Europe in the World economic crisis: comeback of Keynesian politics or launching of a "financial coup d'état"

A view on Spain's current state and policies

Happy families are all alike; every unhappy family is unhappy in its own way.
Leo Tolstoy, Anna Karenina.

1.

In 1971 Ernest Mandel wrote that 'growth in the Spanish economy shows a peculiarly jerky behaviour. Each episode of internal expansion translates into accelerated inflation and a growing trade balance deficit. Any temporary difficulty in the imperialist international economy immediately reduces the external resources that should reabsorb these unbalances'[1].

President Zapatero, who obviously has not read Mandel, stated at the beginning of a conference attended by the Presidents of the Autonomous Regions last December that 'Spanish economy has been enjoying an enduring wave of growth for fifteen years until the world crisis came to bring it to an end'. His speech reflects the sort of wishful thinking inspiring Spanish economic policies up to date: 'our banking supervisory system is an example to the world', 'it is not a real estate bubble but only an increase in wealth out of the sheer success of Spanish economy', …; such has been the official way of thinking.

The real fact is that the Spanish growth mirage relied on an extraordinary injection of finance provided by European investors buying bonds and other debt instruments issued by Spanish Banks. The total foreign financing to the Spanish credit system is outrageous: EUR 768 billion[2], which adds up to 40% of the whole system's total liabilities. If you take a look at the left-hand side of the balance you can see that mortgages amounts more or less to the same proportions[3]. This financing fuelled the bubble and brought in the surge in growth, consumption and employment.

Since the break out of the international crisis the subsequent credit crunch disclosed a pressing problem. The maturity of the IOUs issued by Spanish banks is much shorter that that of the assets they back[4], most of them mortgages and loans to developers which in turn are expected to become mortgages. So now Spanish banks have got a serious problem to revolve all this debt. Even if it is true that the tough regulations of the Bank of Spain have safeguarded the nominal ratios of solvency, as the Spanish Government boasts. In fact this only means that Spanish banks have had to make higher provisions in past times than their counterparts but now they are much more heavily exposed to financial risk provoked by the mismatching between the maturity of their assets and that of their financing sources.

In fact Spain's economy was deemed to come to a stop anyway because indebtedness was reaching a peak by the end of 2006. House prices had been rising well over 10% per annum during several years so they had to halt sooner o later. Spanish Government

---

[1] 'Le crépuscle du franquisme'. Quatrième Internationale, janv. 1971. Translation is mine.
[2] Source: Bank of Spain. http://tinyurl.com/deudaexterna09.
[3] Plus other EUR 459 billion lent to developers and builders.
[4] The average maturity is between 6 and 7 years for bonds and other assets issued amounting to 60% of the foreign financing. Since 2007 (see later) this maturity has dramatically been reduced due to the use of 'liquidity facilities' issued by both the Spanish Treasury and the ECB.

pretended to expect a "soft landing", but landing in any case. This can easily be seen in the decline of the rate of increase in lending since 2006 previous to the first burst of the crisis which took place in mid-2007. The rate for real estate purposes stabilized by the first quarter of 2006 and began to decelerate by the end of that same year. Spain would have got into troubles even if the international crisis had not arisen. As has happened in previous episodes, the financial bubble would have moved to other place leaving Spain to pay for its own excesses. Zapatero fully misses the point. Decay began before the collapse of Wall Street. The international crisis only made things worse.

The chain of events has gone more or less like this: the original subprime crisis did not at first affect Spanish banks who had got enthusiastically engaged in securitisation but were not allowed by the Bank of Spain to write off the original mortgages from their balance sheets and thus could not afford to buy toxic foreign assets[5]. But when their lenders became affected (German, French, and other European Banks) they found that the inevitable source of financing was clogged. This caused a major stroke to the whole credit system. Credit suddenly stopped.

The results are well known: a dramatic rise in unemployment, ten points between the third quarter of 2007 and 2009; a four percent decay in GNP and a rise in public accounts imbalance which has passed from a small surplus in 2007 to a near 8% deficit by the end of 2009.

2.

When writing these lines Joaquin Almunia, appointed Commissioner for Competition, has just said at the hearings held at the European Parliament that fiscal measures taken within the UE should be removed by the end of 2010, except for Bank support which may require a 'more flexible framework'. This statement is highly significant. What does it mean if Spanish financial sector is sale and sound? Why is the need for flexibility?

The measures adopted so far by the Spanish State to protect the financial system add up to EUR 88 billion since October. Remarkably enough this is only one half of the total amount approved. This compares to the aid provided to 'real economy' which amounts to slightly more than EUR 16 billion and has been already spent or will be spent for sure.

Apart from this, Spanish banks and 'cajas' (Savings Banks) have relied heavily on the 'liquidity facility' provided by the ECB. The outstanding debt amounted to almost EUR 80 billion by past November. In fact, the ECB was scolded by British and other European financial institutions as soon as the beginning of 2008 because of the 'silent bail-out of the Spanish banks' it was performing.

In fact the emergency financial facilities provided by the Spanish Treasury and the ECB to keep credit flowing have been hoarded to provide for maturing instalments[6]. Ironically the credit provided by the official finance agency, ICO (Instituto de Crédito Oficial) which was initially funded with EUR 28.9 billion has been used up only a scarce 55%. These funds are intended to be channelled to private companies and SMEs through banks and 'Cajas'. Banks admit that they haven't been able to provide all this credit but they justify themselves saying that there is not demand. Which is true by the

---

[5] Although some Banks and private large investors were caught in the Madoff affaire whose 'products' were marketed in Spain by Banco de Santander.

[6] Estimated instalments amount to EUR 76 bn in 2010, EUR 62 bn in 2011 and EUR 100 bn in 2012. Source: Moody's.

way. To add insult to injury a large part of the funds raised form the liquidtiy facilities are invested in short-term accounts within the ECB.

Thanks to all this, big finance in Spain enjoys a privileged situation today. Following BIS[7] the five larger Spanish banks ranked in 2008 among the most profitable in the advanced countries and the two largest, Santander and BBVA, have reported only slight falls during 2009 (2.8% and 7.2% respectively in the third quarter).

This is not the case for a second-echelon of financial institutions, the small and medium sized 'cajas'. Savings Banks in Spain amount for half the financial sector and they have got a special status[8] which puts them largely under control by local and regional governments although in an 'un-holy alliance' with a bureaucratic professional caste of managers drawn from private banks. These institutions are the most affected by the risk of default of loans originated in the housing sector due to their enthusiastic embracing of the housing boom. The solution devised by the Bank of Spain for these 'cajas' is merging with each other as a precondition to be eligible for the FROB (Fund for Bank restructuring). This is a highly political issue in Spain because although it stays short of direct privatization, as desired by big finance, it will reduce the public control over these institutions as the territorial composition becomes diluted.

The second problem, affecting both small and large institutions is that the whole Spanish banking system will have to repay EUR 240 billion in the next three years while the rate of default is expected to rise up to 8% by the end of the year from a current 5%. Banks are already demanding to be allowed to do some financial make-up concerning assets valuation, in particular land and buildings they are swapping for bad loans to developers. Probably the income statements of a large number of institutions will go into the red for 2010. A large restructuring is foreseeable in the next years.

The last time we had a large restructuring many little 'cajas' were forced to merge but respecting territorial limits. Public banks disappeared. And private banks were subject to an intense concentration process. Santander and BBVA emerged as global players from that restructuring. The first one, formerly a family-run medium sized bank acquired Banesto and became the largest bank in Spain. The second one evolved from a regional (Basque) based bank to a large one through mergers and acquisitions including former public banks and the Post Office Savings Bank.

3.

When newly elected President Obama praised Spain's achievements in high-speed rail transport and wind power generators as an example of what could be done to 'green' the economy, Zapatero almost got crazy. These days we are being overwhelmed with propaganda around the so called 'Law of Sustainable Economy'. This star project of the President is presented as the miraculous spell which will bring about the much needed 'change of model' which will release us form our dependency on brick-and-mortar and launch us to the Champions League of international competitiveness and the knowledge-based economy.

A careful scrutiny of the proposed law brings out that is just a new round of liberalization, privatization and market-enhancing measures with some green strokes pursuing very modest targets in carbon emissions reduction. In fact it is an implementation of the National Plan of Reforms which on its part is nothing else but the transposition of the discredited Lisbon Strategy. In these days that neoliberals have

[7] http://tinyurl.com/bisinformeanual
[8] http://tinyurl.com/steinko

converted to full fledged interventionism only coherent social-liberals remain faithful believers in the virtues of market competition and dare to shrine it on the same level than environmental sustainability!

At the same time, public spending in R&D has been cut down by 30%, VAT rates have been shifted and public infrastructures have been opened to so-called private-public partnership. A new labour 'reform' is being thought of to overcome the 'excessive rigidities' in labour markets. It will be the twelfth in thirty years. Ironically the cause this time is to reduce extreme precariousness affecting more than one third of the labour force. The magic word now is the 'single contract' which will lower the compensation paid to workers who get laid-off in exchange for the right of all workers to this compensation. Other proposed reform is the popularly known as 'German system' in which workers are engaged partially at work and get paid a small unemployment benefit instead of the current system, the ERE, which consists in being temporarily laid-off accruing unemployment benefits during that time. These are sensible issues because the Government endears very much its relations with the Unions so it is walking on thin ice here.

Anyway the Unions' mood is not very combative as shown by the dismal spirits they exhibited when it came to call a nation-wide demonstration past December in Madrid. In fact, the much longed for mobilization was a mere formality aimed at showing the more disgruntled sectors that the 'objective conditions' were not in place. On the other hand the political and social Right are growing more aggressive by the day which makes the Unions' leadership very scared. Polls state that there is a growing gap favouring the Right over the Socialist Party, and IU although seems to have stop its decline does not take-off.

Faced to this situation, Zapatero's hopes lay in European recovery being able to pull Spain out of recession before the next elections take place in 2012. Since Spain holds now the Presidency of the EU he has asked for greater 'policy coordination' at the EU level hoping for some kind of EU-wide program which could serve as a lifeboat. This is what came out of a meeting he called some days ago with Jacques Delors, Felipe Gonzalez and Pedro Solbes. This 'committee of wise men' has been created to assist Zapatero during the Spanish term and is clearly aligned with the 'federalist' social-liberal point of view being Delors the extreme-left representative.

But all the same this is wishful thinking at least for the moment as German Governement immediately has reacted denying any possibility that the EU could forcefully enact any macro-coordination. It is a matter of opportunity but also of choice. But even in the improbable case that any program of this sort was launched the problems of Spanish economic structure will only aggravate even if there was some transitory relief as it did during the years of accession.

4.

The Euromemorandum 2008/09[9] states that 'the financial crisis and the EU's own Lisbon strategy together form a hybrid which is particularly explosive and highly dangerous for economic development and social cohesion.' This is even more true in the Spanish case.

There are two major reasons for this. The first one is the persistence of the hegemonic role of the banking sector within Spanish capitalism which has historical roots. The

[9] http://tinyurl.com/yj26thc

second one, connected to this, is the current division of labour in the EU and the absence of industrial policies aiming to correct the unbalances this causes.

Financial deregulation and the progressive reduction of public debt triggered the access of the Spanish financial sector to the global casino. A successful access as Spanish banks rank at the top by profitability and increasingly by size alien to any proportion to the size of Spanish real economy. The accession to the EC did not substantially alter the hegemony of this sector. In fact, most of Spanish privatized public companies were given to this higher echelon of 'ugly' capitalism thus compensating whatever losses experimented through industrial restructuring. Spanish banks had traditionally owned the electricity sector and the civil engineering and building big companies. Now they also own - or share with European groups - all the former public companies.

After exhausting the chances brought by an unprecedented expansion of the banks and their privatised utilities in Latin America, the Spanish big finance turned to a historically recurrent vein: the domestic housing-sector. Profits and savings from EU countries holding trade surpluses flowed into Spain. Low interest rates and the vanishing of currency risk with the euro fuelled the irrational surge in housing. This veiled the deficiencies of the manufacturing sector, the decline of agriculture and the precariousness of services. It even gave rise to a massive entrance of migrants who now account for 10% of the population starting from nil a decade ago.

This particular configuration justifies the sensitivity of Spanish economy to international conjuncture. And explains why it overreacts to any change as Ernest Mandel already detected in the early seventies (see above). Spanish economy is highly dependent on the environment in a very passive way. Joining the EU and the euro has worsened this structural characteristic.

The only way out would be a shift in the productive model towards real social needs, richer and more creative jobs and more resilient local economic closed-loop cycles. But this collides both with the hegemony of the traditional ruling classes led by big finance in Spain and with the division of labour in the EU. Both are highly political issues for obvious reasons and are inextricably mixed. Otherwise one could not explain the smooth way oligarchies inherited from Spanish fascism have found their place among the elites of the countries who appear as the champions of European democracy.

The dream of social-liberals is that of a sort of neo-Keynesian EU with free markets on one side and a reasonable welfare state on the other, supported on a real European fiscal policy and a substantial budget to provide for social and territorial balance. But this is a wild dream with the current balance of forces and original design of the European integration as shown by Bellofiore and Halevi[10]. Conservatives and practical neo-liberals – we are not speaking of academics – support the other way round: ruthless intervention in the economy when needed but hands out of social provisioning. Why should the left refrain itself to distributional socialism? Why must we take the place left by the social-democrats for good?

It seems to me that the lack of attention we pay to the way the geographical division of labour and neo-mercantilism is determining the real process of building Europe is a serious handicap to arrive to a common left position continent-wide. As in the quotation

[10] 'Is the European Union Keynesian-able? A sceptical view'. Riccardo Bellofiore and Joseph Halevi. In 'European Economic Policies. Alternatives to Orthodox Analysis and Policy Concepts'. Eckhard Hein, Arne Heise, Achim Truger (Hg.). Metropolis, 2006.

by Tolstoi , unless we don’t begin to feel and take into account the different ways reality unfolds among us we will remain being separate families.

It is disheartening to look into the Euromemorandum 2009/10 for industrial policies (in the wide sense) and to find only a couple of lines and in the context of job creation. Well, I’m glad it appears for the first time, but it is not enough. We – the heirs of an tradition that understands work as the relation of mankind with nature – must say something on how to provide for social needs and how to grant to everyone a decent and humane way to take part in social reproduction. We cannot limit ourselves to tax and distribute. It is a major challenge now when capitalism appears to have exhausted all its historical progressive potential an remains only as a murderous whirlwind.

Javier Navascués

FIM.Transform!