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**New policy towards the Maghreb**

*Santander Central Hispano seeks to take over UK's Abbey in biggest cross-border bank merger in Europe*

Two years after the Moroccan invasion of the minuscule Spanish-owned island of Perejil (Parsley Island), the two countries have made major progress in improving their relations. Spain's Socialist government, which took office in April from the centre-right Popular Party, reached an historic agreement with Morocco to send a joint peacekeeping mission to Haiti (see separate item below) and it is becoming actively involved in seeking an internationally acceptable solution to the decades-old conflict in the region over the Western Sahara. At the same time, José Luis Rodríguez Zapatero, the prime minister, followed up his visit to Morocco (see *Inside Spain*, Newsletter 2, May 4, 2004) with a visit to Algeria, and Bernardino León, the Under-Secretary of State for Foreign Affairs, went to Libya and Tindouf (south-western Algeria).

The dispute over the Western Sahara (rich in phosphates) dates back to 1975 when Spain abandoned the territory on the west coast of northern Africa under its sovereignty and Morocco annexed it, moving in settlers. Some 200,000 Saharai people fled into exile and still live in refugee camps in Algeria. Others sought refuge in Mauritania and Spain. Fighting ended in 1991 with a UN-negotiated ceasefire that called for a referendum on whether the territory would become independent or part of Morocco. The Polisario Front continues to press for a referendum, but Morocco wants to maintain its claimed sovereignty over the territory and has instead offered the region autonomy. Former US Secretary of State James Baker resigned in June 2004 as the United Nations envoy for the Western Sahara after failing for seven years to resolve the conflict.

Miguel Ángel Moratinos, Spain's foreign minister well-schooled in Maghreb issues, met Álvaro de Soto, who replaced Baker, and told him that Spain wanted to 'provide leadership to all the efforts in favour of peace in that region'. Spain has traditionally stayed away from the dispute, a solution to which has so far escaped four UN secretary generals, two kings of Morocco, four Algerian presidents and four in France. Moratinos did not spell out what kind of solution Spain would like; he will seek the common ground from the parties involved. The Baker plan proposed immediate self-government

for the Western Sahara and a referendum within five years. Morocco and Algeria share one of the last borders in the world that is closed. The frontier between the two countries has not been open since 1994.

Zapatero is making the Maghreb one of the focal points of his foreign policy, unlike the previous government under whose 1996-2004 administration relations with Morocco were fraught long before the invasion of Perejil (Morocco withdrew its ambassador to Madrid in 2001 for more than a year).

Morocco, in particular, is assuming increasing importance for Spain. As well as growing trade and investment ties, Morocco is the main supplier/staging post of legal and illegal immigrants to Spain and the country of origin of most of the terrorists involved in the March 11 bombing in Madrid which killed almost 200 people. The security forces in the Sahel countries and anti-terrorism experts recently reported a terrorist sanctuary in the Tibetsi mountains on the Chadian-Libyan border.

In Algeria, Zapatero was keen to convince the government that the greatly improved relations with Morocco did not mean that Spain no longer considered the country as a 'strategic partner' (the two nations signed a cooperation treaty in 2002), or that it was taking Morocco's side over the Western Sahara. Algeria is building a gas pipeline that will link the two countries between Oran and Almería without passing through Morocco.

Two oil issues could test the strength of the new friendship with Morocco: Repsol, the Spanish oil giant, is awaiting the green light from the Spanish government to drill for oil in waters claimed by Morocco, and the Spanish government sought an explanation from Morocco after Rabat granted prospection rights to two Australian companies and a British one in waters that Spain says are hers.

#### *Spain and Morocco to jointly participate in Haiti as part of UN-backed peacekeeping force*

Spain and Morocco sealed their new relations with an agreement to jointly send around 200 troops and police to Haiti this month as part of the Brazilian-led UN peacekeeping force. Armed gangs still control much of the territory of the Western hemisphere's poorest country, following the three week rebellion that ousted President Jean-Bertrand Aristide in February.

The peacekeeping mission aims to help the Haitian transition government organise free elections and set up democratic institutions.

Both the Haitian operation and the sending of more troops to Afghanistan (see following item) were approved by the Spanish Congress. This was the first time in Spain's post-Franco democracy that the government had sought the approval of parliament for sending troops abroad.

#### *First contingent of more Spanish troops departs for Afghanistan*

An advance party of 70 military personnel has gone to Afghanistan to prepare the deployment of about 1,000 Spanish soldiers within the framework of the International Security Assistance Force (ISAF), backed by the United Nations. Spain is boosting its contingent in Afghanistan from around 140 to over 1,000 soldiers to help provide security for that country's first post-Taliban elections in October.

The Socialist government fulfilled its campaign pledge to withdraw the 1,300 Spanish troops in Iraq as soon as it took power in April, without waiting for a new UN resolution that would satisfy its conditions, and since then has been under pressure from the United States and Nato to make new international peacekeeping commitments. The Socialists, unlike the previous centre-right government, did not support the US-led invasion of Iraq.

Spain is also going to reopen its embassy in Kabul in October. The decisions regarding Afghanistan and Haiti sent a clear message to the international community that while the government fell out with the US administration over Iraq it has no ambitions to live in splendid isolation or neutrality. Spain slipped to 9<sup>th</sup> position in 2004 in the Harris Poll of the US's 25 closest allies from 8<sup>th</sup> in 2003 (12<sup>th</sup> in 2002). The sharp rise in 2003 was due to the previous government's support for the invasion of Iraq (see Table 1).

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

Country	Close Ally	Friendly, Not Close Ally	Not Friendly, Not Enemy	Unfriendly/Enemy	Not Sure/Refused	Rank in 2002	Rank in 2003
1. UK	70	14	6	–	9	1	1
2. Canada	51	29	9	1	9	2	2
3. Australia	45	32	10	–	13	3	3
4. Israel	43	26	16	4	10	4	4
5. Japan	33	34	16	5	13	=8	=8
6. Mexico	29	44	14	2	11	=6	=5
7. Italy	27	43	11	1	18	5	=6
8. South Korea	25	28	23	12	13	14	9
<b>9. Spain</b>	<b>20</b>	<b>43</b>	<b>18</b>	<b>3</b>	<b>17</b>	<b>=12</b>	<b>8</b>
10. Germany	19	40	21	4	15	=6	=14
17. France	15	35	32	10	8	=8	=18

Source: HarrisInteractive.

#### *Gibraltar anniversary celebrations sour relations with UK*

Gibraltar's jubilant celebration of the 300<sup>th</sup> anniversary of the British capture of the Rock, attended by Geoff Hoon, the UK Defence Secretary, the visit of Princess Anne and the brief return of the nuclear submarine HMS Tireless to the colony predictably raised the Spanish authorities' hackles.

Alfonso Perales, the ruling Socialists' secretary responsible for relations between Madrid and Spain's autonomous regions, accused Tony Blair of behaving like an '18<sup>th</sup> century colonialist'. Stephen Wright, the British ambassador to Spain, was summoned by Miguel Ángel Moratinos, the Spanish foreign minister, who expressed 'profound disappointment' at Mr Hoon's visit. British ambassadors are long used to such calls and liken them to visiting the dentist.

Denis MacShane, the UK's Europe Minister, said the 'Union Jack would fly over Gibraltar until such time as the people of Gibraltar, in a free vote, wanted to change the status'. He also pointed out to his counterparts during a visit to Madrid that 'the Spanish flag flies over Ceuta and Melilla, which Moroccans consider part of their region of North Africa'.

No progress has been made between the UK and Spain over Gibraltar since 2002 when, in an unofficial referendum which both countries refused to recognise, 98% of voters in the Rock rejected a proposal for joint sovereignty on an 88% turnout. This echoed the 1966 official referendum when 12,138 people voted against becoming part of Spain, and 44 voted in favour.

In a gesture to overcome the current impasse, Spain lifted its ban on cruise ships docking at Spanish ports after visiting Gibraltar (see *Inside Spain*, Newsletter 3, June 6, 2004). Jack Straw, the UK Foreign Secretary, will visit Madrid in October for talks on the Rock.

*Spain may soften approach to Cuba*

The government has put out feelers to Cuba and EU countries to see whether a rapprochement might be possible. The EU imposed diplomatic sanctions against the Castro regime in June 2003 after the summary execution by firing squad of three people who hijacked a ferry in an attempt to escape the country. The previous 1996-2004 government of José Maria Aznar maintained a tough line against Cuba.

Miguel Ángel Moratinos said during a visit to Colombia that Spain was 'in contact with the Cuban authorities and with its EU partners to examine the current state of relations and their possible evolution'. He expressed satisfaction at the release of the dissident Marta Batriz Roque.

The sanctions imposed in 2003 pushed back EU-Cuba relations to the low level of 1996 when the EU voted a Common Position conditioning a full European cooperation package to reforms to be taken by the Cuban regime.

Meanwhile Repsol YPF, the big Spanish oil and gas company, has completed the drilling of the first ever well sunk in Cuba's 43,000 square mile exclusive economic zone in the Gulf, which could hold large quantities of medium-grade oil. The venture with Cubapetróleo, the government-owned oil company, is being closely watched in Houston, Texas.

A significant find by Repsol would be a shot in the arm for Cuba, which, after the Soviet Union's demise deprived it of oil on preferential terms, imports most of its oil from Venezuela. A discovery would change the dynamics of oil production in the Gulf of Mexico, dominated by the United States and Mexico, and undermine the US embargo.

Repsol took the rights in 2000 to the six blocks closest to the shore and Cuba's northwest oil-producing coast.

*Spain to participate in European exchange of criminal records*

Spain, France and Germany are to share criminal records as of 2005. The data will be shared through countries' judicial systems and enable judges in one country to take into account offences committed previously in others. The system, however, will not be easy to operate because of the possible incompatibility of computer systems, different ways of storing records and different data privacy legislation.

The agreement between the three countries is the first within the EU on ways to boost cooperation between the 25 member states and try to prevent cases like that of Michel Fourniret, a French forest warden who is being held for killings in Belgium and France between 1987 and 2001. He moved to Belgium in the late 1980s after being jailed in France for child sex offences, but was given a job in a school by Belgian authorities who were unaware of his criminal record.

*Santander Central Hispano seeks to take over UK's Abbey in biggest cross-border bank merger in Europe*

Santander Central Hispano, Spain's largest bank, would become the world's tenth largest bank by market capitalisation if it succeeds in its US\$15.5 billion bid to acquire the UK's Abbey. The deal, which Santander wants wrapped up by November, would make it the second largest bank in the UK mortgage market and enable it to reduce its dependence on Latin America with a much greater presence in Europe. If successful, it would be the biggest cross-border bank merger in Europe.

The acquisition, for which the European Commission has already granted tacit approval (regulatory clearance will be given on September 17), would complete Santander's profound transformation from a family-run provincial bank into a multinational financial group (see Table 2). Abbey represents one of the few opportunities to secure a large market share at a time when there are very few alternatives in other markets, like Portugal or Italy. Buying Abbey is probably also the last major merger opportunity within the British banking sector, which has undergone a wave of consolidation in the past ten years. In one fell swoop, Santander would gain 18 million clients in the UK, where Abbey is the sixth largest bank.

**Table 2. Santander Central Hispano's Global Reach**

Country	Entity	Market Share (%)	Branches
Spain	Santander/Banesto	18	4,369
Germany	CC Bank	16	54
Brazil	Santander Banespa	4	1,874
Chile	Santander Santiago	18	370
Portugal	Grupo Totta, Banco Santander Portugal, BSN	11	670
Mexico	Santander Serfin	14	1,018
UK	Abbey National	11	741

Source: Santander Central Hispano

Another bank could launch a counter bid. Under Take-over Panel rules the HBOs banking group (the result of the merger of Halifax and Bank of Scotland) has been given access to the same key documents relating to Abbey's business that were made available to Santander. HBOs said it would complain to the European Commission about Santander's bid for Abbey if it went ahead because of the cross shareholdings between Santander and Royal Bank of Scotland (RBS). Emilio Botín, Santander's chairman, and Juan Rodríguez Inciarte, executive vice-president for Europe and consumer finance, sit on the RBS board while RBS chairman Sir George Mathewson sits on the Santander board. RBS holds 2.8% of Santander while Santander holds 5.1% of Britain's second biggest bank. Santander said it would re-arrange its directorships if it acquired Abbey.

A British buyer, however, looks unlikely but is not impossible. A higher bid by Lloyds TSB in 2001 was stymied by competition authorities.

*European Commission warns Spain on golden shares in privatised companies*

The European Commission has asked the government to bring its legislation governing the golden shares held by the state in Telefónica (telecommunications), Endesa (electricity), Tabacalera (tobacco) and Repsol (oil and gas) into line with EU law. The privatisation of these companies was completed during the previous (1996-2004) government of the Popular Party.

This followed a ruling by the EU's highest court in Luxembourg that Spain's golden shares in the companies are in breach of EU law because they restrict the free movement of capital within the EU. The golden shares require prior authorization from the government for the purchase of 10% or more of these companies.

Although Spain has since adopted a new law, the commission said it does not consider the amendments have fully implemented the court's ruling. The court ruled that in the case of Tabacalera and commercial banking group Argentaria, the legislation could not be justified as the companies' objective is not to provide public services.

However, for Repsol, Endesa and Telefonica, the court ruled that the golden shares may be justified to ensure a continuity in the services these companies offer, but that the Spanish state wields too much power in these companies. Spain was instructed to remove the obstacles to free movement of capital regarding Tabacalera and Argentaria and to reduce its discretion in the management of the other companies.

#### *Government signs its first pact with unions and employers*

The government signed its first pact with unions and employers, aimed at reducing the number of workers on temporary contracts (currently one in every three employees), boosting ailing productivity, reforming collective bargaining and other issues.

The signing of the pact coincided with a report by the OECD calling on Spain to reform its labour market in order to be able to create more and better quality jobs. Spain's unemployment rate of 11% is still the highest among the EU-15 (the fifth highest in the EU-25) and its labour market among the most rigid.

In return for giving more workers permanent contracts, employers are likely to push for lower social security contributions and reduced severance payments.

#### *Spain improves its position in outward FDI ranking*

Spain moved up a notch to 13<sup>th</sup> position in the latest outward FDI ranking of the United Nations Conference on Trade and Development (UNCTAD). The index reflects two sets of factors that determine outward FDI: ownership advantages (firm-specific competitive strengths, such as innovation, brand names, etc) and location factors (primarily economic factors conducive to the production of different goods and services).

The index, which is calculated as the share of a country's outward FDI in world FDI as a ratio of its share in world GDP, shows that small developed and developing countries tend to invest relatively more abroad than big ones (see Table 3). This is the case, for example of Switzerland. The United States (which ranks 29) is a major outward investor in absolute terms but invests little abroad in relation to the size of its economy.

**Table 3. Outward FDI Performance Index of the Top Economies, 1988-2003**

Rank	Economy	1988-1990	1993-1995	1999-2001	2001-2003
1	Hong Kong, China	1.9	4.7	11.7	10.7
2	Switzerland	3.7	4.5	4.9	5.1
3	Singapore	2.6	3.7	3.9	4.5
4	Belgium and Luxembourg	2.4	2.9	3.6	4.0
5	Netherlands	4.5	4.1	4.3	3.8
6	United Kingdom	2.9	2.7	3.0	2.9
7	Panama	8.9	6.3	2.3	2.8
8	Sweden	2.5	2.9	2.7	2.8
9	Finland	0.9	1.2	2.0	2.1
10	Denmark	0.6	1.3	2.0	1.9
11	France	1.0	1.4	1.7	1.8
12	Canada	1.8	1.9	1.8	1.7
13	Spain	0.4	0.6	1.4	1.4
14	Ireland	3.4	2.3	1.9	1.4
15	Malaysia	0.7	1.1	1.3	1.4
16	Germany	1.1	1.0	1.3	1.4
29	United States	0.9	0.9	0.7	0.8
47	Japan	0.7	0.6	0.3	0.3

Source: UNCTAD.

Note: Economies are ranked in descending order of their performance index in 2001-2003. Figures were calculated based on outward stock.

#### *Spain slips in UN Human Development Index ranking*

Spain slipped from 19<sup>th</sup> to 20<sup>th</sup> position in the latest UN Human Development Index ranking, which is a cocktail of life expectancy at birth, per capita income (measured by purchasing power parity as opposed to market exchange rates) and other quantifiable indicators of the standard of living (see Table 4). This was due more to the better progress of other countries than to any deterioration in Spain's indicators. Indeed in life expectancy, Spain ranks 5<sup>th</sup> in the world with an average life span of 79.2 years, the result of the national health system created over the past 20 years and the generally healthy diet.

**Table 4. UN Human Development Index for Spain and Selected Countries**

Ranking (1)	Life Expectancy at Birth (2002)	GDP per Capita (PPP US\$) 2002
1. Norway	78.9	36,600
8. United States	77.0	35,570
12. United Kingdom	78.1	26,150
16. France	78.9	26,920
19. Germany	78.2	27,100
<b>20. Spain</b>	<b>79.2</b>	<b>21,460</b>

(1) Out of 177 countries.

Source: United Nations Human Development Report, 2004.

### *Spain's population to reach 50 million in 2025*

Spain's population will surpass 50 million by 2025, largely because of the sharp and ongoing rise in immigrants, according to the National Statistics Office (INE). The forecast, based on the 2001 population census, is in marked contrast to the projection of the United Nations Population Division which in 2001 forecast that Spain's population would drop from 40 million to 31.2 million in 2050 (see Table 5). The UN did not take immigration sufficiently into account.

**Table 5. Spain's Population, 2002-50 (millions)**

	<b>2002</b>	<b>2025</b>	<b>2050</b>
Population (mn)	41.6	50	53.1

Source: INE.

Spain continues to have one of the world's lowest fertility rates (1.29 children in 2003 compared with an EU-25 average of 1.48), but it is beginning to rise, average life expectancy continues to increase (from 75.5 years in 1980 to 80.4 in 2003) and the number of immigrants arriving in Spain (the largest inflow in the EU in 2003) has surpassed all expectations. Immigrant mothers accounted for 12% of total births in 2003 (3% in 1996).

Spain received one in every three immigrants arriving in the EU in 2003, according to a study by Eurostat, the statistical arm of the EU (see Table 6). The number is based on official figures and does not include illegal immigrants who escaped detection.

**Table 6. Arrival of Immigrants in Selected EU Countries in 2003**

<b>Country</b>	<b>Population (millions) at 1/1/04</b>	<b>Immigrants (thousands)</b>
<b>Spain</b>	<b>42.2</b>	<b>594.3</b>
Italy	57.8	511.2
Germany	82.5	144.9
UK	59.5	103
Portugal	10.4	63.5
France	59.9	55
Belgium	10.4	35.2
Ireland	4.0	28.3
Netherlands	16.2	2.8

Source: Eurostat.

The rise in the population, however, will not prevent the country's rapid 'greying'. Those over the age of 65 represented 16.9% of the population in 2002 (children under the age of 15 accounted for 15.6%) and in 2025 the respective figures will be 21.2% and 15%.

### *Spanish language set to take off in Brazil*

Brazil's parliament is set to finally approve a law that would make the teaching of Spanish obligatory in both private and state secondary schools. The idea was first mooted in 1991 and is expected to take effect in 2005.

Brazil is the largest country in Latin America and the only one where Spanish is not the dominant language. Brazil and Mexico are the two countries where Spanish companies have invested the most.