

## Spain

### Deadlocked

- Spanish political parties are still struggling to form a new government nearly three months after the general elections.
- None of the traditional parties – the conservative People’s Party nor the Socialist PSOE – managed to obtain enough congressional seats to form a government on their own. Podemos and Ciudadanos both lack the means on their own to break the stalemate between the main two parties.
- Only a “grand coalition” would benefit a majority of seats in the Congress of Deputies. Yet the parties are finding it difficult to reach any agreement.
- New elections will be held in late June if Congress fails to elect a new president by May 2<sup>nd</sup>.

Spanish political parties are still struggling to form a new government nearly three months after the general elections. The political landscape is fragmented and several points of disagreement are hampering negotiations. The PSOE and Ciudadanos are firmly attached to Spanish unity and have been unable to reach an understanding with Podemos on the Catalonia question. The political parties now have until May 2<sup>nd</sup> to reach an agreement and elect a new head of government. If they fail to do so, new elections will be called in late June.

#### Impossible to reach an agreement

Despite winning the general elections, none of the traditional parties – the conservative People’s Party (PP) nor the Spanish Socialist Workers’ Party (PSOE) – obtained enough seats in the Congress of Deputies to form a government on their own. Having won 28.7% and 22% of the popular vote in the 20 December elections, they hold only 123 and 90 seats, respectively, out of a total of 350 (see chart 1). The radical left-wing alliance Podemos<sup>1</sup> and the centre right Ciudadanos hold 69 and 40 seats, respectively, in the Congress of Deputies<sup>2</sup>, which means neither of them has the power alone to break the deadlock between the main two parties. Only a “grand coalition” comprised of more than two parties would be able to reach a majority of congressional seats and to elect a new President of Government.

Yet the diverse political parties are finding it difficult to reach any sort of agreement. Mariano Rajoy, the incumbent PP prime minister, turned down King Felipe VI’s request to form a government due to the lack of support from other parties. The Social leader Pedro Sanchez accepted the challenge in early February, but failed to obtain a qualified majority in the Congress of Deputies on the first round of voting for investiture on March 2<sup>nd</sup>, and even a simple

<sup>1</sup> The alliance is comprised of the Catalan coalition “En Comú Podem” (12 seats), the Valencian Community “Compromís-Podemos-Ès el moment” (9 seats) and the Galician contingent “En Marea” (6 seats).

<sup>2</sup> Podemos and Ciudadanos obtained 20.7% and 13.9%, respectively, of the popular vote.

#### An elusive majority

Number of seats in the Congress of Deputies

■ PP; ■ PSOE; ■ Podemos Alliance; ■ Ciudadanos; ■ Others

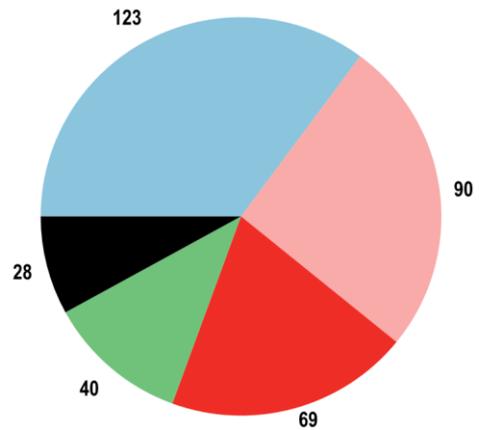


Chart 1

Source: Spanish Interior Ministry

majority in the second round of voting on March 4<sup>th</sup><sup>3</sup>. The PSOE hoped to win the backing of Podemos and Ciudadanos, but only the later provided its support. For the moment, Podemos refuses to join forces with Ciudadanos, which is situated at the other end of the political spectrum. It also disagrees with PSOE and Ciudadanos concerning the best approach to take concerning Catalonia. Although the radical left party is opposed to the region’s independence, it nonetheless wants to hold a self-determination referendum, an idea the PSOE and Ciudadanos refuse to go along with.

#### Heading towards new elections

The PSOE now has until May 2<sup>nd</sup> to reach an agreement with the diverse parties. Parliament has two months after the first investiture vote to elect a president. If it fails to do so, early elections will be called in late June<sup>4</sup>.

The PSOE has few options. It seems highly unlikely that the Socialist Party and Ciudadanos, which are firmly attached to Spanish unity, will manage to reach an agreement with Podemos on the Catalonia question. A “grand coalition” of the left-wing parties seems even less likely. To win a majority of seats, the PSOE must forge an alliance with Podemos and some of the other smaller parties, including a group of Basque nationalists.

A coalition between the PP, Ciudadanos and PSOE does not seem very feasible either. Mariano Rajoy would have to renounce his post as Prime Minister. The incumbent Prime Minister’s image has been tainted by major corruption scandals implicating certain members of his party. Yet, Mr. Rajoy has ruled out this possibility for the moment.

<sup>3</sup> An absolute majority is necessary during the first round of voting. For a simple majority, only votes cast are taken into count.

<sup>4</sup> If necessary, elections would be held on 26 June.

Moreover, the old guard would have little to gain from such a coalition. In December's elections, Spanish voters clearly showed they wanted to bring an end to the 2-party system. It would be a particularly risky gambit for the Socialist party, since left-wing voters could turn even more massively towards Podemos if the PSOE were to throw its support behind the PP.

### An inextricable situation?

Spain is not very accustomed to this kind of wheeling and dealing. For more than 30 years, political power has alternated between the PSOE and PP. Yet holding new elections is not really in the best interest of the various parties either. By showing that it was willing to compromise with the other parties, Ciudadanos has gained some ground in recent polls, but new elections are unlikely to change the current configuration in the Congress of Deputies (see chart 2). Spain would find itself in another impasse, unless the political parties manage to convince their voters that they have no choice but to make greater concessions after the new elections. In that case, Podemos might abstain from the second round of voting and let the PSOE govern with the centre party. Or Mariano Rajoy could renounce the post of Prime Minister in favour of another PP member, in order to form a coalition comprised of the PP, PSOE and Ciudadanos.

### Austerity to be eased soon

Some questions have been raised about Spain's economic policy. Public finance policy in particular is uncertain. In recent years, Spain managed to significantly reduce its public deficit. The budget deficit could narrow to 4.8% of GDP in 2015 after peaking at 10.4% in 2012. This improvement is the fruit of drastic austerity measures maintained through 2014. The structural deficit<sup>5</sup> narrowed from -7.1% of GDP in 2010 to -1.7% in 2014. The country then benefited from the rebound in growth and the decline in the unemployment rate in particular, in order to clean up public finances. After economic activity contracted by more than 9% between spring 2008 and 2013, the country reported its second consecutive year of GDP growth in 2015 (+3.2%, after +1.4% in 2014). At the same time, the unemployment rate has declined by more than 5 points since early 2013, to 21% in Q4 2015.

Yet public deficit reduction could proceed at a slower pace. Ongoing growth (+2.6% in 2016) will provide the new government with some manoeuvring room, but it will apparently have to make some compromises with all of the parties and to scale back austerity efforts. The PSOE would like to reduce the public deficit to slightly below 3% of GDP in 2017, instead of the 1.4% called for in the stability programme submitted to the European Commission in 2015. In that case, public debt reduction targets would also be called into question (99.3% of GDP in 2014) (see chart 3).

While trying to meet the Spanish people's expectations, the new government will also have to strive not to undermine the credibility of the fiscal adjustment process, which could result in higher government bond yields.

<sup>5</sup> I.e. the structural balance that would have been reached if GDP were at its long-term growth rate, adjusted for exceptional measures.

### A sparse political landscape

2-week average of voting intentions obtained from several polling institutions (%)



Chart 2

Source: BNP Paribas

### Persistently high public debt

% of GDP

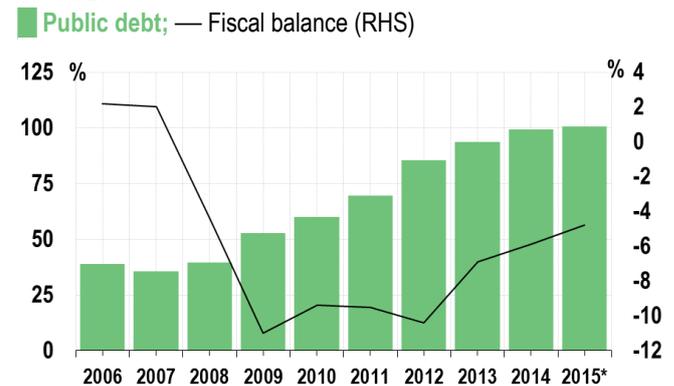


Chart 3

Source: Ameco  
\* BNP Paribas forecast