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Foreign Policy

Spanish and Cuban Governments Re-open Political Dialogue After Four-Year Gap
Spain and Cuba reached an agreement outside of the EU's common policy and re-established full co-operation with the government of Fidel Castro. An institutional mechanism was also put in place to discuss all political issues including human rights, although Felipe Pérez Roque, the Cuban Foreign Minister, reiterated Havana's well-known position that those in prison were 'mercenaries paid by the US government' and not political prisoners.

The visit by Miguel Ángel Moratinos to Cuba was the first by a Spanish Foreign Minister since 1998 and the first by an EU Foreign Minister since 2003 when Brussels imposed diplomatic sanctions against the regime, following the summary execution by firing squad of three people who hijacked a ferry in an attempt to flee the country, and the round-up of 75 dissidents.

The agreement was denounced by Spain's conservative Popular Party (PP), the main opposition to the Socialists, and by dissidents inside Cuba. The former PP Prime Minister, José María Aznar, was a prime mover behind the EU's sanctions. It was also criticised by Thomas Shannon, the US Assistant Secretary of State for Western Hemisphere Affairs. Eastern European EU members (and former communist countries), particularly the Czech Republic, were especially unhappy about it.

While it seemed that Spain was going out on a limb, the agreement was not that surprising as Moratinos had long made it clear that the government wanted to end the diplomatic freeze and restore dialogue, which it views as more constructive than continuing to ostracise the Cuban regime. Moratinos began to move this ball in 2004. The agreement should also be seen in the context of Castro's age (80) and ailing health and Spain's long-standing links with Cuba, a former Spanish colony, which are by far the closest among EU countries. Madrid is clearly positioning itself to be the 'privileged interlocutor' in a post-Castro future and believes that in order to have any capacity of influence it has to have an active relationship with the government. 'The relationship with Cuba is an obligation for Spain and an option for other countries', Moratinos told *El País* in an interview.

Pérez-Roque's remarks at the press conference announcing the agreement did not augur well for improving the situation. While seven dissidents were released in April, one of whom had served a 17-year sentence, in what looked like a gesture for Madrid, two others were tried secretly and jailed, according to a Cuban human rights group. Lawyer Rolando Jiménez Posada, in detention since March 2003, was sentenced to 12 years for disrespecting authority and revealing secrets about state security police, and journalist Óscar Sánchez Madán received a four-year sentence for 'social dangerousness'.

Moratinos' decision not to meet dissidents drew fire from Castro's opponents. Miriam Leyva, the wife of Óscar Espinosa Chepe, one of the 75 dissidents arrested in 2003 and released since then for health reasons, accused him of 'betraying our prisoners'. Aznar –who is the only Spanish Prime Minister to have received Castro in the Moncloa palace (in 1998)– called the agreement a 'calamity'. His remarks should be seen in the context of the PP's strategy of confrontation with the Socialists. Javier Sandomingo, a senior Foreign Ministry official, stayed on a day in Havana and met the more moderate dissidents. Those in favour of a harder line demanded to see Moratinos or no other official, something that was regarded as unacceptable.

Spain is the leading direct investor in Cuba (between US\$2 billion and US\$3 billion), particularly in the tourism sector, and the country is the third-largest export market in Latin America (close to US\$800 million in 2006). As a result of the deal, Madrid will reopen its cultural centre in old Havana, a project put on hold since 2003, and is prepared to renegotiate Cuba's debt and reopen some official credit lines.

Former Portuguese President to Head Spain and Turkey's 'Alliance of Civilisations' Initiative

Jorge Sampaio, the former President of Portugal, was appointed High Representative for the Dialogue of Civilisations of the United Nations, created after the UN assumed in 2005 the 'Alliance of Civilisations' initiative launched by Spain and Turkey in 2004.

The Alliance, said Sampaio, aimed to be a counterpoint to the 'disseminated and fatalistic idea of a clash of civilizations'.

Domestic Scene

General Franco's Courts Martial Declared Illegitimate in Civil War Bill

More than 30 years after General Franco died, the dictator's courts martial, public order tribunals and other courts established to punish people for political reasons are to be declared illegitimate under a draft law, agreed by the ruling Socialists and the communist-led United Left coalition, which looks set to be approved later this year.

The agreement overturned a key element of the Law of Historical Memory, which passed the first stage of its controversial passage through parliament last December (see *Inside Spain*, Newsletter 31, 1 February 2007). At that time the government wanted a five-person committee elected by the parliament to oversee cases. The conservative Popular Party (PP), the only party to still reject the law, could block the committee's decisions as they would require a majority of three out of five. This committee has now been eliminated. The Socialists also refused to annul the verdicts and name those who administered the courts until Franco's death in 1975.

By declaring the courts contrary to law and illegitimate, the government has paved the way for all victims to have their sentences symbolically annulled. The government, however, is anxious to put in place safeguards that ensure there will not be a flood of requests for compensation. The Socialists have 164 seats and the United Left group five in the 350-seat lower house so the support of other parties will be needed for the bill, yet to be finalised, to become law.

The PP accused José Luis Rodríguez Zapatero, whose Republican paternal grandfather, an army captain, was shot by a Nationalist firing squad in 1936 for refusing to support Franco's uprising against the democratically-elected government, of 'definitively burying the transition to democracy'. 'Parliament has never before been used to look back at that tragic and dramatic moment of history, the civil war,' said Eduardo Zaplana, the PP's parliamentary spokesman.

The transition implicitly incorporated a *pacto de olvido* (agreement to forget, or overlook) which the left (the losers) believes has gone on far too long. While Argentina, Chile, Guatemala and South Africa have had truth commissions, Spain's politicians, until now, have preferred not to rake over the past and run the risk of inflaming the passions of the 'winners' and 'losers'. The focus has been more on restoring the rights of those who were deprived of them: for example, 574,000 cases of pensions and compensation have been resolved in the last 30 years at a cost of €16.3 billion from public funds.

The British historian Paul Preston, author of the definitive biographies of Franco and of King Juan Carlos, told the newspaper *ABC* that he felt 'very uncomfortable' about the Memory Law, although he could understand the reasons for it. The government had to be 'careful' in the current political atmosphere of permanent confrontation between the two main political parties which very generally speaking represent the 'winners' and 'losers'.

The agreement was reached on the eve of the 44th anniversary of the death by firing squad on 20 April 1963 of Julian Grimau, an exiled communist leader who returned to Spain clandestinely. The death sentence for his role during the civil war, not for his activities in Spain after it was over, provoked an international outcry. His family have unsuccessfully tried to have his case reassessed and could be among the first to benefit from the new law.

European Parliament Report Slams Coastal Developments

A European Parliament committee approved a hard-hitting report which criticised the rapid urban growth along Spain's Mediterranean coast and accused regional governments in the area of continuing to 'violate' the 'fundamental rights of European citizens to their legitimately acquired property'.

The Parliament's report, approved by the Petitions Committee, was drawn up after a visit to Spain by MEPs in response to over 15,000 complaints about coastal development. If the assembly approves the report, the European Commission will have to decide whether to carry out recommendations to act against the authorities, particularly in Valencia, and elsewhere. The conservative Popular Party (PP), which governs Valencia, rejected the report and said it was politically motivated.

Tens of thousands of homes have been built in the last few years in a property boom that has made speculators wealthy, brought a spate of corruption cases to the courts and raised serious concerns about the destruction of coastal ecosystems and water supplies. The report said some families had 10% of their land expropriated and had to pay tens of thousands of euros for roads and infrastructure serving developments built on their former land.

The Valencian parliament approved its controversial new urban development law in 2005, despite a call by the European Parliament for changes (see *Inside Spain*, Newsletter 20, 13 January 2006).

In a separate development, a magistrate decided to bring charges against five senior officials in the PP government of Murcia, one of the other regions mentioned in the Parliament's report, for reclassifying land protected for environmental reasons so that homes could be built on it. The case was investigated after a local socialist politician said he had been offered a bribe of €1 million by an intermediary working for the promoter of the housing project.

Valencia and Murcia account for around one-third of the urban developments rejected by the water authorities because a regular water supply cannot be guaranteed. Despite the negative reports, which are not legally binding, a total of around 300,000 homes are being built.

Integration Plan for Immigrants

The government launched its plan to strengthen education, healthcare and social services in the main areas where immigrants have settled. More than 40% of the €2 billion budget between now and 2010 will go on education. State schools in areas where there is a high concentration of immigrants are becoming overcrowded. The network of these primary and secondary schools only accounts for 66% of total students, but 80% of the children of immigrants go to them.

Spain has received more than 4 million immigrants in less than a decade, increasing its population by around 10%.

Spain: Third Oldest OECD Country in 2050

Spain will have the third-oldest population among OECD countries in 2050 and its ratio of inactive elderly to the total labour force will increase from 38.2% in 2000 to 90.5% in 2050, according to the latest OECD estimates. The proportion of the population aged 65 or over is forecast to double to 35% in 2050, three times higher than the share in 1975 (see Figure 1).

Figure 1. Population Aged 65 and Over (% of Total Population)

	2000	2050
France	16.1	26.2
Germany	16.4	29.6
Italy	18.3	33.7
Spain	16.8	35.7
Sweden	17.3	23.6
UK	15.8	25.3
OECD average	13.0	25.5

Source: OECD Factbook 2007.

This means for every elderly inactive person there will be only one person in the labour force. The sharp increase in the old-age dependency ratio is a Europe-wide problem, but substantially more acute in Spain, despite the influx of immigrants, and only surpassed by Italy (see Figure 2).

Figure 2. Ratio of Inactive Elderly to the Total Labour Force (%)

	2000	2050
France	36.4	68.9
Germany	33.3	67.0
Italy	42.5	92.8
Spain	38.2	90.5
Sweden	31.9	46.4
UK	30.8	54.7
OECD average	24.8	53.8

Source: OECD Factbook 2007.

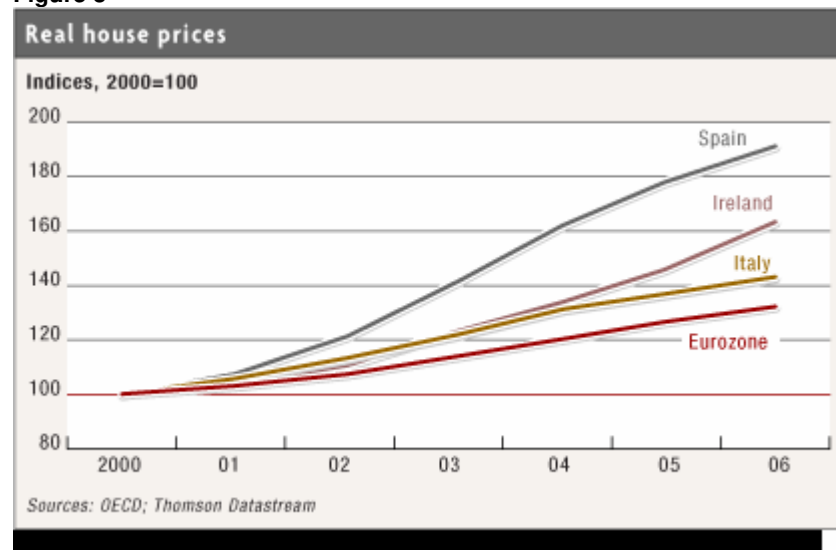
Since a 'greying' population is fundamentally caused by a combination of declining fertility (no longer the case in Spain) and increased life expectancy, the effects have implications on the composition of all age groups, young and old alike. This means that its consequences affect all institutions of a society and will entail reforms not only of the pension system but also education, the labour market and public health care. Few reforms in these areas have been undertaken.

The Economy

Real Estate 'Bubble' Fears Hit Stock Market

Spain's stock market was hard hit by fears of a crash in Spain's booming property sector (see Figure 3), sparked by a free-fall in the share price of Astroc Mediterráneo, the sector's star company, and data showing a slowdown in house prices and an oversupply problem. The government, anxious to stem any panic, wasted no time in saying that some stocks had grown 'excessively' and that what had happened was simply a 'correction'.

Figure 3



The share price of Astroc fell 65% over six days in April after reaching a peak of €72.60 in February, 11 times its initial public offering price of €6.40 in May 2006. That surge helped push Astroc Chairman Enrique Bañuelos onto Forbes magazine's annual billionaires list. The Astroc share recovered a little.

Astroc's fall dragged down other real estate companies and the Ibex-35, the Spanish market's main index (see Figure 4). Bañuelos said there was no justification for it.

Figure 4. Falls in Real Estate Stocks (€)

Company	Maximum share price and date	Price on April 26	Price on May 7
Astroc	72.60 (26/2/07)	15.95	16.44
Colonial	77.30 (19/1/07)	55.75	56.50
Fadesa	36.87 (20/2/07)	27.35	28.01
Inbesòs	37.35 (6/2/07)	27.98	25.10
Inmocaral	6.06 (11/12/06)	4.33	4.64
Metrovacesa	128.50 (18/12/06)	84.95	87.20
Montebalito	25.98 (26/2/07)	21.95	21.02
Urbas	3.40 (23/1/07)	2.36	2.17

Source: Bolsa de Madrid.

House prices rose 7.2% year-on-year in the first quarter, the lowest increase in eight years, according to the Housing Ministry. The Ministry said there was now oversupply, with licences issued for 800,000 new housing starts compared with an estimated demand for 600,000. Some property developers have been offering a free car to prospective house buyers in a bid to lure them and there have been reports of people selling investment homes before they were completed at considerably less than they paid for them.

The labour intensive construction sector and related services are the driving force of the Spanish economy and a hard –as opposed to a soft– landing would severely damage the economy. The economy is too ‘lopsided’, according to the IMF. Spain has one of the world’s highest levels of home ownership (84% compared with an EU average of 66%). The total value of mortgages is lower in GDP terms than the EU average (48% against 56%) but almost all of them are at variable interest rates which means that borrowers could be squeezed by interest rate rises.

The jitters took some of the shine off the first state of the economy address by José Luis Rodríguez Zapatero, the Prime Minister, to a select audience in the Madrid Stock Exchange. Last year was the best in the country’s 30 years of democracy, he said. GDP expanded 3.9%, unemployment was down to 8.3% (close to the EU average), inflation was 2.5% (0.6 pp more than the average), the public debt ratio stood at 39.8% of GDP and Spain was one of the few EU countries to record a general government budget surplus (1.8% of GDP).

While last year crowned a 13-year period of uninterrupted growth and the strong expansion is set to continue (projected GDP growth of 3.5% this year), the economy is accumulating problems and headed towards what the most pessimistic observers view as a ‘perfect storm’.

Productivity growth is very sluggish, investment in R&D is among the lowest in the EU (at just over 1% of GDP), competitiveness is ailing, household debt is very high, the education system has serious problems (the drop out rate in secondary education is very high and the average number years of schooling for adults over the age of 25 is nine compared with 13 in the US and 11 in the EU, see Figure 5), the current account deficit in 2006 was the second largest in the world (€86 billion or 8.8% of GDP) and shows no signs of abating (see *Inside Spain*, Newsletter 33, 2 April 2007).

Figure 5. Young People with Upper Secondary Education (%)*

	2000	2005
France	81.6	82.8
Germany	74.7	71.0
Italy	68.8	72.9
Poland	87.8	90.0
Spain	65.9	61.3
Sweden	85.2	84.8
UK	76.4	77.1
EU-25 average	76.3	76.9

(*) People aged between 20 and 24.

Source: Eurostat.

Zapatero, who took office in 2004, launched what he hopes will be an annual event by the Prime Minister of the day (see www.la-moncloa.es/NR/rdonlyres/7DCB0865-0304-4C8A-ABF8-FA976DBFC78E/80868/IEPG_2008.pdf for the full document in Spanish).

Telefónica Acquires Stake in Telecom Italia

Telefónica is to take part of a controlling stake in Telecom Italia (TI). It will pay €2.3 billion as part of a €4.1 billion operation to buy out Pirelli, the Italian tyre company.

Spain's telecoms giant joined forces with the Benetton family, insurer Generali and Italian banks Intesa Sanpaolo and Mediobanca to hold 23.6% of TI. Telefónica's own stake will be 6.9% and it will have two TI board directors while the Italian investors will have 13.

The power arrangements were designed to ensure the deal was not scuttled by political opposition to Telefónica's entry into Italy's dominant telecoms company. An earlier deal between Pirelli and the US's AT&T and Mexico's América Móvil collapsed because of political resistance.

Telefónica's deal was preceded earlier in April by Enel, 30% owned by the Italian government, and Acciona, a Spanish infrastructure company, joining forces and outbidding Germany's E.on for Endesa, Spain's largest electricity company, which resulted in the resignation of the stock market regulator (see separate story below). The two deals suggested a closer political relationship between Madrid and Rome and could result in the resurrection of the merger of Spain's Abertis and Italy's Autostrade to create the world's largest toll-road operator and infrastructure company. This marriage was blocked last year by the Italian government.

Santander Joins Consortium in Battle for ABN Amro

Grupo Santander, Spain's largest financial group, joined forces with Royal Bank of Scotland (RBS), an old ally, and Fortis, the Belgo-Dutch banking and insurance group, to make a US\$24.5 billion bid for the LaSalle Bank, the US arm of the Netherlands' ABN AMRO. The offer is conditional on being able to buy the rest of ABN, which Barclays has made a bid for. ABN rejected the offer. The consortium of European banks is offering around €72 billion for ABN, trumping Barclays' offer of €66 billion.

The battle for ABN looks like being bogged down in legal battles over LaSalle. Bank of America (BofA) filed a lawsuit in New York claiming ABN had breached its contract by halting the separate sale to it of LaSalle. BofA is seeking a court injunction to block the sale of LaSalle to a rival bidder.

ABN's shareholders challenged the sale to BofA because it undermined the bid by the European consortium.

Stock Market Regulator Resigns Over Battle for Endesa

Manuel Conthe, the head of the National Securities Market Commission (CNMV), resigned after claiming the government dented the CNMV's independence by blocking an investigation into the rival and winning bid for Endesa, Spain's largest electricity company, by Italy's Enel and Acciona, its Spanish partner.

Conthe compared the rival and higher bid, made hours after the final binding offer by Germany's E.on to two runners who 'joined a marathon half-way, even though they had failed to register for the race. And then the referee fails to disqualify them'. The government made no secret of its opposition to E.on's bid –launched in February 2006– but denies inviting Enel and Acciona, which rapidly built up a 46% stake in Endesa, to mount a challenge.

The CNMV's executive committee agreed by three votes to two to investigate the rival bid, but the Board overturned this by four votes to three. The Board's voting is not made public, but it is believed that one of the two votes against was that of the Bank of Spain's representative.

The new Chairman of the CNMV, Julio Segura, a former Director of the body, proposed reforms including limiting the term of office to one period of more than the current four years so that it did not coincide with the changeover of governments.

Spain Slips in Networked Readiness Index

Spain slipped from 31st to 32nd place in the World Economic Forum's latest Networked Readiness Index which ranks countries according to their potential to use Internet-based technologies to boost economic growth on the basis of 67 variables (see Figure 6).

Figure 6. Networked Readiness Index 2006-2007 rankings*

Rank and country	Score
1. Denmark	5.71
4. Finland	5.59
7. US	5.54
9. UK	5.45
16. Germany	5.22
23. France	4.99
28. Portugal	4.48
31. Chile	4.36
32. Spain	4.35
38. Italy	4.19

(*) Out of 122 countries.

Source: World Economic Forum.

The US lost top spot to Denmark and Italy was ranked 38th, up four rungs but still well below Spain.

Between 2001 and 2006 Spain's broadband subscribers per 100 inhabitants increased from 1.2 to 15.3, below the EU-15 average of 18.6 (see Figure 7).

Figure 7. Broadband Subscribers per 100 Inhabitants

	2001	2006
France	1.0	20.3
Germany	2.3	17.1
Italy	0.7	14.8
Poland	0.1	6.9
Spain	1.2	15.3
Sweden	5.4	26.0
UK	0.6	21.6
EU-15 average	1.6	18.6

Source: OECD.