

ECONOMIC RELATIONS BETWEEN SPAIN AND PORTUGAL SINCE 1986. TOWARDS THE FORMATION OF AN IBERIAN MARKET?

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1. THE BACKGROUND: AFFINITY, PROXIMITY AND YET SCANT ECONOMIC RELATIONS

The economic relations between these two Iberian countries have historically been much weaker than one would expect in the light of their cultural ties and geographic proximity. Fortunately, the past twenty years have seen not only an end to this traditional standoff but in addition both economies have become strategic and privileged partners. It had to be an extra-peninsular factor, namely, both countries' membership of the European Economic Community (EEC), which in a few years has redressed a situation that centuries of proximity had failed to change.

The economic relations prior to both countries' entry into the EEC, in January 1986, were informed by a lack of stable lines of cooperation between their respective governments, in stark contrast to the manifest affinity between the two societies in terms of cultural and religious values and their shared geography. The enormous potential for cooperation and exchange has been outweighed by mutual distrust, customs barriers and a refusal to cooperate with the neighbouring country.

Those who have studied the relations between these two countries in the past have highlighted the presence of high-sounding agreements almost devoid of true content, and it was only when both countries emerged from their respective dictatorships that the economies on each side of the border began to look each other in the eye, with a firm will to get to know each other and have more and better dealings. Nonetheless, within the field of political relations, only when it became clear that both countries were set to join the Common Market at the same time did the political classes realise that the strengthening of bilateral economic ties would be to their mutual advantage. In April 1985, an agreement was reached in Lisbon to fully deregulate bilateral trade in industrial products without waiting for the seven-year transitional period established by Brussels.

2. ECONOMIC ASYMMETRY OF SPAIN AND PORTUGAL: DO EXCHANGES BENEFIT THE TWO IN EQUAL MEASURES?

2.1. Asymmetry of market size

The differences in size between Portugal and Spain are more accentuated at economic level rather than in terms of geography. Portugal's gross domestic product (GDP) in 1986 was only 14.6% of Spain's, whereas per capita income regarding the average for the 12 members of the EEC was 53.1% in Portugal as opposed to 72.1% in Spain. The years of shared membership of the EU have not significantly altered the general parameters for the two economies: in 2006 Portugal's GDP was 15.6% of Spain's, after having reached 19% in 1999; and Spain's per capita income is approaching the average for EU-25, whereas Portugal's stood at 71.4% in 2005. The clear differences in size and development underpin Spain's attitude of ignoring its neighbour, whereas in Portugal there is widespread feeling that the Spanish economy could colonise them.

2.2. Asymmetry of the productive system's structure and its evolution from 1986 to the present

During the time leading up to the country's membership of the EEC the Portuguese economy revealed a structure that was clearly out of step with Spain's. In 1985, its primary sector was oversized with an end contribution to the GDP of 6.8% whilst accounting for 24% of the workforce; the organisation of industry in terms of branches of production was less evolved and balanced than in Spain and the service sector suffered from a lack of diversification. By contrast, Portugal was more open than Spain to the international market. In 1985, its index of Foreign-Market Orientation (FMO) was 0.28 as opposed to only 0.10 for Spain (Buesa: 1985). Portugal's greater international openness is due mainly to its major inability to meet the demand for commodities in numerous branches of production. The huge deficit in its trade balance is one of the structural problems plaguing the Portuguese economy (Buesa: 1985; Romao and Sousa: 1985; Clause: 1985). Spain, with a much more consistent structure for its system of supply and demand, has a much lesser degree of openness to the outside.

From 1986 to the present, it is generally agreed that the political stability brought by democracy lies at the heart of the far-reaching changes and progress achieved by these two countries. The changes and structural reforms made would not have been so profound had there been political instability or major social upheaval. The economic performance by both countries since 1986 has been radically different to that recorded beforehand. The weak average rise in the GDP in 1984/1985 in both countries was followed by a period of high annual growth rates (exceeding 5% in 1987 and 1990 in Portugal and in 1987 and 1988 in Spain) which slowed in 1991 and gave way to a three-year downturn that included a period of recession (in 1993 the Spanish economy shrank by 1.2 points) in both economies that ended in 1995, when the GDP in Spain grew by 2.8% and in Portugal by 2.5%. This new period of joint economic expansion was characterised by modest average growth rates; yet perhaps the most salient feature was that as from 2001 there was an end to the parallelism recorded in the growth rate by the two economies, as whilst the Spanish economy has to this day

upheld regular annual growth rates in its GDP of no less than 3%, since 2002 the Portuguese economy has been immersed in a period of stagnation and sluggishness.

The per capita GDP has been closing in on the EU average. In Portugal's case, it has risen from the 53.1% it recorded when it joined the EEC to 74.9% in 1996 and 71.4% in 2005. Spain's per capita GDP was 72.1% of the European Community's average in 1986, rising to 87% in 1996 and approaching the average for EU-25 in 2005 with 98.7%, according to Eurostat. However, the indicators for economic productivity are far from encouraging, especially in Portugal's case, as in 2005 the output per person employed in Spain was close to the average for EU-25 at 98.9% whilst it was just 65.6% for Portugal.

3. ECONOMIC RELATIONS BETWEEN SPAIN AND PORTUGAL

3.1. Ignoring each other: Weak economic relations prior to EU membership

The nature and volume of trade exchanges, as well as the barriers placed in their way, and the capital flows in the years prior to EU membership are addressed in this section. Trade relations were very scarce and profoundly asymmetrical, with a high structural deficit for the Portuguese balance of payments. Even in 1984 exports from Portugal to Spain were only 39.9% of the imports from Spain. The volume of the mutual exchanges has a very different meaning for each one of these economies: whereas imports from Spain account for 5.5% of Portugal's total foreign purchases, imports from its neighbour make up a mere 0.8% for the Spanish economy. The nature of the goods exchanged is another significant factor of this bilateral trade, with Portugal's share presenting a more traditional make-up with lower value added. Indeed, its sales are heavily focused on traditional consumer goods and raw materials, with a smaller weighting of intermediate goods and the absence of end products and capital goods, with these latter products featuring prominently in Spanish exports to its neighbour.

Protectionism on both sides of the border, albeit more pronounced on the Spanish side, has acted as a brake on the growth of exchanges. On the verge of EEC membership and despite the 1979 agreement between Spain and EFTA countries, Portuguese goods had to bear an average rate of protectionism of 19% when accessing the Spanish market, whereas the average rate in the opposite direction was only 9%. It was widely accepted that the deregulation of trade brought about by the two countries' EU membership would be of greater benefit to the Spanish economy than to the Portuguese.

Although in the 1970s both countries lacked a true policy on the internationalisation of their commercial and financial markets, as Spain evolved towards a democracy during the so-called *Transición Política* it revealed a growing interest in investing in the Portuguese market, which would rise from 13th place in 1981 to 3rd place in 1984 in Spain's FDI ranking.

3.2. Growing economic integration between the two countries from 1986 to the present

As if on 1 January 1986 the winds from Europe had swept away the ridiculous intra-peninsular barrier, referred to by Prof. Cabo Alonso as the *absurdo murallón intrapeninsular*, releasing powerful pent-up forces of communication, the following years witnessed a huge increase in economic and even tourist interaction. There was a spectacular increase

in trade during the five years following EU membership, especially for Portuguese sales. The dynamism of Spanish exports to Portugal was a feature of the 1990s, to be followed by the intensity of the economic crisis that hit the Portuguese economy at the beginning of this century, which explains the slowdown in the growth of its exports from 2001 to 2005. Spanish exports to Portugal recorded a year-on-year growth rate from 1984 to 1990 of 64.9%, with a rate of 57.9% from 1990 to 2001, falling to 3.1% in recent years (below overall foreign trade). In Portugal's case, the rates for the same periods were: 103.5%, 32.8% and 38.6%. It was clearly an extremely important and exceptional process for the Iberian economies given that Spain, for example, which significantly redirected its foreign trade to EU countries (from 48% of its exports in 1984 to 72.1% in 2005), did so in a manner that was in no way comparable with the year-on-year rates for its bilateral trade: from 1983 to 1990 the rate was 40.9% and from 1990 to 1999 it was 35%.

Capital investments multiplied, with Portugal occupying a prominent position in Spain's FDI, to the extent that there were years in which Spanish capital stood in second place (1996 behind the United Kingdom; 2000 behind Germany) in the FDI made in the Portuguese economy. Nevertheless, countries such as the United Kingdom, Germany and France maintained a level of investment that outpaced Spain's, providing yet more proof that the threat of Spanish "colonisation" so often proclaimed by Portuguese nationalists had little of substance.

3.3. Nature of today's economic relations between Spain and Portugal

Spain still fails to appreciate the significance its neighbour's market has for its domestic economy, for although it is true that it has been overshadowed by Spain's desire to belong to Europe's fast-lane and by the culture of globalisation, it should not be forgotten that the exchanges made in parallel with Portugal are growing at much faster rates than those with the EU and the rest of the world. The Portuguese market is now a vital one for the Spanish economy, as today it is not only its third largest customer in the EU-25 but also its purchases amounting to €14.84 billion in 2005 exceed the USA and Latin America combined (€12.11 billion) and far outrun those of the emerging Chinese economy (€1.5 billion).

The sharp increase in trade dealings has been accompanied by a sea change in the nature of the goods exchanged as regards previous decades. Spanish exports have furthered their diversification and increased the qualitative component as regards technical complexity and/or value added. Although to a lesser extent, imports from Portugal have gained in diversity and complexity. The major imbalance between the final values of the reciprocal imports/exports in favour of Spain still remains.

Spanish firms and capital are now very present in key sectors of the Portuguese economy, and it also appears that Spanish businesses look upon the Portuguese market as an extension of Spain's and, as such, firms providing personal services that prioritise their proximity to end consumers are present in extremely high numbers in the main cities such as Lisbon and Porto. Central sites in these cities are soon occupied by Spanish banks, large retail chains and the most internationally recognised brands (Zara). Large hotel chains extend their presence further afield to the major seaside resorts in Portugal. The purchase of iconic buildings as head-offices or their construction for commercial purposes or as offices, as

well as the building of shopping centres and hotels, in addition to the building of physical infrastructures, has driven the presence of large Spanish construction firms.

The territorial origin of the exports to Portugal is an excellent indicator of the degree of development, diversification and competitiveness of the economy in Spain's regions. Accordingly, exports in 2006 proceed mainly from Catalonia, followed by Madrid and Galicia. These three autonomous regions account for 54.5% of the total. On the other hand, note should be made of the poor contribution made to bilateral trade by the frontier provinces. This shows that geographic proximity in itself is no assurance of intense trade relations between the two countries on each side of the border. Much more advantageous is the presence of a sound, diversified and competitive economic base. It should be remembered that Portugal has a sharp territorial disparity regarding the distribution of its economic activities, with the Atlantic seaboard concentrating the population, industry and services and a sprawling hinterland stretching to the border that is much less developed. Despite their proximity, the economies on each side of the border have little to offer trade exchanges, in contrast to the major business centres in each country.

4. IN OR TOWARDS AN IBERIAN MARKET?

Over and above the political debate regarding the future integration or otherwise of Portugal and Spain, the Iberian market has laid ample and solid foundations in a very short period of time. As well as visiting the neighbouring country, above all when geographical proximity is indeed an advantage, Spanish people feel increasingly at home; so, too, within the sphere of economic relations and business dealings. One may speak of being comfortably at ease at not feeling a stranger in Portuguese society. These are feelings that reflect the way people in both countries and bilateral business dealings are quicker off the mark than politicians to forge practices and attitudes of trust and common belonging. Nevertheless, they are heading in the same direction, as shown by political initiatives in different fields; for example, when drawing up joint schemes for improving physical communications (motorway and railway networks) and for the use of water from shared watercourses, the creation of natural parks on each side of the border or agreements in sensitive economic sectors, such as the Iberian electricity market scheduled since 2001 or the natural gas supply network. In short, we understand that in both Spain and Portugal, from the Atlantic to the Mediterranean, the prevailing wind is blowing towards mutual trust and true convergence.

