



In a nutshell

- The Spanish general election is the third one in less than four years.
- The party system remains in flux. There is scope for surprises.
- Economic and market consequences could be substantial – and long-lasting.

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Spain's crucial elections

On Sunday, April 28, Spain elects a new parliament. The consequences for the country and beyond could be substantial.

Europe has a busy electoral calendar this year. This makes it hard to decide which votes to pay attention to. In this note, we describe why we think Spain deserves a closer look than it has gotten so far by financial-market participants.

1. Parties and polling

Start with the basics. On April 28, all 350 seats in the Congress of Deputies and 208 of 266 seats in the Senate are up for grabs. Pretty consistently since last summer, polling has put Prime Minister Pedro Sánchez's center-left Partido Socialista Obrero Español (PSOE) ahead. In recent months, PSOE has seen its numbers rise and is currently hovering at around 29%.¹ That's an improvement compared to the just under 23% PSOE won in 2016, but well below its typical vote shares of around 40% from the early 1980s until 2008.

After the death of military dictator Francisco Franco in 1975 and Spain's transition to democracy, PSOE long appeared like the natural party of government. It has occupied La Moncloa, the Palacio where Spain's prime minister resides, for almost 22 years in total. Several of PSOE's stints in government have been at the head of minority administrations, typically propped up by various regionalist and nationalist parties. So, the fact that Sánchez's outgoing minority government has had to rely on minor parties from Basque, Valencian and Catalan regions isn't particularly unusual in the Spanish context. But everything else about the political backdrop is.

PSOE returned to power in June 2018, after it brought down the government of Mariano Rajoy of the center-right Partido Popular (PP) through a motion of no-confidence. Rajoy had been prime minister since 2011. He eventually stumbled over a party-financing and corruption scandal, going back to "at least 1989," according to the verdict by Spain's Audiencia Nacional, the national high court for criminal justice.²

Both PP and its traditional rival PSOE have had their fair share of corruption scandals over the years, as have some of the regionally strong smaller parties.³ With the PSOE having been out of office at the national level in recent years, however, PP has been the main target of voter anger over corruption and an "out-of-touch" political class. Ever since Rajoy's ouster, PP has languished in the polls at around 20%, compared to 33% at the last general election.

¹As a starting point for polling data in Spain and elsewhere, we recommend the pan-European polling aggregator <https://pollofpolls.eu/ES>

²For further details, see <https://www.theguardian.com/world/2018/may/24/court-finds-spain-ruling-party-pp-benefited-bribery-luis-barceas>; <https://www.corruptioneurope.com/case/q%3%BCrtel-case>; <https://www.theguardian.com/news/2019/mar/01/spain-watergate-corruption-scandal-politics-gurtel-case>; and <https://www.theguardian.com/world/2018/jun/01/fall-of-mariano-rajoy-gurtel-spain>;

³https://www.transparency.org/news/feature/after_quertel_what_next_for_spains_struggle_with_political_corruption

Indeed, one way of understanding recent Spanish political history is as a series of interrelated populist revolts, resulting in increasing fragmentation of the country's party system. Leave aside Catalonia's independence movement (which we tackle in the final section) and focus on the rest of Spain. The global economic crisis that started in 2008, bank bail-outs and rising unemployment helped to propel PP to victory in 2011, as might be expected in Spain's traditional two-party system.

By 2014, however, unpopular austerity measures, corruption scandals and the moribund state of PSOE had created an opening for a left-wing populist alternative. This was rapidly filled by anti-austerity Podemos. Together with leftish allies, it won 21% in the 2016 election. That share has since declined fairly steadily, particularly since Podemos helped bring down the Rajoy government and began supporting Sánchez's minority government last summer. Podemos is currently at 13%.

At 15%, Ciudadanos, another recent addition to Spain's political landscape, is slightly ahead of Podemos in the polls. Ciudadanos might best be described as a centrist, liberal party with strong pro-European credentials. Ciudadanos and Podemos are diametrically opposed policy positions, notably in economic matters. Despite this, political scientists have noticed a surprising amount of overlap in voter attitudes notably in distrusting "ruling elites."⁴

Finally, the last party we need to mention is the far-right Vox. Set up in 2013 by former members of the PP, it was barely registered at all in either polling or various elections until quite recently. Its electoral breakthrough came in December 2018, when it won 11% at the Andalusian regional election. Vox is currently at an average of about 11% in national polling. It is worth noting, though, that there has been an unusually wide range in recent polling results for such a small party (ranging from under 8% to almost 13%).

2. The electoral system

It has become quite fashionable to be dismissive of polling. As we have previously argued, this grossly misreads the lessons from events such as the Brexit referendum of 2016 and the U.S. presidential election the same year. Polling misses in the magnitude of a few percentage points are roughly in line with what might be expected from historic experience. Recent quantitative studies underline what we have come to suspect from our experience in forecasting various national elections around the world. There is simply no evidence that the democratic world as a whole has a polling problem. In fact, the data suggests that polling accuracy may actually have improved in recent decades.⁵

To be sure, polling is better in some contexts and countries than in others. Despite quite a volatile party system, it would appear that polling in Spain has actually tended to be remarkably accurate.⁶

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⁴Anduiza, E., Guinjoan, M. and Guillem, R. (2018), "Economic Crisis, Populist Attitudes, and the Birth of Podemos in Spain", in Giugni, M. and Grasso, M., Citizens and the Crisis: Experiences, Perceptions, and Responses to the Great Recession in Europe (Palgrave Studies in European Political Sociology), pp. 61-81

⁵The most recent comprehensive look at polling accuracy worldwide we have seen is Jennings, W. and Wlezien, C. (2018) "Election polling errors across time and space," in Nature Human Behaviour Volume 2, Issue 4, pp. 276-283

⁶Recent number crunching by the newspaper El País using data from all elections since 1986 found an average deviation of only about 2% from each party's polling average in the final stages of the election campaign. See: https://elpais.com/politica/2019/04/08/actualidad/1554742089_430037.html and, for further background: https://elpais.com/elpais/2016/07/08/opinion/1468002744_086098.html, as well as: <http://progressivespain.com/2019/04/09/just-how-reliable-are-spains-pre-election-poll-results/>

That said, an unusually large number of voters still appears ready to change their mind, including a disproportionate number of female voters.⁷ The timing of the vote may be playing a role, with Easter interrupting what has anyways been a fairly short election campaign. Two televised debates among the four biggest parties on April 22 and 23 might also have caused some last-minute shifts in momentum.⁸

Spain's electoral system creates scope for upsets, even if overall national vote totals were to be roughly in line with recent polling averages. Recall that all 350 seats in the Congress of Deputies and 208 of 266 seats in the Senate will be elected by popular vote on April 28.

For the Congress of Deputies, the lower house and main lawmaking chamber, Spain uses a version of proportional representation that is actually quite hostile to parties whose supporters are dispersed across the country. Prospects are especially grim for small, but also medium-sized parties that lack regional strongholds. This is because voters choose their preferred party in each of the country's 52 electoral districts.⁹ The number of Deputies in each district depends – roughly – on each district's population size. Deputy seats are then allocated according to the number of votes each party gets, in the order each party has indicated.

In practice, this means that a vote for any of the smaller parties within a given electoral district is often a wasted vote. Only a handful of districts, typically around large urban centers, elect more than 10 Deputies.¹⁰ In much of the country, there are 5 Deputies or less per district. To make their vote count, voters in less populous districts have strong incentives to choose one of the (locally) leading parties. Historically, this has typically meant the PP, the PSOE or one of regionalist and nationalist parties of known electoral strength within a given district.

It is a strong indication of the wide-spread frustration with the two traditional parties that so many voters are nevertheless willing to vote for one of the newer alternatives. But the current degree of fragmentation does not look very stable. Political science suggests that under Spain's current electoral system, we will eventually see the emergence (or re-emergence) of two big parties plus a regional fringe.

This could already start to happen in 2019 as far as the Senate is concerned. In the Senate, Spain's upper house, each mainland province has exactly four seats. So Madrid, with its 6.5 million inhabitants, has as much electoral weight in the Senate as the rural province of Soria in central Spain, with 90,000 inhabitants. In each of those provinces, each voter gets to pick three candidates and each party typically nominates three candidates. In principle, a voter can choose individual candidates from different party lists. In practice, voters typically cast all three votes for candidates of the

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⁷See, for example: https://elpais.com/elpais/2019/04/09/inglish/1554810504_899111.html

⁸https://elpais.com/elpais/2019/04/17/inglish/1555485592_606737.html; https://elpais.com/elpais/2019/04/12/inglish/1555052464_524300.html

⁹Under Article 68 of Spain's Constitution, these correspond to the country's 50 provinces, plus two autonomous cities in North Africa. See: http://www.congreso.es/constitucion/ficheros/c78/cons_ingl.pdf

¹⁰Madrid, Barcelona and Valencia are the three largest electoral districts with 36, 31 and 16 Deputies respectively in 2016. See Anduiza, E, Guinjoan, M. and Guillem, R. (2018), quoted above, pp. 67, for further details on what the authors quite appropriately call Spain's "disproportional electoral system."

party they also support for Congress. The result tends to be that of the four Senate seats in each province three go to the largest party of the province, with the second largest one securing one seat.

Voting works similarly in Spain's other territories (principally Spain's Balearic and Canary islands), except that each is allocated a fixed number of Senators as stipulated in the constitution. In addition to the 208 Senators elected by popular vote, 58 will be appointed by regional legislatures. Conventionally that is done roughly mimicking the proportional make-up of regional legislatures.¹¹

Ever since the general election of 1996, the rural bias of the Senate has allowed the PP to capture the largest number of directly elected Senate seats. This looks set to change in 2019. Based on recent polling, PSOE may be able to almost triple the number of directly elected Senators, from 43 in 2016. Conversely, PP is likely to see its numbers of Senators shrink sharply. Unfortunately, most polls do not include separate estimates for the Senate. However recent simulations of how the national vote might be distributed on behalf of the newspaper El Mundo suggest PSOE is well on track to win control of the chamber.¹²

3. The scope for surprises and a fairly decisive win for Spain's center left

For Congress, many observers in Spain and elsewhere expect a fairly inconclusive result, perhaps followed by fresh elections later in the year.¹³ By contrast, we would not be surprised if PSOE ended up outperforming recent polling and, in particular, seat projections for both Congress and the Senate. Our reasoning is fairly straightforward. PSOE has re-emerged as the main force of the left, while PP, Vox and Ciudadanos look set to split the vote on the right. Given Spain's electoral system, the consequences for PP are likely to be especially brutal in the Senate, but could also harm its prospects even more than many observers expect in Congress. The same is probably true for Vox and Ciudadanos.

A big source of uncertainty is the likely performance of Vox at the ballot box as well as the distribution of its vote. Like Podemos and, to a lesser extent, Ciudadanos, Vox voters appear primarily motivated by a genuine desire to vent their anger. Tactical concerns over the likely consequences of electoral choices may hold less sway. There is genuine uncertainty among parties, forecasters and indeed voters how well Vox might perform at the level of individual districts.

Our take on Vox is that for the current election, it is best seen as a protest vote against and – mainly – at the expense of PP. Observers may also read too much into its success at the Andalusian regional election in December 2018. This was a low-turn-out event. PSOE

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¹¹To clarify the relationship between electoral districts of Congress, the Senate and regional legislatures, it might help to illustrate with reference the example of Catalonia (also quite relevant for the final section). Under Spain's constitution, the country is divided into 17 autonomous communities (plus two autonomous cities). Each regional autonomous community typically represents a historic region and each has its own set of devolved powers. The extent of such powers varies across different autonomous communities, which was a key source of contention in the case of Catalonia, as we will see. However, each does get to elect a regional legislature. Regional autonomous communities are in turn divided into administrative provinces. In Catalonia, there are four provinces: Tarragona, Girona Lleida and Barcelona. These four provinces also form Catalonia's electoral districts for both Congress and the Senate. The difference lies in how many seats electoral success in any given province translates to. For Congress, Tarragona and Girona each got to elect 6 Deputies in 2016, Girona 4 and Barcelona – reflecting its far larger population – 31 Deputies. For the Senate, each of those provinces elects four Senators, or 16 in total. In addition, Catalonia's regional legislature (as representative of the country's second largest autonomous community after Andalusia), gets to appoint 8 Senators.

¹²<https://www.elmundo.es/espana/2019/03/25/5c96a5c3fdddf60698b4577.html>

¹³<https://www.economist.com/europe/2019/04/20/reading-the-runes-for-spains-general-election>

had held control of the regional administration ever since it became an autonomous community in 1982. The local PSOE leadership had been marred by its own fair share of corruption scandals over the years.¹⁴ Even for Andalusia itself, the experience of similar protest parties in other countries suggests that breakthrough successes at the regional level do not necessarily translate into similar gains in subsequent, higher-turn-out national elections.

This is not to write off the potential of Vox to eventually win a similar share of the vote as right-wing populists have habitually been able to capture in other countries. Alternatively, and more in line with the logic of Spain's electoral system, we could eventually see some agglomeration of Vox and the PP emerge as a more right-wing, nationalistic and eurosceptic alternative to the PSOE than the PP has traditionally been. Demographically, one factor that argues for such an opening is Spain's increasingly depopulated countryside.¹⁵ Recent protests their organizers named the "revolt of an empty Spain" raise some interesting parallels with France's yellow-vest protests. In the longer term, the electoral system would potentially favor such a party. It would be backed up by a coalition of rural voters feeling left behind – similar to the one that caused such upsets as Trump, Brexit and the relative success of Austria's far-right Freedom party at the country's last presidential election.

We just doubt that the net effect, this time around, will boost parties on the right. Our suspicion is that any surprise gains by Vox will be more than neutralized by the vote and seat share of PP and, perhaps, Ciudadanos, coming in weaker than expected. And of course, with Vox, as with any new protest party, uncertainty cuts both ways. It might well do better, but also worse than its recent polling. The principal reason for suspecting the latter is that it typically takes a few attempts to come up with a winning message.

In the current campaign, Vox has positioned itself mainly to provoke. This includes fielding two retired military generals, who last year signed a petition praising General Franco¹⁶, and another one on record belittling the Holocaust and suggesting the 1937 bombing of the Basque town of Gernika by Germany's Luftwaffe was "a myth crafted in England by The Times to justify the British rearmament program."¹⁷ Its policy priorities include repealing Spain's gender violence law (on the grounds that it discriminates against men).¹⁸ And, calling for liberalizing Spain's gun laws in the immediate aftermath of the deadly mosques shooting in New Zealand so that Spaniards can defend their homes.¹⁹

None of this will necessarily hurt the core vote of Vox. But it will probably mobilize voters opposed to it even more. Vox has also dragged both the PP and to a lesser extent Ciudadanos to the right. The PP, under new and fairly inexperienced leadership, has reacted by repeatedly bringing up abortion, until recently a fairly uncontroversial issue in Spain. This has allowed Mr. Sanchez to portray PSOE as the natural choice for voters fearful of the ghosts of

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¹⁴ <https://europeelects.eu/2018/11/20/elections-in-andalusia-seen-as-mid-term-test-for-sanchez/>

¹⁵ https://elpais.com/elpais/2019/04/01/inenglish/1554107629_170580.html

¹⁶ <http://progressivespain.com/2019/03/19/vox-fields-pro-franco-retired-military-on-candidates-lists/>

¹⁷ https://elpais.com/elpais/2019/03/20/inenglish/1553076032_593854.html. The destruction of Gernika was immortalized by Pablo Picasso and contributed to a significant hardening of attitudes towards the Franco regime, notably in the United Kingdom.

¹⁸ https://elpais.com/elpais/2018/12/03/inenglish/1543832942_674971.html?rel=mas

¹⁹ https://elpais.com/elpais/2019/03/21/inenglish/1553170075_849436.html

Spain's past.²⁰ A solid campaign, with a strong focus on pocketbook issues, may also help with late-deciders frustrated with years of austerity.²¹

4. Catalonia and the broader meaning of Spain's elections

In a recent note, we described that a good way to think about contemporary democratic politics around the world is to see it as a return of history "[History Stages a Comeback](#)." That seems especially applicable to Spain and may also turn out to be true for the European elections in May.

In the Spanish case, the dividing lines of the 2019 campaign have not really been between left and right, nor between pro-European and eurosceptic forces. For example, Ciudadanos has traditionally been quite progressive on social issues and pro-European. The reverse is true of Vox. Both are united, however, in wanting Catalonia's "separatists" being brought to heel.²²

Instead, what we have seen is a return of questions that have shaped the history of the Iberian peninsula for at least 500 years. How should Spain be governed? How much centralization is needed? Given regional, linguistic and cultural diversity, how much centralization is even feasible? These questions are, of course, also lingering in many of the EU's other (large) member states. How they might play out has much to do with both recent and not-so-recent history.

In Spain's case, the most remarkable fact is both the recency and the potency of separatist tendencies in Catalonia. For the purposes of this note, it is not necessary to give more than cursory overview of the reasons behind this. As Andrew Dowling, a leading researcher on Spain's history and its contemporary meaning, points out in a fascinating new book, until 15 years ago, "Catalonia was described and analyzed by scholars as exhibiting a non-secessionist nationalism."²³ In other words, it seemed as if Spanish devolution had been quite successful and might even serve as a role model for other European countries.

This began to change in the 1990s, when the PP attempted to centralize more powers in Madrid. A new statute of autonomy was passed under the auspices of the PSOE government in 2006, but a controversial 2010 judgment by Spain's Constitutional Court sharply curtailed Catalan autonomy.²⁴ From 2008 onwards, the financial crisis added further fuel to Catalan desires for more autonomy, if not outright independence. Independence could have a potentially devastating impact on both Spain's and Catalonia's economy.²⁵ Ciudadanos initially organized in opposition to such a split. That helps explain its positioning in the current campaign in opposing the PSOE. And Vox is in part a reaction to the unauthorized

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²⁰Other, smaller parties are of course also trying to benefit from polarization. For an illustration, see: <http://progressivespain.com/2019/04/17/animal-rights-party-slams-vox-in-campaign-video/>

²¹<http://progressivespain.com/2019/04/02/pensions-hit-campaign-trail-as-psoe-pp-trade-barbs/>

²²For a summary of the policy positions taken by various parties, see: https://elpais.com/elpais/2019/04/15/inenglish/1555313118_338133.html?rel=mas

²³Dowling, A. (2018), *The Rise of Catalan Independence: Spain's Territorial Crisis*, Routledge. Also see some of his recent Op-eds: <https://www.historytoday.com/miscellanies/catalonia-spain%E2%80%99s-biggest-problem>; <https://braveneweuropa.com/andrew-dowling-the-late-arrival-of-right-wing-populism-to-catalonia-and-spain>; <https://www.ft.com/content/bf9b908c-a788-11e7-ab66-21cc87a2edde>

²⁴https://www.tribunalconstitucional.es/ResolucionesTraducidas/31-2010_%20Op%20June%202028.pdf also see: <https://www.theatlantic.com/international/archive/2017/10/catalonia-referendum/541611/>

²⁵<http://www.realinstitutoelcano.org/wps/wcm/connect/01e82708-49a4-463c-a65a-a632517a2e80/Commentary-Chislett-Potential-impact-Catalan-crisis-Spanish-economy.pdf?MOD=AJPERES&CACHEID=01e82708-49a4-463c-a65a-a632517a2e80>

– and quite disorderly – referendum Catalan nationalists held in October 2017.

If our prediction for a fairly decisive PSOE victory turns out to be right, one likely implication is that it may lead to a de-escalation of the Catalan conflict over time. PSOE and its allies look almost certain to win enough Senate seats to block any moves to impose direct rule in Catalonia. Under Spain's Constitution, the make-up of the Constitutional Court could also change fairly swiftly.²⁶

For markets, signs of a political (rather than legal) resolution to the conflict would certainly be welcome. For quite a while, Spanish government bonds have already been trading like those of the Eurozone's more stable, semi-core member states. For rating agencies, a key factor will be whether we see increases in spending under a new Spanish government. Beyond Catalonia and government finances, a PSOE victory might also be seen as a boost to center-left parties in the run-up to the European elections. A strengthened center-left government in Madrid could also change the dynamics in discussions over austerity and broader Eurozone reforms. As usual, however, we would caution against drawing too heavily on interferences from one EU member state to what might happen in others.

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²⁶The twelve judges of the Constitutional Court are appointed by the King for one term only, lasting nine years. A third of judges is replaced every three years. Four judges are nominated by Congress and four by the Senate (by a majority of three-fifths of its members in both chambers). Of the remaining four, two are nominated by the government and two by the General Council of the Judiciary, which itself consists of Spain's most influential judges and magistrates. (Articles 122 and 159 of Spain's Constitution.)

Glossary

Brexit

Brexit is a combination of the words "Britain" and "Exit" and describes the exit of the United Kingdom of the European Union.

Ciudadanos

Ciudadanos ("Citizens") is a liberal, pro-market and pro-European party in Spain."

Eurozone

The **Eurozone** is formed of 19 European Union member states that have adopted the euro as their common currency and sole legal tender.

Freedom party

Freedom party is a far-right populist party in Austria.

Partido Popular (PP)

The Partido Popular (PP, "People's Party"), is Spain's traditional party of the center-right

Partido Socialista Obrero Español (PSOE)

The Partido Socialista Obrero Español (PSOE, "Spanish Socialist Workers' Party"), is Spain's traditional party of the center-left.

Unidas Podemos

Unidas Podemos ("United We Can") is a left-wing populist and anti-austerity party in Spain.

Volatility

Volatility is the degree of variation of a trading-price series over time. It can be used as a measure of an asset's risk.

Vox

Vox is a far-right populist party in Spain.

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