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Summary

Grappling with a second wave of the pandemic, as cases hit more than 1 million.

Judicial reforms heighten tensions with conservative opposition.

Government weighs up pardons for Catalan separatists.

Sánchez hopes EU's recovery fund will create over 800,000 jobs.

Fiscal deficit forecast at 11.3% of GDP this year.

Domestic scene

Grappling with a second wave of the pandemic, as cases hit more than 1 million

Spain was one of the countries most affected during the first wave of COVID-19 (March to June) and is now being hard hit by a second wave. Cases of the virus are rising fast and the total hit more than one million, the highest number in Europe and the fifth in the world (see Figure 1)

Figure 1. Notified cases by selected countries

	Total cases	Cases per one million population
US	8,424,753	25,503
Spain (1)	1,015,795	21,723
France	910,277	13,936
UK	741,212	10,901
Italy	423,578	7,009
Germany	373,821	4,456

(1) This figure is some 40,000 higher than that reported by the Spanish authorities in the table below. Worldometer says there are many issues with Spanish data including a number of historical downward adjustments that have not been documented through revised reports (which still show the original –higher– numbers being reported), nor explained.

Figures at 19/X/2020.

Source: <https://www.worldometers.info/coronavirus/#countries>.

The situation is aggravated not just by weaknesses in some parts of the health system but by political polarisation and the decentralised system of government that is hampering containment.

The poisonous political atmosphere is exemplified by the battle between the Madrid regional government, controlled by the mainstream conservative Popular Party (PP), and the minority national government, led by the Socialists in a coalition with the hard-left Unidas Podemos, over imposing a lockdown in Madrid.

The national government declared a 15-day state of emergency on 9 October and a new partial lockdown for Madrid after seeing its measures introduced on 2 October struck down by a court, following a successful appeal against them by the Madrid government. Similar lockdowns are in place in Paris and parts of the UK, among other European countries.

Isabel Díaz Ayuso, the head of the Madrid government, claimed the actions in place were working and the state of emergency, which restored the measures lifted by the court, was not needed. They include a ban on leaving and entering the Madrid region, with 6.6 million citizens, except for non-essential trips.

The aggressive stand-off is part of the PP's strategy of painting the government as authoritarian and ruining the economy.

With 439 cases per 100,000 over 14 days, Madrid is not the worst hit region in the second wave of the virus (see Figure 2). That number is down from 750 at the start of October, but this could be due to a sharp fall in PCR tests.

Tougher restrictions were also imposed in Catalonia as of 14 October including the closure of bars and restaurants. They can provide takeaway services only. In Madrid, bars are limited to 50% capacity and must close at 11pm.

Figure 2. Coronavirus (COVID-19) cases by region (1)

	Notified cases (PCR test)	Cases per 100,000 people in last 14 days	Deaths
Andalucía	93,960	271	2,137
Aragón	44,322	509	1,528
Asturias	8,443	247	371
Balearic Islands	16,195	130	327
Basque Country	54,200	351	1,986
Canary Islands	15,955	77	257
Cantabria	7,924	151	247
Castilla y León	64,171	486	3,346
Castilla-La Mancha	53,841	341	3,330
Catalonia	176,860	360	5,913
Extremadura	14,686	298	651
Galicia	26,905	167	825
Madrid	281,388	439	10,014
Murcia	27,047	347	261
Navarre	25,799	945	652
La Rioja	10,591	531	439
Valencia	49,648	116	1,685
Spain (2)	974,449	312	33,992

(1) Figures at 19/X/2020.

(2) Including the North African enclaves of Ceuta and Melilla.

Source: Health Ministry.

The *Lancet*, a highly respected British medical magazine founded in 1823, took Spain to task in an [editorial](#) published on 16 October, saying the second wave 'in some parts of Spain was quite predictable' as some regional authorities were too fast at reopening when the national lockdown was lifted and too slow at implementing an efficient track and trace system. The test-trace-isolate trypic, the cornerstone of the response to the pandemic, remains weak.

With 5.9 nurses per 1000 inhabitants, Spain has one of the lowest ratios in the EU (an average of 9.3), and too often relies on temporary contracts that can run for just a few days.

The central and regional governments have ignored a call by health professionals in the *Lancet* to set up an independent evaluation of their COVID-19 responses.

Judicial reforms heighten tensions with conservative opposition

The leftist minority coalition government sought to unblock the refusal of the conservative Popular Party (PP), the main opposition, to renewing the body governing the justice system by fast-tracking a law that would enable its members to be elected by an absolute and not a qualified majority of three fifths of MPs, as has been the case since 1985.

As a result of two inconclusive elections since 2019, the appointment of new members of the General Council of the Judiciary (CGPJ) by a qualified majority has not been possible. The bill to change to an absolute majority is a *proposición de ley*, a faster procedure that is introduced by MPs, as opposed to a *proyecto de ley*, which comes from the government.

The latter would require reports from the CGCP and opinions from the Council of State and the Prosecutorial Council. The government can probably muster an absolute majority of MPs in support of the bill.

The Socialist Prime Minister, Pedro Sánchez, said he would drop the planned reform if the PP agreed to negotiate on the basis of an accord reached in July. That would involve the government and the PP each selecting 10 members. But the PP insists on the hard-left Unidas Podemos, the junior partner in the government, not being involved, which is politically unacceptable.

The move to an absolute majority, attacked by the PP as 'dictatorial' and weakening the separation of powers, came soon after the European Commission, in its first report on the rule of law in all EU countries, raised concerns about the long period the CGPJ has been exercising its functions *ad interim* –since December 2018–.

With the deterioration of the rule of law in Hungary and Poland, the Commission is sensitive to such changes. It is not happy with the government's reform as it would heighten the perception that the CGPJ is vulnerable to politicisation. A three-fifths majority requires greater consensus.

Professional associations legally challenged the competence of the acting CGPJ to continue with appointments for top judicial positions. The CGPJ decided in January 2020 to suspend these appointments. Carlos Lesmes, the President of the Supreme Court who also chairs the CGPJ, has repeatedly called for the nomination of new members and warned that prolongation of the impasse could discredit the body.

The Socialist government of Felipe González changed the system for the CGPJ's members from all 20 members being elected by the legal profession to being elected by the Congress and the Senate equally. Twelve of the members must be judges or magistrates chosen from a list of 36 candidates proposed by associations of judges or by non-associate judges and the other eight are attorneys or jurists.

EU countries have bodies similar to the CGPJ, but Spain is the only one whose parliament elects all its members. It appoints, transfers and promotes judges, and is also responsible for the training and recruitment of judges. As more than half of the CGPJ is appointed by parliament and the CGPJ appoints judges to the Supreme Court, that key Court is effectively decided by political parties. Although judges are granted full independence during their tenure, they can be seen to have acquired 'political debts' at the moment of their appointment, regardless of whether they are elected by a qualified or an absolute majority.

The judges' political colour can also be ascertained to some extent from which association or not they belong to. Of the four associations, only the 'progressive' Judges for Democracy (JJPD) clearly supports the government's reform. The other three are more conservative, particularly the *Asociación Profesional de la Magistratura*. It is far from certain that the Constitutional Court would rule in the government's favour if the PP appealed the reform.

The level of perceived judicial independence in Spain is average, according to the European Commission. In 2020, 44% of the general public and 42% of companies perceived it as 'very good' or 'fairly good'. The 2020 EU Justice Scoreboard ranks Spain 19th out of 27 countries in perceived judicial independence.

The European Commission also brought up the issue of the relation between the prosecutor general and the executive. The prosecutor is appointed by the head of state, acting on a proposal of the government, and after consulting with the Council and obtaining an assessment of the candidate's suitability from the corresponding committee in parliament. The government cannot dismiss the prosecutor but the mandate ends at the same time as the government's, laying the system open to criticism that the term of office may affect the perception of independence.

Turning to corruption, the European Commission said Spain does not have a dedicated overall anti-corruption strategy in place. The 2020 Eurobarometer showed that 94% of respondents in Spain perceived corruption as widespread (with an EU average of 71%). Almost nine in 10 companies (88%) said corruption is very or fairly widespread (with an EU average of 63%). Just over half of companies (52%) said corruption is a problem when doing business (with an EU average of 37%).

Spain is ranked 10th in the EU and 30th globally in Transparency International's 2019 Corruption Perceptions Index which covers 180 countries.

Supreme Court asked to investigate Deputy Prime Minister Pablo Iglesias

A judge called on the Supreme Court to investigate Pablo Iglesias, the co-founder of Podemos and the junior partner in the coalition government, following the theft of a mobile phone and the publication of information on the handset's memory card. The phone belonged to Dina Bouselham, a colleague of Iglesias, when he was a MEP.

The High Court investigating judge, Manuel García-Castellón, believes Iglesias may have committed criminal acts including filing a false complaint, disclosing secrets and computer-related crimes, which carry jail sentences totalling up to nine years. As a minister, Iglesias can only be tried in the Supreme Court as he has immunity in the lower courts.

The card contained information on Podemos's finances and files of a personal nature. It was given to the magazine *Interviú*, which did not use it, and came into the hands of José Manuel Villarejo, a police commissioner who has been in prison awaiting trial since November 2017 for creating an alleged spy network that gathered material against politicians and business leaders. The 'Dina' case is an offshoot of the 'Villarejo' case. The right-wing *OKDiario* published some of the content.

The judge accused Iglesias of keeping the phone card for a long time before returning it (damaged) for reasons of 'political opportunism'. He implied Podemos sought an electoral advantage by establishing a false connection between the theft in November 2015 and the publication in *OKDiario* in order to fuel conspiracy claims.

Iglesias refutes this and pointed out that the criminal division of the High Court had earlier ruled that he was an affected party in the investigation. He has gone from being a victim to a possible suspect.

Government weighs up pardons for Catalan separatists

The government has started to hear requests for pardoning nine jailed Catalan separatists found guilty in October 2019 of sedition and misuse of public funds for organising in 2017 an illegal referendum on independence for the region and a unilateral declaration of secession.

The longest sentence (13 years) was given to Catalonia's former Vice-president, Oriol Junqueras.

The minority coalition government, led by the Socialist Pedro Sánchez, announced the possibility of pardons during a parliamentary session on the 2021 budget. The government, with 155 of parliament's 350 seats, was formed after the December 2019 election, thanks, in part, to the support of the 13 MPs of the pro-independence Republican Left of Catalonia. Sánchez also needs their support to get the budget approved.

The jail sentences are viewed in some legal circles as excessive. A pardon, unlike an amnesty, would not wipe the slate clean for the nine. The mainstream conservative PP and the hard-right VOX are incensed by the idea of pardons.

The announcement was followed by the Supreme Court confirming the December 2019 sentence against the Catalan Premier Quim Torra, which ordered him to step down from the post for 18 months for disobeying the central electoral body after he refused to remove a banner from a public building during the general election campaign in April 2019.

Torra is the second Catalan Premier to be deposed from office, following the sacking in 2017 of Carles Puigdemont by the Popular Party government of Mariano Rajoy for holding the referendum and declaring secession.

The banner read 'Free political prisoners' and referred to the jail sentences. The electoral body construed the banner, displayed at the seat of the Catalan government, as breaking neutrality at a time of elections.

Republican Left of Catalonia and Junts per Catalunya, the two pro-independence parties with 66 of the Catalan parliament's 135 seats, said the sentence was one more episode in the 'state's repression' of Catalonia. These two parties are able to govern thanks to support from small parties.

In another blow for the secessionists, the Council of Europe, founded after World War Two to uphold human rights, democracy and the rule of law, delegitimised their strategy of using Catalan institutions to call referendums on independence, and in a recommendation said the only legal way was through a change in the 1978 Constitution and an *ad hoc* law passed by the national parliament after consulting with bodies like the Constitutional Court. Such a referendum would also involve all Spaniards and not just Catalans, as has happened so far.

Pere Aragonès is Catalonia's interim Premier until elections are held in the region, probably in February. A survey by the Catalan government's research centre showed the main priority for Catalans now is public services, which have deteriorated, and not resolving the political problem with the central government in Madrid as was the case last year (see Figure 3).

Figure 3. 'In your view, the Catalan government should give priority to...' (%)

	2019-20	Total	Cs	JxCat	ERC	PSC	Com	CUP	PP
Trying to resolve the political problem between Catalonia and Spain	56.0 39.9	39.9	34.7	55.0	44.8	30.1	23.8	45.9	22.2
Managing public services for which it is responsible	36.8 56.6	56.6	64.0	41.2	55.9	68.0	75.2	44.3	77.8

Note: Cs is Ciudadanos; JxCat is Junts per Catalunya; ERC is Republican Left of Catalonia; PSC is the Catalan Socialist Party; Com is CatComú-Podem; CUP is Candidatura d'Unitat Popular; and PP is Popular Party.

Source: Catalan government research centre.

In another development, the Constitutional Court annulled the Catalan government's Public Diplomacy Council (Diplocat), a network of offices abroad that promoted the cause of independence, among other things.

Surge in immigrants and asylum seekers

Spain received 408,500 permanent immigrants last year, the largest number since 2008 and the biggest rise over 2018 (+19%) after Portugal among OECD countries (see Figure 4).

Figure 4. Inflows of permanent immigrants, 2018 and 2019

	2018	2019 estimates	% change
Portugal	64,000	87,700	+37
Spain	344,200	408,500	+19
France	277,300	292,300	+5
UK	342,800	345,700	+1
Germany	630,800	612,100	-3

Source: OECD International Migration Outlook 2020.

There was also a sharp increase in the number of new asylum applications, from 52,750 to 115,190, the largest absolute change (see Figure 5).

Figure 5. New asylum applications 2018 and 2019 and main countries of origin

	2018	2019	% change	Seekers per 1mn pop (2019)	Main countries
Spain	52,750	115,190	+118	2,456	Venezuela, Colombia, Honduras
UK	37,370	44,320	+19	663	Iran, Albania, Iraq
France	111,420	119,920	+8	1,722	Afghanistan, Albania, Georgia
Germany	161,930	142,510	-12	1,710	Syria, Iraq, Turkey
Italy	53,440	35,010	-34	578	Pakistan, El Salvador, Peru

Source: OECD International Migration Outlook 2020.

The economy

Sánchez hopes EU's recovery fund will create over 800,000 jobs

Prime Minister Pedro Sánchez expects more than 800,000 jobs will be created over the next three years, thanks to the €72.7 billion in grants Spain expects to receive from the EU's pandemic recovery fund.

Overall, Spain could obtain €140 billion in grants and loans, more than the cost (€112 billion in today's money) of the US's 1948 Marshall Plan to help re-build non-communist war-torn Europe, and from which Spain was excluded because the Franco dictatorship took Hitler's side.

Green investment would take 37% of the €72.7 billion and digital transformation 33%, helping to create what Sánchez called a 'new modernisation of the Spanish economy.' The targeted sectors for investment include energy transition, business digitalisation, education and updating the tax system.

The €750 billion recovery fund for the whole of the EU comes with strict conditions and oversight. Spain cannot use the money however it wants, particularly on yet more physical infrastructure. The European Commission wants countries to include in their investment plans and reforms the following areas:

- Power up – Frontload future-proof clean technologies and accelerate the development and use of renewables.
- Renovate – Improve the energy efficiency of public and private buildings.

- Recharge and refuel – Promote future-proof clean technologies to accelerate the use of sustainable, accessible and smart transport, charging and refuelling stations and extension of public transport.
- Connect – Roll out rapid broadband services to all regions and households, including fibre and 5G networks.
- Modernise – The digitalisation of public administration and services, including judicial and healthcare systems.
- Scale-up – Increase European industrial data cloud capacities and develop the most powerful, cutting edge, and sustainable processors.
- Reskill and upskill – Adapt education systems to support digital skills and educational and vocational training for all ages.

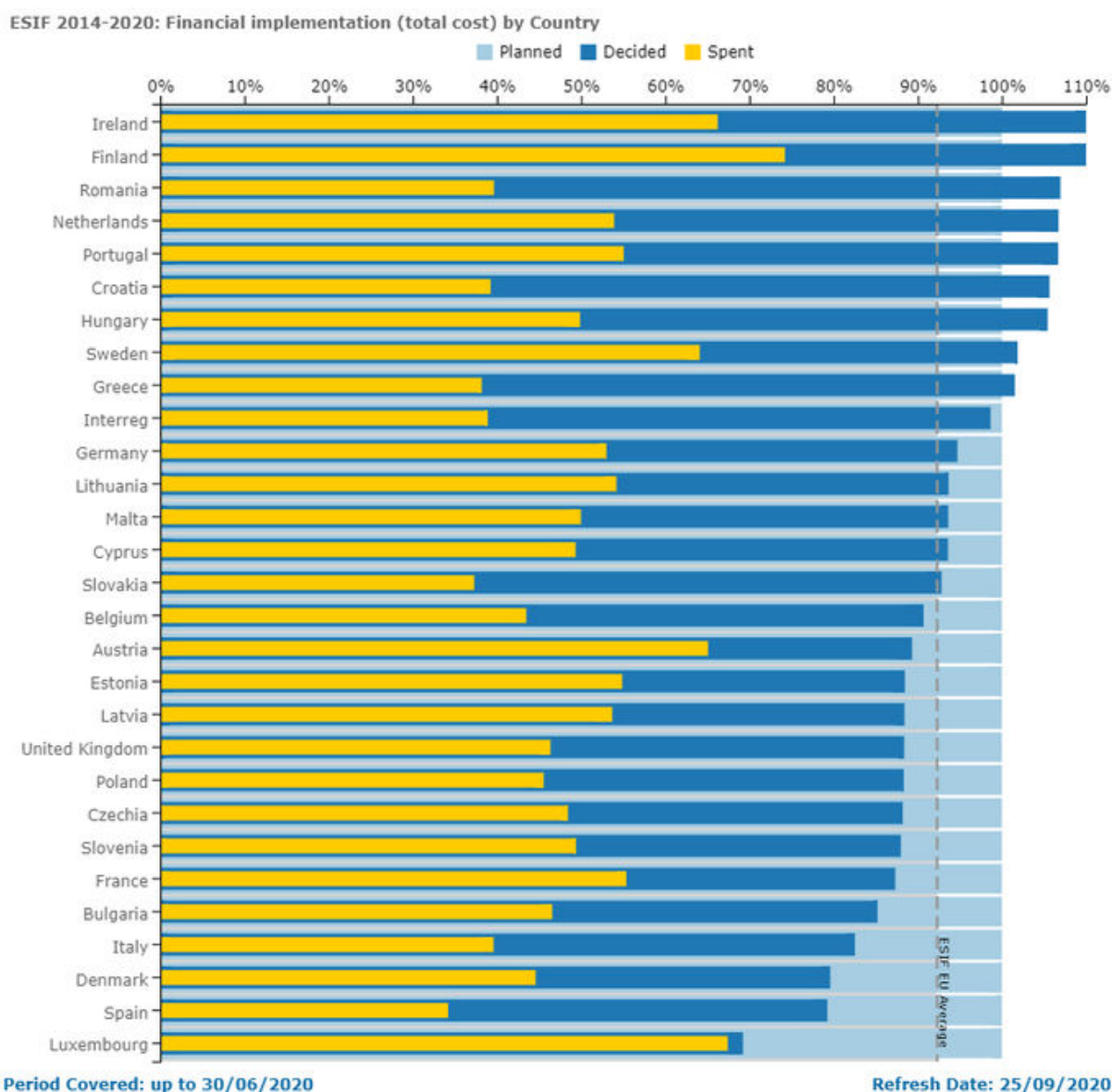
There are serious doubts on whether Spain has the capacity to plan, absorb and execute the tsunami of funds, and fears that their administration will be politicised. Control of the funds will be centralised in the Prime Minister's office. The PP, the main opposition party, wants a non-partisan agency to administer the funds.

'We would be making an enormous mistake if we thought that just receiving the funds will enable our country to get the most out of them', the Bank of Spain's Governor Pablo Hernández de Cos, told parliament. 'If we make bad use of the funds, and basically use them for current spending... the multiplier effect will be very reduced'.

The AIReF independent fiscal watchdog warned there was a 'high risk of delays in the absorption of these funds and the execution of projects'.

As of 30 June 2020, Spain had spent less than 40% of the money it was due from the European Structural Investment Funds (ESIF) for the 2014-20 period, one of the lowest amounts (see Figure 6). Under the N+3 rule if funds have been committed the period for executing them can be extended until 2023.

Figure 6. ESIF 2014-20: financial implementation (total cost) by country



Source: EU.

Fiscal deficit forecast at 11.3% of GDP this year

The government finally presented its 2021 budget, which incorporates a fiscal deficit of 7.7% of GDP, down from a projected 11.3% this year and 2.8% in 2019 (see Figure 7).

So far, the Prime Minister has had to rely on rolling over the 2018 budget of the previous PP government. Parliament's rejection of the minority coalition government's 2021 budget could trigger an election, the fifth in as many years.

Figure 7. Government's macroeconomic forecasts (%)

	2019	2020	2021
GDP growth	2.0	-11.2	7.2
Unemployment	14.1	17.1	16.9
Fiscal deficit (% of GDP)	2.8	11.3	7.7

Source: Finance Ministry.

The IMF believes the deficit this year will be much higher at 14.1% and the economy will shrink by 12.8%, more than any other developed country (see Figure 8).

Figure 8. IMF's GDP forecasts for 2020 and 2021 (annual change in %)

	2020	2021
France	-9.8	+6.0
Germany	-6.0	+4.2
Italy	-10.6	+5.2
Spain	-12.8	+7.2
Euro zone	-8.3	+5.2
UK	-9.8	+5.9
US	-4.3	+3.1

Source: IMF.

The economy, with high unemployment (14%) and public debt (95% of GDP) before the pandemic, will be slow to recover because of:

- The severity of the pandemic and the restrictive measures taken to contain it, which have been far from successful so far.
- The weight of the tourism and hospitality sectors (26% of GDP –five points more than the EU average–), which have been decimated. The number of tourists in August, the high point of the year, was 76% lower year-on-year at 2.4 million.
- The small average size of companies (37% of GDP), which are particularly vulnerable.
- The high proportion of temporary contracts (27% of total jobs).

- Reduced opportunities for teleworking (68% of workers unable to do this during the lockdown).

The registered unemployment rate at the end of September was more than 16% (3.7 million people, 530,438 higher than February at the start of the pandemic, and double the OECD average). But for furloughed workers, the jobless rate would be much higher. The government and trade unions agreed to extend the job retention scheme (ERTEs) until the end of January. Youth unemployment is at a whopping 44% (see Figure 9).

Figure 9. Youth unemployment (% of workforce under 25)

	%
Spain	43.9
Greece	39.3
Italy	32.1
Sweden	28.4
Portugal	26.3
France	19.8
Euro zone	18.1
UK	12.9

Source: OECD.

The Ibex-35, the benchmark index of the Madrid stock market, is showing no signs of recovery, while other markets are doing so gradually (see Figure 10).

Figure 10. World stock markets, % change, 1 January-19 October

	%
Ibex-35	-28.16
Euro Stoxx 50	-13.61
FTSE 100	-21.98
DAX	-2.98
Dow Jones	-1.20
Nikkei	+0.06

Source: Stockmarkets.

Anti-tax fraud bill bans tax amnesties

The government's bill to combat tax fraud, a serious problem, will limit the amount of cash that can be used in transactions and prohibit tax amnesties. The Finance Ministry believes the measures will bring in a much-needed extra €828 million a year.

Cash payments between companies and professionals are reduced to €1,000 from €2,500. Transactions by persons whose tax domicile is not in Spain are reduced from €15,000 to €10,000. The name and shame policy is tightened: anyone owing the Tax Agency more than €600,000 will appear in an annual public list, down from a previous €1 million.

Spain has had several tax amnesties in the last 40 years and their effectiveness has been questioned. They have also angered the great majority of people who pay their taxes.

The fight against tax fraud last year netted €15.7 billion, 4.1% more than in 2018.

Spain's tax burden at 35.4% of GDP is much lower than the EU average, although marginal personal tax rates are similar to the bloc's average (see Figure 11). The problem lies with the effective rates for individuals and companies because of tax benefits, exemptions, deductions, rebates and loopholes, as well as fraud and evasion.

Figure 11. Tax-to-GDP ratio, 2002, 2007 and 2018 (1)

	2002	2007	2018
France	44.1	44.5	48.4
Italy	39.7	41.5	42.0
Germany	39.6	39.3	41.5
EU	38.6	39.2	40.3
Portugal	33.9	35.0	37.2
Spain	34.1	37.3	35.4
UK	33.2	35.0	35.1
Ireland	29.1	32.1	23.0

(1) The sum of taxes and net social security contributions as a percentage of GDP.

Source: Eurostat.

Former IMF chief Rodrigo Rato cleared in Bankia fraud trial

Rodrigo Rato, a former head of the IMF (2004-07) was acquitted in a fraud trial over the listing of Bankia, when he was its chairman. The prosecution had sought an eight-and-half years jail sentence.

Rato, who was the economic supremo in the mainstream conservative Popular Party government (1996-2004), was one of 33 people and entities cleared over Bankia's ill-fated listing in 2011. The bank, the product of seven ailing savings banks, was bailed out and nationalised at a cost of €24 billion after Rato resigned in May 2012. It is currently in the process of merging with CaixaBank.

More than 300,000 retail shareholders lost their investments in Bankia. In separate civil proceedings, Bankia has paid out some €1.9 billion in compensation related to losses from the initial public offering (IPO).

The court said the financial information in the IPO prospectus, backed by all the main supervisory groups, was 'more than sufficient' for investors to form a reasoned opinion on the listing.

Bankia's new management restated a 2011 profit of just over €300 million with a €3 billion loss. Rato said the accounting changes reflected writedowns against future losses and not losses while he was chairman.

The acquittal raised howls of protest from consumer associations and questions about the reliability and transparency of supervisory bodies. Financial experts said the prospectus should have warned that Bankia was a high-risk investment.

The High Court granted the 71-year-old Rato a semi-release from his four-and-half-year jail sentence for embezzlement over the misuse of Bankia credit cards following his acquittal in the fraud trial. He is allowed to leave prison during the day.

He faces another legal case for tax fraud.

Corporate scene

OHL wins €58 million US motorway contract

The construction group OHL is to modernise the Tri-State motorway in the US state of Illinois after winning a €58 million contract.