Zapatero asks for funds while claiming Spain needs no bailout

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This week Spain's Socialist Party (PSOE) Prime Minister José Luis Zapatero visited the Far East pleading for funds. His visit comes just after a similar tour of the Middle East in March.

Following meetings with Chinese Premier Wen Jiabao, Zapatero dismissed the possibility of the Spanish government defaulting on its debt and needing a bailout. "It is the consensus among analysts that as Portugal has requested a bailout, risk associated with the euro-zone sovereign debt crisis is basically over", he claimed. "What we have told Chinese leaders and investors was that they should be confident in Spain."

"China's assistance has been instrumental in the moments of greatest difficulty, to restore confidence in the economy of Spain," Zapatero said.

China has already intervened to buy Spanish government bonds twice over the last 12 months and has promised to do so again. It currently holds more than 12 percent of Spain's government bonds (about €25 billion), up from less than 4 percent a year ago. China also said it would take part in a fund to restructure Spanish local savings banks (*cajas*), which have been at the centre of the financial crisis.

Spain's Finance Minister Elena Salgado has also been trying to reassure the financial markets. After Portugal's application for a bailout, Salgado spent most of her time at a two day summit of European Union (EU) finance ministers last weekend stressing that "contagion" affecting Greece, Ireland and Portugal would not spread to Spain. Salgado said her country "won't go down this way because … our economy is bigger, more diversified. We have a very good track record."

This is what the EU wanted to hear. Most of the austerity policies Spain has been implementing have been worked out in close association with the EU and International Monetary Fund (IMF). At the end of the summit, EU ministers paraded before the world's press to insist that Spain will not need a bailout—though the value of this assurance is limited, as they made similar comments about Portugal last year, before it applied for a bailout this year.

"Spain isn't a problem", declared French Finance Minister Christine Lagarde. "Now I do not see any risk of contagion … I think we are totally out of this."

German Finance Minister Wolfgang Schäuble reiterated, "The risk of contagion has lessened … Not that our worries have passed, but we're on the right track."

"Spain is making enormous efforts to consolidate its budget", said European Financial Stability Fund (EFSF) chief Klaus Regling, adding, "The country is much better today and in the opinion of the markets, it has clearly separated itself from the three small countries."

Not all market analysts agree with this rose-tinted assessment, especially as there are fears of big bank losses tied to the collapse of Spain's housing bubble. Loans to the construction and real estate sector stood at €440 billion at the end of 2010.

Wolfgang Münchau, writing in the *Financial Times* on April 10, the day after the summit closed, declared, "Complacent Europe must realise Spain will be next". He wrote, "The mix of high external indebtedness, the fragility of the financial sector and the probability of further declines in asset prices increase the probability of a funding squeeze at some point. … And that means that Spain will be the next country to seek financial assistance from the EU and the IMF."

Financial analysts have produced estimates that Spain could escape a bailout if its banking losses are less than €75 billion. The Spanish government claims the losses are below €20 billion, but many insist that the government is dramatically underestimating and even concealing the depth of the crisis. Some estimates put the losses as high as €120 billion.

Spain's government debt stands at €750 billion, or 62 percent of Gross Domestic Product (GDP) and is therefore fairly small compared to the size of its economy, by EU standards. However, its private debt—owed by individuals, companies and banks—stands at a massive 170 percent of GDP and is seen as unsustainable.

The bulk of debt in Portugal and Ireland, which have both applied for bailouts, was also privately owned. The Portuguese and Irish governments bailed out the private sector, took on much of its debt, and then were forced to borrow at exorbitant rates to make up the shortfall. When this failed, they went cap in hand to the EU and IMF for multi-billion euro bailouts.

According to Jupiter Strategic Bond fund manager Ariel Bezalel, "Spain's private sector also holds the lion's share of the country's debt and we find this particularly worrying … [I]f the situation in Spain were to deteriorate, in our view this would represent a tipping point. The market certainly sees it this way".

A bailout of Spain—estimated at more than €400 billion—would dwarf those so far and virtually empty the European Financial Stabilisation Fund (EFSF).

The *cajas* have had to take over unsold or foreclosed homes, hoping that they would be able to sell them when the housing market began to pick up. That has not only failed to materialise, but the situation has worsened as real estate values have dropped. Between 2001 and 2007, house prices rocketed 150 percent. But whereas prices have fallen by 50-100 percent elsewhere, in Spain they have as yet fallen by less than 20 percent. Huge numbers of homes—one million, three times more than in the US—sit, suggesting that there will be an "oversupply" for years.

The *cajas* have been left holding tens of billions in assets. They are also seen as among the most vulnerable in Europe to European Central Bank (ECB) interest rate rises. Not only will their profits be squeezed, but many more Spaniards will default on mortgages on their homes, now worth a fraction of what they paid for them.

The *cajas* crisis came to a head early last year when the government had to step in with a €9 billion bailout of Caja Castilla La Mancha and then mount a rescue of the Catholic Church-run CajaSur. The Bank of Spain began merging most of the country's 45 *cajas* into a handful of new institutions and instructed them to seek more capital from the private sector. Since then, the work force has been cut by over 15 percent and a quarter of all local offices closed.

In March the Bank of Spain revealed that eight *cajas*, along with two Spanish banks and two subsidiaries of Deutsche Bank and Barclays Bank, still had insufficient capital and were ordered to make up the shortfall ahead of an upcoming European-wide bank stress test. In the last tests in 2010, five of the seven banks that failed the criteria were Spanish.

Last week the merger of the Alicante-based Caja de Ahorros del Mediterráneo (CAM) with three other *cajas* broke down after it was discovered it still had insufficient capital. The government has exerted pressure on Spain's big banks, including Santander and BBVA, to take over CAM to little effect. The state-backed Fund for Orderly Bank Restructuring might have to intervene.

For the Spanish bourgeoisie, the EU and the money markets, the key aim is to force the working class to pay for the crisis. Bank of Spain Governor and ECB Governing Council member Miguel Ángel Fernández Ordóñez declared it was "essential" for the government to step up its "ambitious pace" of reforms, particularly those affecting the labour market. The IMF on Tuesday echoed his demands saying more austerity measures were required to reduce the budget deficit to 3 percent of GDP by 2013 from this year's estimate of 6 percent.

The PSOE's harsh austerity measures including public sector pay and pension cuts, slashing of welfare and other public services, VAT rises and further privatisations have kept the speculator wolves away from Spain's door and prevented the interest rates the Spanish government has to pay on its borrowing soaring to the unsustainable heights experienced by Portugal.

Spain's unions have received from the ruling class the task of working with the state and big business to impose the cuts. Currently, they are holding secret talks with business leaders on "reforming" the country's collective wage-bargaining system, to stop index linking of wages to inflation and force them down. Both parties were promising an agreement this week, but the employers suddenly demanded additional measures to cut workers' insurance and sickness benefits.

Cándido Méndez, general secretary of the PSOE aligned General Workers Union (UGT), explained that the delay should not cause "anyone to be nervous or frantic". Communist Party (PCE) leader Ignacio Fernández Toxo, head of the PCE- aligned Workers Commissions (CCOO), said an agreement was still "most likely".

Employers' association president Joan Rosell said, "We're trying to put on the table something that we have never had before" and that the reforms would be "significant and deep".