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Foreign Policy

Seventeen troops killed in helicopter crash in Afghanistan

Seventeen Spanish soldiers were killed in Afghanistan when their helicopter crashed. The 17, who died in what looked like an accident, were part of a 500-strong force sent by Madrid to help oversee parliamentary elections on September 18. They are due to return in October.

The crash rekindled the debate in Spain about the safety of the country's troops abroad and exposed the meagreness of the defence budget (€7 billion, one-fifth of France's or the UK's). In 2003, under the previous centre-right government of the Popular Party (PP), 62 Spanish troops returning from duty in Afghanistan died when their chartered aircraft crashed in Turkey. An investigation revealed that senior officers had complained about the safety of such aircraft arranged through middle-men, and the defence ministry bungled the identification of bodies.

José Luis Rodríguez Zapatero, the prime minister, pulled Spain's peacekeeping troops out of Iraq last year, but has no desire to do the same in Afghanistan. The withdrawal of troops from Iraq and the strong presence in Afghanistan –the latter backed by parliament– are the two sides of the Socialists' policy towards terrorism. On the one hand, they regard the war in Iraq as counterproductive in the fight against terrorism and, on the other, they have no qualms about being actively involved in Afghanistan because it was a training base for terrorist networks, and there was a wide consensus, unlike over Iraq, in the international community on the need for firm action. This policy continues to enjoy majority public support. 'We are in Afghanistan for the same reasons that we pulled out of Iraq, in order to defend peace, the United Nations and international law', said Zapatero.

A contingent of 540 Spanish soldiers was moved from the relative calm of Kabul, the capital, earlier this year to the more conflictive western part of the country as a provincial reconstruction team (PRT). Underlining its commitment, Madrid has appointed an ambassador on special mission for the reconstruction and political stability of Afghanistan. José Luis Solano took up his position in September and is based in the same area as these troops.

The PP accuses the government of using Afghanistan as a way to curry favour with the US government. The PP's discourse, however, is not coherent: on the one hand, it never ceases to criticise the Socialists for pulling out of Iraq and, on the other, it questions the government's 'pacifist spirit' as it says Spanish troops in Afghanistan are in a 'war situation'. The PP wants to have its cake and eat it.

The rotating command of Nato's International Assistance Security Force (ISAF), which has 10,500 troops from 35 countries, is currently in the hands of Italy and it is Spain's turn at the end of 2006 or early 2007.

Zapatero and Blair finally hit it off

José Luis Rodríguez Zapatero, the prime minister, and Tony Blair, his UK counterpart, agreed at their meeting in London to work closely together on various issues during the UK presidency of the EU. These range from Zapatero's plan to create an 'Alliance of civilizations' between Western and Muslim countries in the fight against terror, reinvigorating the stalled Lisbon agenda for economic reform to make the EU more competitive and actively promoting Turkey's EU membership.

Zapatero did not take issue with the UK's support for the war in Iraq, as he had done in the past, to Blair's intense annoyance, and Gibraltar, the other sensitive subject, was also not mentioned. As a result, the meeting went off well, according to officials on both sides.

The Spanish prime minister could be a useful ally for Blair as he is the only leader of a large EU country who is not a spent force. Gerhard Schröder, the German chancellor, is unlikely to be re-elected in this month's general election, Jacques Chirac, the French president, is a lame duck, following the French No vote in the European constitution referendum, and Silvio Berlusconi's government in Italy is not very stable.

Zapatero is open to reforming the Common Agricultural Policy (CAP), provided Spain's EU cohesion and structural funds are gradually phased out. Spain accepts that it will move from being the largest net recipient of these funds to a net contributor during the 2007-13 budgetary period (see *Inside Spain*, Newsletter 15, July 15, 2005). It would help the Socialists sell the idea of CAP reform to their electorate if they could show that many of the main beneficiaries are large estate owners and not small farmers.

Until the French No, it looked certain that Turkey, which is co-sponsoring Zapatero's 'Alliance of civilizations', would begin its EU negotiations on October 3, as scheduled. Chirac, once a fervent supporter of Turkey's entry, is changing his tune and calling for Ankara to recognise the state of Cyprus, the island divided by Turkish invasion since 1974, although this was not one of the conditions laid down to Ankara for the start of talks at an EU summit in June. Turkey wants a comprehensive settlement of the Cyprus dispute. Blair and Zapatero will press Turkey's case with France.

On Gibraltar, the Spanish press is reporting that Miguel Ángel Moratinos, Spain's foreign minister, Jack Straw, the UK foreign secretary, and Peter Caruana, Gibraltar's chief minister, will meet in October under the formula known as 'two flags, three voices' (see *Inside Spain* 7, November 4, 2004). UK officials, however, say this has not yet been agreed and would probably only happen if there was something of substance to announce, such as a deal on joint use of the airport at Gibraltar, as Straw's agenda during the UK presidency of the EU is already very full.

Spain significantly changed its policy towards Gibraltar almost a year ago when it decided to give the Rock, for the first time, a seat at the negotiating table and pursue its centuries-old sovereignty claim in a friendlier atmosphere.

The Socialists would also like better relations with New Labour. Relations between the two parties have been frosty, epitomised in January 2004 when the Socialists were in the opposition and José Bono, the current defence minister, called Blair an 'imbecile' (a polite translation of what he actually said). His remark was not intended to be heard, but was recorded by a television team.

Domestic Scene

EU to ship cereals to drought-stricken Spain

The European Union has come to the rescue of Spain's harvest, devastated by the worst drought in 60 years. It has approved the shipment of 100,000 tonnes of barley from Germany, 100,000 tonnes of maize from Slovakia and 100,000 tonnes of maize and 200,000 tonnes of wheat from Hungary. It is also expected to approve the shipment of 500,000 tones of rye from Germany. Meanwhile, the government is drawing up emergency plans to ship water in tanker boats to the worst hit areas.

Spain's production of cereals will be halved in the coming year, according to official forecasts. Under the Common Agricultural Policy (CAP), member states are allowed to buy crops from each other but this rarely happens. The fact that it has highlights Spain's dramatic situation, intensified by widespread forest fires and water shortages including in tourist areas.

This year's forest fires so far are the second worst in a decade. Between January and August 14, 107,524 hectares of trees were destroyed compared with an average of 79,621 for the same period over the last 10 years. The great majority of the 19,000 wildfires were started by arsonists or were the results of human carelessness –11 voluntary firemen died in one fire in the province of Guadalajara–.

The level of Spain's reservoirs continues to fall rapidly; at the end of August they were on average at 42% of their capacity. The reservoir at Buendía was at around 10% of its capacity. This reservoir is the epicentre of the 'water war' between the regions of Castile La Mancha and Murcia as water is sent from it through an open channel so that Murcia can grow its crops and, it is suspected, water golf courses. Murcian farmers say that if there is no rain during the autumn, the fruit harvest will be reduced by half and unemployment in the region will soar.

The Murcian government has challenged the decision of the Castilian government to reduce the water supply. 'This year is the worst for rain since reliable records began to be kept and the drought is very serious', said Cristina Narbona, the environment minister.

Villages in the worst affected areas are relying on water tankers for their supply and farmers are giving priority to animals as their livelihood depends on their wellbeing.

Almost two-thirds of Spaniards in favour of negotiating with Eta, if it lays down its arms
A majority of Spaniards would like the government to negotiate with the Basque separatist terrorist organisation Eta if it gives up its weapons. The survey by Euskobarómetro also shows that 50.7% of respondents believe the Socialists' anti-terrorist policy is better than that of the previous centre-right Popular Party government.

Of the 61.1% of people in favour of negotiating with Eta, 49% said the group had to first lay down its arms.

More than half (54.4%) expressed support for outlawing the Communist Party of the Basque Lands (EHAK), which acted as a proxy for Batasuna (EH) in May's elections in the Basque country. EH was banned two years ago because of its ties to Eta. These elections were won again by the Basque Nationalist Party but it was far short of an absolute majority and was only able to muster sufficient support in the region's parliament thanks to EHAK's support (see *Inside Spain*, Newsletter 13, May 10, 2005).

The Economy
France Telecom buys Amena
France Telecom (FT) bought 83.5% of Amena, Spain's third-largest mobile operator, for €6.4 billion. The deal was its biggest take-over of a foreign operator since FT acquired the Orange mobile phone network in 2000, and when completed FT will be the second-largest integrated operator in Spain.

The sale generated a capital gain of around €2.5 billion for Amena's main shareholders –Santander, Endesa and Fenosa–.

José Montilla, the industry minister, refuted reports that the government favoured the take-over by FT.

Ferrovial acquires a Texan construction company and the largest independent handling company
Ferrovial, Spain's largest construction group on the basis of its market capitalisation, has gone on a spending spree, acquiring Webber Group in the United States and Swissport International, the largest non-airline linked passenger and cargo handling company.

It paid €178 million for Webber and €646 million for Swissport. The purchase of Webber dovetails neatly with the contract that Ferrovial's subsidiary Cintra won in 2004, together with the Texan company Zachry, to develop the first phase of the Trans-Texas Corridor (TTC-35) –a visionary transport system for the future of the Lone Star State–. The proposed Corridor will be a multi-use, state-wide network of transport routes that will include separate lanes for passenger vehicles and large trucks, high-speed commuter railways, freight railways, infrastructure for utilities (such as water lines and oil and gas pipelines) and transmission lines for electricity, broadband and other telecommunications services.

The first phase of the TTC-35 involves building a US$6 billion toll road between Dallas and San Antonio by 2010.

BBVA abandons take-over bid for Italy's Banca Nazionale del Lavoro
BBVA, Spain's second largest bank, threw in the towel for Banca Nazionale del Lavoro (BNL) after it was outmanoeuvred by Unipol, an Italian insurer less than a quarter of BNL's size but with powerful domestic allies (see *Inside Spain*, Newsletter 14, June 6, 2005).

Unipol offered €8.25 billion cash while BBVA's all-share bid was valued at €8.3 billion. BBVA had hoped to become the first foreign bank to buy a large Italian bank, but met with fierce resistance from parts of the entrenched business establishment, including the Bank of Italy which dragged its feet over the issue, and whose governor was seen as favouring bids from Italian investors. The central bank is majority-owned by the private sector banks that it regulates.

BBVA has a 15% stake in BNL and has not yet decided what to do with it. It has challenged the price that Unipol wants to pay for its shares.

Unemployment drops below 10% for first time in 26 years
The stated jobless rate was 9.3% at the end of June, its lowest level since 1979. The total number of unemployed was 1.94 million, also a 'psychological' barrier as it was below 2 million. Spain's unemployment rate is now more or less in line with the EU-25 average.

In the year to June, 897,100 jobs were created (+5% over the previous 12 months), bringing the total number of jobholders to 18.89 million in a work force of 20.8 million.

The National Statistics Office (INE) introduced a new labour force survey earlier this year which detects more accurately who is working sporadically, on a part-time basis or helping out in family-run businesses. Anyone over the age of 16 who works more than an hour a week and is paid in cash or in kind is regarded as employed.

The latest figures underscore the impact on the labour market of the 'regularisation' of almost 700,000 illegal immigrants this year (see *Inside Spain*, Newsletter 11, March 4, 2005). The number of foreigners paying into the social security system hit a new record of 1.6 million in July (8.7% of the total) and compared with 260,000 in 1998 (1.9%).

The proportion of workers, however, on temporary contracts inched up from 31.8% in March to 33.2% in June, almost three times the EU average.

Zara, first Spanish company to join the Interbrand top 100 brands
Zara, the flagship of the textiles and clothing group Inditex, entered the Best Global Brands list at number 77. Until then, no Spanish company had been included in the list drawn up by Interbrand and *Business Week* every year. Among companies of its own sector, it was ranked higher than Levi's (96) but below Gap (40).

Having just one very well-known global brand can make a big difference, as it acts as a flagship for other lesser-known brands, particularly if they are in the same sector. Finland, for example, whose share of global exports is half that of Spain's at around 1%, has one brand in the top 5 –Nokia, the world's largest manufacturer of mobile phones–.

Institutions such as ICEX, the foreign trade body, and the Association of Well-known Spanish Brands, have made a big push in recent years to promote Spanish brands.

Government announces massive infrastructure plan
The Socialists plan to invest close to €250 billion over the next 15 years in building 6,000km of new roads and 9,000km of high-speed railway track. The key question, however, of where such a huge amount of money will come from was left unanswered.

The announcement of the Strategic Infrastructure and Transport Plan comes at a time when Spain is set to lose most if not all of its EU funds during the next budgetary period (2007-13).

Spain's infrastructure, an important area for the country's ailing competitiveness, has been transformed beyond recognition in the past 20 years, largely thanks to EU funds. However, the pace of improvement will lose momentum from 2007 unless the government (via higher taxes) or the private sector invest more money. Spain, currently the largest net recipient of EU funds in absolute terms, will almost certainly be a net contributor by 2013. EU funds financed around one-third of the previous infrastructure plan. It is estimated that more than €3.5 billion of the €17 billion invested every year by the development and environment ministries comes from Brussels.

UK, the largest investor in Spain
The stock of foreign direct investment (FDI) in Spain stood at €118.2 billion at the end of 2003 (15% of GDP) and the number of people employed in companies with foreign capital was just over 1.1 million (5% of the working population), according to the first ever study of this subject by the Foreign Investments Registry (see *www.mcx.es/polco/default.htm*).

The largest foreign investor in Spain, based on the ultimate as opposed to the immediate investing country, is the United Kingdom (18.4% of the total), followed by France and the United States (see Figure 1). This is a true picture of FDI in Spain by countries as figures based on the immediate investing country would underestimate the inflows from countries such as the United States which tend to invest via the Netherlands and Luxembourg for tax reasons. On the basis of immediate investing countries, Netherlands is by far the main investor (€30.5 billion compared with €3.7 billion using ultimate investing countries).

Figure 1. Total Stock of Direct Investment in Spain by Ultimate Investing Country

	Shareholders' Funds (1)		Employment	
Country	Amount (€ mn)	% of Total	Number of People	% of Total
OECD countries	104,952	88.77	1,136,299	93.88
EU countries	76,381	64.60	812,504	67.13
Belgium	1,459	1.23	27,514	2.27
France	21,414	18.11	269,929	24.53
Germany	13,621	11.52	176,134	14.55
Italy	5,773	4.88	42,722	3.53
Luxembourg	2,381	2.01	14,085	1.16
Netherlands	3,737	3.16	85,367	7.05
Portugal	2,138	1.81	9,992	0.83
Sweden	2,419	2.05	35,780	2.96
United Kingdom	21,760	18.40	100,699	8.32
Non-EU countries	4,761	4.03	65,805	5.44
Switzerland	4,499	3.80	62,806	5.19
Non-European OECD countries	23,809	20.14	257,989	21.31
Japan	3,134	2.65	31,383	2.59
United States	19,832	16.77	220,994	18.26
Tax havens	1,328	1.12	5,322	0.44
Latin America	3,761	3.18	7,890	0.65
Mexico	3,311	2.80	5,237	0.43
Spain	7,268	6.15	53,596	4.43
Other countries	925	0.78	7,287	0.60
Total	118,233	100.00	1,210,393	100.00

(1) Based on the weighted equity of companies with foreign direct investment.
Note: These figures exclude direct investment in Special Purpose Entities. They cover investments in branches and equity stakes in unlisted companies and in listed companies if the stake equals or exceeds 10%.
Source: Foreign Investments Registry.

The stock of Spanish investment abroad amounted to €115.3 billion, only slightly less than the FDI in Spain (see Figure 2). Portugal is the main recipient in Europe (11.4% of the total) and Brazil (11.2%) in Latin America. These figures, however, are based on the immediate investing country as figures by ultimate investing country are not available.

Figure 2. Total stock of Spanish Investment Abroad by the Immediate Investing Country of Destination

Country	Shareholders' Equity (1)	
	Amount (€ mn)	% of Total
OECD countries	63,127	54.71
EU countries	51,352	44.51
Former EU-15 countries	49,774	43.14
France	5,151	4.46
Germany	4,487	3.89
Italy	4,213	3.65
Netherlands	11,190	9.70
Portugal	13,216	11.45
United Kingdom	7,033	6.10
New EU countries (10)	1,577	1.37
Non-EU countries	2,306	2.00
Switzerland	2,135	1.85
Non-European OECD countries	9,470	8.21
Australia	2,095	1.82
United States	6,819	5.91
Tax havens	4,286	3.71
African countries	1,750	1.52
North Africa	1,366	1.18
Latin America	45,537	39.47
Mexico	8,363	7.25
Argentina	10,104	8.76
Brazil	12,914	11.19
Chile	7,731	6.70
Colombia	1,828	1.58
Peru	2,112	1.83
Other countries	-687	-0.60
Total	115,378	100.00

(1) Based on the weighted equity of companies with Spanish direct investment.
Note: These figures exclude direct investment in Special Purpose Entities. They cover investments in branches and equity stakes in unlisted companies and in listed companies if the stake equals or exceeds 10%.
Source: Foreign Investments Registry.

(*) This Newsletter covers the main developments in Spain since the last one on July 15.