European Financial Crisis and Political Economy of Austerity Measures in Spain

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Introduction

Europe has been always seen as a place where social contract has engineered to a great deal leadership in making national policies. It is a place where public service is cherished in order to guarantee every individual with promised tranquil retirement, life, and social community. It is a place well known where women are respected, a place where public education creates the gist of national assets in every tangible industry and social life. It is Europe where the poorest and the leader fortunate are taken care of, and where market exist to harness good for society rather than the laissez faire spirit of capitalism. Yet, Europe has failed to escape the doomed bailouts of financial firms as in United States, and countries have also reached state of default, which contradict the underlying values cherished in the continent.

Spain has been one of the countries that suffered from the double-dip financial crisis sprang up in 2008 and having caused a sovereign debt crisis in Europe. This paper attempts to analyze what is the real cost and benefit of the austerity measures that were implemented by Spain, alongside the provision of financial resources from ESFS in July 2012. To make long story to short, the authority of Spain implemented the austerity measures in response to the first dip of global financial crisis, which caused a deterioration of condition of the national and regional public finance there. This caused, in turn, the second economic downturn due to the deteriorated public finance and bad loans in financial sectors that made the financial market unease.

Following these economic background, this paper focuses on the outcome of the austerity measures in relation to the general election that was held in 2011 November. In short, the reason why Spain could have relatively smooth provision of financial policy is because the austerity measure in response to the crisis in 2010 prepared the spontaneous fiscal entrenchment and originally satisfied the conditions of the provision of the resource from EFSF, European Financial Stability Fund. Furthermore, the market fierce for the collapse of the fourth largest economy in Europe was the common concern between Spain and the supra-national body, EU headquarters and other major economies.

In the end, this paper concludes that the major reason of the successful provision of financial injection from EFSF was due to the two reasons; the spontaneous entrenchment and common profit to avoid the deterioration of Spanish economy.

This paper is composed of three parts. The first chapter reviews the main economic indicators and major events, and sort out the major events regarding the theme alongside the chronology. The second digs more into detail about the austerity measures implemented in Spain to tackle the crisis and attempts to figure out the relationship between the timing of these austerity measure implementations and the general election, from the political perspective. Thirdly, this paper reviews the international side of the theme; which are the economic side of the crisis focusing on the significance of Spain in international financial market and the politics of EFSF, and in turn tries to analyze the distribution of the cost of the measures and the crisis according to the previous researches. In the end, this paper concludes that the successful provision of the financial support from the supra-national body EFSF was due to the spontaneous fiscal entrenchment of Spanish authority, and the match of the profit between the major other economies in terms of international financial market.

Chapter 1; the background indicators during the financial crisis and chronology of the response of Spanish government

As widely known, the global financial crisis sprang up in America in 2008 due to the depreciation of financial derivatives such as Mortgage Backed Securities(hereinafter, MBSs) or complicated financial product. According to Crotty (2008), in the pre-history of the global financial crisis, “Banks earned large fees securitizing mortgages, selling them to capital markets in the form of mortgage backed securities (MBSs) and collateralized debt obligations (CDOs), and servicing them after they were sold.” This caused a tremendous damage to the international economy as a whole with various extent

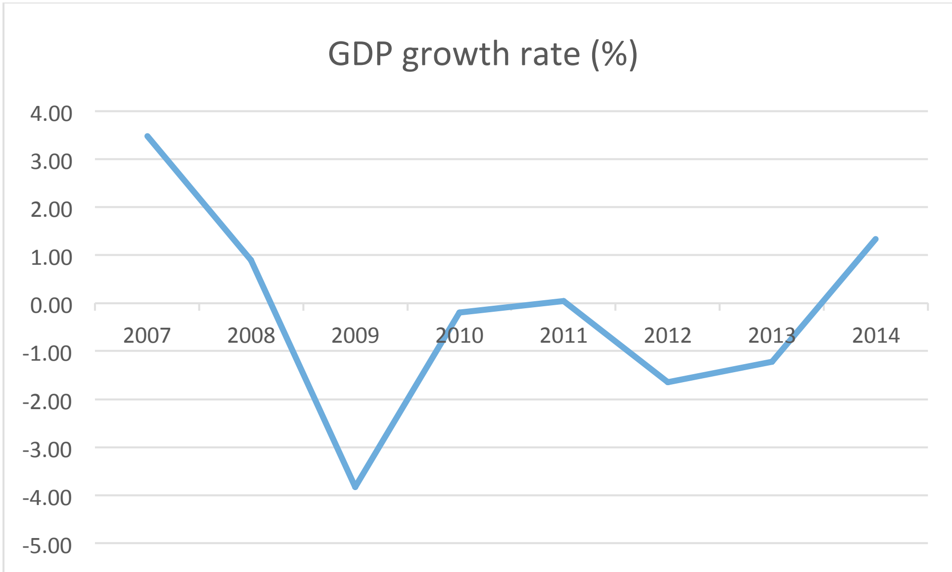

Figure 1 GDP growth rate of Spain from 2007 to 2014 (Source; World Bank database)

As mentioned in the introduction, this crisis had two-dipped curve in during the crisis in 2008 to 2009 and in 2011 to 2012, where the growth rate fell down to almost 4% in 2009 and -1.5% in 2012. The first strike was the American origin and the second one is the so-called European debt crisis, whereas the second dip was the European origin due to the market uneasiness about the ability of reimbursement of public debt by the peripheral countries such as Spain, Italy, Greece and Portugal.

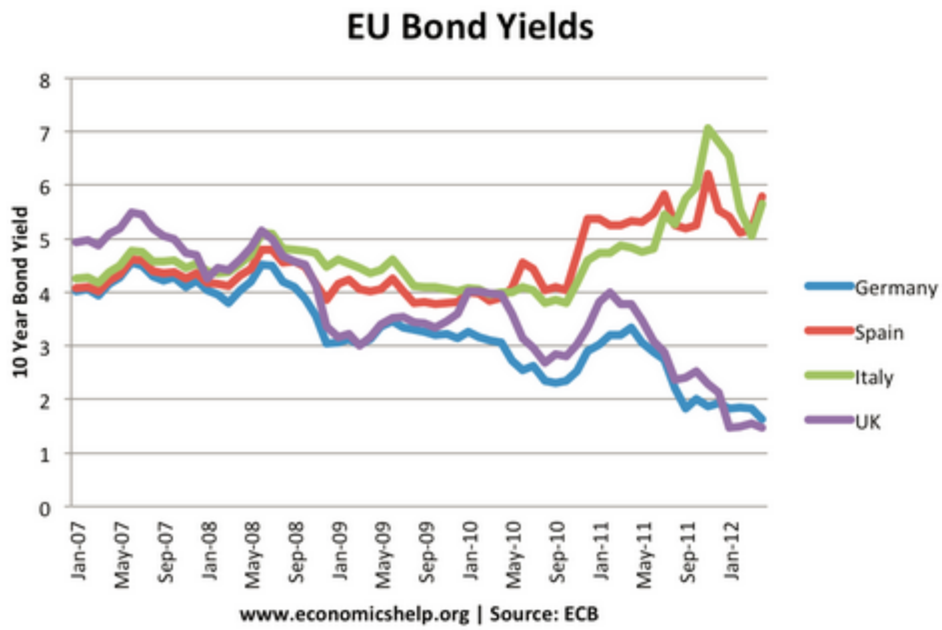

Figure 2 the Bond yields of the EU economies from 2007 to 2012

The figure 2 shows the bond yields of 4 countries in Europe, Germany, Spain, Italy and UK. This figure represents that the gap of the bond yields of Spain and Italy started deriving from the ones of Germany and UK which were regarded relatively safe assets in the European economy, and reached even just over of 6%. This means that the uneasiness of the market was pervasive during this period for the deterioration of public deficit of the south European countries.

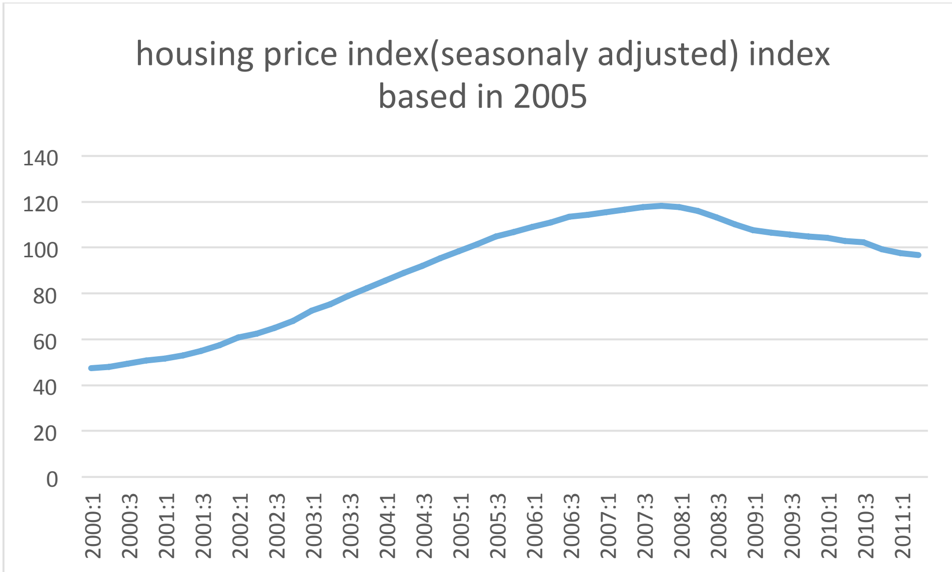

Figure 3 housing price index in Spain (source; Queens University database)

In addition, what is not ignorable when arguing about the Spanish economy is that the existence of the housing bubble from around 2000. As easily be seen in the figure 3, the housing price had been steadily rising from January 2008 to 2011, with the substantial amount of current account deficit throughout the period. This means that the investment to the construction sector was bolstered by the inflow of foreign capital to the economy and the withdrawal of such foreign capital from the market caused the sharp decline of housing bubbles and GDP. In this regard, Akin et al. (2014) suggests that by saying "despite some adjustment in lending conditions in the good times depending on borrower risk, the results suggest too soft lending standards and excessive risk-taking in the boom." the lack of the consolidated governing structure of the small saving banks called "cajas" in Spain led to the more softened standards of lending during the boom and worsened the real estate bubble. It will be mentioned later that the bad loans in the "cajas" with less financial transparency and governing structure led to the difficulty of the assessment of the bad loans in the political response.

The chronology of the political actions of Spanish government

During the crisis aforementioned, the government of Spain was forced to implement austerity measures, along the stage of the crisis. In this part, the history of the actions of the government and events are provided in order to clarify the interactions between the government and other entities with which it becomes possible to analyze the academic implications in this paper.

According to the sets of articles from newspapers and magazines, the chronology listed below can be led.

March 2008

Prime Minister Jose Luis Rodriguez Zapatero wins a second term in office, but without an outright majority.

Third quarter 2008

Economy officially enters recession. Standard & Poor's is the first credit rating agency to downgrade Spain, cutting its treasured AAA rating by one notch to AA+.

Spain adopts an economic stimulus plan worth an estimated 5pc of GDP, including €8bn (£6.5bn) euros of infrastructure projects.

The Bank of Spain bails out regional lender Caja Castilla-La Mancha, the country's first bank rescue in recent years.

May-June 2009

Spain creates a bank bail-out fund, known as the FROB, with firepower of up to €99bn euros and urges weaker savings banks to merge to improve solvency.

First quarter 2010

Spain's economy exits recession.

April 2010

As talks intensify on granting Greece an economic bailout, **attention turns to Spain amid worries over its public deficit** - 11.2pc of GDP in 2009.

May 2010

After initially denying Spain was in trouble, Zapatero announces austerity measures worth around 1.5pc of GDP. Austerity measures passed over the following six months, including a two percentage point rise in VAT, are worth an estimated total of 5pc of GDP.

June 2010

Spain's cabinet approves a labour market reform. The bill is passed through parliament in September.

December 2010

The central government forces the country's 17 autonomous regions, considered the weak link in spending cuts, to publish more details of their accounts.

January 2011

Spain passes pension reform that will gradually raise the retirement age to 67 from a previous 65.

June 2011

Zapatero decides to bring forward national elections to November, four months early.

September 2011

Parliament passes a constitutional amendment forcing governments to keep balance budgets.

November 2011

Mariano Rajoy's centre-right People's Party wins an absolute majority in November 20 elections as voters punish the outgoing Socialist government for the economic crisis.

December 2011

New government says on December 30 that the public deficit for 2011 would come in at 8pc of GDP, well above a target of 6pc. The government also announces new austerity measures with a cut in public spending by €8.9bn in 2012 for all ministries. Treasury Minister Cristobal Montoro announces tax hikes to focus on the wealthy, raising around €6bn.

January 2012

Spain ends 2011 with almost one-in-four of its economically active population out of work. The jobless rate jumps to 22.85pc, or 5.27m people - the highest in the European Union.

March 2012

Spain will aim to save more than €27bn in its 2012 budget through corporate taxes, freezing civil servant wages and ministerial spending cuts. Rajoy has said he will reduce the budget deficit to equal to 5.3pc of GDP in 2012 from 8.5pc of GDP in 2011.

First quarter 2012

Economy falls back into recession.

April 2012

Thousands of people protest across Spain against government cuts aimed at tackling the debt crisis.

May 2012

Government says 2011 public deficit 8.9pc of GDP.

May 2012

Bankia asks for a €19bn state rescue on May 25. Spain is nationalising Bankia, which holds some 10pc of the country's bank deposits, weighed downn by heavy losses from the property crash.

June 2012

Montoro says Spain's high borrowing costs mean it is effectively shut out of the bond market and the EU should help Madrid recapitalise its debt-laden banks. Spain still needs to refinance about €82bn of debt in 2012, while helping its regions to repay maturing debts of about €16bn in the second half of 2012.

June 9, 2012

Spain bows to bailout of struggling bank sector. Eurozone finance ministers agree to lend country up to €100bn to shore up its banks and Madrid said it would specify precisely how much it needs once independent audits report in just over a week.

(source; Telegraph http://www.telegraph.co.uk/finance/financialcrisis/9319175/Spains-economic-crisis-a-timeline.html

Partly edited by author)

The shown above is the outline of the events. And the latter is the more in detailed descriptive information about the chronology.

When the PSOE (Partido Socialista Obrero Espanol) came to power after winning the election in March 2008, the Government repeatedly refused to speak about “crisis” and only admitted an economic “desaceleración”. It was not until June 2008 that Zapatero admitted that Spain was in a dire situation and started adopting an austerity plan starting with reduction of public spending in the public administration. It was followed further with major reduction of public job offers in 2009 with sharp decrease comparing with that of 2008 the freezing of salaries of high positions in the public administration. The government launched a plan with 24 economic measures which influence major sectors including transport, energy, telecommunication, environment, housing and financing of small and medium enterprises.

In 2008, the Spanish government announced new plans for economic activation along with 11,000 million Euros for public investment, 8000 of which to be destined to town halls to finance public jobs (Fondo estatal de inversión local).

In January 2009, four major fields were prioritized for new economic measures called the Plan E(Plan español para el estímulo de la economía y el empleo) with 82 economic measures in particular on: 1) aid to families; 2)promotion of employment;

3) modernization of the economy, and; 4) support to the financial sector. Promotion of subsidized housing was also created, which marked one of the most important measures in terms of social rights.

In September 2009, the Spanish government decided to increase the IVA (VAT) and the abolition of the (Estrada-Cañamares et al, 2014).

In May 2010, the Spanish government again announced reduction of 15000 million Euros in public spending, mainly relevant to the salaries of public officials, the retirement pensions (which already had frozen since 2010), the abolition of the cheque-bebé (which was introduced in 2007) and the Ley de la Dependencia. The main controversy was revolving around the impact that those cuts were bringing about to two major government spending, on the healthcare system and on the education system.

In September 2010, a new labor reform was introduced by the Spanish government, which constituted reducing the cost of dismissals and introduction of new instruments to deal with unemployed better.

In June 2011, a reform on retirement pension program was initiated by the government, with the major change of the retirement age from 65 up to 67 years.

In February 2012, the recently elected Government of the PP (Partido Popular) introduced a new market reform. The reform aimed to reduce the cost of dismissals, allowed for collective dismissals of public officials and gave more freedom to employees to modify working days, salaries, timetables and positions. A 10,000 million Euro cut by the government in April was followed, which greatly affected the healthcare system and the education system. Roughly about 7,000 million Euros cut was counted in the healthcare system, with introduction of the copago (co-payment) of medicines, which greatly depended on the income of the individuals because it set up fixed rate on medicines to be paid by individuals including those who did not pay any under pension. In details, employed individuals with annual income below 18,000 Euros had to pay 40% of the price of medicines as before, but now those whose annual income ranged between 18,000 and 100,000 Euros now have to pay 50% of the price of medicines, and those who earn above 100,000 Euros per year have to pay 60% of the price. Meanwhile, on the education system, it increased the maximum number of students per class and the amount of class hours per teacher.

In May 2012, the Spanish government bailed out Bankia, the fourth largest bank of the country, with more than 23000 million Euros injected in the process. By the end of May, Spain's risk premium rose to 530 points, and the EU warned Spain that it should reduce public spending in order to control its public deficit.

In June 9th 2012, the Spanish government publicized officially its interest to ask for European financial assistance to recapitalize banks, and it argued tha the Eurogroup had responded positively to its message in the meeting they had on the same day. Later in June 25th 2012, the Spanish government officially made a request for financial support for banking industry in particular. The European Commission along with IMF, the European Central Bank (ECB), and European Banking Authority (EBA) reached an agreed assessment that Spain was indeed eligible for requested financial assistance. Once they reached an agreement, they also came to an agreement with Spanish authorities upon the specific policy terms and conditions on financial sector, which were to be attached to the financial package, culminating in a Memorandum of Understanding on Financial-Sector Policy Conditionality and a Financial Assistance Facility Agreement.

This Memorandum states that the main objective of the bailout is "*to increase the long-term resilience of the banking sector as a whole, thus, restoring its market access*". The central objective following was to reinforce the weak components of the Spanish financial industry. As Estrada-Cañamares rightly points out, however, the memorandum also stipulates the fact that "*there is a close relationship between macroeconomic imbalances, public finances and financial sector soundness*", which was in its implication, the reason why Spain was then compelled to ensure the attainment of deficit targets of 6.3% of GDP for 2012, 4.5 of GDP for 2013 and 2.8 of GDP for 2014. In addition, the Memorandum "invites" Spain to introduce changes, ratifications, and modification in concrete fields such as its taxation system as to be "more supportive to growth" and to impose and implement relevant labor market reforms.

In July 13th 2012, new reforms were introduced by the Spanish government, and among them the most important reforms were the increase of the IVA (VAT), the increase of the Impuesto de Sociedades (Corporate Income Tax), the reduction of housing assistance, the cut of unemployment benefits, the modification of the Ley de Dependencia, and the reduction of public spending in public officials (e.g. the extra pay of December is abolished) (Estrada-Cañamares et al, 2014).

In August 2012, the Government withdrew the tarjeta sanitaria to irregular immigrants, which made the access of those irregular immigrants to the healthcare system now is limited to very specific cases only such as emergency care.

During the second half of the year 2012, especially from September to November the Spanish press repeatedly warned the imminence of the second bailout in Spain, at this time for Spanish public debt after the first bailout in financial banks. The Spanish government then organized a commission to conduct a set of reforms for the public administration and public service, against suspected dysfunctional and malfunctioning bureaucracy, corruption, and duplicities. The Spanish government also implemented the labor market reform that was introduced in February of the same year, for collective dismissals in public administration.

The establishment of EFSF as an supra national body for financial stability

When the topic of this theme is considered as an issue, the system setting and the politics in there cannot be ignored as a counterpart of one sovereignty. The EFSF was created as a temporary crisis resolution mechanism by the euro area Member States in June 2010. The EFSF has provided financial assistance to Ireland, Portugal and Greece. The assistance was financed by the EFSF through the issuance of bonds and other debt instruments on capital markets[1]. This institution is a company which was agreed by the countries that share the euro on May 9th 2010 and incorporated in Luxembourg under Luxembourgish law.

However, Gocaj(2013) points out the existence of path dependency "in the subsequent management of an unrelenting crisis, enshrined intergovernmentalism as the modus operandi, and led to suboptimal solutions". Furthermore, it also suggests that "Historical institutionalism[2] aims to explain how a policy outcome at a particular critical juncture triggers feedback mechanisms that reinforce the recurrence of a particular political pattern and restrict the policy options available later on in the historical sequence.

From this perspective, the establishment and the function of the EFSF as a supra-national body are not necessarily optimum or the best solution to the response

[1] the introduction of the institution from the HP http://www.efsf.europa.eu/about/index.htm
[2] For more in detail, refer to Steinmo(2008)

to the crisis, whereas the contradictory approach, rational choice approach, suggests. While the rational choice approach implies institution is fruition of rational choice based on material motivations such as economic profit, historical institutionalism suggests in a practical level that the conditionality that the institution imposes does not necessarily leads to the economically best solution. Actually, Gocaj(2013) suggests that the establishment of EFSF entailed "political sunk cost" in each country to pass the bill for approval, for the purpose of being persuasive to market, by pointing out the volatility of the downgrading of EFSF in the case of the one of advocating countries.

Therefore, when discussing the provision of financial support from EFSF, it should be noted that the conditionality and the policies implemented in fact are not necessarily optimum and in turn does not mean that It can contribute to the revitalization of the Spanish economy.

Chapter 2; Evaluation of the facts

As partly mentioned in the first chapter, the more intensive attention began to be paid to Spain, by being triggered by the profligate fiscal management of Greece in 2010. For the fact that the external dependence of Spanish economy was high, the concern of the market toward the fiscal management of Spain was reflected as the soured bond yields and the gap of it with German bonds. Therefore, it can be said that Spain had an incentive to, more precisely saying it has no choice but to, implement austerity measures for sustaining the fiscal conditions even if the measures are unpopular and in contradiction to the political claims as a leftist ruling party.

The model of responsiveness and responsibility

Here. In order to consider the relation between the election and the perception of the result of the austerity measures, the theory Bosco et al (2015) suggests explains. According to this theory, there are two concepts in contradiction, responsiveness and responsibility, imposed upon incumbents in authority. This claims that while it put a premise that “political parties are in contemporary democracies have shown a diminishing capacity to exercise simultaneously the basic function that allowed the development of modern democracies to govern and to present”, “its organizational changes that moved parties away from civil societies and reduced the size of their membership” and “the diminishing levels of party`s identification have parties less able to listen to their electoral base, to express the demands and to mobilize their voters”.

In fact, the case of Spain in Europe financial crisis, the government of Spain was at first hesitated to admitted that the economic crisis as crisis but continued to say it was a “de-acceleration” for the first time, in terms of the relationship with the domestic voters, and in the next stage the government turned to a stimulus package in 2008.However, the worse the public deficit becomes, the less they are willing to, or just could not, take political responsibility as a leftist party that has a more propensity for the bigger role of the central government, and inclined to pursue for the responsiveness to the crisis major in front to end up with the series of austerity measures.

This forced a large extent of burdens to its domestic voters in various fields such as employment, welfare in general and so on. In this sense, the interpretation that the distribution of the cost of the crisis in terms of austerity measures and the tax burdens due to the solvency measure for the banking sector could not avoid being perceived as unfair by the voters is compatible, and it is consistent to anticipate that this perception of the voters led to the land-slide victory of the rightist party, Peoples Party, in 2012 election. As a matter of fact, Bosco et al(2015) states that “The economic storm that has broken out in Southern Europe has shown that when incumbents are ‘responsible’—abiding by the agreements with the external actors—they end up neglecting their voters’ demands. This has imposed a heavy electoral toll on South European government parties”, meaning the trade-off of their responsibility for its fiscal management and the popularity from the voters.

Furthermore, the fiscal retrenchment during this periods in southern European countries could not ignore the response of market response. Mascio et al(2012) suggests that “there is a broad consensus that the New Public Management(NPM) has constituted the most visible attempt to reform the public sector across the western world and beyond”, where the NPM is market-familiar direction. This is because that were familiar with the concept of Marketization and Modernization which decentralization and agencification.

In this sense, It should be noted that if they had inclined to responsiveness to the crisis too much, they would not have satisfy credibility of the other countries for the financial rescue and of the international market. As pointed out, as the EFSF has a fragile system setting, not only would it have been more difficult for them to satisfy the conditionality of the financial support but also the financial procurement of EFSF per se would have been more jeopardized in the sense where there is a high correlation between the grading of the issued bonds of EFSF and advocating countries such as France and Germany.

Evaluation of voters, from the rational perspective

On the other hand, whereas there was suggested the dilemma between responsiveness and responsibility, it is necessary to consider the perception of the voters toward the austerity measures. Anderson (2000) says “there are different ways to conceptualize how political contexts may help to mediate the relationship between economic performance and political preferences" and it "refers to them as institutional clarity of responsibility, governing party target size, and clarity of available alternatives". As for the criteria of governing party target size, it suggests that the target size of the incumbents' parties in ruling position affects the dilution of and the allocation of responsibility of the economic damage.

The analysis of the austerity measures

As mentioned above, the evaluation and the ideological analysis of the sets of austeiry measures are important to address the perception of the voters.

According to Blyth (2013), austerity is the deliberate deflation of domestic wages and prices through cuts to public spending designed to reduce a state's debts and deficits, increase its economic competitiveness, and to restore though somewhat vaguely conceptualized "business confidence". Austerity in theory guarantees less intervention of the government comparatively than before, as to boost private investments in market with consumers and produces confident about the future therefore more inclined to spend more, which will lead to economic growth coming out of the recession.

However, reality has been suggesting a different answer, where Portugal, Italy, Ireland, Greece and Latvia all point out to far from economic growth. More than enough statistics are available today, which contradict the promised result of austerity plans. Then, the lingering puzzle goes as following: why austerity has been around and remains as the central policy response to financial crisis around the globe and in the Eurozone in particular? According to Blyth, this is due to both material and ideological reasons. This is materially, because there are not many other options available at this time: unlike United States, the EU does not have counterpart system due to its institutional makeup like a central Treasury of the United States and a central bank capable of dealing with any sorts of collateral impact. The EU had at best some additional liquidity, spending cuts, and incantations of its “unshakable commitment to the euro”. Austerity is also ideologically attractive, because simply of its core claim that you cannot cure debt with more debt.

However, some factors challenge the austerity regime in its claim to serve as crisis cure. The first factor is distributional relevance. When government cuts its public spending, the blow hits the country with different intensity across the social class and different levels of society. Those who are the least fortunate and the poorest feel it more sharply because they depend more heavily on government spending. It consequently makes the poorest and weakest to pay the cost of austerity by reducing public expenditure while those who can are not asked to.

The second factor to be considered is a matter of chronicle. Austerity theoretically assumes that public frugality will eventually induce more private spending. However, when the unit of the actors become states in European context, it contradicts the very nature of the European Union, as in supposition Spain reduces their cut in spending with deeply interconnected trading partners in Europe, the regional economy itself will be in contradiction. In other words, for Spain to benefit from a reduction in its domestic wages with expectation that by doing so it will produce more competitive costs, there must be another country willing to spend its money on what Spain produces. Therefore, European countries have to work in punctuality for the plan to work while the reality has been that many countries are trying to save or buy at the same time.

The last factor to suggest is logical. This goes back to the preposition of the austerity theory suggests mentioned briefly before in the previous paragraph-the frugality of public spending will eventually promote more private spending. As the economist Paul Krugman has argued, this claim assumes that consumers anticipate and incorporate all government policy changes into their lifetime budget calculations. When the government signals that it will cut its expenditures in a dramatic degree, the argument is that consumers will then realize that their future tax burdens will decrease, which make them consequently to spend more money now than they would have done without the cuts in government expenditure, all to at the end put a period on the recession. However, it is also an assumption, a improbable one, that financially illiterate, consumers at all kinds of level of social context will also act as it expects, despite the eminent threat of losing their jobs in the midst of the recession.

Austerity in this sense ignores the externalities it produces, impact on one individual's choices another's, and the low chance that people will actually comply with the expectations the theory imposes (Blyth, 2013).

In case of Spain, it has just escaped from two consecutive years of recession with a third quarter growth rate of 0.1 percent by 2013. By this data, the Spanish recession is officially over. However, micro context of the country yet suggests a long way to recover before it can confidently say that it is officially over not only with the recession but also with the diminishing sides of austerity that was implemented for the past couple of years, imposed indirectly but also aggressively by Germany-led European Union.

In Spain as of 2013, unemployment still remains stubbornly high at 26 percent, while half of those age 25 and under in labor market are still unemployed. More than half those age 25 and under in Greece and Croatia are also unemployed. In Europe, only in Germany and Austria is youth unemployment under 10 percent. Greece and Spain lead the sorry list of European countries with more than 25 percent unemployed, and 13 more are enduring joblessness at more than 10 percent (Wapshott, 2013).

When Spain only finds economic growth in some of the export sectors, there is only weak message to be offered that the economy has been genuinely cured by this protracted austerity regime. Domestic demand is still far from satisfaction with confident claim of full recovery. Wapshott elaborates further that such growth is not enough to create jobs and the labor regulation reforms that have accompanied austerity mean growth now has to be at somewhere between 1 and 1.5 percent before new jobs are created; to spur on job growth, labor-intensive industries like construction need to expand. Yet there is little sign of that happening.

The origins of Austerity trace back to liberal economic thinking about the state. The seventeenth-century English thinker John Locke in his literature *Two Treatises on Government*, acknowledge that there will be an inevitable inequalities that market creates, and in such case the state should intervene to deal with inequalities. However dilemma comes when the state does that duty effectively, because then it means that the state is also strong enough to threaten the property holders it was supposed to protect in the first place; how to find the balance to live in the state that can threaten the property holders, but nevertheless the state that property holders cannot live and live without.

This question was later articulated further by David Hume and Adam Smith in eighteenth century, with the answer they found out and they were not really font of and only to conclude that it should be avoided at all cost: government debt.

Later in nineteenth century, while David Ricardo was seeking for extreme measures such as abolition of the state from economic intervention at all, John Stuart Mill pondered on the role for the state and government debt with more creativity.

Mill's argument is that government debt should not have to bankrupt a country and can be used so as to use for beneficial social investments. To add, Mill predicted more precisely that self-regulating and equilibrium-reaching market is not likely to be able to exist because of labor agitation, volatility in the market especially with business-cycle, political externality, and poverty pervasive at the time.

In twentieth century, this resulted in two schools of thoughts splitting from traditional liberalism, commonly known as Austrian School following Ricardo on one hand with rejection to state intervention, and a group of British economists following Mill on the other with advocating active intervention and, if needed, indebted state.

The Austrian School of Economics argued that the binge of debt financing could be cured only by the purge of austerity, and the role of the state was to get out of the way and let the profess unfold (Blyth, 2013). "Liquidationism", letting failing enterprises be liquidated as a solution to economic problems, was the underlying idea, which the United States also used during the Great Depression only to turn out to be a failure. Although in1930s Keynes along with his literature *General Theory*, raised considerable criticism against the Austrian School, the financial crisis of 2008 brought and marked a sharp return of the Austrian model as the default model for crisis response in the Eurozone today.

When there have been clear arguments that austerity does not work, question as to what would be the alternatives to austerity are yet subject to fevered debates. Although a government already in debt to go on spending sprees is obviously not a desirable option, keeping simplicity, one can suggest at least that governments in recession should not cut spending. As Richard Koo has argued, countries cannot simultaneously shed their public and their private debts although this is exactly what Europe has been doing. Rather, governments should get the private sector to pay down its debts while maintaining public spending. Then, as the private sector recovers, tax revenues will increase, and the accumulated debts and deficits can start to go down (Blyth, 2013).

Figure 4 ***Impact of Austerity on Social and Human Rights in Spain***

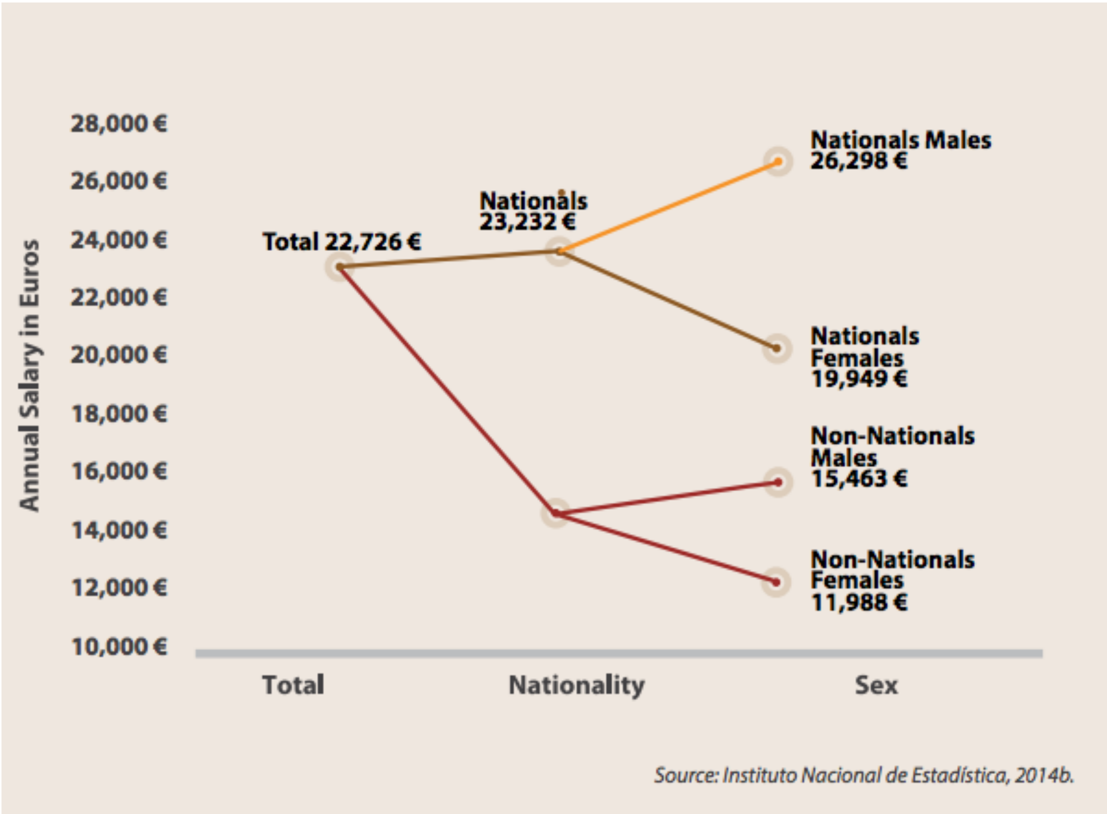

Figure 5 Evolution of Annual Minimum Wage Compared to Annual Average Wage (2007-2013)

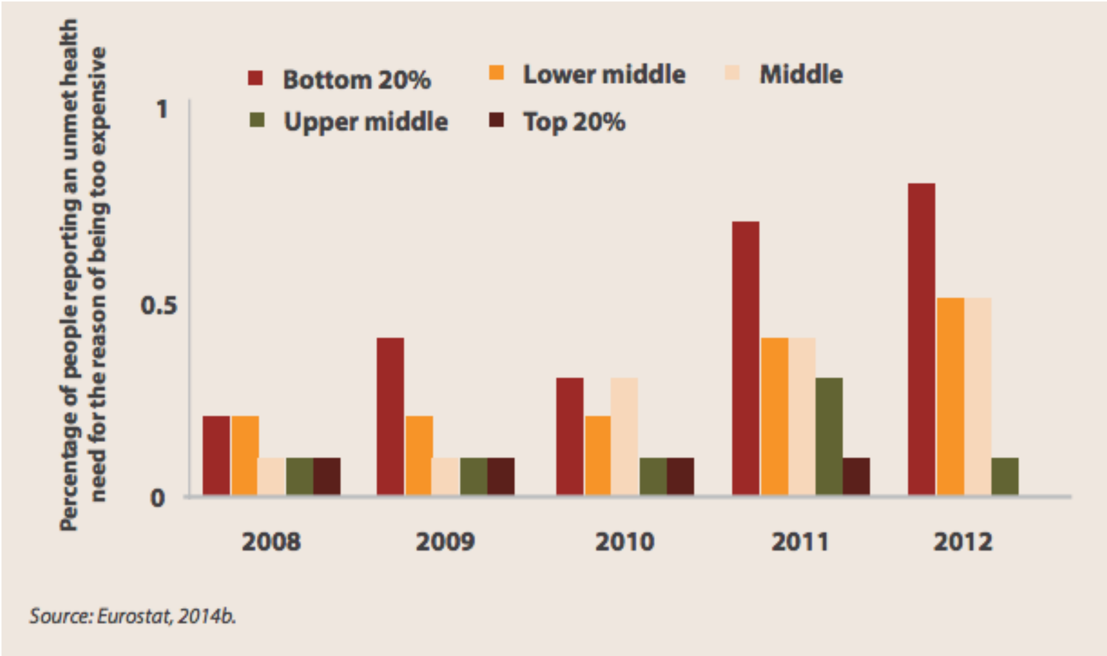

Figure 6 Incidences of Unmet Health Needs Due to Cost

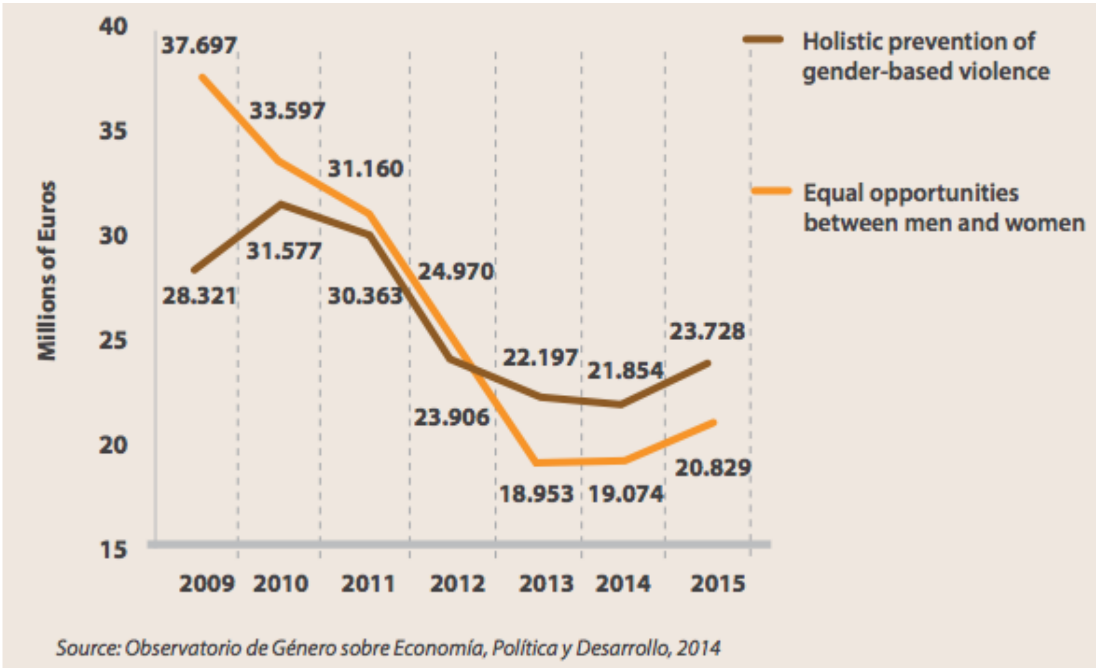

Figure 7 Budget Allocations to Address Equality and Gender-Based Violence 2009-2015

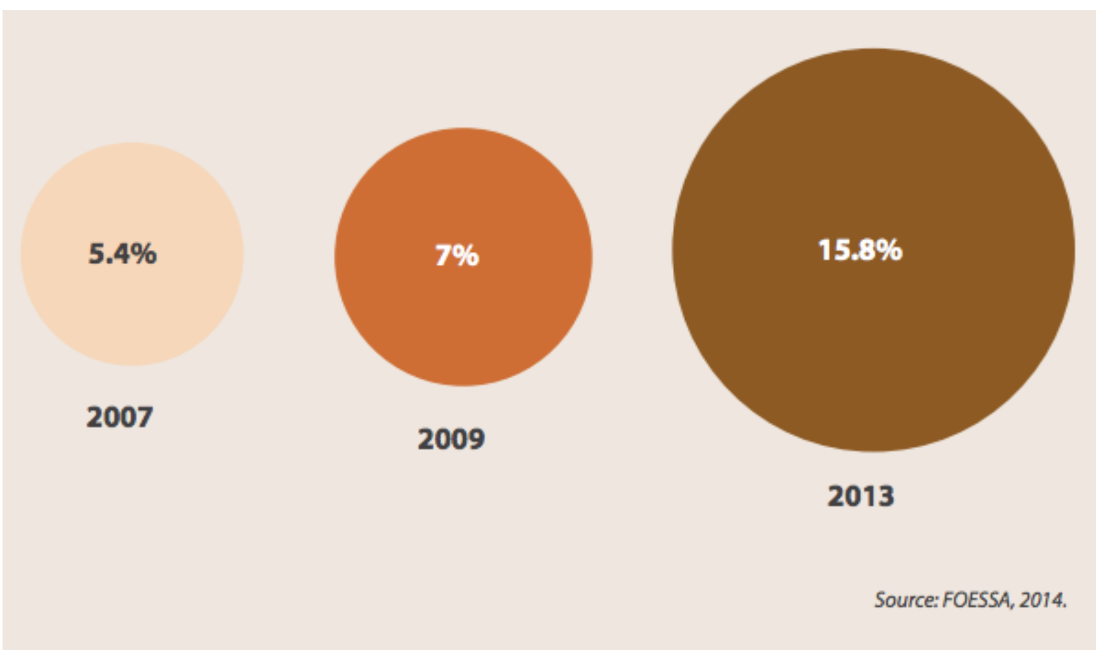

Figure 8 Proportion of the Spanish Population Who Can No Longer Afford to Pay for Medicines Due to Low Wages (2007-2013)

All of the hitherto figures suggest that Spanish austerity policies have not been so conducive to the country in many aspects, and even detrimental especially to the socially disadvantaged groups in health care, education, gender equality and many others. The case of healthcare highlights a complicated nature of looking at austerity with cautious view. Spain in its determination to seek for short-term cost recovery at any circumstances in the thrust of austerity measures, it decreased the already low level of spending on health care with dramatic reforms. Consequently, Spain's universal public health care system has shrunk and fragmented while now the undocumented immigrants who had an access to the public health services before find themselves stripped off of that right. More precisely, such healthcare reforms dragged 15 percent of the population in the country to live with no healthcare to cover their medicines and of them are the most socially vulnerable and poorest of the society.

The case of Spain and cautionary reviews that can be taken is that they all stress that the Spain's spending cuts has endured and remained notwithstanding more equitable fiscal alternatives that are available in options, such as progressive taxation and meaningful efforts to tackle tax evasion and avoidance that would both balance the country's budget and comply with its human rights duties under international law to deploy the maximum available resources to fulfill economic and social rights.

Those who have been worst affected by the crisis in Spain as suggested in figures relevant to gender violence and inequality, were women, (illegal in particular) migrants, and children. In May 2012, United Nations Committee on Economic, Social and Cultural Rights came up with guidance for Spain about protection of human rights in the midst of Spain's financial crisis, which asked Spain to rekindle the efforts to protect these rights.

The definition of growth complicates itself due to the multifaceted volatility of human life and the number of the indicators that can be considered for growth. However, in terms of addressing human rights in a proper manner and suitable encounters have not seemed to be found in Spain in its pursuit of austerity policies during the financial crisis, with human rights duties largely ignored in the process.

Lessons from Spanish Crisis

To recap of the CESR report of 2015, austerity measures in the Spanish crisis introduced drastic budget cuts in health, education, and social protection, disproportionately affecting the most disadvantaged and marginalizing individuals and groups. It also brought about increase in population living in poverty that entails social exclusion as well, most prominently to the immigrant households. Unemployment still if not worsened remains with erosion of domestic wages. Lastly, there also came a considerable disparity in economic equality between men and women with discriminated earnings, gender-based violence and bias, and relevant services.

The Spanish crisis highlights the flaws of the idea of integration to an incomplete monetary union (one not backed by a political union: "… Lower interest rates and the loosening of credit will likely lead to a credit boom, driven by potentially overoptimistic expectations of future permanent income, which in turn may increase housing demand and household indebtedness, as well as lead to overestimations of potential output and expansionary fiscal policies (Royo, 2015)".

Second problem to be pointed out is rather a traditional one in financial crisis in the world. Government and banks should be open and proactive about the danger of default before bubble pops and should recognize that political interests should be put aside if they are seeking for economic stability in long term for the country as whole, which can cause other social and political instabilities with intensity in the case of crisis.

They need to try to avoid any complacency and examine the country's business confidence in check which can be overstated and overoptimistic.

Royo points out that a crucial problem for the case of Spain was its comparative advantage in dramatic erosion. The emerging countries such as India and China brought about considerable damage in the European continent, agitated additionally by the Euro appreciation and the increase of unit labor costs less competitive than those emerging countries. For Spain however, the problem was that too few companies export, and those who do export have differentiated products because they are the large corporations, which explains why the market share of Spanish products in world trade did not fall in the last 15 years (Royo, 2015).

Final point that can be taken into account is that countries inevitably need a certain degree of flexibility, which will allow to encounter times of crisis and to increase productivity in necessary situations. As Royo rightly points out, this will help Spain's productive sectors to respond to the increasing demand and to ensure that their economies can withstand the pressures of membership to a single market. In the process, it is also highly suggested that the state parties will wage a constant review on the reforms that have already been undertaken to make sure that those austerity measures uphold the level of protection to be attained in economic, social, and cultural rights. One of the hardest missions still to bear will be to ensure that such austerity measures do not negate or impinge on very economic, social and cultural rights in any given countries.

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The reason of the smooth provision of the financial support

As being reviewed in the first part of this paper, the government of Spain implemented a stimulus package for the first move, but then turned to the austerity measures, which were like a neo-liberal policy. IMF(2014) suggests that the austerity measures implemented by 2013 were consistent with the policy suggestion of IMF, which means by 2013 Spain was successfully introduced the measures in the first chapter in a way that it matches the expectation of the international organization in cooperation with EFSF body. There are supposedly two reasons for this match, in terms of financial market stability.

Firstly, it can be pointed out that coherent motivation of countries both the credit-serving sides and the recipient side in the international market facilitated their negotiations of the financial injection. As mentioned in the first chapter as the feature of the EFSF, it is a limited liability company established in Luxemburg under the auspices of Luxemburg law, with the dominant power of Germany, France and so on. Additionally, the financial procurement of the body was completely relied on the one from the financial market as a form of security by compensating the lack of credibility with the highly-graded bonds such as German and French ones. Therefore, as a matter of system mechanism, the more stable financial market was the common concern and profit for both of the parties, EFSF and Spain, in terms of stable financial procurement.

In addition, the insolvency measure in the banking sector of Spain was the acute and common concern problem at the moment.

	Loans to private sector from domestic banks and other credit institutions (percent of GDP)		
	1998	2002	2007
Greece	31.8	56.5	84.4
Ireland	81.2	104.4	184.3
Portugal	92.1	136.5	159.8
Spain	80.8	100.1	168.5
Italy	55.7	77.3	96.5
Germany	112.2	116.7	105.1
France	81.0	85.6	99.3

Figure 9 Loans to private sector from domestic banks and other credit institutions (source; World Bank financial database)

First, figure 4 shows the amount of loans from domestic banks to private sectors in each countries. This shows that the figure of Spain more rapidly rose from 1998 to 2007, during which investment bubble to the construction industry and real estate occurred. Auter(2012) explains the part of the reason as "The European periphery experienced strong credit booms, in part because joining the euro zone meant that their banks strong credit booms, in part because joining the euro zone meant that their banks could raise funds from international sources in their own currency—the euro— could raise funds from international sources in their own currency—the euro— rather than their previous situation of borrowing in a currency not their own".

Secondly, there was an acute necessity for the financial injection to the banking sector to resolve the credit crunch. The table below shows the result of the assessment of the bad loans in the financial sector in Spain.

	Core Capital
BBVA	9.6%
Banco Popular Esp.	9.4%
Santander	8.6%
Banco Pastor	8.5%
Banesto	8.3%
Banco Sabadell	8.2%
Banco de Valencia	7.2%
Bankinter	6.8%

Figure 10 the result of the stress test In 2011, showing core capitals in Banks in Spain

	Core Capital
Unicaja	13.1%
Kutxa San Sebastian	12.5%
C. Vital	12.1%
C. Pollensa	10.6%
BBK	10.1%
Ibercaja	9.7%
La Caixa**	8.6%
Banco Mare Nostrum	8.4%
Banco Caja3	8.3%
Banca Civica	8.2%
Banco Base	8.2%
*incl. CAM**	6.6%
Caja España Duero	8.0%
C. Ontinyent	8.0%
NovaCaixaGalicia	<8.0%
Unnim	7.0%
Banco Financiero y de Ahorros	7.0%
incl. Caja Madrid	7.1%
*incl. Bancaja**	7.2%
CatalunyaCaixa	6.6%

Figure 11 Spanish cajas core capital in the 4Q of 2010

The two tables above show the result of the stress test showing the amount of core capital of each banks. According to these, the minimum requirement for the core one capital of each financial institutions was 8% and under some conditions it was 10% at least[3]. Taking into consideration the financial conditions of Spanish banks and the less transparency of the small financial firms, cajas, the necessity for the financial injections can be said having been quite high at that time.

[3] The financial report of Natixis in 2011 says "As already announced by the Spanish Finance minister, Elena Salgado, Spanish financial institutions will have to hold core capital (defined in accordance with Basel III rules with the addition of instruments subscribed by the FROB and convertible instruments that must be converted into shares before 2015) of at least 8% of total risk-weighted assets at any time (with a minimum in 2011 equal to those assets included in the calculation as of December 31st, 2010). That requirement of 8% will be raised to 10% for credit institutions verified to be evidencing the following two conditions: (i) their proportion of funding in wholesale markets exceeds 20% and (ii) at least 20% of their share capital has not been placed with third parties. T"

Chapter 3; Conclusion

As argued up to this part, the response of the government of Spain was an unpopular and contradictory to the European welfare state tradition pervasive in Europe as well as there were actual damages and ignorance of the profit of the citizens, which can be a persuasive reason for the negative perception of the citizens toward the government action. Meanwhile, there were simultaneously acute necessities for the fiscal retrenchment and austerity measures to deal with the deterioration of public debt that provoked an anxiety of the international financial market, represented as a widening gap of the bonds yields in the market. Upon such an analysis, there were an oversight of supranational bodies, EFSF and IMF, to monitor the fiscal conditions to prevent from contagion of recession to other European economies and there was a match of political motivations between them. This was proven by IMF article 4 report in 2012.

Therefore, as a conclusion, it can be led that the successful provision of the financial support from EFSF was due to the spontaneous implementation of the austerity measures and the coherence of the motivation of the government of Spain and EFSF including the other major economies in Europe.

For the further research, the more chronological interactions between Spain and the authority of EU should be scrutinized, since this paper was rather inclined to the ideological analysis of austerity measures and the historical approach. With regard to the policy response in the time of economic crisis in general, the analysis about how sovereign governments respond to turbulences is a long lasting academic issues to be addressed. Although neo-liberal policy is deemed as a dominating direction for the time being, it is an arguable topic whether such neo-liberal austerity measures are desirable or not, seeing the result of the response of Asian economies toward the Asian financial crisis.

For the bridge to the point, this paper could have successfully introduced Historical Institutionalism that positions international organization as the product of path dependency. If the international organization or the supra national mechanism are sub-optimal product of international politics, the propagation of certain policy should be doubt in terms of its justifiability. As a writer of this paper, I would like to make this the further research issue.

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