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Foreign Policy

Spain signals it will lift job curbs on migrant workers from new EU members

Spain is expected to lift its job curbs on migrant workers from the 10 new EU countries as of 1 May when the transitional arrangements come up for renewal. When these countries, mostly from central Europe, joined in 2004 12 of the 15 existing EU members imposed restrictions on labour. So far only Britain, Ireland and Sweden have fully opened their labour markets (see Figure 1).

Figure 1. Stance on labour restrictions

Country	
Austria	Five more years
Belgium	Mulling liberalisation
Denmark	Mulling liberalisation
Finland	Will scrap curbs
France	Modest liberalisation, at most
Germany	Five more years
Greece	Likely to liberalise
Italy	Unclear
Luxembourg	Mulling liberalisation
Netherlands	Mulling liberalisation
Portugal	Will scrap curbs
Spain	**Likely to liberalise**

Source: The Economist.

The European Commission has expressed concern that the restrictions have created a system of second-class European citizens. Freedom of movement is supposedly a fundamental right of all EU citizens.

Spain is the largest recipient of migrant workers in the EU, most of them, however, from Latin America and North Africa. Last year it received roughly one-third of the total of 1.9 million people who arrived in the EU. Close to 700,000 illegal immigrants, who were able to provide some form of employment contract and prove they had lived in Spain for six months, were granted an amnesty in 2005. Spain's foreign-born population has been growing inexorably and is now close to 9% of the population which at 1 January 2005 (the last official figure) stood at 44.1 million. This is more than double the level it was in 2001.

The huge influx of immigrants into Spain over the last 10 years has so far been very positive for the economy, particularly the construction and agricultural sectors, and is one of the drivers behind the country's sustained growth at a much faster pace than the EU average. It has also helped to produce a record surplus in the social security accounts as migrant workers move from the black to the recorded economy.

Spain to await outcome of new constitution for Gibraltar before striking any deals
Spain wants to see the new Gibraltar constitution, which is being drawn up, before reaching any agreements over contentious issues. As a result of this and technical matters still to be cleared up, the latest round of talks between Spain, the UK and Gibraltar failed to strike any deals over joint use of Gibraltar's airport and the pension claims of former Spanish residents of the Rock.

The talks were held under the trilateral process announced in 2004 under which Spain agreed to discuss vexed issues in a more co-operative spirit and give Gibraltar, for the first time, a seat at the negotiating table (a formula known as 'two flags, three voices'). Madrid has not dropped its sovereignty claim –Gibraltar has been a British territory since the 1713 Treaty of Utrecht– but it is not actively pursuing it.

Gibraltar's constitution is being modernised. Madrid is hoping there will be no surprises, such as a direct or indirect reference to the right to self-determination, which would make it politically impossible for it to continue its current line.

Nevertheless, some progress was reportedly made.

Foreign Minister seeks Vatican's support for dialogue between the West and Islam
Miguel Ángel Moratinos, Spain's Foreign Minister, and Cardinal Ángel Sodano, the Vatican Secretary of State, held their first working meeting since Benedict XVI became Pope. Both sides were keen to play down considerable differences between the two sides over issues such as the Socialists' legalisation of same-sex marriage and changes to religious education (see *Inside Spain*, Newsletter 19, 2 December 2005). Moratinos called the meeting 'positive and cordial'.

The Vatican said Moratinos had sought support for the Spanish-government initiative called 'An Alliance of Civilizations between the Western World and the Arab-Islamic World' which is co-sponsored by Turkey. It did not elaborate.

Pope Benedict XVI has often expressed the need for dialogue and reconciliation among peoples.

Government pledges more development aid for Vietnam
Vietnam will receive up to €55 million of official development aid from Spain over the next four years.

Juan Pablo de Laiglesia, Secretary General of the Spanish Agency for International Co-operation (AECI), said during a visit to the country that Vietnam is a priority in its development aid policy for 2006-09. King Juan Carlos visited the country afterwards.

The Vietnamese economy is one of the fastest growing in Asia and is seeking greater foreign investment.

Domestic Scene

Speculation intensifies over end to violence by Eta
The government's belief of a breakthrough in ending terrorism by the Basque separatist

group Eta was at odds with a much-heralded statement by the group which called for negotiations but failed to declare a ceasefire or even mention giving up violence.

José Luis Rodríguez Zapatero, the Prime Minister, who went out on a limb by earlier suggesting that Basque terrorism was 'at the beginning of the end', dismissed the call unless Eta first laid down its arms and renounced violence.

The optimistic atmosphere was also fanned by Juan José Ibarretxe, the Premier of the Basque country, who said 'we must be ready for good things'. Spanish newspapers also made much of the fact that between 30 May 2003 and 23 February 2006 –1,000 days– Eta had not killed anyone. The group, however, placed several bombs during February.

Eta has been weakened considerably by the wave of arrests and the discovery of arms. A total of 416 people have been arrested in Spain and France since 2003.

The centre-right Popular Party accuses the Socialists of sidelining the victims of Eta's violence in its search for a peaceful solution to a problem that has dogged Spain since 1968 and left 817 people dead. The issue has become very politically charged. Tens of thousands of people, including relatives of those killed and injured in Eta bomb attacks, marched through Madrid and urged the government not to negotiate a peace deal. PP leaders took part including José María Aznar, the former PP Prime Minister, and Mariano Rajoy, who succeeded him at the head of the PP and lost the 2004 election to Zapatero.

Spain's corruption 'largely in the construction sector'
The classification of land for building purposes, particularly on the outskirts of cities and in coastal areas, is the main source of corruption in Spain, according to Transparency International (TI), the NGO, in its 2006 Global Corruption Report (*www.transparency.org/publications/gcr/download_gcr#download*). Unless the financing system for town halls changes, the construction sector would be a 'permanent focus of corruption'.

Town halls receive substantial income from agreements with property developers which leave plenty of room for 'negotiation'. Property taxes in Spain, which along with funds from the central government are the main sources of financing for local governments in most other European countries, are generally much lower in Spain, although they have risen. TI's report said there was little supervision of illegal construction or planning alterations, and sanctions almost never lead to demolition.

The construction sector accounts for a very high 17% of GDP (the residential sector for 8%), double the EU average, and is the driving force of the economy. This is more than in Germany right after unification.

Corruption and the 'rape' of the Spanish coasts by property developers are two issues that feature in the lively and learned book, *The Ghosts of Spain,* by Giles Tremlett, the Madrid correspondent of *The Guardian* and *The Economist* which will be published later this month in the UK. This is an affectionate warts-and-all portrait of a country which has changed more than any other European nation in the last 30 years.

The Economy

Tremlett's book naturally includes a lot about the eight years of the centre-right Popular Party government between 1996 and 2004. This period, a golden one for the Spanish economy, which began before the PP took power and continues, is also seen through a series of 500 indicators (economic, demographic, labour market, social policies, the environment, etc) produced by FAES, the PP's think tank (see *www.fundacionfaes.es/documentos/indicadores_web.pdf*). Combining the two books gives a very full picture of Spain's transformation and progress. For example, average per capita income rose from €13,300 to €21,800 in purchasing power parity terms (from 78.9% of the EU-15 to 89.7%); the general government accounts went from a deficit of 6.6% of GDP to balanced books and the unemployment rate was halved to 11.5%. As Aznar points out in his introduction, 'governments do not create wealth or employment, but their policies can foster this'. But it was not all roses. For example, the number of civil servants working for the central government was cut by 61% to 235,256, but those employed by regional governments rose 82% to 1.15 million, signifying the creation of more, not less bureaucracy.

German bid throws planned energy merger into disarray
The government's hopes of creating an integrated gas and electricity group and a national champion through Gas Natural's take-over of Endesa were knocked sideways by the rival offer for Endesa by Germany's E.on (see *Inside Spain*, Newsletter 21, 7 February 2006).

Just as it looked as if Gas Natural's hostile €21 billion bid for Endesa, Spain's largest electricity company, had cleared all the hurdles after five months, and that shareholders would have the last word, E.on took the market by surprise with a €29.1 billion all-cash offer. The bid would create the world's leading power and gas company.

The government initially responded by saying it would do 'everything in our power to ensure Spain's energy companies remain Spanish' and then softened its approach after the European Commission warned Madrid not to use illegal protectionist means to try to block E.on's take-over bid. Madrid retains a 'golden share' in Endesa (formerly state-owned), which could block the deal, though José Luis Rodríguez Zapatero, Spain's Prime Minister, said the government would only use it in exceptional circumstances.

The 'golden share' allows the government to veto any sale of more than 10%. Last November, Spain agreed to scrap its 'golden shares' in Endesa, Telefónica, the telecoms group, Repsol, the oil and gas group, and Iberia airlines, under pressure from the European Commission.

Enel of Italy offered itself as a 'white knight' to help Gas Natural fend off E.on with a joint bid for Endesa, but the offer was rejected.

Zapatero wants domestic consolidation in the energy sector before allowing in foreign companies. In what was seen as an attempt to block E.on's bid for Endesa, the government said it would use decree powers to widen the jurisdiction of the national energy commission (CNE) to include foreign companies. This could enable the government to intervene in the deal or even block it.

Another option would be to invoke a controversial 1999 law to curb foreign investment in Spanish energy groups, although the European Commission has repeatedly found that the legislation broke European law. Brussels was reportedly preparing a legal challenge at the European Court of Justice, the EU's highest court, to force Spain to scrap this law.

Meanwhile, Gas Natural was preparing to improve its offer for Endesa and might launch it with another Spanish company.

Ferrovial mulls take-over of UK's airport operator
What began as a flotilla of Spanish companies buying up UK firms looks like becoming an armada. Ferrovial, one of Spain's biggest construction and services groups, is considering making a bid for BAA, the airport operator. If it does, it would join other Spanish big guns in the UK –Santander, which owns Abbey, and Telefónica, which recently acquired the mobile phone operator O2–.

Ferrovial is no stranger to the UK: it operates Bristol airport with Macquarie, is the sole operator of Belfast airport and in 2003 bought Amey, the facilities management group that runs and maintains three of London's underground rail lines. In February of this year it acquired Owen Williams, a UK support services company.

Ferrovial has also broken into the US market. Cintra, its toll road subsidiary, has a 99-year concession to operate the Chicago Skyway and this year was awarded, in partnership with Macquarie, a 75-year concession on the Indiana Toll Road. Cintra is also developing, with the state of Texas, a new cross-state corridor. Last September Ferrovial bought the Webber Group, a Texas-based construction company.

The company also has toll road concessions in Chile, Italy, Ireland, Spain and Portugal and last year it acquired Swissport, one of the world's largest independent airport services companies.

Ferrovial is also among the world's biggest private car park operators.

General Motors picks Spain over Poland for new van
German car manufacturer Adam Opel, which is part of US car group General Motors (GM), is to build the next generation of its Meriva compact van in Spain and not in Poland.

Carl-Peter Forster, head of GM Europe, said the Zaragoza site had been chosen over Gleiwitz, despite its higher labour costs, because of the large investment required to expand the Polish plant. A relocation would have put 2,000 jobs at risk in Spain.

The victory was particularly important because some auto component firms in Spain have been moving out of the country and relocating in ones with lower labour costs. Spain's motor industry, a major exporter and entirely in the hands of multinationals. generates 6% of GDP.

There was also other good news. Nissan decided to produce light trucks at its plant in Ávila and Renault reached an agreement with trade unions to produce the new Clio model in Valladolid.

Acciona to build world's largest solar energy plant in 15 years
Acciona, the Spanish construction and services group, is to invest €220 million in the construction of a solar electricity plant in the US state of Nevada. No solar energy plant this size has been set up anywhere in the world during the last 15 years.

The Spanish group obtained the contract as a result of acquiring 55% of Solargenix Energy, the promoter of the construction of the solar plant. Acciona already operates two wind farms in the US.

Zara opens its first outlet in China
Inditex, the Spanish fashion retail giant, opened the first Chinese outlet of its Zara chain in Shanghai. Inditex is very strong in Europe and is seeking to improve its market position in Asia, where it currently operates 35 Zara outlets in countries such as Japan, Thailand, Malaysia, Indonesia and the Philippines.

Telefónica suspends US$2.8bn claim against Argentina
Telefónica Argentina, the subsidiary of Spain's telecoms giant, suspended a claim worth US$2.8 billion against Argentina in a World Bank tribunal. Its claim was one of many filed by foreign companies after Argentina's meltdown in 2002 which produced a massive devaluation of its currency and price freezes in utility companies, many of them foreign-owned.

Nestor Kirchner, Argentina's President, made the suspension of these claims a prerequisite for the renegotiation of new contracts which have progressed very slowly since he was elected in 2003.

Telefónica's move was described as a 'turning point' by the Argentine government. Telefónica said it would not raise its prices in 2006. Uitlity companies were hard hit by the freezing of their tariffs. France's Suez is attempting to withdraw from Argentina.

In a separate move, the European Union's top competition regulator issued formal antitrust charges against Telefónica, alleging that the group had abused its dominant position in the fast-growing market for broadband services. The wholesale prices that Telefónica is demanding from rival operators are so close to retail prices for consumers that other companies are in effect excluded from competition, according to the regulator.

Economy grew 3.4% in 2005, but current account deficit highest in developed world
Spain's GDP grew 3.4% in 2005, the highest rate since 2001 and two points higher than the average for the 12 Euro-zone countries of 1.3% (see Figure 2). But the current account deficit reached €60.7 billion in the first 11 months and at 7.3% of GDP was the highest in the developed world.

Figure 2. Spain and the Euro zone, real GDP growth

	2000	2001	2002	2003	2004	2005
Spain	**5.0**	**3.5**	**2.7**	**3.0**	**3.1**	**3.4**
Euro zone	3.8	1.9	0.9	0.7	2.1	1.3

Source: Eurostat.

Buoyant private consumption, construction and investment in capital goods offset the external sector's negative contribution.

The current account deficit stemmed from the huge trade deficit resulting from the soaring cost of the energy import bill (+40%). The trade deficit reached a record €63 billion in the first 11 months. Exports were up 4.4% and imports 11.4%. But for the massive surplus on tourism (€24 billion), the current account deficit would have been even higher. Tourism revenues were €1 billion lower than a year earlier.

In the past Spain could correct the deficit by devaluing its currency. But it cannot do this now as it is part of the euro. The European Commission forecast last autumn that Spain's current account deficit would be more than 8% this year and 9% in 2007. These levels cannot be sustained for ever.

The pace of inflation is also outstripping the Euro-zone average. It was 3.7% in 2005 compared with 2.2% in the Euro zone.

Another sign of the economy's overheating was the surge in total household debt in 2005 to €650.9 billion, 21.% higher than in 2004 and representing 72.6% of GDP. Close to three-quarters of this debt is mortgages whose holders are in a vulnerable position if interest rates rise sharply and Spain's housing bubble bursts. A major factor behind the growth in mortgages is that Spain's interest rates are negative (Euribor, the main reference for loans, is lower than Spain's inflation).

Tax burden rises significantly in first year of Socialist government
Spain's tax burden (tax receipts from all sources and social security contributions) rose 0.6 points in 2004, the Socialists first year in government, to 35.4% of GDP. Although Spain's tax burden is still well below the Euro-zone average (41.1% of GDP), the increase in 2004 was the largest in a decade (see Figure 3).

Figure 3. Euro-zone tax burdens (% of GDP)

Country	1995	2004
Austria	43.6	44.3
Belgium	45.9	47.4
Finland	46.2	44.5
France	44.5	45.3
Germany	41.3	40.0
Greece	34.7	37.7
Ireland	34.9	31.7
Italy	42.9	42.1
Luxembourg	43.7	41.1
Netherlands	40.5	38.8
Portugal	32.7	35.6
Spain	**33.6**	**35.4**
Euro-zone average	41.2	41.1

Source: Eurostat.

The rise, however, was due to greater economic activity and some success in combating tax fraud and not to higher tax rates. One of the largest rises was in social security contributions (from 12% to 12.2% of GDP), reflecting the incorporation of hundreds of thousands of immigrants to the labour force. The government plans to cut tax rates as of 2007 (see *Inside Spain*, Newsletter 20, 7 February, 2006).