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SPAIN AND THE EUROPEAN UNION-RUSSIA CONFLICT: The impact of the sanctions

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Relations between the European Union and Russia are at the lowest point in their history. Some Russian analysts even warn that we are approaching the point of breakdown. Moscow is attempting to impede the tightening of the sanctions and, at the same time, destroy the fragile—although for the moment holding—European unity on the subject. This unity is inseparable from the leadership of the German chancellor, Angela Merkel, and rests upon deep divisions between the member states.

Spain is widely seen to be one of most sympathetic countries to Moscow (along with Greece, Italy, Hungary and Bulgaria) and is one of the most openly reluctant to taking a hard line with Russia. This Spanish policy produces irritation and incomprehension in other Eu-

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Though Russian tourism only accounts for 2.7% of total arrivals to Spain, the government sees it as a priority market with high expectations for the future.

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In its official narrative, Spain gives strategic character to its relations with Russia but there is an evident asymmetry in the degree of importance given to the relationship by one side and the other.

The harmony between Madrid and Moscow materialises, for example, in the defence by Spanish diplomacy of the idea that Russia has “legitimate interests” in Ukraine. As a result, these “Russian interests” must be considered in any attempt to resolve the Ukrainian conflict sponsored by the EU.

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ropean societies, particularly among Russia’s neighbours. Madrid’s position seems to swing between a desire to prompt dialogue with Moscow and a fear of appearing to be a belligerent partner, or one who obstructs the common EU position.

The roots of the Spanish position towards Russia lie in a degree of historical inertia and are the result of a combination of political and economic considerations. The perception of distance between the two countries and the absence of elements of genuine strategic weight at stake for Spain play a crucial role in shaping Madrid’s point of view. Russia, for example, is one of the main suppliers of oil to Spain (14% of the total in 2013), but the supply sources of crude are highly diversified and, at the same time, Russian gas is not consumed in the Iberian peninsula. Political and diplo-

matic relations are fluid, but they are neither special nor truly strategic for either of the two beyond the official rhetoric. In fact, Spain does not seem to receive any significant benefit from this position. Both the ministry of foreign affairs and the Spanish business community agree that Moscow neither facilitates access to the Russian market nor gives particular political backing to Madrid.

Bilateral economic relations, although promising in some sectors, are not particularly strong. But they nevertheless occupy a privileged place on the Spanish agenda, in line with the unquestionable primacy Mariano Rajoy's government gives to economic and commercial activities in its foreign policy. Until now, the impact of the EU-Russia sanctions on Spain has been moderate and highly concentrated in the agricultural sector. However, the consolidation and extension of the sanctions could have significantly negative effects, particularly in the fields of energy, railways and advanced technologies. Perhaps the business that will be most heavily affected is Repsol, but it may also mean that the first steps taken by Indra are blocked off. In this field of discussion, the impact of the sanctions must be evaluated not only in terms of the resources invested so far, but also in terms of the consequences of a market that is so costly to enter being closed off and all the efforts made up to now being lost. For this reason, the companies that are not affected—principally the large companies of the energy and infrastructure sectors—fear a possible fourth package of sanctions, and mean it is likely that Madrid will resolutely oppose any attempt to impose further punitive measures.

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The economic dimension: the impact of the sanctions in Spain

The Russian countermeasures in response to the EU sanctions may mean losses of some €550 million annually to agricultural producers, which are likely to increase due to the future closure of the market.

Commercial impact

Since the beginning of the last decade, Spanish exports to Russia grew continually until a peak value of €2.84bn in 2008. As a consequence of the crisis, exports declined sharply but grew again between 2008 and 2012 when sales to Russia totalled €2.95bn, exceeding the high point reached in 2008. Nevertheless, in 2013 sales to Russia fell to €2.82bn. The contraction in Spanish sales to Russia in the past year can be explained by the restrictions on imports introduced by Moscow in 2013 affecting meat, fish and dairy products, for which health reasons were given as justification. In fact, if the level of exports of this type of product in 2013 had stayed at the same level as before, the total volume of Spanish sales would have grown.

In order to appreciate the impact of the Russian countersanctions, the export pattern up to August 2014 may be analysed (existing up-to-date information) and compared with previous years. The most striking case corresponds to the consignments of animals and meat that by 2013 had already fallen to half the level of the previous year (€125.8 million) and which in 2014 were practically liquidated and recorded a volume of just €9.2 million.

In the case of vegetable products, which were also affected by the countersanctions, when the first eight months of the years are compared a continuous contraction since 2012 is observed. Nevertheless, the reduction in 2013 is attributable to other circumstances. In fact, the evolution of Spanish exports of vegetable products in the March-May quarter (prior to any effect of the countersanctions) shows a fall from 2012 levels to €48.4 million, rising again in 2014 to €61 million. Notwithstanding this, if we take the last quarter for which we have information (June-August: a period in which the impact of the counter-sanctions was already being felt) the decline is continuous. In fact, while in 2013 exports with a value of €64.7 million were made, in 2014 the figure fell to €52.8 million. Since the counter-sanctions came into play in summer 2014 the expectation is that the change effected will be similar to that of the meat and animal products.

The countersanctions give us a glimpse of how, as a collateral effect, the restrictive measures applied in 2013 will be consolidated. In this sense if we consider that the level of exports of meat and vegetable products in 2012 (before the trade restrictions were introduced by Russia) was more than €550 million (that is to say, close to 20% of Spanish exports to Russia), and if we consider that this was a level that was reproducible over the coming years, then an estimate may be made of the losses to the Spanish economy. In addition, this figure is compounded by the extent to which the loss of a growth in sales to this market is considered definitive.

Impact on services: tourism

One of the relevant parts of Spain-Russia relations is tourism, in particular, that of Russians visiting Spain. In the second half of the last decade a tendency towards growth was consolidated in the trips made by Russian tourists to Spain, peaking in 2008 at more than a million tourists. In 2009 the crisis meant a decrease in that figure, but, from then on, the growth has been more than notable: in 2012 it went past the 1.2 million mark and in 2013 it reached nearly 1.6 million Russian tourists. In the past year, tourists from Russia have been the national group that that has grown the most, with the number quadrupling since 2009. In addition, their level of expenditure is considered to be fairly high and exceeded €2.2bn in 2013. Though Russian tourism only accounts for 2.7% of the total arrivals to Spain, the government sees it as a priority market with high expectations for the future, and it is considered as such in the National and Integral Tourism Plan 2012-2015.

However, this past year the Russian market has shown signs of stagnation and it is predicted that the number of Russian tourists in 2014 will be lower than that recorded in 2013 with the clear possibility that this decline will be consolidated in the future. This result is explained by two linked factors deriving from the economic crisis that began to reveal itself last year. First, there is the reduction in economic growth, and, second, the weak rouble has caused a trend towards depreciation. This last factor may have been accentuated by the North American and European sanctions. These circumstances have restricted the income of Russian people, dampening their desire to travel to, among other places, Spain.

The fall in Russian tourist numbers is partly explained by the annexation of Crimea. This new Russian territory is a significant tourist hub that became fashionable and was popularised among Russians last summer, but its capacity to overshadow Spain is more than questionable, for the time being at least. Nevertheless, the consolidation of a depreciated rouble could establish Crimea and, in general, the whole Russian Black Sea coast as a competitor to Spanish tourist destinations.

Impact on investment flows: from Russia to Spain

Russian investment in Spain is fairly residual. While in the three-year period 2008-2010 it amounted to €31.5 million, in 2012-13 it grew to €114.2 million. Among the sectors that have attracted the most resources are real-estate, hotels and catering. Also important are investments in commercial activities, those related to the purchase of vehicles, and those related to tourism. That is to say, the greater part of Russian investment in Spain is directed to the attention of those Russians temporarily or permanently located in Spain. In this respect, activities related to the real-estate sector to facilitate the sale of Spanish properties to Russian citizens stand out. In this sense, it is worth pointing out that in 2012 Russians were the second largest purchasers of houses in Spain after the English.

As an initial estimate, it might be predicted that the sanctions would have a reduced impact on property investment as they are highly decentralised and their point of reference is a community that already has a direct connection to Spain. Nevertheless, the possibility exists that the sanctions could produce uncertainty or a loss of confidence about the situation of properties bought by Russian citizens in Spain because of increased controls and the apparent possibility that restrictions on movement or investment will be extended to all Russian citizens and not only to a few leaders, as has been the case until now. This situation, along with the devaluation of the rouble would lead to a reduction in the volume of this kind of investment in Spain.

Impact on investment flows: from Spain to Russia

Spanish investment is greater in volume than that coming in the other direction, but it is still not particularly large. From 2008-10, this investment amounted to €528.4 million but fell over the next three-year period to €218.2 million. Spanish investment is concentrated in the sectors of metal products and in the manufacture and sale of vehicles. In the past three years

some significant investment has been made in the chemical sector and, in certain cases, investments have been made in the finance sector. In these cases, it is also unlikely that the sanctions will have a particularly negative effect and it does not appear that the Russian government will adopt special measures (countersanctions) that will harm them.

Spain-Russia corporate collaborations

One of the most significant collaborations between Russia and Spain is in the energy sector, which has, in the end, been included as part of the EU sanctions on Russia. Above all, the activities of Repsol stand out. The company arrived in Russia in 2006 when it acquired part of West Siberian Resources. Later, in 2011, it signed a cooperation agreement with Alliance Oil Company to create a joint venture company, AROG, in the field of oil exploration and extraction. In productive terms, Repsol has rights in 27 blocks, of which 13 are in the exploration phase and 14 are in development. As a result of its activity in 2013 it managed to produce 14,600 equivalent barrels of oil a day, rising by mid-2014 to 17,640 barrels.

The company Técnicas Reunidas, for its part, already has level of experience in working in the Russian market. In 2006, in particular, it contributed to the engineering works for the reconstruction of an oil refinery in the far-east of Russia (Khabarovsk). In 2013, Técnicas Reunidas won a contract worth €1.1bn from Lukoil to carry out the design of the construction of an oil refinery in Volgograd. Iberdrola also has experience in the Russian market. In 2011 it delivered a turnkey combined-cycle gas power plant in the Urals. This involved the use of new technologies in adverse climatic condi-

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tions. That same year it won a tender for the construction of an electrical sub-station, also in the Urals, to be delivered this year. Depending on the interpretation of the sanctions, their coming into effect could hinder the activities of the Spanish companies mentioned and, further, roll back their expansion into this market that has great prospects for the future and presents serious difficulties to those attempting to enter it.

Another significant productive area is that of capital goods. In 2013, the Russian government made its interest in building a high speed train network known. In this case, Talgo found itself well-positioned and in 2011, along with Adif, it won a contract to manufacture 6 trains of 20 carriages each. OHL had also won a contract in the railways field. Nevertheless, the economic crisis in Russia, the sanctions, and the desire of the Russian authorities to carry out an import substitution as a reaction to the sanctions imposed, could limit Spanish expectations for growth in this kind of business in Russia.

Special mention should also be given to the case of Indra, who had established a collaboration agreement with Rostej to develop joint projects in the field of advanced technologies. However, as the Russian company has fallen under the sanctions as it includes companies in the defence field, the prospects for the future in this line of production are in ques-

tion. Also in the field of advanced technologies is the Spanish company Fluidmechanica, which makes equipment for use in icebreaker boats. The company has been collaborating with Russia for 15 years and, if, for the moment, its activity does not fall under sanctions because of its strictly civil character, it could be harmed if the sanctions are widened.

Political dimension: seeking a balance between Berlin and Moscow?

In its official narrative, Spain gives strategic character to its relations with Russia. The framework document in this area is the Strategic Partnership Agreement signed in March 2009 by Prime Minister J.L. Rodríguez Zapatero and President D. Medvedev. This agreement has been followed by other diplomatic milestones such as the celebration of the Spain-Russia Dual Year in 2011 and the Dual Year of Spanish Language and Literature in Russia and of Russian Language and Literature in Spain in 2015. In 2016, the holding of a bilateral year of tourism is also planned. This series of initiatives tells the story of the fluidity of the relations and harmony between Madrid and Moscow. However, it should be borne in mind that the link is not genuinely strategic and there is an evident asymmetry in the degree of importance given to the relationship by one side and the other. Seen from Moscow, Spain is a potential ally in a broader strategy of relations with the EU, but one which has little importance of its own.

The Russian countermeasures in response to the EU sanctions may mean losses of some €550 million annually to agricultural producers

Traditionally, Spain has shown either scant interest in eastern Europe or a degree of suspicion that the expansion of the EU towards the east would reduce European interest and aid to the southern border and the Mediterranean as a whole. Also, as with other European partners, Madrid's focus on the former-Soviet space (excluding the very particular case of Kazakhstan) has been to favour relations with Russia ("Russia first"). Furthermore, the institutional inertia shaped by geographical distance, the good image that both countries have of each other—frequently based on cliché—and the absence of historical conflicts with Russia should be remembered. This historical legacy has given shape to the dominant perceptions of the Spanish politicians, diplomats and military, whatever the colour of the government in power.

The harmony between Madrid and Moscow materialises, for example, in the defence by Spanish diplomacy of the idea that Russia has "legitimate interests" in Ukraine. And that, as a result, these "Russian interests" must be considered in any attempt to resolve the Ukrainian conflict sponsored by the EU. In this sense, it is no surprise that the official Spanish reaction to Euromaidan was, at best, half-hearted. In the eyes of Spanish diplomacy, the transformation of the Ukrainian crisis into an armed conflict in the east of the country only serves to confirm the appropriateness of its initial prudence and, in private conversations, senior Spanish officials con-

gratulated themselves on what they saw as an exercise of political and diplomatic coherence.

Nevertheless, at times, this closeness has caused a degree of irritation with Spain among her Euro-Atlantic partners. A particular example was the meeting in Madrid between ministers García-Margallo and Lavrov on March 5th, 2014, with the conflict in escalation due to the deployment of Russian troops at strategic points on the Crimean peninsula. In the joint press conference, the Spanish minister for foreign affairs emphasized the importance of the respect for the law as a first principle (implying the recognition of Ukrainian territorial integrity) while also underlining that "the current difficulties began when president Yanukovich decided not to sign the association agreement with the EU, an association agreement that was erroneously presented as an exclusive and exclusionary alternative to the Eurasian Customs Union that Russia and other countries have put in place."

Crimea is, from the Spanish perspective, the most problematic issue of all. But, in a similar way to Kosovo, the Spanish position is shaped by its tendency to internationally project its domestic concerns about Catalonia and the Basque country. García-Margallo himself, prior to the referendum held in Crimea in March 2014, did not hesitate to say that the parallel between Catalonia and Crimea was "absolute" and affirm, with his mind undoubtedly focussed on the Catalan issue, that "a referendum that violates an internal constitution by

definition violates international law and cannot have legal effect... a territory that breaks away in flagrant violation of an internal constitution cannot aspire to international recognition".

This hard line on Crimea has not prevented Spain from systematically appealing for the EU to reopen dialogue with Russia. This implies, from the Spanish perspective, the need to find a legal solution to unblock the situation. It is in this line that we should understand the proposal made by the Spanish minister to his European colleagues on January 10th to resolve the issue of the annexation of Crimea by Russia in the International Court of Justice in The Hague. In the words of García-Margallo "if the conflict needs thawing, and the most difficult conflict is Crimea, let us seek an imaginative solution that allows both parties to save face".

Spain has shown very little enthusiasm for the adoption of sanctions against Russia. In large part this is for economic reasons. Current economic relations with Russia, as has been pointed out, are modest. In 2013, Spanish exports brought in a total of €234bn: of those only €2.8bn came from Russia, putting the country in 19th place on the list of importers. Direct investment from Russia to Spain is minimal, and that by Spain into Russia is low at only €218 million in 2013. Nevertheless, after years of effort by Spain, the relationship is beginning to take off. And what is more, the Spanish government considers Russia to be a key partner in the tourism and property sectors that are so fundamental to Spain's economic recovery. Considering this, the crisis in Ukraine could not have come at a worse time.

Madrid has combined reluctance to take a hard line with Moscow with a desire not to show itself to be a European partner that makes a habit of blocking consensus decisions and much less when they are the clear result of initiatives led by Germany. In this sense, in order to try to mitigate the suspicions of certain European partners with regard to the Spanish position, García-Margallo has been due since May 2014 to visit Kiev as a sign of the Spanish commitment to Ukraine following its presidential elections. The visit, postponed for several reasons, was finally made on the 10th of February 2015.

Until now, the three sanctions packages imposed on Russia by the EU and the Russian countermeasures have had limited impact in Spain. As noted above, the losses may be estimated at around €550 million annually. The main preoccupation of the Spanish government is the concentration of this impact in the agriculture and livestock sectors of three regions: Aragon, Catalonia and Valencia. Wine and olive oil have been kept out of the veto on European foodstuffs imposed by the Russian Federation. This has been interpreted, in certain places, as a concession by Moscow to the countries of southern Europe—Spain, Italy and Greece—that are the largest exporters of these products and are traditionally receptive to Russian positions. Nevertheless, it must also be seen as proof of how difficult it is to replace those two products, given that the importation of Moldovan and Georgian wines are also subject to restrictions in Russia.

A striking aspect is that, for the first time, a developed crisis in eastern Europe has provoked intense debate and polarised public opinion in Spain. The Popular Party (PP), the Socialist Party (PSOE) and Convergence and Union (CiU) and their representatives in the European parliament, in particular, have aligned themselves with Europe's more critical opinions on the Russian military intervention in Ukraine. However, United Left (IU) and Podemos have taken the Russian narrative on the Ukrainian conflict as their own, particularly with reference to the "fascist junta in Kiev" and the "anti-fascist" nature of "the war in the Dombas". Their extremely critical position on the role of the EU and their insistence on the need to uncouple from the USA and promote global rapprochement with Russia makes a pro-Russia turn in Spanish foreign policy probable if Podemos does lead a government. It is just one more of the crucial unknowns to be resolved in this electoral year in Spain.

In 2014 tourists from Russia have been the national group that that has grown the most and their level of expenditure is considered to be fairly high