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AEP: Spain's export-led recovery comes at a price

Booming car factories behind the country's expert-led revival leave question marks over the true health of Spanish economy, reports Ambrose Evans-Pritchard

The revival in exports masks whether the Spanish economy has genuinely turned a corner Photo: Bloomberg News

By Ambrose Evans-Pritchard, in Valladolid

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Spain's car industry has come back from the dead, saved by drastic wage cuts that transform the social character of Europe.

The French group Renault has restarted night shifts at its plant in Valladolid this month for the first time in a decade as demand surges for its snazzy bi-tonal Captur, much of it from South Korea of all places.

It is a moment that traumatised workers here in the heartland of old Castile never expected to see again after Spain's economy crashed into depression six years ago, and then crashed yet deeper before hitting rock bottom in 2012.

"We all thought this factory was going to be closed. It was a terrible time," said Luis Estevez, a manager of the assembly plant.

Other countries may be mothballing lines or cutting shifts as Europe flirts with a triple-dip recession, but Spain’s 17 car factories are firing on all cylinders. Output has risen 20pc over the last two years, on track to reach 2.4m this year and 3m by 2017, leaving Britain, Italy, Russia and, above all, France ever further behind.

Nissan began night shifts last week at its Pulsar factory in Barcelona. Ford is shutting its Belgian plant at Genk, and switching output of the Mondeo and Galaxy to Valencia. The long-running saga of General Motors’ operations in Zaragoza has ended happily after all. The factory will survive, and thrive. Output will jump 15pc this year, and jump again in 2015 as 80,000 Opel Mokkas come on stream.

The car industry is the spearhead of Spain’s great plan for export-led recovery. Some 85pc of all vehicles built in the country last month were shipped abroad, chiefly to France, Germany and Britain.

The pro-business government of Mariano Rajoy and its allies point to this remarkable surge as a vindication of their policies, proof that it is possible to claw back competitiveness within the eurozone by means of an “internal devaluation”, a euphemism for deflationary wage cuts. “Spain shows what reforms can do. We have become the export champions of Europe,” said Ana Botín, the chairman of Santander.

Keynesian economists counter with equal vehemence that this is a beggar-thy-neighbour strategy, a race to the bottom that shifts the pain within the eurozone to other states that try to defend their social models – chiefly France and Italy at this point – and ultimately sucks the whole currency union into a self-feeding deflationary vortex along the lines of the 1930s.

Renault’s plants in Valladolid, the old capital of the Spanish empire, are so highly mechanised that at first glance they seem post-human. Self-guided carts move around the factory floors on magnetic strips.

The Captur dashboards are lifted and punched into place by Swiss and German robots. Another set of robots lifts the under-carriages from below, snapping them in with a single action, one car every minute. Quality control for the motors is carried out by an array of computerised cameras, programmed to pick up defects down to 40 parts per million.

All the fiddly bits that the workers need to finish off arrive already placed inside the chassis as it moves along the line. It is a method pioneered in Japan, designed so that nobody wastes valuable seconds turning round to fetch things. The speed and repetition is dizzying to watch.

“We want the fewest possible number of people, working as fast as possible,” said the line manager. Output has jumped 150pc in two years to 210,000 vehicles.

Spain’s trade unions have had to accept once unthinkable terms to save their car factories, caught between mass unemployment (27pc at the peak) and new labour laws that make it much easier for employers to demand flexible hours. The term “Spanish practices” has lost its meaning.

A deal reached with Renault after much soul-searching in 2012 cuts entry pay for new workers by 27.5pc, to roughly €17,000 a year (£13,400). Older workers keep their jobs at frozen pay, but with fewer holidays and tougher conditions. Joaquin Arias from the trade union federation CCOO said the terms amounted to blackmail. “The alternative was slow death. We would never have accepted such a plan if the crisis hadn’t been so bad.”

Wage costs are now 40pc below levels in comparable French plants in France, the chief reason why Renault and Peugeot have cut their output of vehicles in their home country by half over the last decade. French unions may rage against “social dumping”, but they now face the asphyxiation of their industry unless they too knuckle under.

“The French factories are going through exactly what we faced five years ago. It is very hard for everybody, but they too are having to follow the Spanish model,” said Mr Estevez.

The Renault expansion is a shot in the arm for the 300,000-strong city of Valladolid, bolstered by flourishing wine exports from the vineyards of Ribera and Rueda along the Duero River, once the frontier between Christian Spain and the Moors. The company has just taken on 700 new workers to cover the night shifts and is adding a further 800 at a nearby factory in Palencia, including a few from the homeless shelters of the Catholic charity Caritas.

In a remarkable reversal of fortunes, Spain is now the fastest-growing of the eurozone’s Big Four economies. Madrid forecasts growth of 1.3pc this year and 2pc next. The jobless rate has dropped from 25.7pc to 23.7pc, and no longer because of mass emigration. The numbers in work have jumped 530,000 in six months.

What is far from clear is whether Spain’s economy has genuinely turned the corner, or whether the boom in car exports reflects competitiveness in the rest of the economy.

Raoul Ruparel from the independent think-tank Open Europe says most of the rebound in growth this year has come from a local spending spree, an unleashing of pent-up demand as confidence returns after years of self-denial.

Fernando de Acuña, head of Spain's top property consultancy RR de Acuña, warns that the country is going through an illusionary mini-bubble, with people betting on a fresh cycle in the housing market when the crippling effects of the last boom-bust cycle have yet to be cleared.

"We think prices will fall by another 20pc over the next three years. There is still an overhang of 1.7m unsold homes in an annual market of around 230,000. The developers have 467,000 units on their books, and half of these are indirectly controlled by the banks. It is extend and pretend. There are another 150,000 in foreclosure proceedings that are backed up because the courts are saturated," he said.

"People don't want to hear any of this. We were called criminals and terrorists when we warned in 2007 the country was going to Hell, but we were right, because we base our analysis on the facts and not on wishful thinking," he said.

It has always been debatable whether Spain can hope to pull itself out of a low-growth trap by relying on exports alone, given that it still has a relatively closed economy with a trade gearing of just 34pc of GDP, far lower than Ireland at 108pc.

The current account is already slipping back into deficit in any case as imports surge, suggesting that Spain is still nowhere near a competitive equilibrium within the eurozone. It is already "overheating" – in a sense – even with 5.6m people unemployed. The International Monetary Fund says Spain's exchange rate is up to 15pc overvalued.

Ominously, the export boom has been fading despite the success of the car industry. Total shipments rose just 1pc in the year to August compared with the same period in 2013, with falls of 11pc to Latin America, and of 13pc to the Middle East. Exports actually contracted by 5pc in August from a year earlier.

Trade experts say the export rebound after the Lehman crisis was the result of a frantic search for overseas markets by firms battling for their lives as internal demand collapsed by 15pc. This is a one-off effect by its nature. It cannot be sustained without an investment blitz, yet the IMF says bank credit to firms is still contracting at an annual rate of 11pc, with a "steadily-rising share of firms under financial distress".

The IMF warns that the country is still acutely vulnerable. "Spain is heavily indebted to the rest of the world. The net international investment position (NIIP) deteriorated further in 2013 almost 100pc of GDP," it said.

The IMF called into question whether Spain really has pushed through deep structural reforms, noting that its "Doing Business" ranking has slipped yet further. Total factor productivity (TFP) is on a “declining trend”, though flattered by the perverse fall of unemployment for now. The labour market remains “segmented between well-protected 'insiders’ on permanent contracts and precarious 'outsiders’, who cycle between temporary jobs and unemployment,” it said

What is clear is that any recovery so far has scarcely reached the victims of the long slump. “The economy has at least stabilised, but we are still helping 4pc to 5pc of the population,” said Father Jesus Garcia Gallo, head of the Caritas network of shelters, soup-kitchens and charities in the region.

“We are seeing a chronic deterioration that gets worse every day, the longer this goes on. There are a lot of people who have exhausted their unemployment pay and simply can’t survive,” he said. Two million people in Spain live in households where nobody has a job.

Caritas has a warehouse at the episcopal headquarters stacked to the rafters with suitcases, each listed to somebody living out on the streets or camping on the floors of distant family or friends. It is like a locker. They drop by to fetch things. Another room is full of washing machines that they use in turns before disappearing again, maintaining a disguise of normality to the untrained eye.

Yet the acute phase of Spain’s ordeal is over, or at least in remission. “It no longer feels anything like 2012, when we feared that the Spanish state might actually go bankrupt and they would kick us out of the euro. Those were really alarming moments for this country that everybody wants to forget,” he said.