECD's Education at a Glance (based on 2003 data). Only the Slovak Republic, Turkey and Mexico are in a worse situation.

Spain spends an average of €4,900 per student a year between primary and tertiary education as against an OECD average of €6,100. Spending, however, is not necessarily a guarantee of higher quality in terms of education. Australia and Finland, for example, have moderate expenditure on education per student at the primary and secondary levels but are among the countries where 15-year-olds perform strongest in key subject areas. And Spain's teachers are among the better paid so low salaries is not the cause of the problem.

One of the most striking results of the latest report is that Spain is the only country where students' chances of finding a job are not enhanced by having a degree. An OECD education expert said one reason for this was the 'massification' of Spanish universities.

The report followed another one by the OECD at the end of 2004 which pointed out the bad scores by Spanish secondary school students in reading, mathematics and science (see *Inside Spain*, Newsletter 9, 12 January 2005).

The government has made education –an area in constant flux and something of a political football– a priority sector for public investment, but it will take a very long time before any results are seen. Without a major turnaround in the drop-out rate in upper secondary education, Spain's prospects of making meaningful progress in the EU's Lisbon Agenda are slim. The Agenda was launched in 2000 to make the EU by 2010 'the most dynamic and competitive knowledge-based economy in the world capable of sustainable economic growth with more and better jobs'.

## **The Economy**

*Gas Natural seeks to take over Endesa and create one of the world's largest energy groups*

Gas Natural, the energy group, launched a hostile €22.5 billion bid for Endesa, Spain's largest electricity generator, which is being fiercely fought off. Analysts believe Gas Natural will be successful, but in the process a lot of blood will be spilled.

The proposed deal would create an integrated group with assets of more than €60 billion in Spain (where it would have, before announced asset sales, around 40% of power generation and 80% of the gas market), Portugal, Italy and Latin America. Gas Natural, the smaller of the two companies, was twice thwarted during the last centre-right government of the Popular Party (PP) in its attempts to acquire Iberdrola, Spain's second largest power group.

In a separate and controversial move, Gas Natural said it would sell to Iberdrola €7-9 billion worth of Endesa's assets, making its take-over bid look like a joint effort.

The PP waded into the acrimonious debate, accusing the Socialist central government of favouring the deal in order to pay off political favours. Gas Natural is 30% owned by the Barcelona-based La Caixa, Spain's largest savings bank (savings banks have a measure of political control), and the Catalan regional government is in the hands of Catalan Socialists. The Catalan Republican Party (ERC) is also an ally of the Socialists in the national parliament in Madrid.

The bid is subject to regulatory approval. The government is believed to favour a national champion over competition.

### *Injection of funds for ailing health systems in regions*

The central government came to the rescue of regions struggling with health financing deficits and approved a transfer of funds. The six regions governed by the opposition Popular Party (PP) out of a total of 17 abstained from backing the deal.

Madrid (under the previous PP government) transferred the running of health systems to the regions several years ago and will provide more money (€1.6 billion), although it is not strictly obliged to do so. The overall deficit is estimated to be as much as €7 billion.

The influx of immigrants has strained health systems, particularly in Madrid (ruled by the PP) and Catalonia (the Socialists) where most immigrants are concentrated. Other factors are the 'greying' of the population –Spaniards live on average close to 80 years (more than Americans, see Figure 4)– and the millions of tourists that come to Spain every year, quite a number of whom need hospital treatment while they are on holiday.

The ruling Socialists' proposal urging the regions to use their capacity to raise taxes on tobacco and alcohol as a way to raise more revenue for their health systems was roundly rejected by the PP, although it makes eminent sense. After all, cigarettes and alcohol in Spain are still cheaper than in most EU countries; and it is universally recognised that they are the two main self-inflicted sources of health problems. The PP controlled regions rejected what they defended when their party was in power nationally (1996-2004).

### *Spain's labour costs on a par with Canada's*

Spain's hourly labour costs in manufacturing are close to Canada's even though its standard of living and level of development are far from the North American country's.

In 2004, the average cost was €16.59 in Spain compared with €16.82 in Canada (see Figure 5). The growth in Spain's labour costs is one factor behind the gradual shift of multinationals from the country to Hungary, Poland and other eastern and central European countries that joined the EU last year.

**Figure 5. International Labour Costs**

<b>Country</b>	<b>€</b>
West Germany	27.60
Finland	24.88
France	20.74
UK	19.89
Ireland	18.11
Italy	18.79
United States	18.76
<b>Spain</b>	<b>16.59</b>
Portugal	7.21
Hungary	4.53
Poland	3.29

Note: cost per hour in 2004 in the manufacturing sector.  
Source: German Economy Institute in Cologne.

### *IMF forecasts higher growth this year for Spain*

The International Monetary Fund has increased from 2.7% to 3.2% its GDP growth forecast for Spain this year. This is in striking contrast to its substantial reduction of the euro zone's overall growth rate (from 1.6% to 1.2%). Spain's consumer price inflation is projected at 3.1% (2.1% for the euro zone) and the unemployment rate at 9.1% (8.7%).

### *Spain, still the largest recipient of EU funds*

Spain, which faces becoming a net contributor by 2013, was once again the main beneficiary of EU funds in nominal terms in 2004. The country, in the first budget for the enlarged EU-25, received €16.4 billion, 17.8% of the total and ahead of France (€12.9 billion), Germany (€11.7 billion), Italy (€10.4 billion) and the UK (€7.1 billion).

It terms of gross national income, Greece was the biggest recipient (3.5%), followed by Portugal (3.5%) and the new member states Lithuania (2.8%), Estonia (2.5%) and Latvia (2.4%). As regards net funds received, Spain's represented just over 1% of its gross national income, the third largest among the EU-15 after Greece and Portugal and sixth among the EU-25 (see Figure 6).

**Figure 6. Operating Budgetary Balances of EU Countries (% of Gross National Income)**

Country	% of GNI	Country	% of GNI
Austria	-0.16	Latvia	+1.82
Belgium	-1.19	Lithuania	+2.13
Czech Republic	+0.33	Luxembourg	-0.41
Cyprus	+0.53	Malta	+1.02
Denmark	-0.33	Netherlands	-0.44
Estonia	+1.79	Poland	+0.75
Finland	-0.05	Portugal	+2.37
France	-0.19	<b>Spain</b>	<b>+1.08</b>
Germany	-0.33	Slovakia	+0.51
Greece	+2.52	Slovenia	-0.47
Hungary	+0.25	Sweden	-0.38
Ireland	+1.3	UK	-0.16
Italy	-0.22		

Note: A minus sign means the country is a net contributor and a plus sign a net recipient. The figures exclude administrative expenditure and include UK correction payments.

Source: European Commission.

Spain has been the main beneficiary in nominal terms since 2001 when it overtook France. Of the €6.4 billion that Spain received (just over 2% of GNI), €9.6 billion were structural funds (cohesion and regional development), 28.2% of the total and almost double that of Germany, the next largest recipient. In agricultural funds, Spain was the second largest recipient after France (€6.3 billion).

The government would like to reach an agreement on how the 2007-13 budget will be carved up during the current UK presidency, and it is still pressing to remain a net recipient as long as possible. The longer it waits the less favourable Spain's deal could be as the country's wealth is steadily rising (the GDP was revised upward earlier this year). Spain will have received around €48 billion net during the 2000-06 budgetary period and according to the latest thinking it would receive €4.8 billion in the next one.

#### *Spain's inward FDI falls, outward surges*

Spain's inward foreign direct investment (FDI) continued to fall in 2004, but its outward jumped sharply, according to UNCTAD's 2005 World Investment Report.

Inward investment dropped to US\$18.3 billion from US\$29 billion in 2003 and outward soared from US\$30.8 billion to US\$54.2 billion (the record was US\$54.8 billion in 2000, see Figure 7). The main reason for the increase in 2004 was Santander's €13.4 billion purchase of the UK bank Abbey. Spain was placed 47th in the inward FDI performance index ranking, down from 37th in 2003, and 10th in the outward ranking (9th in 2003).

**Figure 7. Spain's Inward and Outward FDI, Selected Years (US\$ billion)**

	1985-95 (Annual Average)	2000	2001	2002	2003	2004
Inward	8.2	39.9	27.9	43.6	29.0	18.3
Outward	2.3	54.8	32.6	36.4	30.8	54.2

Source: UNCTAD, World Investment Report 2005.

Three Spanish companies –Telefónica, Repsol YPF and Endesa– remained among the world's largest 100 non-financial transnational corporations (TNCs) ranked by foreign assets. Telefónica was 36th with US\$33.4 billion, Repsol YPF 47th with US\$27.9 billion and Endesa 53rd with US\$25.4 billion. The ranking is based on foreign assets in 2003. The banks, Grupo Santander and Grupo BBVA, were ranked 37th and 47th respectively among the world's 50 largest financial TNCs, with foreign assets of US\$421.6 billion and US\$361.8 billion.

*Spain falls six places in competitiveness league*

Spain suffered a sharp fall in the World Economic Forum's Global Competitiveness Index. It was ranked 29<sup>th</sup> out of 117 countries, down from 23<sup>rd</sup> in 2004 (see Figure 8). Only Greece and Lithuania, among EU countries, fell more and Italy remained last in 47<sup>th</sup> place. Finland was top for the third year running.

**Figure 8. Global Competitiveness Index**

<b>Country</b>	<b>2005 Rank</b>	<b>2004 Rank</b>	<b>Changes 2004-05</b>
UK	13	11	-2
Germany	15	13	-2
<b>Spain</b>	<b>29</b>	<b>23</b>	<b>-6</b>
Italy	47	47	0

Source: World Economic Forum.

Among the main disadvantages cited by businessmen were restrictive labour regulations, inefficient government bureaucracy and tax rates.

Spain's ailing competitiveness is one factor behind the relocation of multinationals and some Spanish companies to central and eastern European countries.