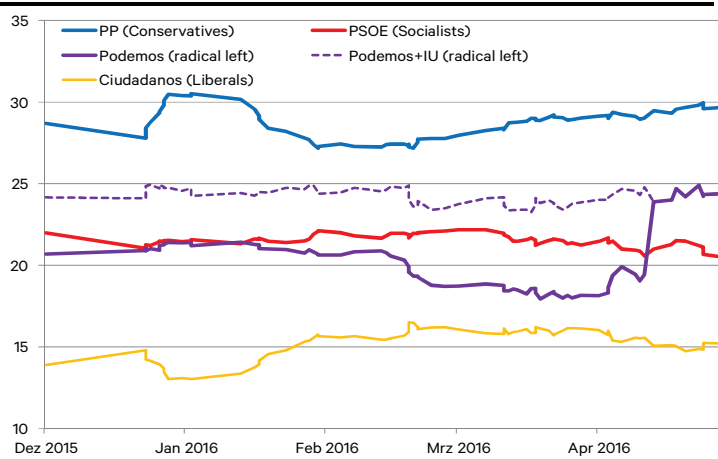


20 May 2016

The risk in Spain

Voting intentions for Spanish repeat elections on 26 June 2016



Voting intentions in %. The starting value is the result of the 20 December 2015 election. The dotted purple line gives the combined share for radical-left Podemos and the Communist Izquierda Unida, which joined forces for the 26 June election in April 2016. Source: Various Spanish polling institutes, Berenberg calculations.

- The economic outlook for the Eurozone remains quite satisfactory:** Growth is oscillating around its trend rate of 1.6%, unemployment is receding and the ECB's additional stimulus of March 2016 should help to keep domestic demand on track, despite a lessening tailwind from cheap oil. After a likely dip in growth in Q2 as a payback for an exceptionally strong Q1 result, we expect the drag from the recent emerging market crisis to fade over the summer, allowing growth to return to its trend rate from Q3 onwards.
- The year of political risks:** Political upsets pose the major risk to the outlook for stable growth this year. Beyond the much-discussed Brexit referendum in the UK on 23 June, we also have to keep an eye on Spain's repeat elections on 26 June and the Italian referendum in October on downsizing the Senate.
- Stalemate in Spain:** On 20 December 2015, Spain's Prime Minister Mariano Rajoy lost his majority. A numerically possible coalition between Socialists, Liberals and the radical-left Podemos did not materialise either. This was largely because the Socialists and the Liberals, who both strongly oppose Catalan demands for independence, could not agree on Catalonia with Podemos, which has promised an independence referendum for the region.
- No change in the polls:** Voting intentions for the repeat elections on 26 June are similar to those five months ago, with only minor gains for the Conservatives and Liberals. However, Podemos has now teamed up with the Communists, who had won 3.7% in December. Because of the quirks of the voting system, the combined ultra-left may gain some 10 more seats than the two parties won separately in December with the same share of the vote. That could offset the slight advantage that polls would otherwise suggest for a Conservative-Liberal alliance.
- What if?** A left-left alliance between Podemos and the Socialists remains a risk. But disagreement about Catalonia makes it unlikely that the Socialists would accept such a coalition, especially as they could well be the junior partner. Unless the Conservatives and Liberals manage to jointly gain a majority of seats for a pro-reform coalition, the most likely way to resolve a stalemate would be a coalition between Conservatives and Socialists. For that, the Socialists would likely demand that the Conservatives nominate a new prime minister rather than Mr Rajoy.
- A problem for Europe?** Probably not. Any coalition including the Liberals and/or the Conservatives would pursue largely sensible policies. A left-left coalition, which we view as unlikely but not impossible, would reverse some of the reforms that have turned Spain into one of the fastest-growing economies in Europe. That would be bad for Spain. But, as in Portugal, a leftist government would likely shy away from a full-blown confrontation with the European Union. Support for the euro remains strong in Spain. We would expect some noise but not a real crisis.

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