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Recovery planning in the age of Pandemic Politics: Can you handle the truth (debt), Mr. Sánchez?

May 15, 2020

Spanish politics are currently driven by the age of pandemic politics. As a result of the current political situation, one could argue that Spain's recovery will be necessarily painful. The Spanish Congress this week held the first Committee meeting for Social and Economic Reconstruction, which will work on a recovery plan for the Spanish economy.

This Committee has been the result of a weak 'entente' between the two main Spanish political parties, the governing PSOE (Social democrats) and the main opposition Popular Party (Conservative). President Sánchez will use this Committee as a platform to boost the government programme, but the question is: will he be able to do so?

The politics of the recovery plan –What does it look like?

The Committee for the Social and Economic Reconstruction reveals a very profound shift that is taking place recently in the national political landscape. At the last parliamentary vote to extend the state of alarm, President Sánchez reached an agreement with Ciudadanos (Liberals), to exchange support for increasing coordination, while the Popular Party shifted its support towards abstention. Ciudadanos, who recently elected a new party leader following the defeat at the last November general election, wants to depart from the 'fierce opposition' bloc and play a more influential role in the government's policymaking.

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The move has been welcomed by some within the PSOE and the business community, as Ciudadanos could act as a counterbalance to the influence that the coalition's junior partner, Unidas Podemos (far left), could have in the recovery planning. However, this move entails risks for the PSOE, as its parliamentary majority would still rely on the Basque nationalist and Catalan independentist parties that supported the investiture of Sánchez, who are antagonistic towards Ciudadanos, a party that built past electoral success on fierce opposition to Catalan independentism.

Despite the Committee being a concession from the government to opposition parties in exchange for the parliamentary support needed to maintain the state of alarm, it has been born amid controversy. On the one hand, the coalition government parties and others such as Ciudadanos support fast-track proceedings in order to be ready to release a concluding report by the end of June. On the other, the Popular Party and far-right wing party Vox, would like to see the committee's works last much longer and shift its focus from the reconstruction planning to evaluating how the pandemic has been handled by the government since early March. However, President Sánchez knows that without some kind of agreement with the Popular Party, any reconstruction plan will lack credibility.

Will the plan work?...

The biggest risk currently facing President Sánchez is a scenario with a delayed recovery, spiraling debt and record unemployment numbers that leads its government to face a restructuring programme overseen by its creditors. This is the underlying reason that Economy Minister, Nadia Calviño, insisted this week in a Bloomberg interview on asking for a EU common recovery fund to rebuild the bloc's economies and for this fund to award grants, not loans, in order to prevent that the worst-hit southern countries come out of the crisis in a weaker position in relation to better-off member states. The last time a Socialist government was forced to undertake cuts in order to control the fiscal deficit (President Zapatero's decision to change Spain's constitution to introduce a

budget deficit cap in 2011) this was followed by a landslide victory by the conservatives in the 2011 general election, thanks in part to abstention from left-wing voters.

In order to avoid this, President Sánchez announced last Saturday that he wants the Committee for Social and Economic Reconstruction to focus on the four main areas of the government programme: a tax reform, a labor reform, the ecological transition and digital transformation of the economy, and increased spending on education and innovation. What this means is that President Sánchez is not ready to change plans and give up the agreement reached with Podemos last January that permitted his investiture as president. Mr. Sánchez, whose political memoirs released last year were titled 'Manual de resistencia' ('The handbook of endurance') wants to stick to plan A and does not even consider a plan B as a result of the pandemic.

The Spanish government strongly supports a green and ambitious recovery position. Ever since the PSOE came back to office in 2018, Spain has been seeking a leading international role in climate change, which was demonstrated last year when the country offered to host the COP25 – which was finally held in Madrid in December 2019 – after Chile had to withdraw due to social unrest. More recently, Spain was among the twelve EU countries that in early March urged the European Commission to adopt a more ambitious climate action commitment by 2030. Now, Ecological Transition Minister Teresa Ribera has been entrusted by President Sánchez with the coordination of the de-escalation plan.

Moreover, despite the fact that the government focus has been on the Covid-19 response in the last month and a half, some key policy making initiatives within the ecological transition field have continued during the state of alarm period, such as the submission to public consultation of the National Plan of Adaptation to Climate Change (PNACC) for the period 2021-2030, part of the government's strategic framework for energy and climate, and the Packaging and Packaging Waste Directive transposition, due in principle by July 2020.

The key question that remains, is how is Spain going to increase higher government spending with a drop in economic activity (the current government forecast is a 9.2% drop while some analysts have pointed to a worst-case scenario of a 20% GDP contraction) and debt-to-GDP ratio reaching 115% (current government estimate), an all-time high. Similar to many other governments around the world, the Spanish government has already started to mobilize a €200 billion rescue package, mainly through a public

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guarantee scheme to ensure that liquidity continues to reach SMEs and self-employed workers. In addition, the government has successfully reached agreements with the main trade unions and employers' organizations in order to support business through temporary layoff schemes – with the government bearing most of the cost. Most significantly, plans have already been laid out for a universal basic income, which will be passed in the next few weeks.

Also, on the tax reform front, the state of alarm has so far wiped out some of the tax plans that the coalition government had designed to implement imminently. For instance, the Ministry of Finance has been forced to put on standby the proceedings to pass a tax on air tickets and another on single use plastics, as well as a tax increase on diesel. Both the aviation and plastics taxes were in an early phase and had been placed under public consultation just before the Covid-19 outbreak. On the contrary, the government is pushing a 3% levy on revenues obtained in Spain by digital companies with an overall turnover of more than 750 million euros and more than 3 million euros in Spain (the so-called 'Google tax'). Despite the opposition from centre-right parties and previous statements by Minister Calviño saying that Spain would follow OECD and EU guidance, the government now seems to be willing to pass such a levy as soon as possible.

...Maybe, but no so far!

Despite all the talk about recovery planning, Spain still lacks a clear short-term plan that paves the way for a swift recovery of economic activity in key sectors for the national economy, such as tourism and hospitality, airlines, the automotive industry and high street retail. Tourism alone accounted for almost 15% of Spain's GDP in 2018 and the current season will be lost if a quarantine is imposed on

incoming travelers. Therefore, the roadmap outlined this week by the European Commission regarding the resumption of tourism in the European Union should be an indicator that some answers may start to come from Brussels.

The government is betting on recovery kick-starting in the second half of this year and a strong rebound of the economy in 2021. Even though current funding conditions for the country are positive, it is understood that whatever the scenario, Spain will need EU funding in order to come out of the crisis as soon as possible. Hence, Spain's proposal at the last EU summit for a mutualisation of spending through a €1.5 trillion coronavirus recovery fund financed through perpetual EU debt.

However, in order to do that, Spain will have to persuade its European partners. Indeed, increasing its EU influence has been a key focus for President Sánchez since he took office and, following last year's electoral cycle, the appointment of PSOE veteran Josep Borrell as High Representative of the Union for Foreign Affairs and Security Policy was a foreign policy success, while the PSOE consolidated its position as the largest national party within the Social & Democrats group in the European Parliament.

José Ortega y Gasset, Spain's most renowned 20th century thinker, once famously stated that "Spain is the problem, Europe is the solution". President Sánchez could well be thinking the same as he attempts to convince his European counterparts of the need for debt mutualization. The final question is whether the support of the EU may entitle conditions or covenants. If so, how much political credit will Sanchez lose regarding his time remaining in office. Perhaps we could be facing a new election in 2021.

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