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CATALAN QUESTIONS

Berenberg Macro Flash

Yesterday's contested referendum will make headlines for a while. Although it remains highly unlikely that Catalonia will become independent in the next few years, Catalonia's pro-independence forces have scored a tactical victory. The pictures of clashes between the Spanish police and citizens who wanted to cast a vote can

- broaden support for independence in Catalonia, where public opinion has so far been almost evenly split;
- tilt public opinion in Europe and elsewhere a little towards the pro-independence forces, who had so far been largely ignored in Europe;
- make it more difficult for Spain's prime minister Mariano Rajoy's minority government to rule effectively. Finding the votes needed to pass a budget for 2018 could be very tricky.

Is the referendum result a surprise? No. According to the Catalan regional authorities, 90% of the 2.26 mn Catalan who cast a vote endorsed independence. However, as some 5.3 mn were eligible to vote, the roughly 42% participation did not surpass expectations. The vote seems to accurately reflect the division in Catalan society, with around 40% in favour of full independence.

How dangerous is the situation? Reckless behaviour by both sides has inflamed passions. More demonstrations and clashes look likely. Spain faces a political crisis. Still, Spain is a stable democracy under the rule of law. Most likely, its institutions and citizens will be able to cope in the end.

What happens next? Expect a period of significant confusion. Before the vote, the Catalan regional government announced that it would formally declare independence within 48 hours of a "yes" vote. Madrid may respond by formally curtailing the powers of the regional government. If Barcelona declares unilateral independence, the practical consequences would likely remain limited despite a lot of noise including strikes and mass protests. Catalonia would not have the means, including the fiscal means, to enforce a full independence. Problems would abound soon: who collects which taxes, who controls the regional police etc.. At some point in time, Barcelona and Madrid will need to talk.

Could the political uncertainty derail the economic recovery? The period of confusion may cause a dent in Spanish economic sentiment and – possibly – slow down Spanish growth modestly from its exuberant pace of 3.2% to, say, 2.5% until the tensions ease. But the overall Spanish recovery looks too broad-based and well-entrenched to be derailed by Catalan uncertainties. For the Eurozone as a whole, the possible Catalan impact will probably be too small to make a noticeable difference.

Will Catalonia gain full independence soon? No. For the foreseeable future, we see no practical way for Catalonia to become an independent country within the EU, as most supporters of independence want. The EU can accept new members only if all existing members agree. Catalonia would thus need Spain to say yes. That Madrid would agree to outright Catalan independence looks highly unlikely for the time being, that is in the absence of a major shift in the Spanish political landscape away from the centre-right and centre-left parties that strongly oppose Catalan (or Basque) independence.

Will the EU intervene? Only in a low-key way, if at all. The EU is the club of its member states, not of the regions within its member states. Madrid represents all of Spain at the EU. Catalonia would have to settle



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its differences with Spain first before the EU could talk to Barcelona in a meaningful way. The EU will be reluctant to get deeply involved and probably shy away from official intermediation.

Is there a way out? Yes, but it will take a while until Madrid and Barcelona go down the only viable route. The legitimate wish of many Catalans to have more say over their affairs requires a political solution. In a way, the solution has been obvious for a while: Catalonia stays part of a reformed Spain while Spain grants Catalonia special status with much more power over taxation, akin to the special status of the Basque region. Such a deal may be very difficult to achieve immediately. With luck, the shock of yesterdays clashes will make both sides realise after a while that they both have overplayed their hand and need to talk. If and when that happens, the Catalan side will likely now have a stronger hand in these negotiations than before.

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