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Summary

Madrid and London strike tentative free movement deal over Gibraltar.
COVID-19 incidence rate more than trebles to 689 cases per 100,000 people.
Parliament approves law allowing euthanasia and assisted suicide.
Pandemic suspends Catalan election amid declining support for independence.
Government holds to its recovery forecast, despite third pandemic wave impact.

Foreign Policy

Madrid and London strike free movement deal over Gibraltar

The British and Spanish governments reached an agreement in principle on free movement between Spain and the disputed British Overseas Territory of Gibraltar, less than a day before the deadline expired on 31 December, narrowly avoiding the creation of the only hard border because of Brexit.

Without the agreement Gibraltar, ceded to the UK under the 1713 Treaty of Utrecht and claimed by Spain, would have become the external border of the EU, complicating life for the 15,000 people who cross it every day to work in the territory. More than 95% of Gibraltarians voted to remain in the EU in the 2016 Brexit referendum.

Unemployment in the Campo de Gibraltar frontier area is more than 30% (80% in some parts) compared with almost zero in Gibraltar. Mayors of the eight towns in the area said the lack of a deal would bring 'dire economic, social and political consequences'.

Gibraltar is not covered by the Brexit trade deal between the EU and the UK. The agreement between London and Madrid paves the way for a separate treaty between the UK and the EU seeking 'maximised unrestricted mobility'. This would make Gibraltar part of the passport-free Schengen zone and convert Gibraltar's airport and port into the EU frontier, not the land border between Spain and the Rock.¹

The issue of who controls passage through the airport and port is a sensitive one because of the sovereignty issue. Neither side has changed its position on sovereignty.

¹ My analysis of the consequences of Brexit for Spain includes Gibraltar along with the trade, investment and tourism effects. See http://www.realinstitutoelcano.org/wps/portal/rielcano_en/contenido?WCM_GLOBAL_CONTEXT=/elcano/elcano_in/zonas_in/ari1-2021-chislett-the-consequences-of+brexit-for-spain.

Spain, as Gibraltar's closest Schengen member state, will be responsible for ensuring Schengen checks are applied. The Schengen Information System will provide information remotely to Gibraltar's border agents.

Chief Minister Fabian Picardo said Gibraltar would not accept during the agreement's four-year initial period agents of Frontex, the EU border and Coastguard Agency, wearing a Spanish armband. He says Gibraltar guards will have the final word on who enters.

After that period Spain and the UK will consult on how they should move forward. If another system acceptable to all sides cannot be agreed, the UK and Gibraltar have a veto on Spanish officials carrying out the checks and could terminate the agreement, raising the prospect of a hard border.

Removal of the border fence, possibly within six months, would integrate the Rock and the La Línea-Algeciras-Gibraltar triangle and enable Gibraltarians to move across the passport-free Schengen zone. The UK never signed the Schengen agreement. Madrid would like more of Gibraltar's wealth to flow into one of Spain's most deprived areas.

Former Popular Party Spanish Foreign Minister and current MEP Juan Manuel García-Margallo, who has been advocating co-sovereignty for Gibraltar for years, said the government has failed to seize the opportunity that Brexit had offered.

Prime Minister Pedro Sánchez decided to take a pragmatic approach. Juan González-Barba Pera, Spain's Secretary of State for Europe, said the agreement was one of 'co-responsibility' not co-sovereignty, an idea rejected by Gibraltarians in a referendum in 2002.

In a separate move, the government allowed Gibraltarians to continue to hold Spanish public sector jobs, work in professions that require EU residency and study in Spanish universities.

Domestic Scene

COVID-19 incidence rate more than trebles to 689 cases per 100,000 people

Like other countries, Spain is paying a high and predictable price for relaxing its COVID-19 restrictions during the Christmas and New Year period and lax adherence to the rules. The third wave of infections, also aggravated by the highly contagious coronavirus variant first found in the UK, is putting some hospitals at breaking point and producing cancellations of routine treatment and non-urgent operations. Hospitals have also been hit by the Filomena snowstorm and sub-freezing temperatures that have caused accidents and put even more pressure on the public health system.

As a result of the sharp rise over the last month in the number of cases to 2.33 million on 18 January (the world's ninth largest), the 14-day notification rate per 100,000 inhabitants for Spain as a whole more than tripled to 689. The number of cases at the

end of the first state of emergency on 21 June stood at 246,272 and at 1,098,320 when the second and six-month state was declared on 26 October.

The official death toll from the pandemic was 53,769 and including 'excess deaths' since March –the difference between the observed numbers of deaths in a specific time period and expected numbers of deaths in the same period– more than 80,600. This is 24% above the average number of deaths in 2015-2019, the highest rise among countries providing excess death figures.

The third wave is worse than the second. The 14-day incidence rate is above 1,000 in three of the 17 regions and more than 600 in nine (see Figure 1). Extremadura's rate, the worst, rose tenfold to 1,384.

The Socialist-led minority government, however, does not see the need to follow the example of other hard-hit countries, such as the UK, and impose a full stay-at-home lockdown, as happened last March in the first wave. Some regional governments are pushing for this, but they do not have the legal means to do so. In a baffling move, the decision of the government of Castilla León, governed by the Popular Party (PP), to bring forward the curfew in the region from 10pm to 8pm was challenged by the central government, which took the issue to the Supreme Court on the grounds that this curtailed a fundamental right not supported by the second state of emergency. Galicia, Catalonia, La Rioja, Murcia, Navarra, the Balearic Islands, Castile-La Mancha and Extremadura also tightened their restrictions.

Figure 1. Coronavirus (COVID-19) cases per 100,000 people in past 14 days by regions, 2020 and 2021

	16 December 2020	18 January 2021
Andalucía	136	628
Aragón	219	615
Asturias	209	318
Balearic Islands	307	680
Basque Country	267	350
Canary Islands	124	175
Cantabria	217	352
Castilla y León	180	911
Castilla-La Mancha	244	1007
Catalonia	215	631
Extremadura	141	1384
Galicia	170	484
Madrid	248	790
Murcia	142	1082
Navarre	197	386
La Rioja	201	921
Valencia	239	896
Spain (2)	201	689

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

Source: Health Ministry.

Meanwhile, the roll out of the COVID-19 vaccine is picking up after a slow start (see Figure 2).

Figure 2. COVID-19 vaccination doses administered per 100 people, 18 January (1)

	Doses per 100 people
UK	6.65
US	3.71
Italy	1.91
Spain	1.92
Germany	1.37
France	0.74

(1) Total number of vaccination doses administered per 100 people in the total population. This is counted as a single dose, and may not equal the total number of people vaccinated, depending on the specific dose regime (eg, people receive multiple doses).

Source: <https://ourworldindata.org/covid-vaccinations?country=ESP~FRA~DEU~ITA~GBR~USA>.

Parliament approves law allowing euthanasia and assisted suicide

Spain became the sixth country in the world to approve physician-assisted suicide and euthanasia for long-suffering patients of incurable diseases in a 198-138 vote.

Belgium, Canada, Colombia, Luxembourg, the Netherlands and Switzerland have already approved some form of legislation. In the US, some states including California allow patients to obtain lethal prescriptions if terminally ill.

The issue in Roman Catholic Spain is a heated one. The law was opposed by the conservative Popular Party and the hard-right VOX. The Church issued a statement headlined 'Life is a gift, euthanasia a failure'.

María Luisa Carcedo, a former Socialist Health Minister and MP, said the law allowed Spain to take 'a step forward in civil rights, which will bring more liberty to citizens'. Far from being 'an imposition by the state', she added, the law meant that 'it is the patient who decides'.

The law sets various conditions including ensuring patients have been granted all information about their condition and specifies that the request to die must be made in writing and be repeated 15 days later.

Pandemic suspends Catalan election amid declining support for independence

Catalans were due to go to the polls on 14 February amid waning support for independence, but the election have been suspended because of the surge in COVID-19 cases.

The regional election follows the Supreme Court's ruling last September barring Quim Torra, the former Premier of Catalonia, from public office for 18 months for disobedience

for failing to remove banners from a public building during an election campaign calling for the release of nine jailed pro-independence leaders. Deputy Premier Pere Aragonès took Torras’s place.

The election was supposed to be held by 14 February and not by next December, when the Catalan government’s four-year term would normally expire, but the pandemic has changed this. May 30 is the earliest date agreed by some of the political parties, although the final word might lie with the courts as the Catalan Socialists and some organisations are expected to appeal against the Catalan government’s decree.

The 2017 election was called by the previous Popular Party government of Mariano Rajoy after it dissolved the Catalan parliament, following the illegal referendum on secession and parliament’s unilateral declaration of independence. Nine politicians and activists were jailed for between nine and 13 years in October 2019 after they were found guilty of sedition.

A GAD3 survey this month showed support for a break with Spain had dropped from 45% last September to below 43% (see Figure 3) and 62.7% of respondents said the push for independence (known as the *procés*) was harming the economy.

Figure 3. Opinion poll on Catalan independence (% of respondents)

	Yes	No	Don’t know
Do you believe the dialogue between the central and Catalan governments will help to find a solution to the Catalan conflict	48.9	46.2	4.9
Should the central government pardon the Catalan politicians jailed for organising an illegal referendum in 2017?	60.6	32.6	6.8
In a referendum would you vote in favour of independence?	42.6	48.9	8.5

Source: GAD3, January 2021.

The Socialist-led minority government, in which the hard left Unidas Podemos (UP) is the junior partner, agreed to negotiate with the pro-independence Catalan Republican Left (ERC) in return for it supporting the government’s formation in January 2020. ERC has 13 seats in the national parliament and are vital to keep the government in power.

Since then, however, negotiations have not advanced the cause of independence, though the rhetoric on both sides is less aggressive. Both sides are sticking to their red lines: the government opposes a referendum (not so UP) and ERC wants one.

A higher share of respondents (27.5%) than in September (26%) are in favour of a reform of Catalonia’s financing system as a way to end the conflict (see Figure 4).

Figure 4. In the event of a bilateral negotiation, how would you like the conflict to be resolved

	January 2021	September 2020
A better financing system	27.5	26.0
A referendum on independence	26.8	26.1
A reform of the Spanish Constitution	24.0	28.8
A new Catalan statute	10.8	10.5
Don't know	10.9	8.6

Source: GAD3, January 2021.

The decision of the Catalan Salvador Illa, the Health Minister in the central government, to head the Catalan Socialist Party's list in the election appears to have substantially boosted that party's fortunes over the last month. According to an opinion poll by GESOP published in *El Periódico*, the socialists would double their seats in the Catalan parliament to 34 of the 135 on 24.1% of the votes, up from 16.8% in 2017, if the election was held next month, while ERC, the secessionist Junts and the Popular Unity Candidacy (CUP) between them would win 68 seats, very narrowly enabling them to maintain control of parliament (see Figure 5).

Figure 5. Catalan elections, seats by party, February 2021

	February 2021	2017 results
Catalan Socialist Party	34-35	17
Catalan Republican Left	32-33	32
Junts	29-30	34
Ciudadanos	12-13	36
Popular Unity Candidacy	7-8	4
Catalunya en Comú-Podem	6-7	8
Popular Party	6-7	4
VOX	5-6	-

Source: GESOP for February and Catalan government for 2017.

The biggest loser will be the liberal Ciudadanos, which will see its seats drop from 36 in 2017, the largest number, to 12-13. Their voters are mainly deserting them for the Socialists.

Meanwhile, a Belgian court denied a request by Spain's Supreme Court to extradite Lluís Puig, a former Culture Minister in the Catalan government who fled to Belgium in 2017 after the referendum. This makes it unlikely that Carles Puigdemont, the Catalan Premier at the time of the referendum, will be extradited.

The government is studying whether to grant pardons to the nine prisoners. Transport Minister José Luis Abalos said the government 'has the legal obligation to process the pardons' and the 'moral obligation to relieve tensions that can damage co-existence'. The Popular Party and Ciudadanos called the government's decision a 'shameful and lamentable favour' in return for ERC's backing of the 2021 budget.

Deputy Prime Minister Pablo Iglesias, leader of Unidas Podemos, added fuel to the debate on pardons when he compared the situation of Puigdemont to that of Republican exiles during the Franco regime. This triggered a flood of criticism, and particularly enraged exiles' descendants who said it was an insult.

Spain, main destination for irregular migration to EU

More than 41,000 migrants crossed by sea from Africa into Spain last year (32,500 in 2019), compared with 34,113 into Italy and 15,518 into Greece. Almost half of them arrived in the Canary Islands (22,249), 10 times more than in 2019 (see Figure 6).

Figure 6. Irregular migrant arrivals in the Canary Islands, 2001-20

2001	2004	2006	2008	2012	2016	2019	2020 (1)
4,105	8,426	31,678	9,181	173	672	2,168	22,249

(1) Until 27 December.

Source: ACNUR and Interior Ministry.

Spain also received the largest number of people seeking asylum in the EU. Eighty per cent of the 88,762 seekers were from Latin America, mostly Venezuelans and Colombians.

The Economy

Government holds to its recovery forecast, despite third pandemic wave impact

The government is sticking optimistically to its GDP growth forecast for this year of around 7%, despite the virulent third wave of COVID-19 infections. The measures to tackle the pandemic caused the economy to shrink by around 11% in 2020, the bleakest year in living memory. BBVA estimates growth at 5.5% in 2021.

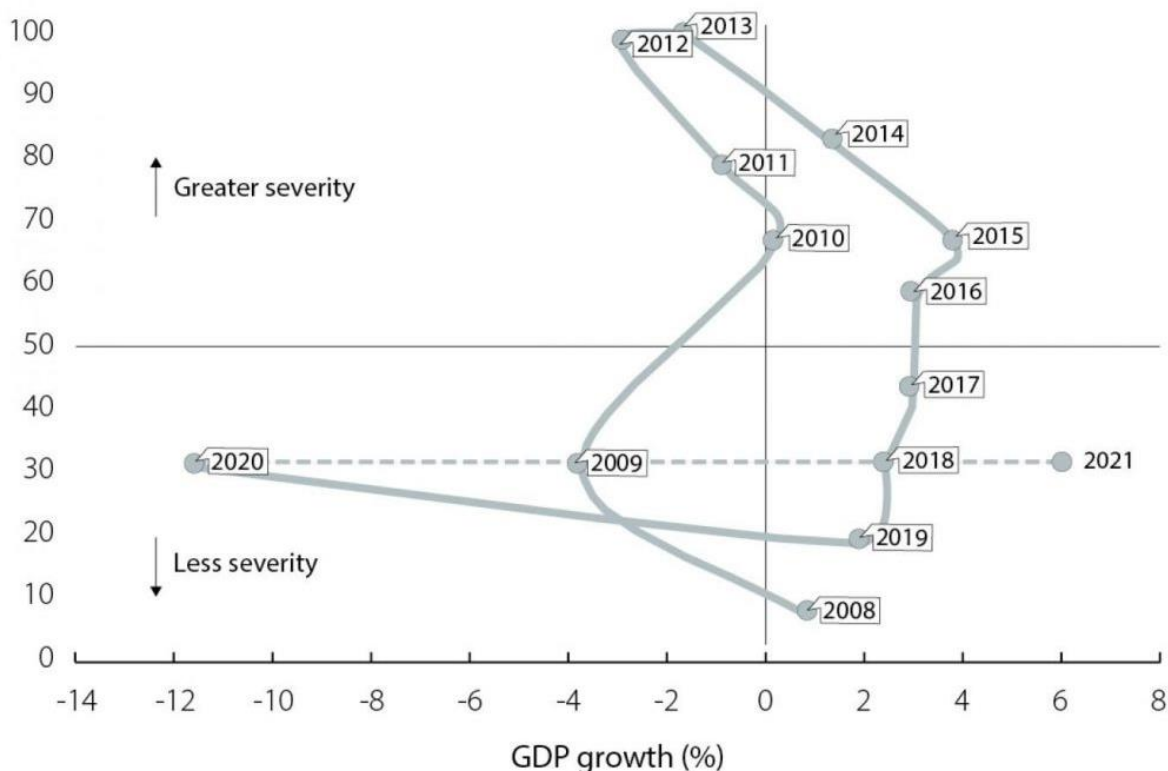
The pandemic's impact on the economy, compounded this month by the Filomena snowstorm, is unprecedented. Whereas at the height of the 1993 and 2008 crises GDP fell to 2.5% and 9% below the pre-crisis level, respectively, during the COVID-19 crisis GDP reached 22% below the pre-crisis level at one point.

Yet the speed of recovery is proving to be quicker than in previous crises, because this crisis originated from a health emergency and monetary and fiscal policy has played a key role in alleviating the pandemic impact. For example, at the end of 2020, 755,613 workers were still furloughed under the job retention scheme which looks like being extended until the end of May.

Other government measures taken were debt moratoriums and tax deferrals, as well as the decisive action of the European Central Bank. The economy recovered 60% of output in the third quarter of 2020, compared to the nine quarters it took during the 2008 financial crisis.

The deep recession has been accompanied by a much smaller deterioration in the severity index than might have been expected. Figure 7 shows the relationship between a synthetic index of the severity of the economic conditions (built using the unemployment rate and the sovereign risk premium) and annual GDP growth.

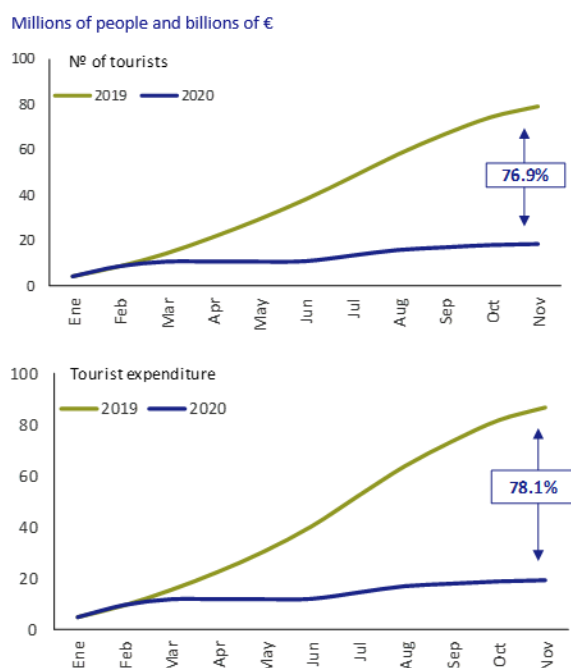
Figure 7. Economic conditions index and GDP growth: synthetic index of the severity of economic conditions



Source: CaixaBank Research, based on data from the National Statistics Institute and Bloomberg.

A key factor this year will be the extent to which the vital tourism sector recovers. Last year was *annus horribilis*: the number of international tourists plummeted from 83.7 million in 2019 to below 20 million, the lowest figure since the late 1960s and generating just 4% of GDP compared to the usual 12% (see Figure 8). The tourism and hospitality sectors account for 26% of GDP, five points more than the EU average. Tourism by Spaniards was also decimated.

Figure 8. Spain: number of tourists and tourist expenditure, 2019 & 2020 (January-November)



Source: Círculo de Empresarios based on INE, 2020.

The economy will receive a much-needed boost from a massive injection of Next Generation EU funds (NGEU). Parliament’s approval of the 2021 budget unlocked the €140 billion Spain expects to receive from the EU’s €750 billion coronavirus recovery fund, €26.6 billion of which Spain will borrow against the prospective grants from the bloc. The €140 billion in grants and loans is more than the total 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.

The Ibex-35 index of the Madrid stock exchange has picked up after falling 15.5% in 2020, one of the worst performances in the world (see Figure 9). By 18 January the index had risen 2.24%

Figure 9. The world's worst performing stock markets in 2020

	% annual change
Mauritius SE	-24,3
JSE market (Jamaica)	-22.8
EGX 30 (Egypt)	-22.3
Sofix (Bulgaria)	-21.2
Laos Composite Index	-17.8
BLOM (Beirut)	-16.3
Ibex 35	-15.5
FTSE 100 (London)	-14.3

Source: Bloomberg.

Corporate Scene

Unicaja and Liberbank to merge and create fifth largest bank

In the second bank merger in less than six months, Unicaja and Liberbank are to join forces and form Spain's fifth largest bank with assets of more than €100 billion.

Their merger follows that between CaixaBank and Bankia last year which created the country's biggest bank with assets of €665 billion. Another merger, between BBVA and Sabadell, was called off last year.

Both Unicaja and Liberbank were formed from ailing savings banks in 2014 and 2011, respectively.