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The web of austerity and Europe's weakened democracy: the case of Portugal

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Introduction

Portugal is probably a single case in the context of financial assistance programs in the Euro area. Between 2011 and 2015, the European institutions and the IMF have had in the Portuguese right-wing government coalition[2] the perfect partner to implement the Financial Assistance Programme, which ended on 30 June 2014. During this period, it was clear a true mutual understanding between the two parts.

The Troika met a government that has agreed ideologically and without constraints with the outlined policies and for the government, the memorandum of understanding was the opportunity to pursue some economic policies that would never dare to implement in another context and that the ordinary citizen never thought that would be taken. The government since the beginning assumed that it wanted to "go beyond the memorandum" in order to further accentuate its neoliberal matrix (Mota *et al.*, 2012). In this sense, one

[1] We want to express our thanks to Júlio Marques Mota by the careful reading of this article and the suggestions made that we believe helped the ideas presented here to become more incisive and illuminating.
[2] The Portugal's right government coalition was made up of the Social Democratic Party (PSD), the main party, and the Social Democratic Centre - Popular Party (CDS-PP). Both parties belong to the European People's Party group in the European Parliament.

cannot say that the Portuguese government has recognized as external interference the presence of European institutions and the IMF in Portugal, and always considered as normal, with the argument of the economic situation of the country, and therefore necessary.

This joint governance has left devastating social and economic effects that will last beyond the medium term. The question that arises now to Portugal is how to overcome the economic and social weaknesses created by austerity policies and the vulnerability of the productive structure that existed before the crisis and that continue to persist or have worsened. The question is, firstly, political. The architecture of the macroeconomic policies of the Euro area can hardly allow expansionary fiscal policies and the ongoing surveillance of European institutions does not virtually give any space to national governments policies and even less when they are oriented towards alternative economic policies. This text aims to accurately reflect on the "straightjacket" where Portugal is currently in face of the urgency to meet the aspirations of citizens reflected in the last elections results, where the majority has expressed against the right-wing coalition policies.

1. The European "adjustment process" in Portugal

Between 2011 and 2014, Portugal was under a Financial Assistance Programme in the Euro area context. This program meant the interference of the European institutions and of the IMF in the Portuguese policy-making process. It was also clear the overvaluation of the individual/national causes to explain the economic problems and as a consequence the application of the individual/national responsibility principle which are so dear to the neoliberalism. Thus, it was assumed that the situation in which Portugal was in 2011 was due to the economic policies of national governments that have left worsen the competitiveness of Portuguese exports and worsen public deficits. No responsibility was attributed to external factors such as the architecture of macroeconomic policies of the Euro area. If existent at all, in this regard, would only be necessary to improve surveillance at EU level and eliminate some imperfections in its realization. But, contrary to what this principle could imply, they do not let Portugal to delineate the economic strategy necessary to revive its economy. The European institutions took advantage of Portugal's vulnerability to impose a program of economic policies according to their ideological matrix, based on diagnostic that was taught specifically for the implementation of these policies. However, if part of the 2011 macroeconomic imbalances are the result of the Portuguese economic policies of the last 25 years, the other part must be analysed and understood within economic and institutional framework of the EU, as we will explain.

The situation in Portugal, in 2011, more than revealing the fragility of the budgetary situation, reflects mainly the weakness of its productive structure. This weakness results from an economic policy that has favoured the non-tradable sector, and from the new conditions of global trade that have undermined Portuguese industry. These realities have resulted from the global economy model that was adopted in Portugal when it joined the EU as the European Single Market was being launched. There was a move towards the redefinition of state functions and the economic policy that included privatizations and the commodification of the public sector, the economy and financial sector liberalization, labour market flexibilization and the promotion of supply-side policies. To reinforce this, in 1990, the government decided that the escudo should join the European Monetary System in 1992, and adopted an anti-inflationary policy through escudo appreciation and raised interest rates, in conjunction with a wage moderation policy. This political choice reversed a deliberate policy of exchange rate devaluation and reduced the competitiveness of the export sector. It also undermined the intended objectives underlying the European funds specifically addressed to the renewal of the productive sector as well as of the export sector.

For some authors (Silva Lopes, 1996; Amaral, 2010), that decision structurally biased the incentives towards the non-tradable sector. The outcome was a fall in agricultural and industrial production, a slowing of investment and a reinforcement of the specialization in labour-intensive sectors and a relative favouring of the non-tradable sector. In this period, the Government chose a competitive disinflation policy, seen as a way of modernizing the economy, which meant a change in macroeconomic regulation. Stability became the new imperative, replacing the former Keynesian expansion regime (Lordon, 1997: 33).

These political guidelines were reinforced when the government decided that Portugal should be in the founding group of the European Monetary Union (EMU). The escudo overvaluation together with free circulation of capital, financial sector liberalization, tax incentives, interest rate reductions and the positive economic expectations generated by the euro, created the conditions to reinforce the relative favouring of the non-tradable sector, disincentivising productive investment in the tradable one. As a result, household and firms debt increased, which to a great extent explains the degradation of the Portuguese current account, whose deficit was 10.7% of GDP in 2000, i.e. an increase of 7 percentage points in five years. The resulting demand rise, associated with the cycle of public investments, helped Portugal to fulfil the budgetary criterion for accession to the EMU (in parallel with interest rate reductions and privatizations that were intensified for this reason).

In what concerns the conditions of global trade, there are two factors that have penalized the Portuguese tradable sector. One is the emergence of new players directly competing with Portuguese labour intensive products. The other one is the new international supply chains framework.

Therefore, Portugal began its integration in the EMU already with a macroeconomic imbalance and a decreasing competitiveness, neither of which were detected by the convergence criteria. The euro overvaluation, justified by the price stability priority, was a negative and asymmetric real economic shock that contributed to the relative preference given to the non-tradable sector. One estimate has been that the escudo/euro appreciation may have been responsible for 60% of the competitiveness loss in the export sector (17.3% between 1991 and 2006). In this case, wage developments were not responsible for the loss in competitiveness, it was the overvaluation, which may also explain the market share loss in industry (17.7 per cent between 1998 and 2006); the dependence of the export sector on imports also increased (Ferreira do Amaral, 2009).

Despite the vulnerabilities of productive structure, the budgetary situation was not different of the EMU average. In 2007, the Portuguese public debt-to-GDP ratio stayed just a bit above 60% and the public deficit-to-GDP ratio was a little lower than 3%. The budgetary situation clearly deteriorated with the crisis in 2008, which worsened more with the sovereign debt crisis.

It is clear that this deterioration was a consequence of the crisis and not the cause. This was not the understanding of the European institutions which distorted the diagnostic to impose an adjustment programme of the type “one-size-fits-all”, which by definition does not take in account the needs of each country.

The major explicit objective of the memorandum of understanding was then the “consolidation of public accounts”. In this respect, what has been achieved? The public deficit-to-GDP ratio decreased from -11.2% in 2010 to -4.5% in 2014, a figure that is far from the initially estimated, -2.3%. As for the public debt-to-GDP ratio, it was observed a substantial increase. The memorandum estimated a 22 percentage point rise but actually rose 34 percentage points in 2014, the public debt amounted to 130% of GDP. It is true that public debt interest rates fell sharply, but more due to the ECB's intervention in the secondary market than to the sense of any improvement by financial operators and rating agencies. Portugal has thus had luxury public debt interest rates but junk rating, which is a major contradiction in the current framework of the functioning of financial markets, contradiction that is not questioned.

These results are far from justifying the joyful manifestations of European institutions by the adjustment process in Portugal, considered by them a success. Today it is known that the "clean exit" from the Financial Assistance Programme, which ended on 30 June 2014, was carefully staged at the expense of solving some serious problems in the Portuguese financial system, which only became public now. This is the case of BANIF, a small bank in the Portuguese financial system, which was only resolved at the end of 2015, by the current government, when their problems were dragging on for years. Postponing the decision resulted from another collusion between the right-wing coalition government and the European Commission, "because of the need to not jeopardize the clean exit of Portugal from the Financial Assistance Program" (Alves, 2016). It was recently known that it have been the ECB and the European Commission to choose Santander as the buyer of BANIF and that the order was given by the ECB through an e-mail sent by the Chairman of the Supervisory Board of the ECB to the Portuguese Minister of Finance. As transcribed the Social Democratic Pacheco Pereira (2016b), a recognized analyst of Portuguese society, "the European Commission was very clear in this respect, so we recommend not to waste time trying to pass these [other] proposals". According to him, it was a deliberated "leak".

A more careful reading of the results of the "adjustment program" easily identifies serious economic and social consequences that will leave structural marks. Unquestionably, the labour devaluation is one of them, probably the most important. It is not the evolution of the unemployment rate that best expresses this. The unemployment rate increase from 12.9% in 2011 to 14.1% in 2014, with a peak of 16.4% in 2013. However, if the unemployment rate is measured in hours and if it is included also inactive population who is available but not seeking employment and unemployed hours by involuntary part-time workers, the unemployment rate would have been, in 2014, about 21%. The duration of unemployment also marks the difficulties of access to employment. This indicator deteriorated in such a way that the weight of the population who seeking employment for more than 12 months in total unemployment had risen more than 10 percentage points from 2011 to 2014 and, in this population, the percentage of the population who seeking employment for more than 24 months rose about 15 percentage points. The situation of this population has worsened even more as the unemployment protection was severely hit after applying the measures of the memorandum, with the unemployment benefit to be subject to a double conditionality: the fact that the benefit is a public expenditure that should be reduced and the assumption that the benefit should be an allowance for job search and not an income replacement for those who lose their job. Both aspects have led to the reduction of the maximum benefit and the entitlement period.

Labour income was also severely penalized, not only because of civil servants wage cuts from 2011, as also the internal devaluation policy, which meant to be assumed explicitly wages only as production cost. The share of wages in total income, which had not decreased significantly in the past two decades, has reduced 3.6 percentage points between 2010 and 2014. The weight of workers with the minimum wage almost doubled. The worsening of wage insecurity stems partly from increased contractual precariousness. A panoply of employment contracts has emerged arising, many of them, from employment policies, whose logic is to mobilize benefits and social minimums to facilitate the creation of jobs of low quality, low-wage, even lower than the equivalent wage before 2008. In addition to the instability of income of more and more workers, they all saw employment protection be diminished by the reformulation of the individual dismissal concept to make it easier and the reduction of the severance payments.

Another structural consequence of the economic policies initiated is the devaluation of the State figure, felt on several levels. At the level of the public investment, whose share in GDP fell by half compared to 2009. With privatisations, deemed essential to reduce the State role in the economy and lead to increased competition and efficiency, whose final revenues were almost twice the value previewed in the memorandum of understanding. In the public services, in which the quality of access and provision was noticeably deteriorated, especially in education, health and social security. This is being done simultaneously with the strengthening of the commodification of these services and the transfer of competences to the private sector. We may even think there was a political intention to degrade the State figure among citizens in order to impose more easily the presence of the private sector in these services.

These measures, many of them presented as exceptional, caused hysteresis effects on the Portuguese economy that have undermined the economic growth capacity due to the effects on public infrastructure and public services, on long-term unemployment and on private investment. In regarding the private investment, during the Troika period, it has decreased by around 20% and in short-term the chances of recovery are not encouraging, since the firms are in a deleveraging process since they hold more than half of Portuguese debt.

These structural effects add to the existing ones and that were not a concern to the European institutions and to the IMF. The most obvious case is the production structure that remains with the same vulnerabilities. In face to the global economy, they have even worsened. In 2014, the high-tech industries account for only 6.9% of total exports, while have represented 12.4% in 2004. As ten years ago, more than a third of exports are low-tech industries.

2. The European monetary integration and democracy: the Portuguese case

Portugal lives in a democratic regime for forty years. This was the result of the movement of the some military and political activists to which all Portuguese citizens join quickly. Nowadays, more and more Portuguese feel that democracy is in risk, not because the internal forces like in past, but by external interference from the European institutions and financial markets which, in turn, determined in part the European options. With regard to the financial markets, what it is happening is completely illogic in relation to what must be in a democratic regime. It must be the governments — the political power legitimized by the votes — to impose rules on the existence and functioning of these markets and not these markets to limit the central aspects of economic policy, decided by governments. This clearly jeopardizes the democracy and the interests of the majority of citizens. Currently, the situation is aggravated by the fact the European institutions, instead of controlling the markets, they work like them, jeopardizing democracy too, and legitimize their behaviour.

With the EMU, necessarily some instruments of national macroeconomic policies were taken from the hands of democratic governments, that is, some capacity was withdrawn from the citizen's hands of the member states. In first, the governments lost the monetary and exchange-rate policies. In relation to the national fiscal policies, their common rules and proceedings limit the national macroeconomic management and thus reduce the possibility for governments to answer to the citizens' demands concerning public goods, the formation and redistribution of incomes, as well as economic stabilization.

Making the association with Trilemma of Rodrik, it can be said that Portugal, more than other member states, because of the memorandum, cannot aspire to respect the demands of a democracy while simultaneously being a nation-state and belonging to the Euro area. Also here one has left some aspects of democracy behind, to the profit of the other two situations: Portugal took a position on the right side of the triangle (see figure 1).

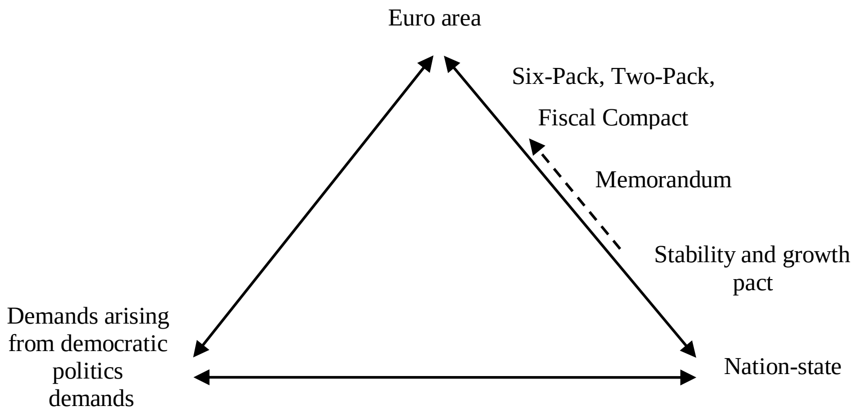

Figure 1

The request for financial assistance to the European institutions was a sovereign decision of the Portuguese national government, but its causes clearly reveal the functioning of a "disciplinary neoliberalism" (Gill, 2000: 4). According to this, governments try to show their credibility and the consistency of their policies, in accordance with the confidence they want to inspire in the financial markets that are determining the national macroeconomic management to the benefit of their own interests, with a similar influence on the European institutions too. Given that, one may say that Portugal is keeping its position on the right side of the triangle, but walking away from the nation-state. With the "adjustment programme", it is the European institutions and the IMF that define the criteria to be treated as "conditionality" even if they prefer to do so in consultation with national institutions, knowing that in any disagreement the bargaining power of the national government will be minimal (Scharpf, 2011: 26). While Portugal was applying the memorandum, the European institutions have created more tools — Two-Pack, Six-Pack and Fiscal Compact — to supervise the national governments and to reduce its leeway, which for Portugal signified that some policies which apparently would be transitory by memorandum became permanents.

This way along the right side of the triangle also means that there is more distance from demands of a democracy, for reasons already mentioned above and also by the need to question the democratic legitimacy of this external interference, that is, to the extent that citizens see it or not as something that may be representative of their own interests. As Carvalho da Silva (2016) says, “for the Portuguese and many other European, the Union has become an external agent, an almost adversary”, by assuming functions which were not previously assigned to it by European treaties, as the definition of the fiscal policies, and sometimes defined against the democratic choices of the citizens as in areas of the employment policies, social policies, education, health, justice. It is therefore observed a continuous growing centralization of EU decisions and a growing disconnection between the EU institutions and the citizens. Additionally there is no democratic accountability in what concerns the EU institutions.

3. Portuguese elections and the democratic fragility in the EU

Strangely, the right coalition was the most voted political force in parliamentary elections late last year, though most Portuguese voters have rejected such policies. These results seem inconceivable, since the austerity policies have profoundly affected the Portuguese, as workers, as pensioners, as consumers, as producers, as citizens. And the governance results were not more onerous because the Constitutional Court turned out to be the only safeguard of certain rights. All State budgets presented by the government had measures that were considered unconstitutional by the Constitutional Court.

How then can we explain these results? There are several reasons that can be pointed out, but we will refer one: the power mechanism exercised by the Portuguese government, including the media, and by the European institutions. Throughout 2015, the government carefully delineated an electoral strategy that had, as one of the pillars, the control of the media at the level of political analysts and news selected, and these on its timing, form and content. It also must not be forgotten that media (almost all) which, by itself, was working in the same direction, given the interests of the underlying economic groups, and the work done on social networks and think tanks. It was built a real machine of ideological and demagogic propaganda, which allowed fixing the traditionally electorate of right-wing and still pick up votes in the centre-left.

For the European institutions themselves it was essential that the right-wing coalition won the elections. Since Portugal is considered by them a success story, it would be strategic the validation of this image at the polls. This would also mean the denial of the idea that the institutions and European governments have ruled against the citizens and in favour of financial markets. Probably, for that reason, throughout the campaign period, there were clear signs of support of these institutions to the Portuguese government, which were amplified by the media. Ironically, you can even say that in this case the European institutions collaborated in a moment of democracy, as in the case of an election in a country with a democratic regime. To this it can be associated the rating agencies, one of them having improved the public debt rating a few days before the elections and stressed the need to continue with the same kind of economic policies.

A clear majority of the electorate that have rejected the right coalition and its austerity policies and the will to establish an agreement of the four parties of the left that form this majority, making concessions and finding convergence points, created conditions to form a government of the Socialist Party (PS) with the parliamentary support of the other three parties (Left Bloc (BE), Portuguese Communist Party (PCP) and the Ecologist Party “The Greens” (PEV)). The common goal, that allowed something that had never been possible in Portugal, the left unit, was well defined: to end right-wing government that from the beginning said it wanted to go beyond the Troika to implement in Portugal the most neoliberal model from Europe.

Surely no one would expect a government too left-wing. As noted Pacheco Pereira (2016a), all Portuguese political spectrum has shifted to the right, having left only a fringe on the left, and in such a way, that, according to him, Pope Francis would be more at the left than the Portuguese radical left. The right-wing turn of the PSD caused that “the very moderate left seemed the Bolshevik with a knife between his teeth”.

This governance solution was eventually taken by surprise the Portuguese society. The President of the Republic himself seemed not to have thought of this scenario. He was since the beginning very reluctant to induct this government and his attitude is more a case of how democracy can be injured because of European commitments and loyalties to financial markets. The president did not consider the two parties further to the left (PCP and BE) committed to the current Euro area and feared the signals that could be sent to financial markets. This behaviour simultaneously turned out to be an explicit recognition of the lack of democracy in the European Union. President instead of having opposed to this trend, collaborated with the situation without discussion as if it were part of normality.

It is true that the PS and now its government has always said that it wanted to keep the European commitments. Therefore, there is no space for alternative economic policies that break with current ones. It is not even possible an expansionary fiscal policy as Portugal objectively needs. The almost generalized stagnation of its main trading partners also makes unfeasible the sustained increase in output through exports. In addition, the private sector, heavily indebted, has no incentives for new investments by the lack of a sufficient aggregate demand.

After all, in the PS government program there is some intention to expand the income of the Portuguese, that is to say to replace the income levels seen before the crisis, and in this sense, is distinguished from the European context by assuming stimulus measures on the demand side. As a result of the commitment to the left, the measures which are reflected in the 2016 State budget, are more extensive and include: (i) a more rapid replacement of civil servants' salaries; (ii) a faster elimination of a surcharge on the income of households launched in 2011 and not foreseen in the memorandum; (iii) the adjustment of certain pensions that had been suspended in 2010; (iv) the reposition of the 2011 value of some social benefits and the restoration of conditions of access and provision of public services. The government has already increased the minimum wage that is currently earned by about 19% of workers. With regard to privatization and concessions to the private sector, these were suspended and the procedures for public transport companies' concession contract that were in progress have been cancelled. The privatization process of the Portuguese airline, TAP has also been reversed.

However, the proposed draft budgetary plans to the European Commission in January was highly criticized because it does not allow to reduce the structural public deficit-to-GDP ratio by 0.6 percentage points, the value chosen by the European institutions. This, and the threat of a rating downgrade in government bonds at the same time, took the Portuguese government to negotiate and take some steps back, having still achieved a decrease of only 0.2 percentage points. To be able to accommodate this change, the government had to come up with new restrictive measures, such as an increase in indirect taxes and other contributions, a reduction of 10,000 civil servants, some savings in some current expenses and the elimination of some expansionary measures such as reducing of the social contributions of workers with wages below 600 euros.

Although the end result raise some doubts about the budget expansionist feature, doubts that the government did not want to exist considering its initial policy intention, the truth is that the government make it a point of honour not to budge an inch in the income reposition to the Portuguese. Perhaps for this reason, the State budget continues to generate mistrust to the European institutions and the Eurogroup. The last has already expressed some reservations about the reasonableness of the budgetary targets proposed by Portugal and asked the Government a contingency plan with austerity measures. IMF follows the same line of pressure and support of the austerity policy that were followed until here. Not long ago, this institution stated that: “the 2016 budget proposal appears insufficiently ambitious to put public debt on a firmly downward trajectory, with significant risks to execution”. Therefore highlights “the importance of developing contingency plans to ensure that the 2016 budget targets are met, rationalizing public spending to contain pressures from public wages and pensions, and maintaining fiscal buffers”(IMF, 2016: 2 and 4).

Probably, what Mario Draghi said at the meeting of the Portuguese Council of State (a political body to advise the President of the Republic), on last 7 April, to which he was invited shows that the democracy is more at stake than we are thinking. According to the newspaper *Público* (Botelho, 2016), in a period of debate, Draghi suggested — in Portugal, but without referring to Portugal — a change in the Constitution of some countries, because this is an obstacle to some reforms such us labour market reforms. He also defended changes in the electoral laws in some countries due to question of governance. Certainly, he was thinking on Portugal and Spain.

Interestingly, it is this whole set of limitations and political circumstances that can solidify the relationship between the leftist parties. The PS government can only case-by-case eliminate many of the right wing government austerity policies, some blindly imposed. And even the slow restoration of the financial situation of households and the quality of public services before the crisis will not fail to face enormous difficulties. The vested interests, the lack of resources that were meanwhile destroyed, the hysteresis effects of policies and the resistance of the right-wing of the PS will be obstacles to face. For example, to redo the health system or the education system it will take years.

Conclusion

The task that the PS government has ahead will not be easy. The current Portuguese Prime Minister António Costa, on his taking office, said that his government was the refutation of the idea that there was no alternatives to existing policies and was also proof that democracy always creates alternatives. Four months later, it is doubtful that he continue to think the same. If in a democracy, like Portugal, it is true that it is always possible an alternative governance, but it is also true that the implementation of alternative policies in the context of the current Euro area is increasingly difficult. Today, the situation is so odd, that institutions that were not elected — European institutions and Eurogroup — supervise (advise, analyse and impose) democratically elected institutions — national governments. Supervise even *ex ante*, meaning that they know and approve national budgets even before elected institutions and the national parliaments knowing them. As evidenced by Weeks (2016): "TSCG [Treaty on Stability, Coordination and Governance] removes national control over budgets. Member governments de facto formulate their budgets for the Commission not their legislatures; after the Commission judges them as satisfactory the national legislature goes through a pro forma approval process. Adopting the TSCG transfers sovereignty from democratically elected institutions to an unelected bureaucracy".

The current Portuguese governmental experience, even in the context of a weakened democracy, will cause some concern in the European Union, not only by the way of being and doing politics but also due to the political impact that could have in certain Euro area countries. It is already the case in Spain. Is fact, with the reproduction in Spain of the Portuguese situation, the political strategy of the European institutions might be completely confused allowing to the creation of conditions to open up a gap in the existing institutional framework.

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