

## Inside Spain Nr 123

17 November - 16 December 2015

William Chislett

### Summary

Seven killed in Taliban attack on Spanish embassy in Kabul.  
Popular Party forecast to win the election but far from an absolute majority.  
Constitutional Court strikes down Catalan independence resolution.  
Ten takeaways from the European Commission's surveillance report.  
Abengoa struggles to stave off bankruptcy.

### Foreign Policy

#### Seven killed in Taliban attack on Spanish embassy compound in Kabul

Seven people, including two Spanish policemen, were killed when Taliban militants attacked the Spanish embassy compound in Kabul, just five weeks after Madrid withdrew its military contingent in Afghanistan.

A car bomb close to the compound's gates was detonated, causing an explosion that shook buildings across the city's diplomatic district and shattering nearby windows.

Spain completed its withdrawal at the end of October from Afghanistan after 14 years. In total, 29,861 Spanish troops were deployed since January 2002, making it the longest military operation of Spain's modern armed forces, with 102 dead (62 of them in an aircraft crash in Turkey while returning home in May 2003) excluding the latest attack.

The presence in Herat consisted of the protection force operating at the base and the city's airport, Air Force military officials in charge of running the airport, the Role 2E military hospital, a logistic unit and personnel at the general headquarters of the Training, Advise and Assist Command West.

### Domestic Scene

#### Popular Party forecast to win the election but far from an absolute majority

Spaniards go to the polls on 20 December in a crucial general election that is expected to significantly change the shape of Spanish politics, forged during the 1975-78 transition to democracy.

Two upstart parties, the centrist Ciudadanos ('Citizens') and the anti-establishment Podemos ('We Can'), are set to break the hegemony of the centre-right Popular Party

(PP) and the centre-left Socialists (PSOE), the two mainstream parties that have alternated in power since 1982 and have been damaged by a spate of corruption scandals and a prolonged recession.

The PP, according to Metroscopia (see Figure 1), will win the most seats (105-112) in the 350-seat parliament, but far from its current absolute majority of 186 seats, followed by the Socialists (85-94), Podemos (55-64) and Ciudadanos (53-67). A poll by the state-funded CIS gives a larger victory to the PP (120-128), with the Socialists in second place (77-89). The percentage of undecided voters (41%) is 10 points higher than before the 2011 election, according to CIS, making the outcome uncertain.

If the Metroscopia poll is correct the PP would need more than the support of Ciudadanos to form a government with an absolute majority (176 seats), be it a minority government supported by ad hoc parliamentary agreements with Ciudadanos, or a coalition government with that party (considered unlikely as Ciudadanos appears to have ruled this out). The Socialists, in the event that the PP fails to strike some kind of deal with Ciudadanos, would need also more than the support of Ciudadanos to form a government.

**Figure 1. Projected results of the 20 December general election**

	<b>% of votes</b>	<b>% now</b>	<b>Seats</b>	<b>Seats now</b>
Popular Party	25.3	44.6	105-112	186
Socialists	21.0	28.7	85-94	110
Ciudadanos	18.2	–	63-66	–
Podemos	19.1	–	55-64	–

Source: Metroscopia.

An aggregate of dozens of polls prepared by Kiko Llaneras for *El Español* also gives victory to the PP (108-129 seats, 50% chance), followed by the Socialists (71-92), Ciudadanos (61-76) and Podemos (39-54). No more polls are allowed before the election.

Ciudadanos' support has risen the most since January 2015, while that for Podemos fell the most until October when it began to rise again. Ciudadanos has moved towards the right, according to voters' perceptions, but is the closest to the centre (see Figure 2). Podemos, despite U-turns in its policies in an attempt to pitch itself as a kind of Nordic social-democratic party, is viewed as way to the left of the Socialists.

**Figure 2. Ideological position of voters (1)**

	January 2015	July	October-November
Popular Party	8.17	8.26	8.26
Ciudadanos	5.14	6.18	6.37
Socialists	4.62	4.38	4.40
Podemos	2.28	2.09	2.30

(1) Taking 1 as extreme left, 10 as extreme right and 5.5 as the centre, where do respondents place the four main parties?

Source: CIS.

To a large extent, disaffection with the political establishment is accompanied by a demand for generational renewal: Albert Rivera, the Ciudadanos leader, is 36, Iglesias is 37, while Pedro Sánchez, the Socialists' leader, is 43 (he replaced the 64-year-old Alfredo Pérez Rubalcaba in 2014) and the Popular Party's Mariano Rajoy is 60.

Ciudadanos, according to CIS, is the party least rejected by voters under the age of 24, while the PP has the largest share of votes of those over the age of 65. Close to two-thirds of voters aged between 25 and 34 (64.2%) said they would never vote for the PP and the same percentage of voters over the age of 65 said they would never vote for Podemos.

Prime Minister Mariano Rajoy campaigned on the government's record of saving crisis-hit Spain from a sovereign bail out after it swept the Socialists out of office at the end of 2011, starting economic recovery, reducing unemployment, though it remains very high, and creating jobs.

The balance of the PP government is mixed (see Figure 3). The main blot is continued high unemployment, though the jobless rate has come down from a peak of 27% in 2013 to 21%.

**Figure 3. Some of the changes during the Popular Party government, 2011-15 (1)**

	2011	2015
GDP growth (%)	-1.0	3.1 (e)
Nominal GDP (€ trillion)	1.05	1.04 (e)
Per capita income (€)	23,900	23,300 (e)
Stated unemployment rate (% of labour force)	22.56	21.18 (2)
Temporary employment rate (%)	24.8	26.2
Number of social security contributors (million)	17.25	17.22 (3)
Social security reserve (€ billion)	66.8	34.2 (3)
General government budget deficit (% of GDP)	8.9	4.7 (e)
Gross public debt (% of GDP)	69.5	100.8 (e)
Inflation (%)	2.9	-0.2 (e)
Current account balance (% of GDP)	-3.3	0.4 (e)
Banks' assets (% of GDP)	338.3	264.2 (e)
Non-performing loans (% of total lending)	7.8	10.9
Number of sales of foreclosures of homes ordered by the courts	77,854	37,615 (4)
Ibex-35 stock market index	8,454.4 (5)	9,711.6 (6)

(e) Estimate.

(1) The 2011 election was held on November 20 and the 2015 one on December 20.

(2) Third quarter of each year.

(3) November of each year.

(4) First half.

(5) 19 November.

(6) 15 December.

Source: INE, General Council of the Judiciary, Employment and Social Security Ministry, Bank of Spain, Bolsa de Madrid and Afi.

While Rajoy played up the PP's experience as the best guarantee of securing a better future, Sánchez reminded voters that it was the Socialists that created Spain's welfare state (when it was in office between 1982 and 1996) and was the best option to defend it following the PP's cuts. Rivera and Iglesias focused on the need to regenerate Spain's democracy, clean up corruption and create a more sustainable economic model than the one based excessively on the construction sector.

All the leaders were not short on making promises. The PP said it would continue to cut personal and corporate tax rates, the Socialists said they would ditch the 2012 labour market reforms, Ciudadanos promised to introduce a single contract to reduce the gulf between workers on permanent and temporary contracts and Podemos said it would hugely increase the minimum wage.

The one area where there are few significant disagreements is foreign policy.<sup>1</sup>

### Constitutional Court strikes down Catalan independence resolution

The Constitutional Court sided with the government and struck down the Catalan parliament's pro-independence resolution, which called for the creation of a breakaway republic.

The parliament also declared that the Court's rulings and other decisions taken by the state were no longer valid inside the region. This declaration of hostility towards the central government raised the political temperature ahead of Spain's general election on 20 December.

The Court said the resolution, which followed the victory of the pro-independence movement in September's regional election, was in 'absolute contradiction' of the 1978 constitution, which guarantees Spain's 'indissoluble unity' and puts national sovereignty in the hands of all Spaniards.

*Junts pel Sí* ('Together for Yes'), an unholy alliance between Artur Mas's Democratic Convergence party, the much more radical Republican Left of Catalonia (ERC) and grass-roots separatists, won 62 of the 135 seats in the Catalan parliament in September's snap election billed as a de facto vote on establishing a separate state. Together with the 10 seats of the anti-capitalist Popular Unity Candidacy (CUP), the pro-independence camp has 72 seats and 48% of the vote against 52% for parties opposed to independence.

Mas, Prime Minister of Catalonia since 2010, has so far failed to be re-appointed because of ideological squabbles between CUP, which is refusing to back him, and *Junts*. He has until 10 January to be appointed Prime Minister. If there is no agreement on backing him or someone else Catalonia will go to the polls for the fourth time since 2010.

Mas did not head the list of *Junts*' candidates for September's election. That spot went to Raul Romeva, a university lecturer and former MEP for the left-wing ICV coalition, in a bid to galvanise greater support for *Junts*. But as the incumbent Mas still expected to be shoed in as president, although he said he was prepared to 'sacrifice' himself for the cause of independence. That promise looked hollow.

---

<sup>1</sup> See the report (in Spanish) by the Real Instituto Elcano on the foreign policy positions of the four parties at <http://www.realinstitutoelcano.org/especiales/elecciones2015/index.php> .

CUP's support is increasing. If there is no agreement and fresh elections, CUP could seek an alliance after or before the polls with Podemos and the ERC, thereby displacing Mas. Podemos was not part of *Junts* as it formed a coalition called *Catalunya Sí que es Pot* ('Catalonia Yes We Can') with several smaller forces.

Podemos rejected the notion that September's election could be considered a referendum on independence and focused on issues such as unemployment and corruption. It is, however, the only party of the four main ones competing in Spain's general election on 20 December that supports the right of Catalans to have a legal and binding referendum on whether to establish a sovereign state.

It is now widely accepted among the political class that whatever the colour of the next national government it needs to reform parts of the Constitution in consensus with the main opposition parties.

Opinion polls show that a significant proportion of Catalans –more than those in favour of the options of independence or maintaining the current situation– favour a so-called 'third way' under which Catalonia would remain part of Spain, but with new powers and special treatment in recognition of the region's unique status (the so-called *hecho diferencial*).

This possibility could be offered by modifying the regional government architecture as part of an overhaul of the Constitution which would then be put to a referendum in the whole of Spain, and if approved in Catalonia could be taken to mean that the region rejects independence.

The Constitution has two articles that could be wielded *in extremis*: Article 116 allows the national government to declare states of alarm, emergency and siege in a disobedient region and Article 155 to take coercive measures, following approval by an absolute majority in the Senate.

### More deaths than births in 2015, for first time in 71 years

A significant change in Spain's demographic trends looks like occurring in 2015, with more deaths than births for the first time since 1944.

The number of people who died in the first half of the year was 225,924, 19,268 more than the number of babies born. This trend is unlikely to change much during the rest of the year.

Average life expectancy is now close to 83 years and the average age when a woman has her first child is 33.3 years. One quarter of women of child-bearing age do not have children, the highest figure since 1916.

The low fertility rate, longer life expectancy and net migration, caused by the economic crisis, are shrinking the population, following a big rise over a 10-year period due to the influx of immigrants. The National Statistics Office (INE) forecasts a population fall of one million between 2014 and 2029 to 45.4 million and to 40.8 million in 2065.

The population fell by 26,501 in the first half of 2015 to 46.42 million. Net migration of Spaniards and foreigners (the difference between emigration and immigration) was 7,385, as a result of the emigration of 164,606 people and the immigration of 157,221. This was the smallest number since 2013 (61,278 in the first half of 2014 and 141,895 in the same period of 2013), and was another sign that the economy is recovering.

The net migration of Spaniards was 27,766 (50,844 left and 23,078 returned), up from 21,828 in the first half of 2014 and 22,116 in the same period of 2013.

The largest foreign resident community in Spain were Rumanians. Their number surged from 66,994 in 2002 to a high of 798,970 in 2012 before falling to 705,333 in July 2015, according to INE. All the 10 largest communities except for the Italians shrank between 2012 and 2015, as migrants returned to their home countries or moved elsewhere (see Figure 4). The resident foreign population fell by 810,000 in two and a half years.

**Figure 4. Resident foreign population by the top-10 countries of origin, 2002, 2012 and July 2015 (1)**

	1 January 2002	1 January 2012	1 July 2015
Rumania	66,994	798,970	705,333
Morocco	267,078	771,632	680,120
UK	104,846	312,959	300,439
Italy	40,935	178,225	187,330
China	30,268	170,839	169,445
Ecuador	240,760	309,777	164,803
Germany	85,245	153,568	143,876
Colombia	188,468	245,835	139,336
Bulgaria	30,548	151,475	133,114
Portugal	43,002	121,271	103,422
Others	639,828	2,021,479	1,699,593
Total	1,737,972	5,236,030	4,426,811

(1) Provisional figures for 2015.

Source: INE.

### Spain rises in the UNHD index, surpasses Italy

Spain was ranked 27<sup>th</sup> out of 188 countries in the UN Human Development Index, up from 26<sup>th</sup> position in 2014 and overtaking Italy.

The index (maximum value one) is based on life expectancy at birth, mean years of schooling, expected years of schooling and gross national income per capita (see Figure 5).

**Figure 5. UN Human Development Index for selected countries**

Ranking (1)	Human Development Index value 2014	Life expectancy at birth 2014 (years)	Mean years of schooling 2014 (years)	GNI per capita (2011 PPP US\$) 2014
1. Norway	0.944	81.6	12.6	64,992
6. Germany	0.916	80.9	13.1	43,919
8. US	0.915	79.1	12.9	52,947
14. UK	0.907	80.7	13.1	39,267
22. France	0.888	82.2	11.1	38,056
<b>26. Spain</b>	<b>0.876</b>	<b>82.6</b>	<b>9.6</b>	<b>32,045</b>
27. Italy	0.873	83.1	10.1	33,030
36. Poland	0.843	77.4	11.8	23,177

Note: the maximum value is one.

(1) Out of 188 countries.

Source: United Nations Human Development Report, 2015.

Despite the crisis, Spain's progress in the United Nations Human Development Index for Spain between 1980 and 2014 was the best among the big four euro-zone countries albeit from the lowest starting point (see Figure 6).

**Figure 6. Change in UN Human Development Index for selected countries, 1980-2014 (1)**

	1980	1990	2000	2010	2012	2014	Change 1980- 2014 (%)
France	0.722	0.779	0.848	0.879	0.884	0.888	22.9
Germany	0.739	0.782	0.854	0.904	0.911	0.916	23.9
Greece	0.713	0.749	0.798	0.856	0.854	0.865	21.3
Italy	0.718	0.763	0.825	0.869	0.872	0.873	21.6
Spain	0.702	0.755	0.826	0.864	0.869	0.876	24.7
US	0.825	0.858	0.883	0.908	0.912	0.915	10.9

(1) The maximum value is one.

Source: UN Human Development Reports



## The Economy

### Ten takeaways from the European Commission's surveillance report

The European Commission published its fourth post-programme surveillance *report*, which sets out the achievements and challenges for the economy, following Spain's exit in January 2014 from the financial assistance programme for the recapitalisation of banks.

Spain used €41.3 billion of the up to €100 billion made available. As of end-October, it owed €35.7 billion. The Commission said the repayment risks for the loan were 'very low'.

- (1) Economic conditions are improving, but significant imbalances remain. The budget deficit is falling (4.7% of GDP in 2015), but remains among the highest in the euro zone.
- (2) The household and non-financial corporate sectors are reducing their leverage. The total stock of private-sector debt was 178.6% of GDP in the second quarter, 39 percentage points lower than the peak in the second quarter of 2010.
- (3) Investment continues to grow strongly, especially in equipment, but also non-residential construction.
- (4) The current account balance has further improved, and the contribution of the external sector to GDP growth is expected to be broadly neutral in 2015. The current account surplus is expected to widen to 1.4% of GDP from 1% in 2014. Spanish economists, however, forecast a much lower surplus.
- (5) The net international investment position remained very negative, although it improved to -91% of GDP in June (ie, Spain's foreign liabilities exceeded its foreign assets), one of the highest in the EU. In order to lower it to around 35% in 2024, and in turn reduce concerns about external sustainability, much larger current account surpluses need to be sustained.
- (6) Banks' profitability is rising but is too reliant on declining funding costs, the reduced need to provision against loan losses, and income generated by banks' fixed-income portfolios. Further mergers cannot be excluded. Access to loans for companies and households significantly improved.
- (7) The reform of public administration continues to advance. By the end of September, 180 out of 220 planned measures had been adopted, delivering €6.2 billion of savings (excluding measures affecting employees), according to the government.
- (8) The youth unemployment rate has decreased, as more young people have gone into employment or education and training, but it remains very high. The rate (for 15-24 year-olds) dropped from 52.4% in September 2014 to 46.6% in the same

month of 2015. The percentage of youth ‘not in employment, education or training’ (known as Neets) fell from 20.8% to 18.5%.

- (9) Duality in the labour market has increased. In the third quarter of 2015, 26.2% of all wage earners were on a temporary contract, up from 24.6% a year earlier.
- (10) Incentives to permanent hires have not had a sizeable impact on increasing permanent employment. The number of workers on permanent contracts increased 1.6% in the 12 months to September 2015, while those on temporary contracts increased 10.2%.

### EBA corrects error in banks’ capital adequacy ratios, but still below EU average

The European Banking Authority (EBA) corrected its error in calculating capital adequacy numbers for Spanish and other banks after lenders’ shares took a hit.

The fully loaded core equity tier 1 ratio under Basel III, which takes into account the application of all new capital requirement rules in 2019 and is the main indicator of capital strength, was lifted from 9% (the lowest ratio) to 10% for Spanish banks, but is still below the EU average of 12% (see Figure 7). The error was caused by double-counting.

**Figure 7. Fully loaded common equity tier 1 (CET1) ratio by banks’ home country (%)**

	%
France	12.4
Germany	12.6
Italy	11.1
Spain	10.0
UK	11.8
EU average	12.0

Source: European Banking Authority, June 2015.

Spain’s banks are out of the woods after a bruising crisis sparked by the bursting of a massive property bubble as of 2008. Since then 31% of branches have been closed, 25% of employees lost their jobs and aid in one form or another was the equivalent of 27% of GDP.

Today, they face a new set of challenges resulting from the combination of increasing regulatory pressure, which requires higher capital, and the need to further improve efficiency, which will have to come from further cost-cutting as the room to boost revenues from core banking activities, such as lending (very competitive), is limited by interest rates that are expected to remain low for some time.

### Tax burden rises more than the OECD average...

Spain's tax burden rose from 32.7% of GDP in 2013 to 33.2% in 2014, an increase of 0.5 percentage points compared to an average one of 0.2 for the OECD as whole (see Figure 8), according to provisional figures. But it was still below the average.

**Figure 8. Total tax revenue (% of GDP), 1975-2014**

	1975	1985	1995	2000	2009	2014 (1)
France	34.9	41.9	41.9	43.1	41.3	45.2
Germany (2)	34.3	36.1	36.2	36.2	36.1	36.1
Italy	24.5	32.5	38.6	40.6	42.1	43.6
<b>Spain</b>	<b>18.0</b>	<b>26.8</b>	<b>31.3</b>	<b>33.4</b>	<b>29.8</b>	<b>33.2</b>
UK	34.2	35.1	31.9	34.7	32.3	32.6
OECD total	28.6	31.5	33.6	34.2	32.7	34.4

(1) Provisional. (2) Unified Germany as of 1991.

Source: Revenue Statistics, OECD

Spain started from a very low base in 1975 (18%), the year that the Franco dictatorship ended. The tax burden peaked at 36.5% in 2007 at the height of the economic boom and then plummeted to 29.8% in 2008, following the bursting of a massive property bubble which triggered a long recession.

### ... R&D spending falls

Total expenditure on R&D inched down to 1.20% of GDP in 2014 from 1.24% in 2013, according to the latest comparative Eurostat figures. It has declined every year since peaking at 1.35% in 2009 and is well below the EU average (see Figure 9).

**Figure 9. Total spending on R&D (% of DGP)**

	2014 (1)	2009
Finland	3.17	3.75
Germany	2.84	2.72
France	2.26	2.21
EU-28	2.03	1.94
UK	1.72	1.75
Italy	1.29	1.22
<b>Spain</b>	<b>1.20</b>	<b>1.35</b>

(1) Provisional figures.

Source: Eurostat.

The Socialist government of José Luis Rodríguez Zapatero set an R&D target of 2% for 2010, but government and corporate spending cuts because of the economic crisis out paid to this ambition.

### Close to 80% of Spaniards own their homes

Spain has the highest percentage of home ownership (78.8%) among the large EU countries. Ownership varied between 96.1% in Rumania and a low of 52.5% in Germany (see Figure 10).

**Figure 10. Share of population living in owner-occupied and rented dwellings in EU countries, 2014**

	Owner	Tenant
Rumania	96.1	3.9
<b>Spain</b>	<b>78.8</b>	<b>21.2</b>
Italy	73.2	26.8
EU-28	70.1	29.9
France	65.1	34.9
UK	64.8	35.2
Germany	52.5	47.5

Source: Eurostat.

## Corporate scene

### Abengoa struggles to stave off bankruptcy

Abengoa, a leading engineering and renewable energy company, was desperately seeking to avoid becoming Spain's biggest corporate bankruptcy.

The company, which filed for preliminary creditor protection last month, reached a deal with its creditor banks for a lifeline of €100 million, but must find another €350 million to guarantee assets.

Abengoa, which employs 27,000 people worldwide, said it was forced to start insolvency proceedings after a potential investor decided not to inject €350 million into the heavily indebted company.

The company's problems go back to some extent to Spain's energy reform in 2013 which reduced subsidies for renewable energy providers after several years of generous support. Abengoa accumulated debt of €9 billion.

A 17-year-old Spanish schoolboy predicted Abengoa's collapse a year ago. Pepe Baltá chose Abengoa for an economics project and spotted oddities in its 2012 and 2013

accounts that were apparently not seen by Deloitte and Standard & Poor's. The latter upgraded its long-term rating of Abengoa only weeks before the company specified the amount of its debts.

Fitch Ratings downgraded Abengoa's long-term issuer default rating from CC to RD (restricted default) this week, following the company's announcement that some series of notes under its €750 million commercial paper programme have not been paid.

### BBVA acquires stake in UK's Atom Bank

BBVA, Spain's second-largest bank, is to invest around €64 million for a 29.5% stake in Atom Bank, the UK's first mobile-only bank, as part of its strategy to become a leader in digital financial services.

Atom is due to begin operating in 2016.

'BBVA believes the digital market in the UK offers excellent growth opportunities and that digital banks that put the customer first are the future', said Francisco González, BBVA's Chairman and Chief Executive. 'BBVA's investment in Atom backs those beliefs in one move'.

### Acciona wins competitive tender to build Canadian clean-energy project

A consortium of Acciona, Korea's Samsung and the Canadian Petrowest was named the preferred proponent by BC Hydro for the main civil works construction of the Site C Clean Energy Project, one of the largest infrastructure projects underway in Canada.

This means that the consortium won the competitive tender but the contract has yet to be signed pending resolution of various details.

The project includes the construction of an earth-fill dam, two diversion tunnels, and a concrete foundation for the generating station and spillways.