

SPAIN: FROM CRISIS TO RENEWAL

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When the Spanish go to the polls on 20 December to elect a new parliament, they will decide on the future of a country that has experienced and shaped changes over the last four years like never before in its democratic history since the transition. The partly painful path of financial consolidation and economic recovery has gone and is still going hand in hand with fundamental changes in the party landscape and a disempowerment of society elites, the consequences of which have yet to be seen. That said, doubts in Spain's stability are as unfounded as concerns about the country's pro-EU orientation under a new government.

The fact that the Spanish have succeeded in mastering times of great economic challenges and social tensions without letting themselves become infected with the demons of violence, radicalisation and xenophobia raging elsewhere deserves great respect and supports the expectation that they will also be able to find the strength to manage the impending process of reconciliation within society. That will also, most importantly, require new and binding basic principles for the collaboration between the democratic parties as well as the state institutions at national and regional level.

BACKDROP

It looked like Spain's new Prime Minister, who had just been elected to office with a comfortable absolute majority of his *Partido Popular* (PP) in parliament, had not yet woken up to the country's harsh reality. But maybe it had also been one of his failed predecessor's most successful moments when he managed to give the fresh and highly motivated new team, which was about to take over the affairs of state in the early winter of 2011, the impression that the situation in the country was far less dramatic than generally claimed.

Be that as it may, after having held his first cabinet meeting on 23 December 2011, Mariano Rajoy began his term in office by issuing an assurance that it would not be necessary to either cut pensions or increase taxes. Many Spaniards raised their eyebrows in surprise. They had expected a “blood, sweat and tears” speech, because Rajoy’s socialist predecessor Zapatero had just thrown in the towel after seven years in office and found himself compelled to call an early general election in view of a deep crisis of confidence, panic sales of Spanish government bonds, and interest rates at unprecedented high levels.

The *Partido Popular* had already won the local and regional elections in May and was in control of the majority of the town halls and of the governments of the 17 Autonomous Communities. Including the results of the elections to the Congress of Deputies and the Senate of 20 November 2011, the PP was able to concentrate political power as no other political party had managed in democratic Spain since the end of the Franco era. The socialists had only held on to power in Andalusia, their traditional stronghold. During the November elections, however, they were overtaken by the PP for the first time, which sent 33 deputies to Madrid compared to the PSOE’s 25. With the exception of Catalonia and the Basque Country, the *Partido Popular* had become Spain’s determining force.

HOW TO DEAL WITH A BURDENSOME LEGACY

After this success, Rajoy hoped to achieve the final breakthrough in the Andalusian regional elections in the spring of 2012. This was probably one reason he initially held back from predicting “atrocities”. But to no avail. The *Partido Socialista* remained in power in Andalusia, albeit without the absolute majority it had been accustomed to.

Rajoy’s credibility suffered when he announced drastic measures affecting taxes, pensions and the labour market not long after the elections. Although most had expected this and many considered the measures essential, people resented the fact that he was going back on his pre-election promise so quickly. His reputation as an upright Galician was damaged. Just six months after his triumphant election victory, 78 per cent of Spaniards stated that they had “no or little” confidence in him. The head of government has been low in the ratings in all opinion polls ever since where the reputation of the Spanish political elite is concerned.



Children in the outskirts of Madrid: In 2011, almost a quarter of all Spaniards lived below the poverty line – defined as 60 per cent of the average income. | Source: © Susana Vera, Reuters.

It has to be said that if asked personally any sensible person would have declined to accept the legacy that Rajoy and his government took on in the winter of 2011. Unemployment had risen to nearly five million, and a truly scandalous youth unemployment rate meant that almost every second young person under 26 had no career prospects. 21.8 per cent of Spanish people were living on less than the 60 per cent of average earnings that was defined as the poverty limit, particularly large numbers in Extremadura (38 per cent) and on the Canary Islands (31 per cent). And while Zapatero had inherited a budget surplus from his conservative predecessor Aznar back in 2004, the coffers were empty when Rajoy took over, Spain was heavily in debt and there was no further scope for measures to boost the economy.

On the very evening of election day, 20 November 2011, Mariano Rajoy therefore described what the main themes for the next few years would have to be: "Our enemies are unemployment, the budget deficit, excessive debt and economic stagnation." And he continued: "We will not cease to think of those who lost their jobs or did not find a way to enter the job market, those who were forced to close down their own business or give up their self-employed activities, those who have to live on a pension that hardly covers their basic needs, those who are ill or have other problems. We want to give the Spanish back their pride in being Spanish."

Those were aspirations that were easy to support considering how generalised they were. The majority of the Spanish also agreed that things could not go on as before. Particularly where the bloated public sector was concerned, 62 per cent of respondents stated that cuts were necessary and bearable, and in the Autonomous Communities as many as 68.9 per cent believed that things could not go on as they were.

However, an essential element for tackling the crisis was missing: the willingness of all political parties and social groups to work together to find comprehensive answers.

Overcoming the crisis in Spain requires shared efforts by the country's politicians, trade unions, employers and society's elite.

The dominance of the *Partido Popular* was so overwhelming that the coming together and closing of ranks would not materialise despite the dramatic situation particularly in the labour market. The debate was characterised by agonising mutual recriminations instead of the efforts of politicians, trade unions, employers and the social elite that were necessary for overcoming the crisis. Such efforts should have been preceded by the general acknowledgement that Spain's problems were to a large extent self-inflicted, the causes including the way the parties exert substantial influence over large parts of the economy and the financial market as well as the overextension of the public sector and the significant amount of redundancy in the public administration through parallel structures. However, when there is insufficient analysis and when problems are not spelt out, it becomes difficult to lead people on a course of reform that asks them to make sacrifices and concessions. Consequently, what was seized upon as an opportunity elsewhere did not materialise in Spain for a long time: the perception of the crisis as a chance to embrace joint responsibility.

Instead, the Spanish found that many of those who had been instrumental in causing the economic and financial crisis or – despite being in positions of responsibility – had done nothing to prevent it, were able to continue with their lives largely unaffected, while the weak and less privileged of all people often became the victims. As confirmed by OECD figures, Spain is thus among the European countries with the largest disparities between rich and poor.

REVITALISATION MEASURES

The reality of the situation came as a shock. For years, the Spanish had enjoyed a virtually unhindered construction boom as well as cheap loans, with which they could easily fulfil all manner of dreams. Politicians and the banks had led them to believe that the (borrowed) prosperity and *joie de vivre* would last forever. While banks had previously encouraged even people on a low income to ignore their (financial) limits, they were now sending their emissaries or even the police to clear the homes of those who could no longer pay the interest they owed.



Cranes on the roof of the former headquarters of the Spanish credit bank: The building will be converted into a five star hotel. In recent years, Spain has experienced an almost unchecked construction boom. | Source: © Susana Vera, Reuters.

It was, in fact, especially the regional *cajas*, semi-public savings banks, whose expansionist aspirations and risky lending had fuelled the economic and financial crisis in Spain. They symbolised a type of self-development that was unfettered by any rationality or monitoring and in which representatives from politics, business and the trade unions eagerly took part.

Consequently, revitalisation of the economy and job creation topped the Rajoy government's agenda. It has since addressed these goals very consistently, demonstrating the courage to make unpopular decisions.

The challenges were many and varied. Directly after taking over responsibility, Finance Minister Montoro, for instance, saw himself confronted by demands from national and international companies for the Spanish state to finally pay invoices, which had in some cases been outstanding for years, to give them back capital and the means to invest. 3,794,532 invoices from 29,107 suppliers totalling 17.7 billion euros were paid; most of them had been gathering dust in the offices of the Autonomous Communities.

In mid-2012, the government adopted a 35-point package of measures intended to generate 65 billion euros of savings, an ambitious and comprehensive undertaking. It included measures such as raising VAT from 18 to 21 per cent, abolishing the Christmas bonus for public servants and cutting the holiday entitlement and unemployment benefit after six months, lowering social security contributions, cutting party and trade union funding, abolishing tax relief on the purchase of residential property, harmonising the remuneration of mayors and town councillors at a local level, abolishing 30 per cent of town council posts, introducing a sustainability factor in social security and revising the early retirement regulations, conducting an integrated administration reform to save public funds, reducing or abolishing state-owned businesses at the local authority level, improving financial oversight, reforming the energy sector, creating a consistent framework for competition and competition rules in Spain, harmonising accreditations and certificates issued by public bodies, abolishing duplication of monitoring functions performed by administrative units, reform and liberalisation of the service sector, creating greater flexibility in commercial opening hours, liberalisation and privatisation of services in the railway sector and at ports and airports.

The major project of reforming the labour market also required courage and determination. The architects of the package of legislative measures put forward for this purpose realised that the benefits would not manifest overnight; on the contrary, greater flexibility, particularly less stringent protection against dismissal, would initially produce job losses. The protests by trade unions and by the opposition, who regularly called for large-scale countrywide demonstrations, therefore fell on fertile ground because the reforms did not immediately bring the results that people had expected them to yield. At 16.7 million, employment remained at the 2002 level, and although unemployment fell by 65,000 during the first year

Since the reform of the labor market did not yield immediate results, many Spaniards joined the protests of the trade unions and political opposition.

of reform, there was an even greater overall drop of 268,000 in the number of people employed. Most new jobs were temporary, while the number of permanent full-time jobs dropped steadily. In 1.6 million households, not a single family member was employed, and the number of long-term unemployed was rising. Labour market experts agreed: a solid reduction in unemployment could only be achieved with an economic growth rate exceeding two per cent.

FIRST SIGNS OF A TURNAROUND?

Against this backdrop, the months before the elections on 20 December of this year could indeed mark the beginning of a turnaround. The Spanish economy is experiencing growth exceeding three per cent, once again reaching the pre-crisis level for the first time. In July 2015, the Ministry of Employment and Social Security was able to announce that at 4,046,276 million unemployed, this key figure had dropped to the lowest level since 2010. In the second quarter of 2015 alone, 477,000 jobs had been created (+2.9 per cent), and in July, 1.8 million job contracts had been signed, a nine per cent year-on-year increase. The proportion of permanent jobs, however, was only 6.9 per cent. The OECD is therefore talking about a “dual job market”, with a (relatively low) proportion of permanent job contracts and a (relatively high) proportion of temporary contracts. Overall, the number of those employed and paying social insurance contributions increased to 17.3 million, a year-on-year increase of 3.4 per cent. “Record numbers” are also reported for new businesses, with a year-on-year rise by 9.6 per cent during the second quarter of 2015. The number of business closures went down by 27.1 per cent over the same period. There were 8,254 new businesses as opposed to 1,426 closures.

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One area where the situation remains totally unsatisfactory is that of youth unemployment. According to OECD figures, it will take a young person employed in Spain an average of six years before securing a permanent position. This compares to an average two years in Denmark. The measures to improve professional and vocational education and training have only shown signs of very modest initial improvements. The situation has further caused a general loss in confidence and optimism among the young. If they remain outside the labour market for too long, the education and training they have undergone ultimately become obsolete because of their lack of practical experience.

The Governor of the Spanish central bank believes that unemployment may decline further to 19.7 per cent by 2016 "if all indicators continue to remain positive". These do, however, include the currently low oil price and export revenues, which have been buoyed by strong demand in the emerging economies and a weak euro. There is no certainty that this situation will continue – considering the developments in China alone. The political crisis in Catalonia and the outcome of the December elections are also bound to have an impact on economic development.

The pension reform adopted in 2013 entailed first and foremost an increase in pension age to 67 and the decoupling of pensions from inflation. These measures are intended to produce savings of 33 billion euros by 2022. The intention is that the sustainability factor, which a commission of experts has set at a minimum of 0.25 per cent, should only be raised in years of economic prosperity. Taking stock for the first time since introducing the reforms, the government has found that the number of people retiring early has fallen by 6.5 per cent and that the average actual retirement age has increased to 64.3.

After Prime Minister Rajoy's government having raised over 50 tax rates in total since coming into office and with the top tax rate at 56 per cent, the 2015 tax reform is intended to stabilise the recovery and reduce the burden on businesses and private households. To this end, income tax rates are being revised, the lower rate being reduced to 15 per cent and the top rate to 45 per cent. As this is a shared tax, the Autonomous Communities will need to decide if and when they will fall in line. The competitiveness of businesses is being improved through a reduction in corporate tax from 30 to 25 per cent.

According to the OECD, there is also still substantial scope where tax collection is concerned. In this respect, Spain lags behind the EU average by two per cent. An expert report

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has estimated the Spanish black economy at 253 billion euros, which is almost a quarter of Spanish GDP. If this situation could be remedied, it would be possible to bring the Spanish budget deficit, which is still notoriously high, down below the agreed three per cent limit.

The government places great importance on reforming the public administration; this is a particularly complex and controversial project, even considering that most of those who will be involved in the implementation belong to the same party. But in view of the circumstances, this undertaking was absolutely necessary. Between 2007 and 2011, under the socialist predecessor government, the number of public sector employees had risen by 288,700. Since the Statutes of Autonomy had come into force in 1982, the number of jobs in the local authorities has quadrupled, that in the regional administrations had multiplied by a factor of 30. When the Rajoy government took office, close to 2.5 million Spaniards worked in the public sector, a quarter of them in public administration at various levels, the rest in the healthcare, education, justice and defence sectors. During Prime Minister Zapatero's term in office, the public employment rate rose from 38.4 to 47 per cent of GDP. What was even more significant, however, was the fact that Spanish citizens no longer knew who was responsible for what and that political control was lost in a chaos of overlapping powers.

In parallel with the major domestic reforming endeavours, Rajoy wanted to win back the world's respect and esteem for his country. It was very hard for the proud Spanish people to see the damage done by the crisis to a country that was once the fourth largest economy in the *Champions League* of European nations and to envisage losing face and prestige in the eyes of the growth regions of Latin America, former colonies and long-term trading partners. Respect and esteem, which the Spanish had always taken for granted, had increasingly given way to a loss of influence.

Rajoy found himself caught between mounting conflicts within the country and a threatening loss of influence abroad. Consequently, integration with Europe and consensus on the reforming efforts were essential to him. He had this to say on the matter: "We will ensure that Spain's voice will once again gain greater respect. We will be the most loyal, but also the most demanding of the EU member states, the most compliant and the most vigilant. We will no longer be the problem, but part of the solution."

The process of *greater integration* in Europe, which Rajoy has called for, has begun in his own country with the willingness to engage in greater transparency vis-à-vis the European institutions and a debate – not popular in this particular case – about what a eurozone member state in a precarious budgetary situation can

afford. Spain has begun to learn that a loss of sovereignty may be the price to pay for the European solidarity it demands.



Harbor in Jaraguá do Sul, Brasil: It was unbearable for the Spanish to see their reputation and weight in the growth regions of Latin America threatened in the context of the crisis. | Source: © Reuters.

The process did not run smoothly. When the International Monetary Fund called upon the Rajoy government to take further steps to consolidate the budget while praising the reform packages adopted to date, the head of government responded by saying that what Europe needed now was “policies rather than directives”.

In the public debate, there were growing indications of nationalist sentiments and increasing criticism particularly of the German stance, which was perceived as being rigid and inflexible. Europe, the argument went, needed Spain at least as much as Spain needed Europe. The “external” assistance that was being sought was ultimately self-help on the part of Europeans and it was therefore appropriate for Spain to claim it. Upon publication of his memoirs, Spain’s former head of government Zapatero boasted that he had not given in to Chancellor Merkel’s urging for him to seek financial assistance.

When it became obvious that Spain would not be able to cope without a bailout package, at least where the consolidation of the banks was concerned, efforts were made to achieve a “bailout without humiliation”. Consequently, Prime Minister Rajoy and

Minister of Economic Affairs de Guindos sold the bank bailout of up to 100 billion euros, which was finally agreed, as the result of their negotiating skills, which had prevented a “submission” such as that suffered by Greece, Ireland and Portugal. This did not make communication with the electorate any easier for Enda Kenny in Ireland and for Pedro Passos Coelho; the only counterargument they could put forward was that they had voluntarily adopted the reform agenda agreed with the troika based on their own insights.

However, by the time the EU finance ministers found that the program of funding provided through the EFSF in July 2012 to bail out the banks had come to an end already by mid-November 2013, Spain had only needed to claim some 40 billion of the available total funds. In the meantime, the Madrid government had made significant efforts to reform the Spanish finance sector. Savings banks were wound up or merged, one *bad bank* now administers toxic (property) securities, the supervisory bodies of the Spanish central bank have been strengthened, and best-practice rules have been put in place. Regional politicians have lost their influence over the way the savings banks are run, and legal proceedings have been initiated against some former supervisory board members.

INTERNAL SECURITY AND MIGRATION

The attacks in Paris have brought back memories of the terror attack in Madrid, which took the lives of 191 people and left over 1,800 injured on the morning of 11 March 2004, three days before the parliamentary elections in Spain. Initially, it was blamed on the Basque organisation ETA; it was subsequently attributed to a group affiliated with Al Qaeda and associated with the Spanish involvement in the Iraq war. Since the attack, the Spanish security services have been successful in foiling a number of attacks, partly in close cooperation with their European and international partners.

They further make a frequently undervalued contribution to securing the external European borders. This includes not only measures for border security and border control but also, importantly, a repatriation agreement with Morocco, which has greatly lessened the appeal of this route to Europe. The agreement also covers the deportation of “undocumented” migrants, whose identity and country of origin cannot be determined.

Spain has maintained its liberal stance towards legal immigration, which is relatively generous by comparison with other countries, largely unchanged even during the times of the economic crisis. There are currently some 4.5 million foreigners living in the country, with Romanians representing the largest group (15.9 per cent), followed by Moroccans (15.4 per cent) and British (6.8 per cent). Many immigrants from Latin America, on the other hand, left the country again during the crisis years since 2009.

By 2012, illegal immigrants had also been granted free access to the Spanish healthcare system. This access was restricted by the Rajoy government, but has since been reintroduced even by regional governments controlled by the PP. According to Amnesty International, this applies to some 750,000 people without a residence permit.

Spain is one of the EU member states that had initially rejected a distribution key for refugees, as was proposed by the EU Commission in mid-2015. This was due to the fact that, from the Spanish perspective, the ten per cent weighting given to the level of unemployment in a member state was clearly too low. But the government now supports the agreed compromise.

One point worth stressing is that the general stance of the Spanish people towards immigrants has hardly changed even with the crisis affecting the job market. None of the traditional parties or the newly founded ones is advocating xenophobic positions or opposing further immigration.

CONCLUSION: OUT OF INTENSIVE CARE

Today, just four years on, Spain presents a different picture in many respects. And the government has contributed significantly to this. Leaving politics to one side, the small and medium-sized businesses in particular have regained courage and are instrumental in helping the country to get back on an even keel. Together with the Spanish corporations operating worldwide, they have become the symbol of a country that has emerged from intensive care.

The crisis has shown that one pillar of society has stood the test of time: family cohesion and solidarity. Families helped to alleviate misery and despair, organised assistance for relatives who were out of work and in need, gave a home and hope to young people without prospects.

King Carlos' abdication was a consequence of the public's frustration over corruption and the abuse of political and economic power in Spain.

It was families that provided help when the economic crisis turned into a social crisis, with deep cuts in the social sector, from education to healthcare. While people of course directed their outrage at the government, they also blamed almost to the same extent the "1978 regime", the elites in political parties, business, trade unions, the media and the Churches, who had determined the country's direction since the transition. Growing numbers of people within society felt that those elites had abandoned them. The anger about that, about corruption and the way the elites seized the instruments of governmental and economic power mobilised entire swathes of the population. The *indignados* (outraged) and the *15M* (15 May) movement as well as the Podemos and Ciudadanos parties later on are manifestations of the longing for regeneration and political change. Juan Carlos' abdication in June last year was offered not least in response to this mood in the country.

Whatever the verdict on the individual new political parties and groupings will turn out to be, they have helped to give people who had previously lost faith in their political representatives the feeling that they are represented once again. The last few elections, from the European elections to the regional and local elections, have since placed many people in positions of responsibility who were not prepared for it and whose only previous political experience had been their involvement in a protest movement. They will now have to pass the political acid test.

While the focus is currently on the competition between old and new parties, the political landscape could soon be determined more strongly by issues and individuals once again, assuming that the PP and the PSOE have learnt from the experiences of the last few years. A new political climate of joint responsibility may then emerge, an essential prerequisite for tackling the largest of the remaining political challenges: ending the conflict in and with Catalonia. This conflict has long moved beyond any political rationale and will only produce losers if it continues to be conducted in the same manner.

The overdue turnaround will require a rethink of Spain's institutional structures and an answer to the question of whether the 1978 constitution, which has only undergone two changes since, can provide the answers for the 21st century as well in its present form. There is no lack of expertise and ideas. It is incumbent upon

those holding political responsibility to demonstrate the will and skills required to conduct the necessary discourse. Should this discourse prove successful, it could become a symbol of a new understanding of responsibility for Spain and Europe.