

The discontent of a small Europe

Conversations on the infrastructure crisis and other real or imaginary crises of the Catalans, during the first decade of the twenty-first century.

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At the end of the golden age

The fiesta had indeed been splendid, wrote the journalist Michael Reid in *The Economist* on 6 November 2008, *and Spain has woken up with a hangover*. The process of accelerated growth in Spain since the eighties, which led the Spaniards to be taller and more European: in thirty years we went from being the *Reserve of the West*, in which even divorce was forbidden, to allowing homosexuals to marry and adopt children, and we even won the European Cup in football, and the Davis Cup several times. The modernization was very rapid, from the old Iberian gauge railways we have gone to the world's more extensive high-speed railway network, and more than ever has been invested in infrastructures, thanks to the economic euphoria and to the famous €118bn granted by Germany and the other developed European countries. All this is very good, continues the journalist Michael Reid, but it has been frivolous and speculative economic growth, based on all these infrastructure investments, on the arrival of industrial companies in the eighties and even nineties attracted by the low salaries, and on rapid urban developments, especially on the coast, on the arrival of large volumes of migration which has increased the number of people working, in construction, in agriculture, in catering, but not the productivity of the economy.

I agree, Pilar de Torres tells me, I believe that Spain is at the end of an era, and that we will now pay for our past excesses!

Pilar de Torres, a member of the Cercle d'Economia, now chaired by Salvador Alemany, had worked for years in Chase Manhattan Bank, then in PriceWaterhouseCoopers, until she made the move to a public company as a result of the so-called Carmel crisis, when a tunnel under construction collapsed below some

houses, causing great social alarm although there were not any victims. The Minister Nadal offered her the presidency of GISA then, and she accepted. A few years later she went on to chair IFERCAT, when Xavier Casas left the City Council and took over GISA. IFERCAT was created by the last government of Jordi Pujol to finance Line 9 of the metro outside the budget of the Generalitat, but this financial engineering objective became obsolete because IFERCAT's debt, like GISA's, is already consolidated with the debt of the Generalitat. Nowadays IFERCAT is basically the public institution in charge of planning new railway infrastructures. IFERCAT is the owner and manager of L9 and is drafting the preliminary studies of the orbital line and the transversal axis.

Pilar de Torres is a music lover, she plays the flute, but it is not exactly about music that I have come to her office on Via Augusta today to talk to her about, but about the end of what some observers, such as those of *The Economist*, call, emphatically, the end of the Second Golden Age in the development of Spain, the last thirty years.

Yes, she tells me, as economists we are capable of explaining very well the reasons for a crisis after it has broken out, but we cannot always foresee when the next one will occur, or what intensity it will have. All in all, it had been very clear for some time that the economic growth was very vulnerable, such a low cost of money made people invest, through debt, in not very productive assets, such as housing, which at first generate employment and wealth, but which do not contribute to improving productivity. Other factors contributed to the crisis, such as the lack of control and the deregulation of the financial sector in other countries, such as the United States. All in all, it led to a lack of confidence in the financial sector, with a very important crisis of liquidity, putting a sudden stop to the above three per cent growth to which we were accustomed. And in Spain, in addition to the international financial crisis there was a crisis which has particular characteristics, as *The Economist* says: we have a very important crisis of the property sector, and certainly in the future we will question the type of growth based on cheap labour, basically because we are already at a level of costs very similar to those of our neighbours. Sectors such as the car industry, or electrical household appliances, will have to reconvert like the textile industry did years ago. It is true that we are experiencing the end of an era of growth that lasted for thirty years.

It is not because of the arguments on the weakness of the Spanish economy that the article in *The Economist* caused such an uproar in Catalonia, but rather because of the journalist's criticism of the state's excessive administrative and political decentralization, which has generated a festival of seventeen Autonomous Communities, *taifa kingdoms* which manage public resources in a capricious manner, and in which the nationalist politicians even spend resources that they no longer have on campaigns to stop Spanish being spoken. The financial and economic crisis should put an end to all that disorder, the journalist concluded. *The party is over.*

In relation to the economic crisis, the administrative decentralization of Spain is completely irrelevant, Pilar de Torres tells me. It is true that the Autonomous Communities accumulate very big debts, while the state has closed the budgets of recent years with surpluses. This is simply due to the fact that services such as education and health have been transferred to the Autonomous Communities, in addition to the prisons and the police in Catalonia. These services have had increasing costs due to the increase in the population since 2000, and the improvement of the quality of the provisions, while the transfers from the state to the Autonomous Communities, or to the municipalities, have not increased. Thus, the state has had relatively higher resources and has moreover had the European cohesion and structural funds, which have led it to concentrate its investments on major transport or environment infrastructures. If in Spain there is a relatively homogeneous level of facilities and of infrastructures, and of public services, more balanced incomes between all the regions, it is because there is a political power distributed throughout the territory, Autonomous Communities which look after the interests of their inhabitants. Managed from Madrid, the public investment decisions or the management of public services which require proximity would probably have been much worse. Moreover, the income of the Autonomous Communities depends on taxes which vary quickly when there is a change of economic situation, while the income of the state is more stable, although it will also go down now in relative terms. That is, the fact that the state has had a surplus in recent years, and that the Autonomous Communities have historical debts, does not indicate that the state is a better or worse manager than the Autonomous Communities, or that to increase autonomous financing is equal to wasting public resources, of course. The

federal rules need to be updated to be made more transparent. Furthermore, apart from the state and the Autonomous Communities, the Spanish public treasury has another serious structural problem: the local treasuries. The municipalities have been excessively inclined to facilitate urban development and housing construction processes, among other reasons to increase their income. It was, in this respect, a mistake to modify the law which prevented them from selling land or buildings that they received in relation to the average uses of the urban sectors of development, because this has contributed to the construction spiral that we were talking about earlier. It is not surprising, in this context, that some experts are asking the state to regain control of the urban development powers of the Autonomous Communities, and to considerably limit those of the municipalities. But I do not think that this will solve the problem.

You told me earlier that the major infrastructures promoted by the state had contributed to the territorial balance of Spain, to a large extent thanks to the existence of the autonomous communities, which oblige the state to maintain a certain distributive balance between them. But many of these investments do not have a minimum socio-economic return, above all the investments in high-speed lines, and, in practice, in the medium and long term, they will certainly have a much smaller economic impact than what it appears they will have, maybe even negative...

Yes, I believe that we should be more rigorous in the future on analyzing the social and economic return of public investments, irrespective of whether or not the past ones were sensible. The government of the Generalitat is very interested in implementing systematic assessment methods, but the inertias of the sector are very strong and it cannot be done overnight. The gains from applying systematic economic assessment methods will be in the medium and long term, and on the other hand they would certainly have important political costs in the short term, if the priorities taken on socially are substantially modified. It is difficult to ask a politician to decide against what society is asking him for. The public sector is less hierarchical than the private sector, much more complex, public decisions require permanent negotiation, always seeking a minimum consensus, unlike the decisions that are made in the private sector, much more executive. In the Cercle d'Economia we are reflecting on investment

assessment methodologies applicable to Catalonia, and they are also doing this in other institutions, such as the Economic and Social Council. Without this more rigorous analysis of social, economic and environmental costs and benefits, I would say that we often discuss policies and projects in an immature way, without enough information, based on prejudices, comparative grievances. We have not always set out the strategic debates well, it's true.

Another question: will we be able to pay for all the infrastructures that we are now building, but that we are financing in the long term on the basis of shadow tolls for dual carriageways, building rights for facilities and other concessionary formulae which transfer the public debt to the future?

Yes, the cost of financing them in the medium and long term is important, but feasible. The total volume of the public investment, and the priorities, have to be adapted to the needs of each time, and this is a political exercise that has to be performed with the cost and benefit data, distributed by social groups and territories. I do not yet have the data to prove it, but I sense that the infrastructure deficits and the costs that they represent for people and companies in Catalonia are higher than the costs arising from having to finance the investments that are made in the future. GISA cannot stop making the three new schools that are needed in Santa Coloma, for example, or the autonomous police stations or the prisons or the healthcare centres. Moreover, we are all relying on the third additional provision of the Statute significantly increasing the resources available to the Generalitat in the short term.

How would you justify the fact that the main investment in infrastructures in Catalonia is now Line 9 of the metro?

L9 has been a very complex project, but it will end well, finally, and the first section will come into operation in 2009, and all of them toward 2014, but the technical and financial management of a project of the size of L9 is hugely complex. L9 could undoubtedly have been budgeted in sections, but an orbital line was needed in Barcelona to link the other metro lines in the north and the sides, increasing the current

system's comfort and mobility. However, having said that, L9 is a project inherited from the previous government, and if we could redo the project, or the construction process, we would do it differently. And we have lost interesting opportunities to maximize the economic impact of such a unique project, which requires a very important technological innovation effort by the construction companies. It would have been logical to have foreseen, for example, processes to internalize in Catalonia all or most of the technological innovation that was produced. It is true that the rolling stock is made by Alston in Santa Perpètua de la Moguda, but there are many other technology transfer opportunities that we are losing, among other reasons because the project began to be tendered with an excessive number of unknown factors, and some sections have certainly not been resolved optimally. For example, from the point of view of project management, with the type of integrated *project* and *works* contracts that were created for the Barcelonès North section, the different contractors had a dominant position in the contract, and they were difficult to coordinate. Overall, if we compare the cost of L9 per kilometre with the costs of similar lines in Europe, for example in Holland, we find that they are not excessive. We are talking about a total construction budget of €6.8bn for 47.8 km (initially it was 42 kilometres) and 52 stations (initially there were 41 stations). According to the forecasts, the line will carry 130 million passengers a year, a sufficient volume to justify the investment, despite the cost. L9 will represent a very important change in public transport mobility in Barcelona and in the rest of the metropolitan area.

You said that the project and works contracts created many problems of coordination in the construction process of the L9.

Yes, they have created problems because it is not at all easy to coordinate the sections of project and of works awarded to different construction companies, above all at a time when the project wasn't at all advanced. Now, with more knowledge, having worked on it a lot, we have used this same type of contract to finance the construction and management of the stations, some of which are hugely complex because they are almost ninety metres deep. Transferring the drafting of the project to the private sector also transfers an important part of the investment risk to it, and the public-private concession agreement is thus justified. The private investor will be in charge of the executive

project and of the construction, and also of the maintenance of the station in accordance with prefixed quality criteria, for which it will charge what we call the *technical rate*, so that the financial stability of its investment is guaranteed, and it obtains a reasonable profit during the period of time fixed. The private licensees will be responsible for the access to the metro, while TMB will be the sole operator of the new lines, integrating them into the fabric of the current metro network, and paying a fee to the licensees for the use of the infrastructures. Transferring the projects and works of the stations does not represent the same degree of difficulty, of course, as transferring sections of line, and has the advantage of diversifying the sources of financing of the L9. At present we have awarded the 13 stations of Section I to FCC, OHL and Copisa, which will invest some €873M to build them, and will charge TMB €79.50M per year, which will bring them an internal rate of return of 7.75%, and also the 13 stations of Section IV, in this case to Cat Concessions (Dragados), Acciona, Comsa, Acsa Sorigué, which will invest €523M and will receive a fee of €51.9M, equivalent to an internal rate of return for the shareholder of these companies of 7.25%. We still have 25 stations of sections II and III to put out to tender.

Abertis, Catalonia's most important licensee and one of the biggest in the world, wasn't interested in participating in the project and construction of the stations.

No, Abertis is not so interested in taking on the risk of the project and works, but rather the risk of demand, which in this case hardly exists because it is a risk of availability and, if all the quality standards are fulfilled, it is covered. The public-private partnerships for the project, construction or management of infrastructures are extraordinarily complex. For example in the agreements between the state and the first motorways a maximum limit was not fixed for the profits possible for the licensee, as they depended on the number of vehicles and lorries using them, and the object of the concession was not fixed very precisely so, for example, optical fibre lines pass along the sides of the motorways because nowhere in the contract does it specify that the land has to be devoted exclusively to the road concession. This is a curious case, because the Roads Act forbids services from passing through or parallel to main roads. This is one example from among many of the difficulty of defining public-private partnerships

which have to stay in force for thirty or forty or more years, under changing circumstances, in an increasingly uncertain world, currently in a crisis.

What other resources does IFERCAT have to finance the construction of the whole line?

IFERCAT has been financed, since 2006, with long-term loans from the European Investment Bank. We currently have loans of this type signed for a total amount of €1.6bn, and we foresee that they will be higher, because they offer the Generalitat of Catalonia access to financing at very competitive rates, apart from being long term, which is appropriate for an infrastructure like the metro. The EIB is a major financier of infrastructures in Spain. At present it has assets of €90bn, and I believe that it has lent money to practically all the autonomous communities, in addition to Ports, for the construction of the high-speed railway. In Catalonia it has lent money to organizations such as the ACA, the Port of Barcelona, Tramvies, and Fira 2000.

And how long will we take to pay all this accumulated debt in the future? What is your forecast for the short and medium-term evolution of the economy?

I can't say much about what will happen in the short term. As I said before, as economists we find it difficult to make forecasts and to explain the future. But in any case the assets must return their real value. In Barcelona it will be difficult for housing to go down by 20% or 30% because it is highly controlled by big construction and property companies which will resist a reduction in prices, but we are too indebted and the prices can only follow a downwards trend. The Autonomous Communities and many municipalities are also indebted, but it should be taken into account that investments in infrastructures or in facilities are not like the investments in housing that we were talking about earlier. Public infrastructures create wealth, they have a multiplier effect on economic activities in the sense that, if they are well planned, they increase the productivity of the companies existing and allow new activities to be attracted. It is to maximize this economic activity that we should prioritize investments in infrastructure adequately, as we said earlier. While an insufficient investment in the medium and long term causes a fall in the productivity of economic activities, an

excessive public investment may be counterproductive due to the opportunity costs represented by not having assigned these resources to other more productive investments. The administrations must invest adequately in the needs of each moment, and at present all governments are investing in productive infrastructures as a mechanism to leave the crisis.

What do you think are the most adequate economic strategies for this historical moment?

What we should do is to start by identifying our competitive advantages, and by exploiting them adequately. Thus, we cannot live without tourism, either in Barcelona or in Catalonia. Tourism should help us, first, to attract talent, and we have to facilitate the creation of companies, offer good public facilities and services. Mass tourism has disadvantages, but now we need to get used to it, encouraging the tourism model to change as fast as possible in order to generate more added value. In Barcelona many four and five-star hotels have already been built, business tourism is growing, and other forms of tourism which maybe should be given another name, training, health, sport or culture tourism, from visiting professors and students in the universities to luxury cruise ship passengers in the port. The Barcelona School of Economics, promoted by Mas Cullell, which reinforces the city's business schools, is an example of the kind of projects that we need in order to attract talent, to create internationally open networks and relations, and expands the current reputation, already created by business schools such as IESE and ESADE. Tourism is one of the motors of the tertiarization of the economy, but in actual fact, rather than tourism, which is associated with leisure and spare time, with sun and sea until not long ago, we should be talking about social and economic opening, opening up the country to the global flows and being capable of attracting and generating advanced service activities. 22@ is a commitment to develop an advanced service economy and, in the Forum, hotels, convention centres and office buildings were also constructed, but on the other hand around La Sagrera I would say that too much housing is been built, whereas the proximity of a new high-speed train station with such good connections to the public transport systems of Barcelona, and even of Catalonia and of Spain, should allow economic activities to be concentrated there. We need more courage maybe in order to focus on strengthening some industries

in which we have big companies and growth possibilities, such as food and agriculture or biomedicine, for example, the textile industry, still, and this entails encouraging, in other words, giving prestige to scientists, promoting more scientific and engineering degree courses. The main challenge is to increase productivity, the added value of economic activities, of public investments. We have to accept that we have some advantages, and not others, and we need to make strategic decisions on the basis of conscientious information, as approximate as possible, of the possible costs and benefits. Maturity entails being capable of recognizing what our real capacities are and having reasonable and achievable ambitions, which we will update successively.

How do you see us, the Catalans, at present, at the end of an era, after what The Economist called the second Golden Age of Spain?

Let me speculate now, at the end of the conversation. I see that as Catalans, all of us, we are not very inclined to analyze the questions with the data available, rationally, at the same time as we feel practical, pragmatic, which is a paradoxical, very curious, combination. We often have ambitions of “fish in the basket”, it’s time to move on, but when we are at times of change and uncertainty, of crisis, at a crossroads, I think that we lack either ideology, and leadership, that is to say *impulse*, or quite the opposite, more *sense*, in order to analyze the data in depth and decide rationally. One of the two. At present we cannot stay half way, filling in holes, or become more embroiled in pointless arguments; we need energetic and well directed actions!