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Foreign Policy

Spain faces tough decisions during UK Presidency of the EU

Spain enters the UK presidency of the European Union determined to remain a net recipient of EU funds in 2007-13 but open to reforming the Common Agricultural Policy (CAP). José Luis Rodríguez Zapatero, the prime minister, might also move closer to London and distance himself a little from France and Germany with whom he has forged closer links in the year since pulling Spain's troops out of Iraq and returning to what he calls 'the heart of Europe'.

Spain rejected the financing deal for the next budgetary period presented to it in the final hours of the Luxembourg summit in June. This offer was less favourable than the previous one, according to the government's calculations, and was interpreted as a sign that its aspirations were not being taken seriously. The net sum placed on the table was close to €5 billion, compared with the €7 billion, at least, the Socialists were hoping to receive and the €12 billion that the centre-right Popular Party, the main opposition party, set as the minimum acceptable. The government would have liked to have agreed a deal on the spot because postponing it means the negotiations for future funds will be based on 2003 statistics which show Spain as a richer country and hence in a weaker position to strike a deal more to its satisfaction. But it felt it would be giving away too much.

As a result of the statistical effect of EU enlargement, which has pushed Spain's per capita GDP over the 90% threshold qualification, it is estimated the country will cease to receive €12.4 billion in Cohesion Funds. The total losses for 2007-13 are put at more than €23 billion (see Figure 1). Around half of the 12 regions which qualified for structural aid during 2000-06 would cease to qualify for regional funds, as their per capita GDP would surpass the 75% ceiling. And as well as substantially reduced payments from the EU budget, Spain would be contributing more. According to Spain's Finance Ministry they would rise from €9,817 million in 2005 to €15,894 million in 2013. The combination of increased contributions and decreased payments would see Spain moving from being the current largest net recipient to a net contributor. The key concern for the government is how quickly this would happen; it will fight hard for a gradual phasing out.

Figure 1. Estimated Losses in Payments from the EU for 2007-13

Item	Losses (€ bn)
Cohesion Fund	12.4
Regions above 75% of per capita EU GDP	8.6
Statistical effect	2.4
Total estimated losses	23.4

Source: European Commission and Elcano Royal Institute.

The government is in somewhat of a bind. Pedro Solbes, the economy supremo, likes the world to know that in 2004 Spain's GDP overtook that of Canada which, unlike Spain, is a member of the G8 group of rich countries (see Figure 2). But the government is less keen to assume the responsibilities that go with being a richer country.

Figure 2. Ranking of Countries by GDP (2004)

Country	GDP (US\$ mn)
United States	11,667,515
Japan	4,623,398
Germany	2,714,418
United Kingdom	2,140,898
France	2,002,582
Italy	1,672,302
China	1,649,329
Spain	991,442
Canada	979,764

Note: All these countries except China and Spain are G8 members, plus Russia (which does not participate in all events).

Source: World Bank.

Zapatero will meet Tony Blair in London on July 27. UK officials are hoping he will stop 'gratuitously' banging the anti-Iraq war drum, which he has done so far in every meeting with Blair, to his intense annoyance, and concentrate on areas of common interest and possible cooperation. Politically Zapatero is closer to Blair than José María Aznar, the former prime minister, but he has yet to establish the close relationship that Aznar enjoyed. For example, Blair and Aznar worked closely together on the Lisbon Agenda to make the EU more competitive. Little progress was made on structural reform, however, partly because of French and German resistance. Blair wants to revive the process. Zapatero shows modest signs of moving in the same direction (see the item below on the Ingenio 2010 plan).

On CAP reform, which Blair will push for strongly in return for cancelling or reducing the British rebate, Zapatero's economic team is studying whether it is small farmers or *latifundistas* (big landowners), as suspected, who are the main beneficiaries in Spain. Backing the UK on CAP reform, however, would mean Zapatero would have to confront Chirac who adamantly opposes any changes (French farmers account for less than 4% of the work force and yet France receives 40% of the CAP funds).

A deal on joint use of the airport at Gibraltar, the British colony that Spain has long claimed, which is reportedly in the pipeline, would smooth the path for closer ties with London.

New US Ambassador arrives in Madrid

Eduardo Aguirre, the new American ambassador, took up his post amidst a hardening of attitudes in Spain against President George W. Bush and an EU agreement to extend the suspension of sanctions against Cuba.

Aguirre is of Cuban origin (he came to the United States when he was 15, see *Inside Spain*, Newsletter 12, April 6, 2005) and speaks perfect Spanish. The Socialists' rapprochement with Cuba is one of the main irritants in Madrid's relations with Washington which, nevertheless, have improved considerably in the year since Spanish troops were withdrawn from Iraq. The issue will be high on Aguirre's agenda.

The Socialists overturned the previous government's isolation of the Cuban regime and spearheaded the efforts of the EU to restore normal diplomatic relations as of January 2005, a decision ratified at the end of June (and supported by 60% of respondents in Elcano's latest barometer). The EU reduced high-level governmental visits and participation in cultural events in Cuba in 2003 after the summary execution by firing squad of three people, who had hijacked a ferry in an attempt to escape the country, and the roundup of 75 dissidents. Countries also decided to invite dissidents to national holiday celebrations at their embassies in Havana as a sign of support for the regime's opponents. Castro retaliated by freezing out embassies from all official contacts. The Socialists concluded that the previous policy was getting nowhere and, furthermore, was preventing Spain, in particular, and the EU in general, from positioning itself in order to exercise influence after the death of Fidel Castro (aged 78) in a possible transition to democracy.

The recently released 2005 Pew Global Attitudes Project, the gold standard of international opinion surveys, shows that Spain's favourable opinion of the United States had risen slightly since 2003, but at 41% it is still the lowest in Europe, along with Germany, and well below the 50% registered in 1999 (see Figure 3). The survey was conducted in the United States and in 15 other countries. Spain's support for the war in Iraq has plummeted, but not as much as in the United Kingdom which still has troops there (see Figure 4). When Spaniards were asked if they thought the world was safer without Saddam Hussein only 13% replied in the affirmative, the lowest level among the European countries surveyed (39% in the UK, 28% in Germany and 23% in France).

Figure 3. Favourable View of the United States (%)

Country	99/00	2002	2003	2004	2005
Canada	71	72	63	—	59
United Kingdom	83	75	70	58	55
Netherlands	—	—	—	—	45
France	62	63	43	37	43
Germany	78	61	45	38	41
Spain	50	—	38	—	41
Poland	—	79	—	—	62
Russia	37	61	36	47	52
Indonesia	75	61	15	—	38
Turkey	52	30	15	30	23
Pakistan	23	10	13	21	23
Lebanon	—	35	27	—	42
Jordan	—	25	1	5	21

Source: Pew Global Attitudes Project, 2005.

Figure 4. Country's Decision on War in Iraq Right Decision to use Force (%)

Country	2003	2004	2005
United States	74	60	54
United Kingdom	61	43	39
Spain	31	—	24
Netherlands	—	—	59
Poland	—	—	24

Source: Pew Global Attitudes Project, 2005.

When asked what was the main problem with the United States 76% of Spaniards said it was mostly President Bush, by far the highest proportion (see Figure 5). A low regard for Bush is more heavily correlated with an unfavourable rating for the United States than any other attitude or opinion tested in the survey.

Figure 5. What's the Problem with the United States (% , 2003 figures in brackets)

Country	Mostly Bush	America in General	Both	Don't Know/Refused
Spain	76 (50)	14 (37)	7 (12)	3 (2)
Germany	65 (74)	29 (22)	5 (3)	1 (1)
Netherlands	63	30	6	1
France	63 (74)	32 (21)	5 (4)	1 (1)
Pakistan	51 (62)	29 (31)	10 (2)	10 (5)
Britain	56 (59)	35 (31)	8 (8)	1 (3)
Canada	54 (60)	37 (32)	9 (6)	0 (2)
Lebanon	47 (51)	32 (32)	19 (16)	1 (1)
Turkey	41 (52)	36 (33)	17 (12)	6 (3)
Indonesia	43 (69)	42 (20)	0 (7)	15 (4)
India	35	35	14	16
Jordan	22 (42)	37 (28)	41 (30)	1 (*)
China	16	34	42	8
Poland	27	49	14	10
Russia	30 (43)	58 (32)	9 (15)	3 (10)

(*) Based on those with an unfavourable opinion of the US.

Source: Pew Global Attitudes Project, 2005.

Domestic Scene

Socialists capture conservative bastion of Galicia in cliff-hanger election

The Socialists ousted the centre-right Popular Party (PP) from the north-west region of Galicia, run since 1989 by Manuel Fraga, a former information and tourism minister during the 1960s and the longest political survivor from the Franco regime.

The outcome was very close and was decided, a week after the elections were held, by the large émigré vote, mostly from Latin America. The PP won 37 seats in the regional parliament, one short of an absolute majority. The Socialists teamed up with Galician nationalists to form the new government.

Fraga (aged 82) founded the Popular Party after Franco's death in 1975 when it was known as the Popular Alliance. He was the hard-line interior minister in the first post-Franco government –he once telephoned a communist leader in the early hours of the morning and told him ‘the street is mine’–. He is credited with forging a conservative party that broke with the past and eventually won power nationally (1996-2004).

Madrid bombing investigation accuses previous government of manipulation

The year-long parliamentary panel investigation into the Madrid rail bombings, which killed 191 people and injured more than 1,800, concluded that the previous centre-right PP government ‘manipulated’ and ‘twisted’ information in order to further its electoral interests. The bombings occurred on March 11, 2004 and three days later Spaniards went to the polls and voted in the Socialists.

The panel's conclusions were backed by all parties except the PP. The government of José María Aznar initially blamed the bombings on the violent Basque separatist organisation Eta and apparently played down the mounting evidence pointing to a Moroccan group tied to al-Qaeda. The PP still maintains that possible links between Eta and Islamist extremists were not properly investigated by the panel.

The 290-page report said the government ignored the warning signs of the increasing threat of an Islamist attack in Spain –the support for the war in Iraq and the 2003 bombs in Casablanca which killed 24 people in a Spanish social club– and that its capacity to prevent an attack was hindered by various factors including the lack of coordination among intelligence services and few Arabic translators.

The panel became a forum for scoring political points and all parties were heavily criticised for this by victims of the bombings.

Government reforms state-run TV

Parliament, and not the ruling party, will choose the head of the state-run TV and its board can be sacked if during two consecutive years it does not meet the budgetary targets that are set.

These are two of the reforms of RTVE, the two heavily indebted and politicised TV channels, which are expected to come into force in 2006. The state will assume RTVE's €7,560 million debt (€133 million in 1991) and convert RTVE into a BBC-style wholly owned corporation. The government ruled out privatisation.

A ten-man board including two trade union representatives, appointed by parliament on the basis of a two-thirds majority of its members, will run RTVE and select the director general.

The rain in Spain is not falling on the plain

Spain's worst drought since records began in 1947 is destroying crops, accelerating the pace of desertification, producing restrictions in some areas and has sparked a 'water war' between two regions.

With temperatures of 40°C or more, the environment ministry warned that Andalusia in the south, Murcia and Valencia in the east and the Canary Islands off the coast of Africa face a 'high or very high' probability of desertification if preventative measures are not taken.

Agricultural losses are so far estimated at more than €2 billion, with a large part of the olive crop in Jaén, Andalusia, destroyed.

Tourism (12% of GDP) could also be affected. Millions of tourists spend their holidays in the south and east of Spain and they might face water rationing. The World Wildlife Fund estimates there are 10,000 illegal wells in the Costa del Sol and they are depleting the water resources. Despite the lack of water, the building boom continues apace along the Mediterranean coast including 58 new golf courses (according to a critical Greenpeace report).

Seven regions (Andalusia, Aragón, Catalonia, Extremadura, Murcia, Castilla-La Mancha and Valencia) have restricted water for agricultural use. The government of Murcia, one of the hardest hit regions, is at loggerheads with the authorities of Castilla-La Mancha, the region that supplies a significant part of the water for its agriculture, especially in times of drought. The central government authorised the transfer of more water from reservoirs in Castilla-La Mancha through an open channel, but not as much as Murcia is demanding and more than Castilla-La Mancha wanted to release. Both

sides said they would appeal against the decision. Aerial photographs of Murcia sneakily taken by the government of Castilla-La Mancha indicated it was not as badly off as it claimed.

In a desperate move, a small number of Murcian farmers have been watering their vegetables with untreated sewage, reportedly triggering outbreaks of a resistant form of salmonella in Britain and Finland.

Spain has always had and will always have a water problem unless something is done to supply the dry south from the wet north –the previous government’s ambitious plan to do this was abolished by the Socialists last year– or a culture is instilled to use water sparingly and rationally. According to Cristina Narbona, the environment minister, farmers (who account for less than 6% of total employment) account for fourth-fifths of water consumption and fewer than 10% use efficient irrigation methods. ‘The remaining 90% still resort to flooding their fields, an incredibly wasteful practice than needs to be eradicated’. Previous governments have said the same thing and done absolutely nothing about it. The culture of waste is also prevalent in towns and cities.

The first thing to do is to establish a water pricing policy that discourages wasteful use of a scarce resource. Those farmers who are billed for water, and many are not, pay 10% of its real cost.

Spain legalises same-sex marriage

Spain became the fourth country in the world, after Belgium, the Netherlands and Canada, to allow same-sex couples to marry and adopt children, to the fury of the Roman Catholic Church which campaigned against the legislation. While supporters of the new law staged massive marches and fiestas, the self-styled Spanish Forum for the Family denounced it and called for a referendum on the issue.

2004 birth rate, highest since 1985

The number of babies born in Spain in 2004 (453,278) was the highest since 1985, consolidating an upward trend that looks likely to gather pace. The number born to Spanish mothers (391,128) was 1.2% higher than in 2003 and those to immigrants (62,150) rose 16.6%. One in every seven children born in 2004 had a non-Spanish mother. The fertility rate of 1.32 was the highest since 1993.

Madrid loses 2012 Olympics, will try again

Madrid was knocked out of the contest to host the 2012 Olympics in the third and penultimate round but has not given up.

The capital has been immersed in a €6.5 billion renewal of its infrastructure and taken on the appearance of a giant construction site, earning its young and energetic mayor, Alberto Ruiz Gallardón, the nickname ‘Ruiz Socavón’ (Mr Ruiz Big Hole).

As well as wishing to use the Olympics to transform the city, in the way that Barcelona did in 1992 when it hosted the Games, a victory would have provided the mayor from the centre-right Popular Party with a national platform for his political ambitions. Ruiz Gallardón is touted as a future PP candidate for prime minister.

The Economy

Government aims to almost double R&D spending by 2010

Spain, one of Europe's laggards in innovation, will almost double its spending on R&D to 2% of GDP by 2010, under a government plan. On current trends R&D expenditure would just about reach 1.4%.

The *Ingenio 2010* plan replaces the previous government's *Info XXI* and *España.es* plans which did little to improve the situation. If successful, however, Spain's R&D expenditure in 2010 would still only be in line with the current average of the EU-25.

Unemployment drops below 2 million for first time in almost two years

For the first time in nearly two years, the number of Spain's registered unemployed dropped to below 2 million. The number of jobless in June was 1.97 million, 10.2% of the work force and still higher than the EU average.

The impact of the almost 700,000 illegal immigrants whose situation was normalised earlier this year was keenly felt in the social security system whose number of contributors surpassed 18 million for the first time. Almost half of the 231,716 new contributors in June were immigrants.

Spain's job creation is impressive, particularly when viewed in the context of a sharply rising population (see *Inside Spain*, Newsletter 13, May 10, 2005). The overwhelming majority of contracts, however, are still short-term. Roughly one in every three employees in Spain has a temporary contract compared with an OECD average of 13%.

Telefónica puts a toe in China

Telefónica, the telecommunications group, has acquired almost 3% of China Netcom (CNC), the country's second-largest fixed-line telecoms operator, for €240 million. It intends to acquire a further 2% in the Hong Kong and New York-listed operator and qualify for a seat on the board.

The great bulk of Telefónica's overseas investment is in Latin America, where it is the largest mobile phone company. It recently bought Czech operator Cesky Telecom. The Chinese purchase is its first one in Asia and follows ill-fated moves into the German and Italian markets which cost Telefónica more than €8 billion.

There are only 16 fixed lines for every 100 inhabitants in China. CNC has a 15.5% share of the market, and is based in ten provinces in the north of the country.

Spain's net investment outflows, sixth largest in world

Foreign direct investment in Spain has been falling markedly in the last few years (less than US\$1 billion in 2004 if investment in special purpose entities is excluded), but outward investment remains high because of continued acquisitions abroad. Between 1995 and 2004 Spain's net outflows were the sixth largest in the world (see Figure 6).

Figure 6. Cumulative Net Outflows in Selected OECD Countries (1995-2004)

Country	Net Outflows (US\$ bn)
United Kingdom	404.1
France	317.0
Japan	223.5
Switzerland	121.2
Netherlands	93.9
Spain	84.0
Canada	69.0
Germany	54.3
United States	50.2

Source: OECD.

Most of the outward investment was due to Santander's purchase of the UK bank Abbey National, but there was also continued activity in Latin America.

US companies in Spain less sanguine about their business

The 2005 Barometer of US Business in Spain shows a significant rise in the number of companies concerned about the Spanish economy (14% vs none in 2004).¹ The survey detected less optimism and a slowdown in investment projects, pointing to a possible change of trend in the future. The results, however, have to be interpreted cautiously, as the number of companies that took part in the survey during the first quarter of the year was not very large. Only 14% of the companies answered the questionnaire (the proportion for companies employing more than 500 workers was higher at 21.5%).

The proportion of companies who said they were completely satisfied dropped from 24% in 2004 to 15% in 2005. Those with a pessimistic view rose from 4% to 14%.

Close to half (49%) the companies said they made investments in 2004, of which 79% was to increase their productive capacity. The increases in capacity, however, were modest: 40% of them were to boost capacity by 10% and 36% by between 10% and 20%, while only 8% were for increases of more than 50%. The main increases in capacity were in the food, chemicals-pharmaceuticals, information society and electrical and electronic material sectors (see Figure 5). Only 27% of the companies, mostly in the services sector, said they planned to invest more than in 2004 (see Figure 6). Almost two-thirds of companies said they were 'pessimistic' about creating employment in the medium term.

Figure 5. Increase in Production Capacity by Sectors (2004)

Sector	Increase in Capacity	
	Yes	No
Food, drinks, tobacco	3	0
Auto	2	1
Electrical and electronic material	4	2
Chemicals-pharmaceuticals	5	1
Metallurgy	1	2
Other consumer goods	1	0
Other manufacturing industries	2	0
Information society	3	0
Consultancy-advanced services	2	0
Financial-insurance	1	1
Other services	3	0
Total number of companies	27	7

Source: Barometer of US Business in Spain, 2005.

¹ *El Barómetro de los Negocios Norteamericanos en España, Perspectivas para 2005*, prepared by Joan Manuel Batista i Foguet and Pere Puig i Bastard, US Chamber of Commerce in Spain and ESADE.

Figure 6. Investment Plans for 2005

In Relation to 2004 Investment Level	Number of Companies	%
Much higher	6	9
Slightly higher	12	18
Same level	17	26
A little below	9	13
Well below	6	9
No investments in 2005	16	25

Source: Barometer of US Business in Spain, 2005.