

Inside Spain nr 130

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Summary

Rajoy against post-Brexit EU talks with Scotland.
Repeat election leaves parties struggling to form a new government.
Registered unemployed falls, GDP growth to be revised upwards.
Deaths outstrip births for first time in 75 years.
Brexit impact on Spanish companies.

Foreign Policy

Rajoy against post-Brexit EU talks with Scotland...

Acting Prime Minister Mariano Rajoy said there could be no separate negotiations between the EU and Scotland, which voted overwhelmingly in favour of remaining in the Union, unlike the UK as a whole.

Rajoy's stance is motivated by the movement for independence in Catalonia, the most economically dynamic region of Spain, which is pushing for a referendum and then to re-join the EU. Any sign of encouraging Scotland along the same path could embolden the secessionists in Catalonia.

First Minister Nicola Sturgeon said a second independence referendum in Scotland was 'highly likely' because of Brexit, followed by an application to re-join the EU.

'If the United Kingdom leaves the EU, so does Scotland', Rajoy said in Brussels. 'Scotland has no competences to negotiate with the EU. The Spanish government rejects any negotiation with anyone other than the United Kingdom'.

EU rules require all governments to approve the accession of a new member, giving Spain a veto over Scotland. France also opposes Scotland's move for a separate deal.

... Margallo urges Gibraltar to share sovereignty

The acting Foreign Minister, José Manuel García-Margallo, said Spain would present to the new British government a plan to share sovereignty over Gibraltar, the British overseas territory long claimed by Madrid, whose status within the EU is uncertain as a result of Brexit.

As soon as the UK referendum result was known, García-Margallo said the only way for the Rock, ceded to the British Crown under the 1713 Treaty of Utrecht and which voted 96% against leaving the EU, to remain within the EU would be by sharing sovereignty.

'It is very cold outside the EU, and there is the possibility of remaining if Gibraltar accepts Spain's outstretched hand', he said.

Shared sovereignty would be temporary and would not mean that Spain had given up its claim for Gibraltar to be incorporated fully into the country, the Minister said. He also offered the prospect of double nationality (Spanish and British) for Gibraltarians.

As with the case of Scotland, which also voted in favour of Remain, García-Margallo said Madrid would not accept Gibraltar forging its own post-Brexit deal with the EU.

Fabian Picardo, the Rock's Chief Minister, told the *Financial Times* the 'sovereignty of Gibraltar is not going to change', but admitted that Spain's position could pose a problem.

He said one option being considered in talks with the Scottish government is the 'reverse-Greenland model' under which the territory of the UK would be redefined to enable Gibraltar, Scotland and possibly Northern Ireland to remain inside the EU. This model is based on a 1985 EU decision that allowed Greenland, a devolved part of Denmark, to leave the EU while Denmark remained.

Picardo also called for a second referendum once a post-Brexit deal is struck.

... Madrid puts itself forward for London-based EU agencies...

The government staked a claim to re-locate the European Banking Authority or the European Medicines Agency from London to Madrid, following the UK's decision to exit the EU.

'Both are of great interest to Spain and we will work on the possibility that at least one of them will be located on Spanish territory', said Sóraya Saenz de Santamaría, the acting Deputy Prime Minister.

Spain joined the EU in 1986 and is home to five relatively minor EU institutions including the EU Agency for Safety and Health at Work and the European Fisheries Control Agency.

Other countries have also put themselves forward.

Obama stops over in Spain

President Barack Obama stopped over in Spain on his way back from the Nato summit in Warsaw and met King Felipe, acting Prime Minister Mariano Rajoy and the leaders of the main political parties.

He was the first US President to visit the country since George W Bush in June 2001.

Domestic Scene

Repeat election leaves parties struggling to form a new government

More than three weeks after Spaniards went to the polls for the second time in six months, there are still no clear signs of a new government.

The Popular Party (PP) was again the victor and with more seats, but unless it gains the support of some kind from other parties, which in the end is likely, it cannot remain in power and the country will be condemned to yet another election that nobody wants.

The PP won 137 of the 350 parliamentary seats, 14 more than last December but 39 short of a majority (see Figure 1). The party, with the most loyal supporters, many of them pensioners, benefited from the lower voter turnout (69.8% as against 73.2% last December) and probably from Brexit and the market turmoil that followed it which probably fuelled a 'flight to safety' among voters.

The Socialists (PSOE) dropped five seats to 85, their worst ever result, the far left Unidos Podemos (UP), an alliance forged in May between the anti-establishment Podemos and United Left, the revamped communist party, confounded the opinion polls and with 71 seats did not overtake the Socialists, and the centrist Ciudadanos (C's) won 32 seats, eight fewer.

Figure 1. Results of general elections, 2016 and 2015 (seats, millions of votes and % of votes)

	2016			2015		
	Seats	Votes	%	Seats	Votes	%
Popular Party	137	7.90	33.0	123	7.21	28.7
Socialists	85	5.42	22.6	90	5.53	22.0
Unidos Podemos (1)	71	5.04	21.1	69	5.18	20.6
Ciudadanos	32	3.12	13.0	40	3.50	13.9
Catalan Republican Left	9	0.62	2.6	9	0.59	2.4
Convergència Democràtica (2)	8	0.48	2.0	8	0.56	2.2
Basque Nationalist Party	5	0.28	1.2	6	0.30	1.2
EH Bildu	2	0.18	0.8	2	0.21	0.9
Canarian Coalition	1	0.07	0.3	1	0.08	0.3

(1) Unidos Podemos won 45 seats and its allies in Catalonia, Valencia and Galicia 26. In 2015, Podemos won 42 seats and its allies 27. United Left won 2 seats.

(2) In 2015, Democràcia i Libertat.

Source: Interior Ministry.

The PP and the centre-left Socialists, the two parties that have alternated in power since 1982, won 222 seats between them, nine more than last December (a whopping 101 fewer than in 2008). Podemos and C's upended the two-party system last December but since then have failed to make further gains.

Having agreed a pact with the Socialists after the last election, which failed to garner support from other parties, C's now looks set to support a PP minority government by abstaining at the investiture vote in parliament as opposed to voting against the PP as it did last time. This, however, would not be sufficient to return the PP to power. C's has ruled out a formal coalition.

The Socialists hold the key to another four-year term by the PP. Their leader, Pedro Sánchez, is playing hard to get as a tactic for extracting concessions. He wants Mariano Rajoy, the acting Prime Minister, to seek his allies elsewhere and not to automatically assume the Socialists will concede him the necessary votes.

One of the conditions of the Basque Nationalist Party, with five seats, for supporting the PP is a change in the policy for jailed members of the Basque terrorist organisation Eta, so that they can serve their sentences in prisons nearer to their home region.

Rajoy's ideal government is a grand coalition with the Socialists and C's. As this is most unlikely to happen, although it would be good for Spain, Rajoy would like advance support from the Socialists and Cs on issues such as the 2017 budget. Otherwise his second term in office could begin with a budget crisis in parliament, to the detriment of Spain's standing in the markets which is already under pressure because of last year's budget deficit overshoot.

Meanwhile, UP is going through a lot of soul searching as it lost one million votes and won exactly the same number of seats (71) as Podemos and United Left achieved separately last December, albeit with fewer votes. By running on the same ticket, Podemos and United Left had expected to benefit from the d'Hondt system of proportional representation and to overtake the Socialists.

Juan Carlos Monedero, one of the founders of Podemos, blamed UP's loss of votes on the other parties and the media playing the fear card and on the confusion created among the electorate by Podemos embracing the discourse of de-ideologisation –the idea that the left-right axis has been overcome– and yet allying itself with United Left.

At the end of the day, the most likely scenario is that the Socialists will let in a PP minority government, which is what public opinion wants to happen rather than a third election (see Figure 2), and will remain in the opposition, but this time in the uncomfortable position of the UP hard on its heels.

Figure 2. If the only alternative to avoid a third election is for the Socialists to abstain and let the PP govern what would you prefer? (% of potential voters)

	Popular Party	Socialist	Unidos Podemos	Ciudadanos
Abstain	95	74	50	89
Repeat elections	3	22	44	8

Source: Metroscopia.

Former Catalan leader faces trial over banned independence referendum

Artur Mas, the former Premier of Catalonia, and two of his Ministers, face trial for staging a mock independence referendum in 2014 in defiance of an order by the Constitutional Court.

A court in Catalonia ruled that Mas ‘intentionally and openly refused to obey the mandate from the Constitutional Court’.

Mas, who was regional Premier between December 2010 and January 2016, used volunteers to man the referendum in an effort to circumvent the Constitutional Court, but the High Court in Catalonia said he had overstepped his authority.

The ‘yes’ vote in the illegal ballot won 80% support, but only 37% of voters turned out.

In a separate development, the leadership of the Catalan branch (PSC) of the national Socialist Party proposed using the ‘Canadian way’ for resolving the independence issue as a last resort if constitutional reform fails to provide a solution or is rejected by the Catalan parliament (currently in the hands of separatist parties).

In response to the 1995 Quebec referendum, Canada’s Clarity Act of 2000 established the conditions under which the government would enter into negotiations that might lead to secession following such a vote.

The idea is a non-starter for the Popular Party, which is likely to head the next government, and provoked uproar within parts of the PSC and among Socialist leaders in other regions. The PSC shelved the proposal.

Deaths outstrip births for first time in 75 years...

More people died in Spain last year than were born for the first time since 1941, underscoring the ageing of the population.

The number of deaths (422,276) exceeded births by almost 3,200, according to provisional figures from the National Statistics Institute (INE), which began to collect data after Spain’s 1936-39 Civil War.

Spain's prolonged recession and high unemployment discouraged women from starting families. The birth rate peaked in 2008 at 519,779 births and dropped to 419,109 in 2015.

The number of women between the ages of 15 and 49 (child-bearing age) dropped by 770,000 between 2008 and 2015, due to the lower number in this age group, as a result of demographic changes in the 1980s and early 1990s, and the arrival of fewer immigrants and greater emigration abroad in recent years because of the economic crisis.

The average number of children per Spanish woman fell from 1.44 in 2008 to 1.33 last year and that of foreign-born women from 1.83 to 1.61.

INE forecast last year that Spain's population (currently 46 million) would fall by one million in the next 15 years and by 5.6 million in the next 50 years.

... Population continues to fall, rise in Spaniards' emigrating

Close to 100,000 Spaniards emigrated last year, 23% more than in 2014, helping to produce a further fall in the population to 46.43 million, albeit a tiny one of 11,142, according to provisional figures from INE.

Of the 98,934 Spaniards who emigrated, 64,136 were born in Spain and the rest are nationalised Spaniards. Net migration (the difference between Spaniards who arrived and those who left) was 46,707. Emigration by Spaniards gathered momentum after the property bubble burst in 2008 and the country went into recession (see Figure 3).

Figure 3. Emigration by Spaniards, 2008-15

2008	2009	2010	2011	2012	2013	2014	2015
33,505	35,990	40,157	55,472	57,267	73,329	80,441	98,934

Source: INE.

Net migration of Spaniards and foreigners was 8,389 (see Figure 4).

Figure 4. Immigration and emigration by nationality, 2015

	Immigration	Emigration	Balance
Total	343,614	352,003	-8,389
Spaniards	52,227	98,934	-46,707
Born in Spain	24,060	64,136	-40,075
Born abroad	28,167	34,798	-6,631
Foreigners	291,387	253,069	38,317
Born in Spain	6,235	14,421	-8,186
Born abroad	285,152	238,648	46,504

Source: INE.

The foreign-born population of 4.4 million represented 9.5% of the total population. It was 35,456 lower than in 2014 but almost 900,000 below 2011. The figures are based on a survey and take into account those registered in town halls. The largest foreign community was Rumanian (see Figure 5).

Figure 5. Foreign population by nationality, 2016 and 2015, Top 10 countries

	January 1, 2016 (1)	January 1, 2015	Change
Rumania	699,502	708,390	-8,888
Morocco	678,467	688,693	-10,227
UK	297,000	301,811	-4,811
Italy	192,053	182,694	9,359
China	171,508	167,539	3,969
Ecuador	158,967	174,372	-15,405
Germany	142,316	144,953	-2,637
Colombia	135,954	145,534	-9,581
Bulgaria	130,506	134,427	-3,921
Portugal	102,318	103,843	-1,525
Total (2)	4,418,898	4,454,353	-35,456

(1) Provisional figures. (2) Including all other nationalities.

Source: INE.

Spain is one of the EU countries that has most successfully absorbed a wave of migrants of singular size, without social conflicts of any note or the emergence of xenophobic movements. More than 6 million immigrants arrived in Spain over the past 15 years.

According to a study by Alejandro Portes, professor of sociology at Princeton University, eight out of every 10 children born of immigrant parents in Spain (second generation) feel Spanish. 'Spain is a friendly society, which does not have an integration model, but there is no general trend of discrimination against immigrants', said Portes. 'Perhaps this is because not so long ago Spaniards were emigrants'.

The country, however, is still a long way from the countries where first-generation immigrants and their children have secured prominent roles in public life, like the recently elected Mayor of London, Sadiq Khan, son of Pakistani immigrants.¹

The Economy

Registered unemployed falls, GDP growth to be revised upwards...

Judging by the employment and economic growth figures, the failure to form a new government since last December has not knocked Spain's recovery off course.

The number of people registered in government offices as jobless (as opposed to the quarterly figure based on household surveys which is higher) fell by 124,349 in June to 3.76 million, the lowest level since September 2009, and the caretaker government looks set to revise this year's GDP growth from 2.7% to more than 3%.

Tourism, a key driver (14% of GDP and the largest job creator), is enjoying yet another bumper year (68 million visits in 2015 and a forecasted 74 million this year), partly due to terrorism in Turkey, Egypt and Tunisia which is sending holidaymakers to Spain instead.

The results of last month's repeat election left another fragmented parliament, but the Popular Party won more seats, albeit still far from a majority, and the upstart radical left Unidos Podemos did not overtake the Socialists into second place, as predicted.

Unemployment has steadily declined since 2014, but the stated jobless rate at 21% (March, the latest figure) is still one of the highest in the western world. Spain's employment rate (those between 15 and 74 with a job) dropped from 59.8% in 2007 to 51.3% in 2015, the steepest decline after Greece (see Figure 6).

¹ See 'Highs and lows of immigrant integration in Spain' by Carmen González Enríquez, http://www.realinstitutoelcano.org/wps/portal/web/rielcano_en/contenido?WCM_GLOBAL_CONTEXT=/elcano/elcano_in/zonas_in/ari47-2016-gonzalez-enriquez-highs-lows-immigrant-integration-spain.

Figure 6. Employment rate (% of population aged 15-74)

	2007	2015
France	55.5	53.7
Germany	59.6	64.7
Greece	53.7	44.7
Italy	51.6	49.4
Spain	59.8	51.3
UK	64.8	65.4

Source: OECD Employment Outlook 2016.

... Pensions reserve fast disappearing

The caretaker government had to take €8.7 billion out of a special reserve in order to make this month's pension payments. The reserve, created during the economic boom, has dropped from €66.8 billion in 2011 to €25.1 billion in July and at this rate will have been depleted by the end of 2017 (see Figure 7).

Figure 7. Social security reserve, 2006-July 2016 (€ billion)

2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016*
35.9	45.7	57.2	60.0	64.3	66.8	63.0	53.7	41.6	34.2	24.1

Source: Employment and Social Security Ministry.

Low unemployment by Spanish standards (8% in 2007 as against 21% today) enabled the social security system to be in surplus until 2012 when the economy was in recession (see Figure 8).

Figure 8. Social security balance, 2006-July 2016 (% of GDP)

2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016 (1)
1.3	1.4	1.3	0.8	0.2	0.05	-0.5	-0.8	-1.3	-1.5	-1.6

(1) July and annualised figure based on the last 12 months.

Source: Employment and Social Security Ministry.

Although the economy is growing again, the number of social security contributors today is still 1.8 million below the peak of 19.5 million in 2007. Another problem is the ageing of the population. The number of pensions is forecast to rise from 9 million in 2012 to 15 million in 2050.

The social security deficit (1.6% of GDP in 2015) coupled with that of the regional governments caused the general government deficit in 2015 to overshoot the 4.2% target agreed with the European Commission (it came in at just over 5% of GDP). Spain has

missed its deficit objective for nine consecutive years. Brussels has given Madrid another year (2017) to meet the EU reference of 3%.

The Council of the EU castigated the government earlier this month for a fiscal effort that ‘fell short of what was recommended by the Council, and it even relaxed its fiscal stance in 2015’. Spain (and Portugal) is on course to become the first of the euro zone countries to face penalties for breaking EU fiscal rules.

The cumulative improvement in the structural balance over the 2013-15 period amounted to 0.6% of GDP, significantly below the 2.7% recommended, and the government is unlikely to correct the deficit this year as required.

The Independent Authority for Fiscal Responsibility (Airef) said six of the 17 regional governments are unlikely to meet their budget deficit targets this year and next (see Figure 9).

Figure 9. Airef’s evaluation of budget deficit targets of 14 regional governments

	2016 (% of GDP)	2017 (% of GDP)	Probability of compliance	
			2016	2017
Andalusia	-0.7	-0.5	Probable	Probable
Aragón	-0.7	-0.5	Very unlikely	Very unlikely
Asturias	-0.7	-0.5	Feasible	Feasible
Balearics	-0.7	-0.5	Feasible	Probable
Cantabria	-0.7	-0.5	Feasible	Probable
Castilla y León	-0.7	-0.5	Feasible	Feasible
Castilla-La Mancha	-0.7	-0.5	Unlikely	Unlikely
Catalonia	-0.7	-0.5	Unlikely	Unlikely
Extremadura	-0.7	-0.5	Unlikely	Very unlikely
Madrid	-0.6	-0.5	Feasible	Feasible
Murcia	-0.7	-0.3	Very unlikely	Very unlikely
Navarra	-0.7	-0.5	Feasible	Feasible
La Rioja	-0.2	0.1	Very likely	Very likely
Valencia	-0.7	-0.5	Very unlikely	Very unlikely

Source: Airef.

The AIREF is obliged to report on the Economic and Financial Plans (EFP) which, in accordance with the Organic Law on Budget Stability and Financial Sustainability

(LOEPSF), have to be submitted by the regional governments that failed to comply with the 2015 budget stability, government debt or expenditure rule targets. According to the Ministry of Finance, only the regions of Galicia, Canary Islands and the Basque Country met all three fiscal rules in 2015 and, therefore, do not have to submit an EFP.

The government plans to raise an additional €6 billion by establishing a 'minimum rate' of corporate tax to help it finally meet the 3% deficit target next year.

With a caretaker government since last December and a repeat election in June that has yet to resolve the formation of a new government, measures to put the social security system on a more even keel and the general government accounts as a whole need to be among the new government's top priorities.

Spain works fewer hours than the OECD average

The average number of hours worked in Spain was 1,691 in 2014, 75 fewer than the average for the 35 OECD countries and 320 more than Germany (see Figure 10).

Figure 10. Number of hours worked in 2014, selected OECD countries

	Hours
Mexico	2,246
Greece	2,042
US	1,790
OECD average	1,766
Italy	1,725
Spain	1,691
UK	1,674
France	1,482
Germany	1,371

Source: OECD.

Government names and shames tax debtors

The Tax Agency published a new list of individuals and companies who owe more than €1 million (see Figure 11).

The first list, in a policy of name and shame, was published last December. Since then the total amount owed has risen by 0.7% and €312 million has been recovered.

Almost all the 20-largest company debtors out of a total of 4,432 are construction firms that got into difficulties after the bursting of Spain's property bubble in 2008. One of them, Reyval Urbis, owes €378.2 million (see Figure 11). The total amount owed is €15 billion.

Figure 11. Top five corporate tax debtors (€ million)

	€ million
Reyal Urbis	368.6
Nozar	203.2
Oceanus Maritime	189.0
Sacyr	116.1
Grupo PraSa	101.8

Source: Tax Agency.

Among the 336 individual debtors with debts of €700 million is Luis Pascual Estevill (€5.4 million), a former judge struck off for corruption and imprisoned.

Spain registers largest rise in EU in number of millionaires

The number of Spaniards with net assets of at least US\$1 million (€906,000), excluding their primary residence and consumables, rose 8.4% in 2015 to 192,500, the largest increase in the EU, according to the latest world wealth report of Capgemini and RBC Wealth Management (see Figure 12).

Figure 12. Ranking of countries with the most high-net-worth individuals (thousand) (1)

	2013	2014	2015
1. US	4,006	4,351	4,458
3. Germany	1,130	1,141	1,199
4. China	758	890	1,034
5. UK	527	550	553
6. France	472	494	523
10. Italy	203	219	229
14. Spain	161	178	192

(1) Out of 25.

Source: Capgemini and Royal Bank of Canada, 2016 World Wealth Report.

The number dropped sharply in 2008, when the Spanish economy slowed down before going into recession, and since then has grown by 51% (see Figure 13).

Figure 13. Number of rich Spaniards, 2005-14

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Number	157,000	161,000	127,000	143,000	140,000	137,300	145,000	161,000	178,000	192,500

Source: Capgemini and Royal Bank of Canada, 2015 World Wealth Report.

Corporate Scene

Brexit impact on Spanish companies

The Ibex-35, the benchmark index of Spain's stock market, fell by 12.4% on 24 June, the day after Brexit, one of the steepest falls in the EU and underlining the importance of the UK market for Spain's leading companies.

The UK is the main destination for Spanish investment abroad (with a stock of £58.7 billion in 2014).

Banco Santander earned 23% of its profits in the UK last year; Banco Sabadell acquired 614 branches of TSB in 2015; Telefónica, with 25 million mobile telephone clients in the country, owns O2, whose sale to Hutchison Whampoa has been vetoed by the European Commission for reasons of competition; Iberdrola bought Scottish Power in 2007; Ferrovial controls various airports including Heathrow and its services division generated 63% of its revenues in the UK in 2015; and the airlines Iberia and Vueling are part of the IAG holding along with British Airways, to name but a few.

The shares of these companies were mainly responsible for dragging down the Ibex. In the last month they have recovered a little (see Figure 14).

Figure 14. Spanish stock market impact of Brexit on main Spanish companies in the UK (share price in €)

	22 June, day before referendum	24 June, day after	18 July	% change since 22/VI
Banco Sabadell	1.453	1.209	1.263	-13.0
Banco Santander	4.050	3.384	3.806	-6.0
FCC	7.568	7.556	7.575	+0.09
Ferrovial	18.550	17.130	18.160	-2.1
IAG	6.615	5.018	5.163	-24.1
Iberdrola	5.985	5.388	6.010	+0.4
Inditex	30.445	28.900	30.750	+1.0
Telefónica	8.962	7.732	8.800	-1.8

Source: Spanish Stock Exchange.

S&P Global Ratings classified Spain as the eighth country most exposed to a UK exit from the EU, ahead of France, Germany and Italy.

Companies in the UK are holding off investment decisions until the panorama is clearer. In Spain, the uncertainty and sterling's depreciation has all but halted house purchases by Brits on the Costas.

Volkswagen to invest €1 billion in Navarra plant...

Volkswagen is to invest €1 billion in its Navarra plant for the production of the new generation of Polo and another new model.

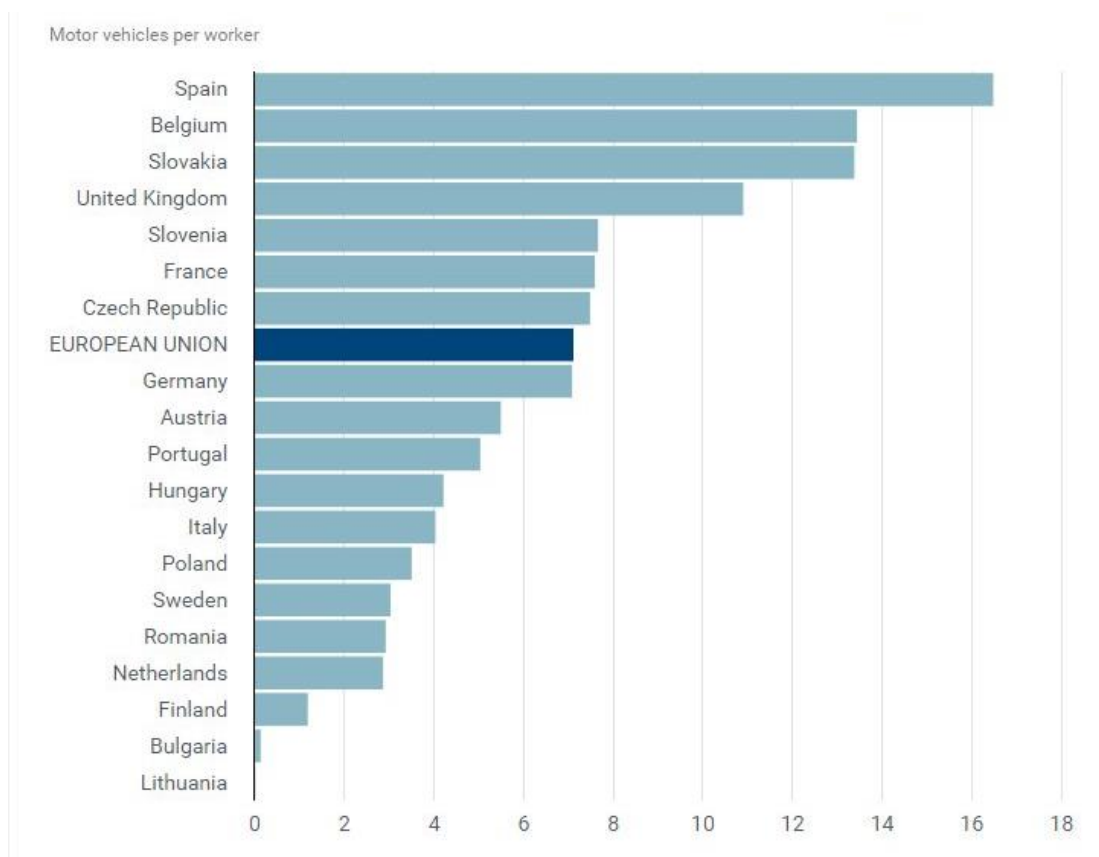
Production will increase from close to 300,000 last year (90% exported) to 350,000.

New car sales in Spain in the first six months were up 12.2% year-on-year at 623,234, making it likely that the figure for the whole year will surpass the industry's forecast of 1.1 million. The first half sales were the highest since the same period of 2008 when the Spanish economy began to slowdown.

Anfac, the motor industry association, forecasts total production of around 3 million in 2017, up from 2.8 million this year, which would return output to the pre-crisis peak.

According to the European Automobile Manufacturers' Association (ACEA), the Spanish motor industry is the most productive in the EU (see Figure 15).

Figure 15. Motor vehicle production per direct manufacturing worker, 2013 (1)



(1) Based on automotive employment most recent data available.

Source: European Automobile Manufacturers Association (ACEA).

Rolls Royce to take control of Basque ITP

Rolls Royce, the UK jet engine manufacturer, agreed to pay €720 million for the 53% of the Basque company Industria de Turbo Propulsores (ITP) it does not already own.

ITP, the ninth-largest aircraft engine and components company by revenue, has worked with Rolls Royce on civil and defence aerospace projects.