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# The European Social Model in a Context of Crisis and Austerity in Portugal

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## 8. The European Social Model in a Context of Crisis and Austerity in Portugal

**Pilar González and António Figueiredo**

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### 1. THE FEATURES OF THE EUROPEAN SOCIAL MODEL IN PORTUGAL: RECENT, CONTEXT-DEPENDENT, UNBALANCED, ENCOMPASSING AND VULNERABLE

The Portuguese implementation of the European Social Model (ESM) has not been immune to the effects of the Great Recession and of the austerity measures adopted subsequent to the sovereign debt crisis and the bailout of the Portuguese economy. We will demonstrate that the Portuguese experience shows both similarities to the effects observed in other countries (under adjustment conditionality or simply affected by the consequences of the Great Recession for public finances) and very distinctive outcomes.

A large number of reasons can be invoked to explain the ambivalence of the crisis effects on the implementation of the ESM in Portugal. In this introductory section, the explanation will focus on the historical context of the ESM in Portugal, responsible for two main characteristics of the Portuguese model: its recent realization and its context-dependence.

In our analysis, three main pillars of the ESM in Portugal will be analysed: the public education system, the national health system and social protection. Regulation of the labour market will be considered as a transversal dimension, being very sensitive to growth dynamics. Other dimensions, such as social cohesion and the regulation of territorial cohesion (the territorial welfare state) are not fully developed, mainly due to their weak manifestation in Portugal before the arrival of democracy.

#### **1.1 Portuguese Version of the ESM: A Recent and Context-dependent Social Achievement**

The existence of these pillars as elements of a coherent system is a contemporary manifestation of 25 April 1974 revolution in Portugal and essentially of the 1976 Constitution that simultaneously ended the unstable post-Revolution period and started the consolidation of democracy in Portugal. The Portuguese Constitution is very generous as far as social rights are concerned, being a complex mix of social and political influences, strongly marked by the revolutionary social dynamics generated by the military coup. A modern social state was then an aspiration completing the political and economic equality that inspired the new Constitutional order.

Paradoxically, the first steps towards building a welfare state in Portugal were implemented at the same time that in Europe the welfare state began to be subjected to numerous criticisms. The countercyclical emergence of the ESM in Portugal and the influence of a very generous Constitution as far as social rights are concerned mark the advent of democracy in the country and characterize the Portuguese experience until today.

In Portugal, the emergence of the ESM is, first, an aspiration of democracy, trying to implement economic, political and social equality simultaneously, and second, the result of EU accession in 1986. The ESM was the modern reference that the new Constitution needed to introduce a comprehensive legal framework for equality.

Thus the ESM in Portugal is a context-dependent as well as a recent achievement. But the ESM's implementation in Portugal is also unbalanced and vulnerable.

## **1.2 A Very Unbalanced System**

The unbalanced nature of the ESM is determined mainly by its historical development. This can be seen as a compromise between improvements in social policy in the last period of the autocratic regime and new developments generated by democratic aspirations and the influence of EU accession. From the creation of a providential (contributory) system in 1935 to the dissolution of the autocratic regime in 1974, one cannot ignore that the coverage of employees against life's contingencies, such as old age, disability and bereavement has been improved (Pereirinha and Carolo 2008). The pillars of public education and of the national health system were more incipient than the contributory pension system. Practical implementation of the vast and generous social rights system established by the 1976 Constitution worked with a very heterogeneous set of achievements from the past.

The low level of social security of Portuguese society at the beginning of the 1970s has been an important burden in the comprehensive implementation of a social model resembling the ESM. For example, although improvements were made during the last and pseudo-modernizing phase of the autocratic regime, social public expenditure was, in 1973, 5 per cent of GDP, following a sustainable trajectory of growth starting from 2.5 per cent in 1960. In 1973, the child mortality rate was very high (44.8 per thousand births) and gross enrolment rates in basic (nine years) and secondary education were 46.8 per cent and 8.4 per cent, respectively. Public expenditure on education and health in that same year was 1.3 per cent and 0.3 per cent of GDP, respectively. These basic figures show in rough terms how great was the social challenge of the advent of democracy.

Successive basic laws in education, health and social security made explicit the aspiration to the universality of social rights established by the Constitution. Simultaneously, the labour dimension of the social system began to be implemented. An experimental form of unemployment benefit was established in 1975. Different milestones at very different moments followed. The evolving trajectory of each pillar has to be understood in line with the political interpretation of the Constitutional aspirations sustained by each government and in line with the socioeconomic progress of the Portuguese economy and its capacity to finance public expenditure.

## **1.3 An Encompassing Model: Based on Universal Social Protection and Education**

### *1.3.1 Social Security*

As far as social security is concerned, the first Framework Law dates back to 1984, establishing a budget for the general social security regime funded by the contributions of both employers and employees and the state budget financing of the non-contributory system (the social system). The unique social contribution rate<sup>1</sup> (first defined at 11 per cent and

<sup>1</sup> In Portuguese *Taxa Social Única* (TSU).

24 per cent applying, respectively, to employees and employers) was established in 1986. However, very important social achievements had been introduced before that. Regarding the universality of the system, it is important to underline the creation, in 1977, of the social pension, a non-contributory form of social protection, targeted at people older than 65 not covered by any other social protection regime. The social pension is usually seen as funding the non-contributory social protection regime (1979, 1980), establishing a universal guarantee of access to health and social security benefits, including access to the national family allowance, social allowances to handicapped adults and disabled minors and social facilities that were previously limited to means-tested support for vulnerable people. The legal status of private social solidarity institutions has also been established, asserting cooperation between regional social security centres and private institutions towards the supply of several forms of social care (family, children, old and handicapped people). This institutional element is still present today at the local level and remains very important in social care, tending to increase its role in a time of severe contraction of public social expenditure.

### *1.3.2 Unemployment Insurance*

The unemployment insurance system was created in 1985 organised around two dimensions: one (the general regime) is associated, in terms of both duration and amount, with the period worked, workers' contributions and lost wages; another (a non-contributory modality) designated as social unemployment benefit, targeted on vulnerable unemployed workers with short contribution records, low income and who have exhausted their entitlement to unemployment benefit. At the same time, policy incentives to foster the recruitment of young and long-term unemployed began to be implemented.

### *1.3.3 Progressively Extending Rights*

Two important achievements for the coherence of the social protection system were introduced in the 1990s. Independent workers gained access to social security in 1993. This is a very important step mainly from the perspective of adapting social security to labour market changes. False independent workers (the so-called *recibos verdes*) had been emerging in the Portuguese labour market as a mechanism of additional flexibility in recruitment and dismissal promoted by firms and previously not covered by social protection. The social security regime for independent workers has been shown to be very important for extending social protection to atypical employment forms. Another important achievement (1996) was the minimum guaranteed income (MGI), which remains a source of political controversy on the frontiers and limits of social intervention in Portugal. The MGI is a very ambitious social measure involving both a monetary allowance and a social integration programme. Empirical research shows that it is very effective in reducing absolute poverty.

### *1.3.4 Adaptation to the 'Social Acquis' before Joining the EU*

The 1990s was also a period of adaptation to EU rules on maternity, paternity and adoption, representing a good example of convergence with the ESM's main orientations. One should also mention a vast reform of disability and old age pensions, the progressive equalizing of the age of access to old-age pensions for men and women and the introduction of new rules for calculating pensions, reinforcing the weight of the last active years

of life. The creation of the dependence complement targeted at dependent disability, old age and surviving beneficiaries represents progress towards higher levels of social protection to pension beneficiaries. At the end of the decade, new orientations to social policy targeted at old people and the creation of the social network involving non-profit private institutions and public institutions, targeted at tackling poverty and social exclusion, were a response to the increasing evidence of the higher level of absolute poverty that the Portuguese growth model was creating. Finally, the creation of the social security financial stabilization fund may be considered a milestone as it establishes new links between the financial stability of the social security system and the financial markets. Instability on the latter may through this mechanism lead to the instability of the former.

### *1.3.5 Latest Reforms: Combining Equity and Efficiency*

At the beginning of 2000, a second Framework Law on Social Security was adopted, introducing for the first time efficiency and effectiveness goals, combined with reinforcement of the system's equity. The system entered into a very unstable period with several basic laws rearranging the system, but tending to stabilize around three pillars: social protection citizenship, contributory social protection and complementary protection modalities. Unemployment, health, family allowances, maternity, paternity and adoption, disability and old age social protection instruments have been the objects of successive changes directed by efficiency and effectiveness goals, with some occasional measures targeted at extending social protection coverage, such as the solidarity payment for old people. The first political decisions were taken to integrate the diverse regimes of social protection (public sector workers, private employees, army) and in line with EU policy, the national social inclusion plans were created. Already in the crisis (2008), the creation of a public capitalization regime, focused on individual and voluntary participation, was an attempt to stimulate beneficiaries to invest in complementary schemes.

This entire trajectory, which combined equity, effectiveness and efficiency goals, has been suspended and significantly changed with policy measures determined by either the crisis's effects on public finances or the austerity policies introduced in response to the sovereign debt crisis and bailout conditionalities.

### *1.3.6 A General and Free-access National Health System*

The effects of the political change in 1974 were significantly broader and stronger in health care policy compared with the social security dimension. The intervention of the autocratic regime in this dimension of the welfare state had been weak and limited to reform of the health and assistance system (health protection was integrated in the assistance system) in 1971 and to the creation of the Ministry of Health in 1973. The impulse of the 1976 Constitution has been decisive: a general, universal and free-access national health system has been the model adopted in order to guarantee the access of all to health protection, independent of economic status. A Ministerial Order from July 1978 and a National Law from November 1979 are usually pointed out as the main sources of the national health system (NHS), which is in our view the main landmark of the ESM in Portugal, principally from the point of view of the persistence of political orientation and improvement of the quality of the services provided. It is a very broad system, involving all the dimensions of health care: prevention, social care and monitoring, diagnosis and treatment, social and medical rehabilitation. Although conceived as a free service, its design had the merit of considering the possibility of introducing health fees as a means of

rationalising demand. Health fees are not generalized to every potential user of the NHS (numerous exemptions have been established). They are seen as an instrument to encourage users to share NHS costs and avoid unnecessary demand on NHS services. The NHS has administrative and financial autonomy, with its own budget, facing increasing deficits financed either by transfers from the national budget or by other non-canonical methods, such as a long story of huge debts to private institutions (pharmacies and drugs suppliers). The creation (1982) of regional health administrations (at NUT II level) and the establishment of a progressive network of primary health care centres (1983, 1984) in which the family doctor (a general practitioner) has gained increasing importance have been crucial to achieving the territorial diffusion of the NHS.

### *1.3.7 Few Nuances Introduced in the Early 1990s: Controlling Costs and Extending to the Private Sector*

In line with the progressive increase of public health expenditure – from 2.7 per cent of GDP in 1978 to 5.5–5.7 per cent around the 2008 crisis – the evolution of the NHS has been marked by changes and concerns on the regulation of the right to access the system, the introduction of new management models and rules (autonomous managing bodies having been created), regulation of medical careers and the adoption of a vast number of efficiency goals, particularly those related to drug prescriptions. It is worth stressing that the second Revision of the Constitution (1989) introduced a *nuance* in free access to the NHS, opening the door to the sharing of costs with the users. The new formulation is very suggestive: health protection is provided by a general and universal NHS, *progressively oriented towards a free health service model*. The legislator, trapped between the Constitutional legacy, the need to introduce higher efficiency and to control increases in health expenditure, opted for a generous and benign principle, which, as the development of the NHS will show, will be increasingly difficult to maintain together with general and universal access.

The Health Framework Law of 1990 introduced another *nuance*: the transition from the right to health protection towards health conceived as a common responsibility of citizens, state and civil society. This is a crucial element in understanding the new possibility of agreements between the state and private (profit and non-profit) institutions to supply health services. This evolution cannot be isolated from the increasing number of private hospitals, owned and often managed by strong Portuguese entrepreneurial groups or from the significant increase in private health insurance systems. For example, the autonomous health protection system of public sector workers (ADSE) and the health system of bank employees allow beneficiaries to seek private medicine with financial co-participation from the employer.

The recategorization of nursing careers, the increased integration of primary and differentiated health care (local health centres with technical, administrative and financial autonomy), the reinforcement of regional health administrations and the creation of a new network of primary health care centres are decisive achievements of the NHS.

In sum, the evolution of the NHS in Portugal until the 2008 crisis has been dominated by a very difficult balance between implementation of the 1976 constitutional order with regard to health and the need to control increases in health expenditure, while respecting universality of access. Two main tensions have persisted during this period: the tension between public and private health systems and the tension between representative social actors within the system: doctors (represented by medical chambers and unions), nurses, managers and politicians, the latter being involved mainly due to the need to

rationalize the NHS network of services. This has become a source of keen local and political debate and social bargaining. Some structural features have always been present: the persistent increase in the relative prices of health care (mainly in sophisticated health technology equipment and some kinds of drugs); the low accountability of the medical prescriptions system; the difficult coexistence of managerial practices in hospitals with the clinical autonomy of doctors; and the tendency for doctors and nurses to seek placements in the littoral urban areas of the country and their low propensity to go into the provinces.

### *1.3.8 Public Education: Challenge of Shifting from an Elitist System to One Accessible to All*

A very high level of illiteracy, the lack of pre-school education, very low levels of gross and net enrolment rates in secondary education and very limited access to universities were the main legacy of the autocratic regime regarding education.

In the pseudo-modernization phase of the autocratic regime (five years before the revolution) a global project to reorganize the education system was tried, involving pre-school, basic, secondary and higher education. It was the first attempt to unify secondary and technical schools and to break with the selective character of the latter.

The modernization initiatives of the autocratic regime have been greatly eroded and lost by the reforms implemented after 1974 targeted at eliminating the elitist pattern of secondary and higher education and promoting generalized and universal access to education. A decade of experimentation and of rejection of the past can explain the fact that the first Basic Law on education was adopted only in 1986. Previously, the unification of high and technical schools led to the progressive elimination of technical and vocational education. The creation of short-term higher education courses (later transformed into higher education polytechnic courses) is interpreted by many as compensation for the disappearance of technical and vocational education at secondary level.

The 1986 Law and the subsequent ordinary laws established nine years of compulsory education organized in a sequence of three cycles of basic education and began to recover vocational education in a preliminary phase, considering it a special educational modality for young people.

The global story of the evolution of the education and training system within the framework of democracy and until the 2008 crisis can be synthesized as follows:

- Progressive generalization of pre-school education in which the role of municipalities has been crucial.
- Explosion of basic and secondary enrolment rates strongly challenging the combination of quantitative (enrolment rates) and qualitative (education and training achievements as measured, for example, by PISA results), reinforcing the former and weakening the latter.
- A continuous fight to reduce drop-out rates.
- Strong growth in the number of teachers within the system and a corresponding increase in the influence of education trade unions, generating a typical example of an input-based system with a high capacity to fix and increase public expenditure.
- Progressive implementation of a vocational education system, developing the preliminary and successful experience of professional (vocational) schools and generating several vocational modalities with strong EU–ESF co-funding.

- Launch of a very ambitious policy programme, called the ‘New Opportunities Initiative’, targeted at certificating the professional experience of workers in educational qualifications (in the first years of the initiative) and aiming in subsequent phases to certificate professional experience into professional qualifications.
- Supported by the ERDF, the 2007–2013 programming period of Structural Funds was in the 2007–2008 crisis the mechanism by which a huge programme of modernization of basic, secondary and integrated schools was launched, with a strong impact on the reorganization of the regional and local schools network.

### *1.3.9 A Highly Vulnerable Social Model: Dependent on Labour-Market and Growth Prospects*

Finally, ESM implementation in Portugal turns out to be vulnerable to the labour market performance and growth prospects of the Portuguese economy. This is a corollary of three decades of attempts to implement a generous version of the ESM on Europe’s periphery.

We argue that the sustainability of ESM achievements in Portugal is, at present, threatened not only by the generalised cuts in public funding generated by the austerity dimension of bailout conditionality, but was already in danger due to the exhaustion of the growth/development model before the 2008 crisis and its associated developments.

This argument may be controversial but it is the outcome of the effects of the new policy approaches on an often neglected feature of the Portuguese economy. In fact, even before the 2007–2008 crisis, Portugal was undergoing a process of significant structural change related to: (i) structural adjustment of the country’s productive specialisation profile linked to (re)globalisation and the effects of an overvalued euro (relative to Portugal’s development level); (ii) a painful transition from a period of high employment creation in low-qualified/low wage jobs towards a new one in which the challenge is to create more skilled jobs in order to integrate a new input of young people much more educated than older population cohorts; (iii) the need to redress the allocation of private and public resources out of non-tradable sectors (services, infrastructure, real estate and finance and banking). These are the main reasons why Portugal must be considered, within the EU, as an example of a latecomer country as far as structural change is concerned (see Banco de Portugal 2013).

The convergence of the undergoing structural crisis and the 2007–2008 Great Recession dramatically changed the entire context of the Portuguese economy, exacerbating the existing trends towards job destruction and making more complex the conditions for the emergence of the needed ‘social pillow’, further exacerbating social tensions and significantly eroding social cohesion.

The exhaustion of the growth/development model occurred simultaneously with a significant change in the Portuguese labour market. Until the emergence of growth exhaustion, the labour market was clearly pro-cyclical: recessions were obviously detrimental to both unemployment and employment rates, but recoveries were an opportunity to reduce the unemployment rate and to increase the employment rate in order that, peak to peak, structural unemployment did not change significantly. The same pro-cyclical pattern was visible in both long-term unemployment and participation rates. In other words, growth showed itself to be a good substitute for active employment policies. Very dynamic flows of firms’ destruction and creation, new – and increasingly used – forms of atypical wage relations and a complex phenomenon of delaying wage payments were the main vehicles through which the economy compensated the rigidity fostered by labour legislation, principally the limitations on dismissing workers in recessions.



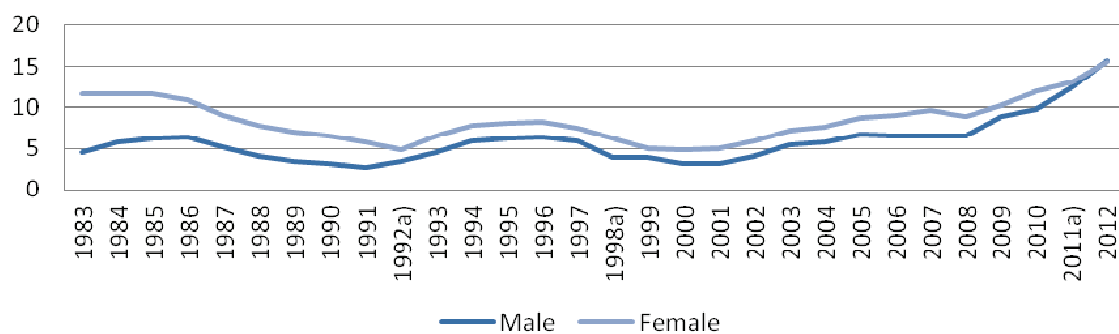


Figure 8.1 Unemployment rate by gender, Portugal, 1983–2012 (%)

Note: a) break in series.

Source: INE, Estatísticas do emprego (EE) – 4th trimester 2012.

This labour market pattern changed significantly together with the increased signs of exhaustion of the growth model.

The increase in the magnitude of structural unemployment is associated mainly with the decline of non-tradable goods sectors (mainly construction but also retail) and the high share of low qualified people working in these activities who cannot easily find a new job without a strong (and not always successful) investment in continuous training.

We can understand the vulnerability of the ESM pillars in Portugal to these unfavourable prospects, bearing in mind that low growth and increased structural unemployment affect all the pillars of the ESM. The intensity of needs is increasing and, simultaneously, public action is being weakened. One example of the complexity of these impacts can illustrate this vulnerability: after a period of significantly increasing pre-school infrastructure at the local level, some are now facing a strong challenge to their financial sustainability, while a significant number of families with both father and mother unemployed are keeping the children at home, sharply reducing the demand for such social facilities.

## 2. MAIN RECENT CHANGES IN THE PORTUGUESE SOCIAL MODEL (PSM)

The previous Portuguese social model (PSM) has been subject to important recent reforms, especially after the outbreak of the crisis and the macro-adjustment programme imposed by the bailout. However, it is important to stress that relevant reforms had been implemented in order to adapt its main institutions to emerging challenges. We will present the main outlines of change in welfare institutions separating the period before and after the emergence of the crisis in order to identify any divergence in the rationale of changes and reforms. We shall argue that recent austerity measures risk completely destroying the rationale of increasing efficiency and effectiveness that were prevalent in changes before crisis.

## **2.1 Reforms before the Crisis**

In this section, we shall concentrate on the changes made before the crisis. Following our previous identification of the main pillars of the Portuguese welfare system, we can provide evidence of important policy action in all of them.

### *2.1.1 Labour Law: Introducing 'Flexibility' While Keeping 'Security' as a Basic Workers' Right*

The design of the Labour Code issuing from the 1974 revolution had, as previously stated, the security of employment as a central axis and a basic workers' right.

The main topic under discussion has been employment security/rigidity. Portugal has been classified as one of the more rigid labour markets, according to the OECD index.<sup>2</sup> In the late 1990s–early 2000s Portugal ranked at the top with regard to employment protection legislation (EPL) indicators, associated mainly with the protection of permanent workers against (individual) dismissal.<sup>3</sup> Following a general trend in OECD countries, the 2000s have been marked in Portugal by a revision of labour regulation. In 2003, a new Labour Code was adopted, revised in 2009 and again in 2012, to promote flexibility on the labour market, while retaining the principle of employment security as a central axis of labour law. The main areas of change in 2003 concerned: (i) the duration of the normal working day (namely reducing the period of time considered as night work; (ii) the extension of the legal duration of fixed-term contracts; (iii) the introduction of geographical mobility clauses in collective contracts; and (iv) changes in collective law made by introducing expiry clauses in collective agreements. The employers' organisations supported the changes, while the two biggest trade union confederations represented in the Economic and Social Committee (CES) opposed the change, though with different positions: CGTP rejected the Labour Code proposal and abandoned the negotiations,<sup>4</sup> while UGT, despite its disagreement with the proposal, participated in the negotiations and contributed to improving it.<sup>5</sup>

Both trade union confederations claimed that the government proposal had some unconstitutional dispositions (namely those limiting the right to strike, the impermanence of collective contracts and the right conferred on employers to ask for information on the health of workers). The Portuguese President sent the document to the Constitutional Court, which declared it unconstitutional on the grounds of fundamental rights stated on the Constitution (the right to privacy in personal life and the safeguarding of collective bargaining).

In March 2005, a new government was elected on a programme that included a compromise on the revision of the Labour Code. On the basis of research and discussions with the social partners,<sup>6</sup> a tripartite agreement was signed in 2008,<sup>7</sup> around five main issues, with measures aimed at (i) increasing the adaptability of firms (flexibility in working

2 See OECD (2004), pp. 61–125.

3 *Idem*, p. 72.

4 CGTP is the oldest (dating back to the autocratic regime as a clandestine organisation) and biggest confederation of workers in Portugal. It is close to the Communist Party.

5 UGT is a confederation of workers created in 1978 to ensure union plurality. It is close to the Socialist Party and also the Social-Democratic Party.

6 Dornelas et al. (2006) and Comissão do Livro Branco das Relações Laborais (2007).

7 The government, four employers' organisations (Manufacturing and Construction Confederation, Trading Confederation, Tourism Confederation and Agriculture Confederation) and one of the trade union confederations (UGT) signed the agreement. The employers' confederations, despite their recognition of the agreement, publicly stated that they would want more changes, namely regarding individual and collective dismissal and short-term contracts (Lima 2008: 1–2).

time arrangements for firms but also for workers on the grounds of more family-friendly parental leave options); (ii) promoting collective agreements; (iii) rationalising and reinforcing the security of both parties in the event of dismissals (mainly by simplifying and reducing the duration of the dismissal process); (iv) improving the effectiveness of labour law (namely by improving inspection of workplaces and fighting against illegal work); and (v) fighting precariousness and segmentation in the labour market and promoting decent work.

### *2.1.2 Social Dialogue: Series of Tripartite Agreements*

Reform of the Labour Code evolved in parallel with the increasing institutionalisation and visibility of social dialogue. The standing committee for social conciliation (CPCS), organised within (although independently) the economic and social committee (CES), played a very important role. Important progress in social dialogue and prevention of social conflict has been intermediated through institutionalised discussion within the CPCS and CES. Also in 2006, other important agreements were achieved by all social partners (CGTP included) on minimum wages. This agreement recognised the ‘low value of the existing minimum wage in Portugal as well as the desirability of its gradual increase’ and the ‘importance of defining the evolution of the monetary value of the minimum wage on a medium-term basis in order to ensure both predictability and trust for firms and workers’ (CES, 2006:1). The social partners and the government decided to increase the minimum wage to 403 euros a month in 2007<sup>8</sup> and to agree on the values of 450 euros and 500 euros to be achieved in 2009 and 2011,<sup>9</sup> respectively.

This was a significant characteristic of the time before the crisis: increasing trust between the social partners had been accumulated in this process of institutional social dialogue, as compared with the conflictive pattern of the 1970s, the 1980s and, largely, the 1990s, and which was to be destroyed by the crisis and austerity policies.

### *2.1.3 Social Security and Health Systems under Reform to Ensure Sustainability*

In 2006, a tripartite agreement (within the CPCS) on social security reform was also implemented to take into account several variables,<sup>10</sup> such as population ageing, the progressive increase in contributory periods and the growth of pensions at a higher rate than that of contributions, and also to reinforce the sustainability of the social security system considered as a fundamental pillar of the Portuguese social model.<sup>11</sup>

The social security reform also introduced a sustainability index<sup>12</sup> (linked to the increase of life expectancy) to be used in the calculation of pensions, and for means-tested social benefits defined according to the PIB growth rate and consumer prices. The principle of maximum value for public pensions was also defined (12 times the IAS) as well as the principle of convergence of existing regimes: the general and the public sector workers’ regimes. The early and mid-2000s were also characterised by changes in unemployment benefits, family pay, parental leave and poverty prevention among the elderly. In brief, before the crisis social security was undergoing reform to ensure its sustainability,

<sup>8</sup> In 2006 the value of the minimum wage was 385.90 euros.

<sup>9</sup> The 2011 goal has not yet been achieved.

<sup>10</sup> The final agreement has not been signed by CGTP (this confederation had signed the preliminary agreement on the strategic outlines of social security reform but did not sign the final one, arguing that it would imply the reduction of pensions). All the other social partners signed the agreement.

<sup>11</sup> CES, 2007: 2.

<sup>12</sup> The IAS – Social Sustainability Index.

an achievement that has been recognized in some international surveys (mainly OECD). Similarly structural reforms concerning pensions had also been undertaken in 2007.

As for social security, the reorganisation and rationalization of the national health system (SNS) was targeted at increasing its efficiency and financial sustainability and, at the same time, ensuring its quality and universality.<sup>13</sup> The main areas of change concerned: implementation of the national network of integrated continuous care<sup>14</sup> (namely to develop a more adequate response to the increasing number of elderly people); the creation of a national network of health care centres providing primary health care to families; reorganisation of the national network of public hospitals in terms of the provision of emergency services; reorganisation of the SNS at national, regional and local levels; introduction of fees to be paid by users of the SNS defined as a ‘moderation rate’, aimed at rationalizing and regulating access to health care, while reinforcing social justice as a prevalent principle of the SNS (many users are not covered by this fee either for health care reasons or family income reasons).<sup>15</sup>

#### *2.1.4 Education: Pre-crisis Reforms Oriented towards Higher Efficiency*

One of the main structural features of the pre-crisis measures in this sector are related to the reorganisation of the education system in order to concentrate resources on bigger institutions providing different grades of education. This was expected to increase efficiency as it allowed scale effects and also the closure of a significant number of widely dispersed small schools. The introduction of an adequate scale in education providers would also allow more adequate provision of complementary education in the regions. These measures evolved in parallel with new local procedures to guarantee transportation to students and huge investment in the renovation of school buildings and facilities, partly (but importantly) supported by European Structural Funds (ERDF).

The rationalization of the system has also taken place through the introduction of an evaluation system among teachers, aimed at making it more adequate and not simply relying on administrative rules and procedures. This has been a very tense process, with a lot of conflicts and strong mobilization of teachers by their strong unions. This process has had ambivalent (and fairly extreme) effects on public opinion.

#### *2.1.5 Reorganization in the Public Sector*

In the 2000s and long before the crisis, Portugal implemented significant reforms targeted at improving public administration by reorganising it and reducing public expenditure. The OECD has classified the Portuguese public administration reform as ‘ambitious’, stating that it ‘is a major component of the budgetary consolidation strategy [that] goes beyond fiscal consolidation, to include enhancement of the quality of public services and strengthening the governance of public institutions.’<sup>16</sup>

This reform has been designed in two main areas: (i) reorganization of central administration (in the PRACE programme) that aimed at reorganising and simplifying the structure of public services and making them more user-friendly (individuals and firms), reducing redundancies (namely by sharing services) and promoting e-government; and

13 Information in this section is based on the official site of the Portuguese Ministry of Health, see: <http://www.portaldasaude.pt/portal/conteudos/a+saude+em+portugal/servico+nacional+de+saude/historia+do+sns/historiadosns.htm>

14 A joint initiative of the Ministry of Health and the Ministry of Employment and Social Solidarity.

15 Those with chronic diseases and pregnant women, for example.

16 OECD (2008), p. 47.

(ii) reform of human resource management with regard to careers and contracts, the introduction of the so-called ‘mobility pool’ and a recruitment-limiting rule for public workers (one new recruitment for every two leaving).

## **2.2 Positive Evaluation of Pre-crisis Reforms**

The reforms implemented in the 2000s have been favourably evaluated by the main international organizations: OECD, the IMF and the European Commission.

In fact, according to the OECD (2008: 63):

Portugal has made very good progress in reducing the fiscal deficit, using a wide ranging programme of structural reforms that will continue to pay dividends well into the future. Challenges that remain to anchor results achieved and reduce the deficit further include: fully implementing the human resources reform in the public administration; improving efficiency in the SOE sector; further closing the financing requirement in the contributory pension deficit; and tackling ongoing pressures of ageing on the health budget.

Also, the IMF (2008:1) has stated that:

Decisive action, focused on the government sector, is being taken to address the imbalances accumulated during the 1990s, and results are being seen. Weaker global conditions make addressing Portugal’s economic challenges both more difficult and urgent. Policies should build on recent achievements, and avoid jeopardizing long-term goals for short-term gain.

Finally, according to the European Commission (2008: 27):

The Commission [...] considered that the action taken by Portugal in response to the Council recommendation represented adequate progress towards the correction of the excessive deficit. In particular, Portugal (i) achieved a 2005 deficit outturn as planned; (ii) adopted a comprehensive package of corrective measures which, provided full and effective implementation, was in line with the required structural adjustment in 2006; (iii) confirmed the deficit target for 2008 below 3% of GDP and a structural adjustment path in accordance with the Council recommendation; (iv) implemented or initiated expenditure-containing measures and kept fiscal targets in spite of a more cautious assessment of GDP growth prospects; (v) planned to bring government debt back on a declining path as from 2008; and (vi) took action to improve the quality of public finance statistics.

Thus reform in the pre-crisis period was unanimously approved. In particular, the IMF considered it important not to introduce short-term biases that could compromise the medium-term benefits of the changes. The ESM in Portugal was an evolving reality towards higher efficiency of public expenditure and also showed (at least preliminary) achievements aimed at adapting it to structural challenges common to most EU countries.

## **2.3 Austerity Policies during the Recession**

### *2.3.1 Lower Growth*

To contextualise the present it is useful to take into account the evolution of the Portuguese economy in recent decades (Figure 8.2).

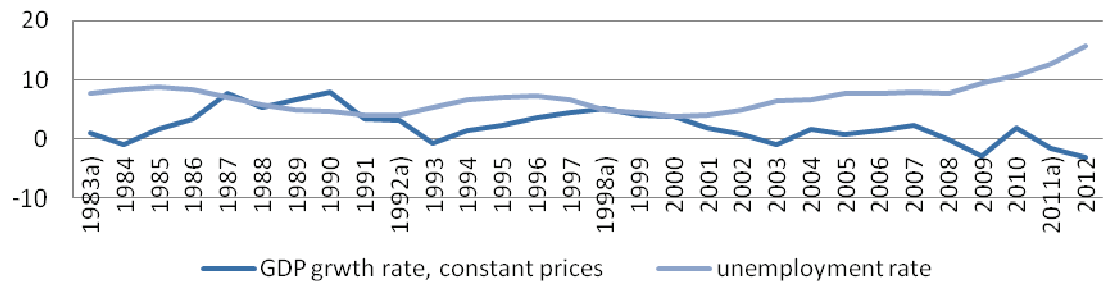


Figure 8.2 Annual GDP growth rate and unemployment rate, Portugal, 1983–2012

Note: (a) break in the series for the unemployment rate.  
Source: PORDATA.

Since the beginning of the twenty-first century Portugal has had fairly anaemic economic growth contrasted with higher growth in other EU countries, especially other southern European ones (Figure 8.3). The rather slow growth went together with a procyclical and fairly low unemployment rate (by EU standards) that has been one of the main characteristics of the Portuguese labour market in recent decades. Nevertheless, since the beginning of the new century, the unemployment rate has been increasing slowly but consistently.

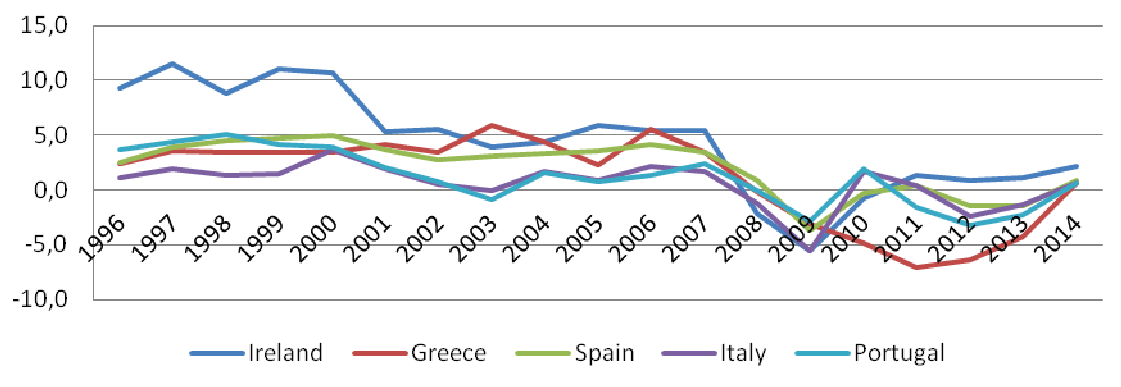


Figure 8.3 GDP growth rates, Portugal and selected EU countries, 1996–2014

Source: EUROSTAT [nama\_gdp\_k].

Three other important structural characteristics of the Portuguese labour market are worth noting: (i) low wages by EU standards; (ii) low educational attainment of the labour force; and (iii) high incidence of temporary contracts,<sup>17</sup> which appear to be the main contractual form for promoting flexibility (normally corresponding to higher employment precarity) in the use of labour (the share of temporary employees in 2012 was 13.7 per

17 According to EUROSTAT temporary employment includes work under a fixed-term contract, as against permanent work where there is no end-date.

cent in the EU27 and 20.7 per cent in Portugal; in that same year only Spain and Poland had a higher share, at 23.7 per cent and 26.9 per cent, respectively).<sup>18</sup>

### 2.3.2 Structural Unemployment But Less Access to Unemployment Benefits

The fairly slow growth went together with a pro-cyclical and low unemployment rate (by EU standards) that has been one of the main characteristics of the Portuguese labour market in recent decades. However, since the beginning of the new century, the unemployment rate has been increasing slowly but consistently. The year 2008 represented the start of a huge unemployment increase that raised the unemployment rate to unprecedented levels, from 7.7 per cent in 2008 to 15.7 per cent in 2012, extending into 2013 (in the first trimester of 2013 it reached 17.7 per cent,<sup>19</sup> but fell in the last months of the year).

Data on the number of families that have both parents unemployed show a dark picture reflecting a particularly vulnerable situation:<sup>20</sup> it rose consistently from 1,530 couples in October 2010 to 13,176 in April 2013.<sup>21</sup>

The unemployment rate, having increased in all age groups, is especially high for young people (currently around 40 per cent).<sup>22</sup> Nevertheless, we must keep in mind that the biggest contributors to unemployment are older people (aged 45 and over), who represented 30.4 per cent of total unemployment in 2012, and the low educated, who accounted for 60 per cent of total unemployment in that same year (old unemployed people tend to have a lower education).

*Table 8.1 Unemployment rate by age group and educational level, Portugal, 2003–2012 (%)*

	2003	2006	2009	2012
<i>Unemployment rate</i>				
Total	6.3	7.7	9.5	15.7
<i>By age group</i>				
15 to 24	14.5	16.3	20.0	37.7
25 to 34	7.5	9.1	10.9	18.1
35 to 44	5.1	6.3	8.5	13.4
45 and more	3.6	5.4	7.0	11.5
<i>By educational level</i>				
Basic	6.2	7.7	10.1	16.2
Secondary	6.9	8.5	9.6	17.6
Tertiary	6.0	6.3	6.4	11.9

Source: INE, Estatísticas do emprego, fourth trimester 2012.

Also it is important to note that the long-term unemployed currently represent the highest share of the unemployed, as well as that 90 per cent of Portuguese unemployed are people in the labour market looking for a new job (Figure 8.4).

18 EUROSTAT [lfsa\_etpga]

19 INE, Estatísticas do Emprego, 1st trimester 2013.

20 Given the precariousness of this situation unemployment benefit is calculated, since 2011, taking this element into account.

21 IEFEP, Informação mensal sobre estado civil do desempregado e condição laboral do cônjuge.

22 INE, Estatísticas do Emprego, 4th trimester 2012.

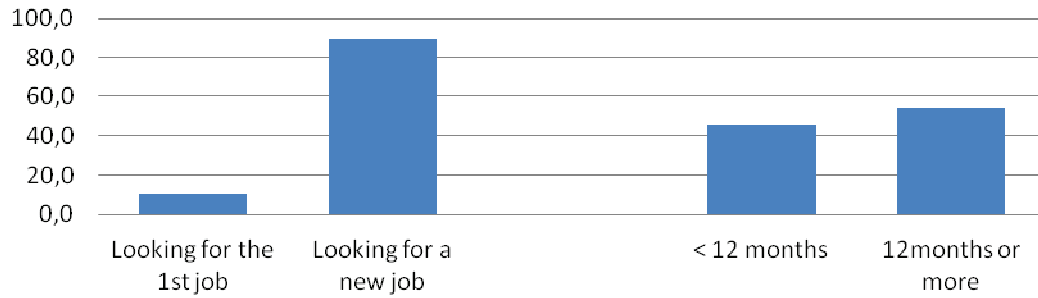


Figure 8.4 Unemployed by type and duration of search, Portugal, 2012 (%)

Source: INE, Estatísticas do emprego, 4th trimester 2012.

A significant threat to social cohesion, unemployment increased together with a fall in the share of the unemployed covered by unemployed benefits: a gap emerged between these two groups due to both the high unemployment and the changes introduced in the legislation on unemployment benefits. In 2008, 61 per cent of Portuguese unemployed received unemployment benefit in comparison with 46 per cent in 2012).<sup>23</sup>

### 2.3.3 Wages and Income Distribution: The role of the Minimum Wage

Portugal is a low-wage country in EU terms. Figure 8.5 shows that in 2010 average gross hourly earnings in Portugal were the lowest in the EU15.<sup>24</sup>

Despite the measurement difficulties, the available empirical data show that Portugal has a gender pay gap in line with (or even lower than) the EU average.<sup>25</sup> However, the recent trend in the EU has been towards a falling gender pay gap (17.3 per cent in 2008

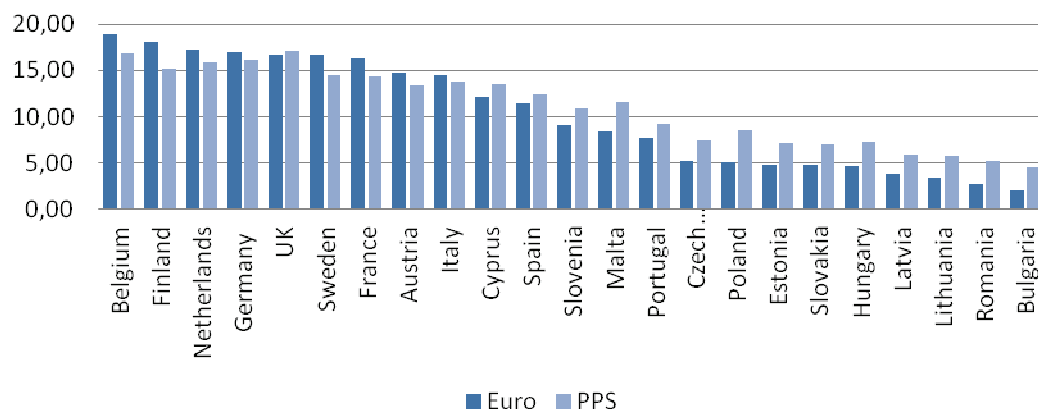


Figure 8.5 Average hourly earnings, Portugal and selected EU countries, 2010

Source: Eurostat.

23 INE, Estatísticas do Emprego – 4º trimestre 2012.

24 This has been a persistent characteristic of the country.

25 EUROSTAT data on the unadjusted gender pay gap refer to private firms employing 10 or more employees.



and 16.2 per cent in 2011),<sup>26</sup> while in Portugal the recent evolution shows an increase (8.5 per cent in 2007 to 12.5 per cent in 2011<sup>27</sup>).<sup>28</sup>

Besides the low average wage the pay system in Portugal is also characterised by a high incidence of low wages, which also have a gender bias (Table 8.2), although minimum wage policies have had an important effect on sustaining the incomes of low qualified workers. Available data show a tendency towards a higher incidence of workers paid at the minimum level, especially among women, young people and fixed-term employment.<sup>29</sup>

*Table 8.2 Low wage earners as a proportion of total employees, Portugal, 2006 and 2010*

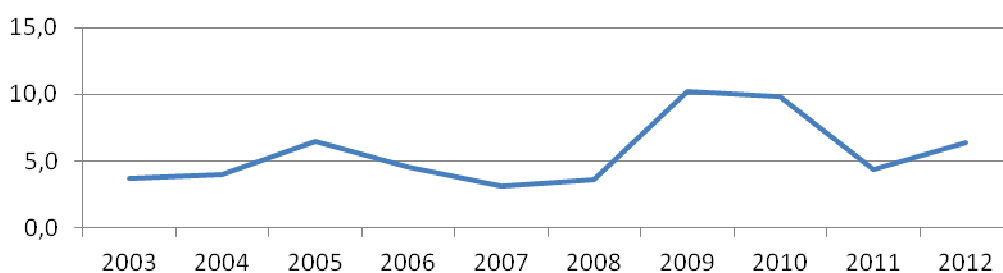
	Portugal			Euro area		
	Total	Male	Female	Total	Male	Female
2006	20.7	15.4	26.4	14.4	10.3	19.6
2010	16.1	10.2	22.1	14.8	11.0	19.2

Source: EUROSTAT [earn\_ses\_pub1s].

A major debate has been taking place in Portugal on the effects of minimum wages. In fact, a social pact had been signed in 2010 between the government, the employers' associations and trade union confederations in order to increase the minimum wage to 500 euros by the end of 2011. That increase has not been achieved, however, due to the austerity measures.

### *2.3.4 Public Accounts Deteriorating*

The evolution of fiscal policy and of the consequent indebtedness of the Portuguese economy (Figures 8.6 and 8.7) has been under particular European control since the launch of the Stability and Growth Pact (SGP).



*Figure 8.6 Government deficit as a percentage of GDP, Portugal, 2003–2012*

Source: EUROSTAT [[gov\_dd\_edpt1].

26 EUROSTAT [earn\_gr\_gpgr2].

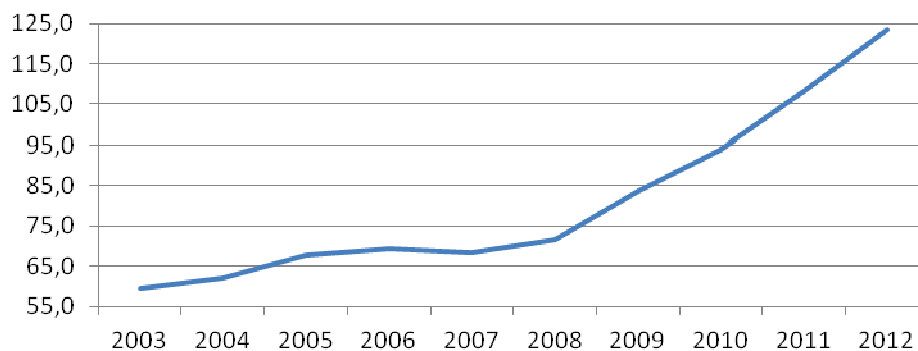
27 Idem.

28 However, this evolution has to be taken with some caution because the data concern only firms with at least 10 employees, reducing their representativeness. Using national data covering all the private firms with at least one employee the evolution over recent years shows a fairly stable (slightly decreasing ) gender wage gap in the past decade (GEP/MTSS, Quadros de Pessoal, 2010).

29 Carneiro et al. (2011).

Portugal in recent times has not had a deficit complying with the Sustainability and Growth Pact (SGP).<sup>30</sup> However, the situation has varied over time: (i) an increase in the deficit until 2005 leading to a peak of the deficit in that year; (ii) a significant reduction in the deficit until 2007 and a slight increase in 2008; (iii) a huge increase in 2009, hardly changing in 2010; (iv) a big decrease in 2011; but (v) a new increase in 2012 reaching the peak value of 2005.

Before the 2008 crisis, Portugal was able to achieve significant fiscal consolidation, whose sustainability was reversed immediately after 2008, not only because the control of public expenditure lacked consistency but also due to a dramatically low growth rate (see Figure 8.2) and increasing social pressure resulting from rising unemployment. Notwithstanding the very tough austerity measures and the reduction of the public deficit, public indebtedness does not show a positive trend due, among other things, to the still unstable financial market conditions and the additional debt due to the bailout.



*Figure 8.7 Government consolidated gross debt as a percentage of GDP, Portugal, 2003–2012*

Source: EUROSTAT [[gov\_dd\_edpt1].

In general terms Portugal has had an anaemic GDP growth rate, an increasing unemployment rate, a public deficit and public debt before the crisis above the Stability and Growth Pact. All these indicators (with the exception of the deficit in 2011) have got worse, reinforcing the vulnerability of the Portuguese social model.

Given the high social costs and declining social cohesion, the Portuguese economy is desperately seeking a difficult balance between sustainable progress with fiscal consolidation and the need to maintain growth and social cohesion. The rationale and concrete implementation of austerity measures are hardly evolving in that direction.

### *2.3.5 Austerity Policy Design*

Since 2010 and in response to the development of the sovereign debt crisis and the EU summits, the bailout conditionality forced Portugal to implement packages of austerity measures essentially aimed at reducing the public budget deficit and at preventing an increase of Portuguese indebtedness.

30 This applies to comparative data since 1995.

### **A shift in EU policy**

In fact this corresponded to a change in European policy regarding the crisis. As stated by the European Commission (2010: 1):

The European Economic Recovery Plan (EERP) was endorsed by the European Council in December 2008 and introduced a sizeable discretionary fiscal stimulus aiming to boost demand and stimulate confidence over 2009–10. The majority of stimulus measures in 2009 and 2010 are temporary and are planned to expire by 2011. These temporary measures have had positive effects on employment and economic activity during the crisis, by supporting private demand and maintaining fundamentally sound activities and jobs that could otherwise have been lost. However, once economic growth resumes on a durable basis, such measures if left in place would add up to an intolerable burden for the public finances; they could also hinder adjustment processes within and across sectors by subsidising existing firms and specific productions.

This change in the European strategy to fight the crises is referred by Caldas (2013:1) as corresponding to the shift from an ‘economic stage’ (December 2008 to February 2010) when the fight against the crisis involved a (temporary) fiscal stimulus to a ‘budget stage’, when the policy concerns ‘were transferred from the economic recovery to the euro and eurozone stability by means of recovering market trust through a coordinated budget consolidation in the EU’. The year 2010 did, in fact, see the adoption of a new European policy to face the crisis, as is clearly expressed by the European Commission (2009: 3):

Ministers agreed at the Informal Ecofin in Göteborg of 20 October 2009 on the need for a co-ordinated and comprehensive approach on exit strategies, encompassing measures to rebuild a stable and viable financial sector, ensure fiscal sustainability and to raise potential output. As to the fiscal exit strategy, it was agreed that substantial fiscal consolidation was required beyond the withdrawal of the stimulus measures of the European Economic Recovery Programme in order to halt and eventually reverse the increase in debt and restore sound fiscal positions.

It was, in fact, a sudden change of EU policy orientation. Portugal followed in strict terms the initial orientation towards a fiscal stimulus, which partly explains the increase in public expenditure between 2008 and 2010.

### **Pre-Troika austerity**

Austerity measures began to be adopted in March 2010. The main changes introduced in these programmes are synthesised in Table 8.5 in the annex.

In March 2011, a new programme (PEC) was proposed but subsequently rejected in Parliament by the opposition. Following this rejection the government presented its resignation. About a month later the government, still functioning, asked for financial help from the European Commission. Negotiations with the Troika were carried out by the government (Socialist Party) and two centre-right (PSD, Social Democratic Party) and right-wing parties (CDS-PP, Popular Party). The Memorandum of Understanding (MoU) was signed by these three parties and the Troika, representing an important political compromise between the main political actors in Portugal, in a process that has been understood as an important indication of political cohesion in the country.

### **Memorandum of Understanding**

On 8 April 2011, Eurogroup and ECOFIN Ministers issued a statement clarifying that EU (European Financial Stabilization Mechanism) and euro-area (European Financial Stability Facility) financial support would be provided on the basis of a policy programme supported by strict conditionality and negotiated with the Portuguese authorities, duly involving the main political parties, by the Commission in liaison with the ECB, and the IMF. Further to the EU support from the EFSM, loans from the European Financial Stability Facility (EFSF) will contribute to the financial assistance. The Loan Facility Agreement on the EFSF financing contribution will specify that the disbursements thereunder are subject to the compliance with the conditions of this Memorandum (MoU 2011: 1).

The MoU<sup>31</sup> states clearly that the conditions negotiated are to be evaluated and implemented strictly. It also details a number of objectives focused on the labour market.

The document is organised in terms of seven main points: (i) fiscal policy; (ii) financial sector regulation and supervision; (iii) fiscal-structural measures (including, among other things, public administration and health care); (iv) labour market and education; (v) goods and services markets; (vi) housing; and (vii) framework conditions (including judicial system competition, public procurement and business environment).

General objectives and very detailed targets are established. The Memorandum (MoU, 2011: 22) lays down labour market measures to:

Revise the unemployment insurance system to reduce the risk of long-term unemployment while strengthening social safety nets; reform employment protection legislation to tackle labour market segmentation, foster job creation, and ease the transition of workers across occupations, firms, and sectors; ease working time arrangements to contain employment fluctuations over the cycle, better accommodate differences in work patterns across sectors and firms, and enhance firms' competitiveness; promote labour cost developments consistent with job creation and enhanced competitiveness; ensure good practices and appropriate resources to Active Labour Market Policies to improve the employability of the young and disadvantaged categories and ease labour market mismatches.

It also refers to the need to:

Address early school leaving and improve the quality of secondary education and vocational education and training, with a view to raise the quality of human capital and facilitate labour market matching.

It includes explicit reference to the fact that:

Reforms in labour and social security legislation will be implemented after consultation of social partners, taking into account possible constitutional implications, and in respect of EU Directives and Core Labour Standards.

In particular, four main aspects of the MoU should be underlined. The first is that unemployment and employment security and working time arrangements, despite the pre-Troika changes introduced in all of them, appear as top intervention areas, alongside

31 Three documents and a letter of intent compose the Economic Adjustment Programme for Portugal. The documents are the following: (i) Memorandum of Economic and Financial Policies (MFEP); (ii) Memorandum of Understanding on Specific Economic Policy Conditionality (MoU); and (iii) Technical Memorandum of Understanding (TMU). All of them are included in EC (2011).

active labour market policies; second, the MoU also highlights the importance of improving human capital; third, it explicitly addresses the importance of social dialogue; and finally it explicitly refers to the need to consider the constitutional implications of the measures to be implemented.

After the signing of the MoU the social partners retained a willingness to negotiate that is expressed in a Tripartite Agreement on Competitiveness and Employment (January 2012).

The Tripartite Agreement on Competitiveness and Employment (January 2012), signed by the government, the employers' confederations and one of the trade union confederations, gave important social support to the forthcoming reforms. However, the difficulties in concluding this agreement can be inferred from its need to rely on the more general statements of the previous 2011 agreement (under the previous government).

### **Austerity measures even beyond the Troika's demands**

The political parties supporting the new government based their election campaign on the ideas that 'cutting wages and firing workers will not be necessary to comply with the MoU',<sup>32</sup> and 'any tax adjustment if needed will be done through indirect taxes and not by income taxes'.<sup>33</sup>

According to the MoU, the measures to be implemented in 2011 were in the existing public budget. Nevertheless, the government decided to go 'beyond the Troika', implementing two extraordinary measures in 2011: (i) 3.5 per cent extra tax on income and (ii) raising VAT on energy.

The measures implemented subsequently have emphasized wages and pension cuts (especially for public sector workers). Tax increases have also been persistent (Table 8.6 in the Annex).

As policy measures were taken mainly in response to pressing short-term needs (related to the Troika evaluation meetings) they have often been designed to ensure short-term results. Most of the changes aimed at an immediate increase in receipts (tax rates, especially of indirect taxes, have been increased) and cuts in public expenditure (cuts in the wages of public sector employees, freezing of new hires and promotions, freezing of insurance benefits and pensions, reduction of means-tested unemployment assistance, family benefit and social assistance).

## **3. MAIN OUTCOMES**

Turning to the main effects of austerity policies and the changes brought to the European Social Model in Portugal we can identify a number of different outcomes.

### **3.1 Social Unrest and Institutional Instability**

#### *3.1.1 A Series of General Strikes and Spontaneous Demonstrations*

Portugal has maintained an image of social stability since the intervention of the Troika. In fact, opposition to the implemented measures has not been extreme or violent. But this does not mean it does not exist. Several streets demonstrations have occurred since the

<sup>32</sup> Prime minister's press statement on 30 April 2011.

<sup>33</sup> Prime minister's press statement on 24 June 2011.

beginning of austerity policy, especially two big demonstrations in 2012. Three general strikes (November 2010, November 2011 and June 2013) have been organised uniting the two trade union confederations for the first time in 22 years. All of them had high participation, particularly in 2010 and 2011.<sup>34</sup> The fact that austerity measures did unite the trade union confederations that, in recent times, have followed diverse strategies (UGT dialogue with governments and employers' confederations and CGTP a more rigid position towards negotiations and a more radical position on strikes) is an important outcome of austerity in Portugal.

### *3.1.2 Political and Institutional Instability*

Political stability, which has also been considered one of the main advantages of the Portuguese context, has also been undermined by conflicts. Two episodes appear decisive in clearly opening up political instability and, by this means, social stability and institutional instability as well.

The first episode was the cut in employers' contributions to social security (TSU) in September 2012. This measure was included in the MFEP (EC, 2011: 41–57) under the heading Fiscal Devaluation:

A critical goal of our programme is to boost competitiveness. This will involve a major reduction in employer's social security contributions. [...] The offsetting measures needed to ensure fiscal neutrality may include changing the structure and rates of VAT, additional permanent expenditure cuts, and raising other taxes that would not have an adverse effect on competitiveness. (EC 2011: 52)

### *3.1.3 Measures Declared Unconstitutional but Followed by Additional Cuts*

The second episode begins in September 2012 and following a declaration of unconstitutionality by the Constitutional Court on the abolition of the thirteenth and fourteenth month pay to public employees and to pensioners (on the grounds they did not comply with the Constitutional principle of equal treatment), the prime minister announced new budget measures to counterbalance this decision.<sup>35</sup> Subsequently, the Constitutional Court, considering the timing of the decision, decided that the measure would not apply in 2012 but only in the following years.

Following this the prime minister, referring explicitly to the Constitutional Court's new decision, stated that 'the 2013 Budget will have to include another combination of charges and sacrifices. The government has decided to increase private sector workers' social security contribution to 18 per cent, allowing as a counterpart a decrease in employers' social security contributions also to 18 per cent. [...]. The increase of 7 percentage points in workers' contributions<sup>36</sup> will also apply to public employees.'<sup>37</sup>

### *3.1.4 Social Partners' Discontent*

The social partners reacted immediately with heavy criticism of this direct redistribution of income from workers to employers, on both the employers' and the workers' side. The

34 For the first time in 22 years, the two confederations joined in the call for a general strike.

35 *Idem*.

36 For the employers the variation was 5.75 percentage points.

37 Prime Minister's statement on 7 September 2012.

head of the Manufacturing and Construction Employers' Confederation has been particularly harsh, saying that 'the pillar of social stability coordinated market economy under attack' and that 'the social partners cannot be used to sign agreements and then not be heard when it comes to decision-making'.<sup>38</sup>

Increased tension and signs of distrust can be discerned in social dialogue. Furthermore, this controversy concerning the TSU has made public clear signs of an increasing tension amongst the two parties in the government.

In June 2013, the four employers' confederations represented on social dialogue committees publicly presented a document criticizing the austerity policies. A few quotations illustrate their strong rejection of the austerity path:

It is urgent to reconcile government targets with reality [...]. The fiscal consolidation policy continues to be based on a reduction of domestic demand, an unwise tax increase and scarce financing opportunities for small and medium-sized firms [...]. Austerity has been a short-term answer (implemented as if it was the only possible answer) but nowadays, given its results, it would be irresponsible to pursue or, even worse, to further develop this approach [...] we cannot insist on a policy that is not a solution for Portugal and from which, if we insist on it, there can be no way back.<sup>39</sup>

### *3.1.5 Criticisms of Austerity within the Government Itself*

Furthermore, in July 2013 the resignation of the Minister of State and Finance (1 July) (accepted) took place, followed by the resignation of the Minister of State and Foreign Affairs (2 July) (not accepted). The Minister of Finance's letter of resignation has been made public and expresses opinions that refer explicitly to a conflict between the government and the Constitutional Court and of tensions within the government.

The Minister stated that:

In a resignation letter one must reflect on one's own limitations and responsibilities. Non-compliance with the limits on the public deficit and the debt in 2012 and 2013 was due to a very strong decrease in internal demand, together with a change in its composition, leading to a strong decrease in tax receipts. The repetition of these deviations undermined my credibility as Minister of Finance.<sup>40</sup>

Thus he resigned with a clear critical assessment of the austerity policy. The prime minister's decision to designate a new Minister among the closer members of the previous Ministers' team and clearly linked to the policy design followed until then was also a catalyst of the resignation of the third most important figure in the government.<sup>41</sup> These episodes have introduced increased mistrust between policy agents and political parties.

## **3.2 Unemployment Crisis without the Tools to Solve It**

The huge increase in unemployment and its structural dimension is the major (and bad) novelty of the recent Portuguese economic and social situation. It has not been generated by the austerity policies (as unemployment was increasing before their implementation)

38 Statement by António Saraiva to Rádio Renascença, 17 September 2012.

39 CAP, CCP, CIP e CTP unidas por um compromisso para o crescimento económico em Portugal, press conference, 24 June 2013.

40 Vitor Gaspar's letter to the Prime Minister, 1 July 2013.

41 Paulo Portas, Minister of State and Foreign Affairs.

but they have contributed to its increase. Under this new situation of massive unemployment, the welfare state would be expected to implement policies (both passive and active) to support the unemployed. However, under austerity, the percentage of the unemployed not receiving unemployment benefits has increased strongly. Partly this has been the outcome of revision of the regulation on unemployment benefits, considered too generous and designed in a way that could be considered an incentive to voluntary unemployment. Reform of this measure, in keeping with the aim of establishing disincentives to voluntary unemployment, in a context of mass unemployment could hardly be understood by the population. Under mass unemployment, voluntary unemployment, even if it existed, is necessarily residual. If such a reform of unemployment benefit had to be introduced in this period of high unemployment and low employment security, the argument would have to be based on social solidarity: under pressure of external financing constraints and the economic downturn, reforms were needed in order to distribute scarce resources among the unemployed in a more equitable way.

The same logic applies to cuts in means-tested benefits, namely family benefits and minimum income. With very high poverty rates (particularly for children) it is hard to understand why family and minimum income benefits have to be frozen (reduced).

### **3.3 Public Sector Affected**

#### *3.3.1 Income Cuts Leading to Demotivation Especially among Public Sector Employees*

Income cuts are also difficult to understand. They were largely accepted in a first stage, when they were presented as a temporary need of a country facing huge financial constraints and designed in a clear and understandable progressive way. It became difficult to understand when minimum wages were kept frozen and the cuts became more and more concentrated on public sector workers, who have been increasingly presented as a privileged group. The simultaneity of cuts in wages, increases in working time, changes in careers and freezing of promotion has been often represented as unfair compared with other social groups. Fairly often, the most important argument has not relied on the need for reforms to rationalize and improve services (clearly supported by evidence), but essentially on the need to reduce the public budget. These changes have increased the vulnerability and sense of unfair treatment of public sector workers, with obvious expected effects on their motivation and so on their productivity. This is particularly evident among teachers.

#### *3.3.2 Lower Quality of Public Services*

Public education faces increased problems because teachers (and other education professionals) are less motivated and public schools face new problems (in a time of crisis with mass unemployment and high poverty rates, a lot of family disruption generates a difficult learning environment). In a period in which schools need more fully committed professionals jobs are being cut and the number of students in the classroom is increasing.

In the health care system the reforms seem less contradictory. Demotivation of health professionals exists, but decisions on careers have been discussed with professional boards in the health sector, leading to less tension compared with the education sector. Also the recent sustainable trend of falling prices has proved very important in guaranteeing access to drugs in a context of cuts and freezes in wages and pensions. (A sustainable trend to reduce drug prices is discernible and has been an important counterpoint to the cuts and freezes in wages and pensions.)



### *3.3.3 The Troika Halting Development of the Education System*

The effects of the 2008 crisis and of subsequent sovereign debt developments has embroiled the education system in disputes, along with an increased number of registered unemployed teachers partly due to a significant fall of the number of young people of school age. The political change after the signing of the Technical Memorandum with the Troika generated additional sources of political and social bargaining: (i) the New Opportunities Initiative presented in previous sections was suspended in order to be revised and to tackle the criticism generated by its extension; (ii) the employability goals gained a political impulse, revising priorities and choices between education and training instruments; (iii) the plurality of vocational education has been criticised and vocational education courses in regular secondary schools became the main priority of the vocational system; (iv) the enrolment in vocational education courses of more vulnerable young people facing complex and diverse risks of social exclusion introduced additional difficulties, challenging regular schools; (v) a preliminary, although not yet implemented experiment to introduce an education voucher targeted at more disadvantaged young people, allowing them to choose between public and private schools, led to a general dispute between those that consider public schools to be the main pillars of the education system and those who believe that private and cooperative schools may play a role in it. Probably, the fight to reduce school drop-outs is the most generally agreed goal within the system, despite generating some controversy as far the solutions to tackle the problem are concerned.

This context should be considered when analysing the social crisis effects of the bailout-related austerity measures in the education pillar of the ESM in Portugal. As far as human resources are concerned, the education system is now facing the consequences of the abrupt consolidation of the state budget at a paradoxical moment. In fact, the number of unemployed teachers has increased a lot but, simultaneously, the number of teachers who are leaving the system due to early retirement, anticipating the deterioration of working conditions within schools and wage cuts, is also increasing. The education system is thus affected in two ways: on one hand, more disadvantaged youngsters are entering the system, requiring more innovative learning environments; on the other hand, the system is now losing more experienced teachers and cannot recruit young and qualified ones.

The increase in the unemployment rate amongst the young and educated, together with all the cuts made in education has introduced potential disruption and other harmful effects in a country with huge shortages of human capital. Many families are starting to question whether it pays to be educated, while the social devaluation of the role of teachers may compromise the renewal (and the quality) of the teaching workforce.

This difficult situation of the education system is a matter of concern, especially considering the low skills endowment in Portugal, despite its pre-crisis attempts to boost education, training and skills as a major pillar of the Portuguese version of the European Social Model. One of our case studies in the next section looks at the skills issue in Portugal and the role to be played by social policy.

### **3.4 Lack of Social Dialogue Disrupting Social Cohesion**

Another basic institution affected by the crisis and austerity policy is social dialogue. Most of the reforms (partially because of short-term pressures) have not been discussed or negotiated or compromises reached with the social partners, further weakening social dialogue.

Was it possible to do it any other way? Given the targets expressed in the MoU and the exigencies of the Troika in the periodic evaluations, maybe not. However, the existence of

intensive social dialogue, able to ensure the benefits of the investment in ‘agreement capital’ – which had significant results in the 2000s – appears to be crucial. They are also fundamental to democracy. There is robust evidence that the institutions represented in the Troika have revealed no capacity to understand that the MoU strategy needed a complete revision in the EU recession in which it has been implemented. In such a recession environment, new combinations of fiscal consolidation, social cohesion measures and timing for adjustment were seen as necessary. The risk of failure both of macro-adjustment and a return to the markets is very high, as are the social costs of adjustment.

In such a context, a large majority of citizens do not understand the ongoing changes, which contributes to a dangerous loss of trust in the state. The emergence of new forms of social contract and the recuperation of trust by citizens will, predictably, be very hard to achieve. Paradoxically, market economies rely on contracts and contracts rely on trust among the parties. Austerity measures, as they have been implemented, have undermined trust, especially in the state due to the widespread belief that the Portuguese state has been breaking contracts for example, with pensioners and public sector workers – to comply with a contract with the Troika related to deficit and public debt targets. The trust of the Troika and of the financial markets is gained at the high price of destroying domestic trust. However, by the end of 2012 neither the fiscal budget as a percentage of GDP (–3.6 per cent in 2008, –10.2 per cent in 2009, –9.8 per cent in 2010, –4.4 per cent in 2011 and –6.4 per cent in 2012) nor the debt/GDP ratio had fallen (increasing every year, rising from 71.3 per cent in 2008 to 123 per cent in 2012). This is difficult to understand, especially if the situation deteriorates constantly.

### **3.5 Rapid Increase in Poverty and Inequalities**

Wages and income distribution policies have obvious effects on social equality and poverty. Portugal is a very unequal country compared with other EU member states.<sup>42</sup> An analysis of Gini coefficients in the EU member states (Figure 8.8) clearly shows Portugal at the top of the inequality ranking (the same applies if we use other common inequality indicators, namely S80/S20).

Portugal has followed fairly different paths during different periods since the mid-1990s (Figure 8.9) as regards poverty. High inequality, compared with the EU average, prevailed. In the late 1990s–beginning of the 2000s inequality did not show important changes despite some short-term variations. After the mid-2000s, however, a clear decrease in inequality is visible, clearly converging towards the EU average. But this tendency was interrupted in 2011, the first year of implementation of the Troika’s Memorandum.

The inequality of income distribution goes together with high at-risk-of-poverty and at-risk-of-poverty-and-social-exclusion rates. Both are high in Portugal by EU standards (Table 8.3 and Figure 8.10) and have not shown signs of significant decrease (nor increase) in recent years. However, it is important to stress that the risk of poverty is not neutral with regard to different population groups.

Portugal has a particularly high risk of poverty or social exclusion among children (aged 17 or below): 28.6 per cent in 2011 compared with 24.4 per cent for the population as a whole (EUROSTAT [il peps01]). Also the family structure has a strong effect

<sup>42</sup> In OECD (2012) a distinction has been made between five groups of OECD countries. The highest inequality group (characterised by a high concentration of labour, capital and self-employment income and a high poverty rate) included six OECD countries: Chile, Israel, Mexico, Portugal, Turkey and the USA.

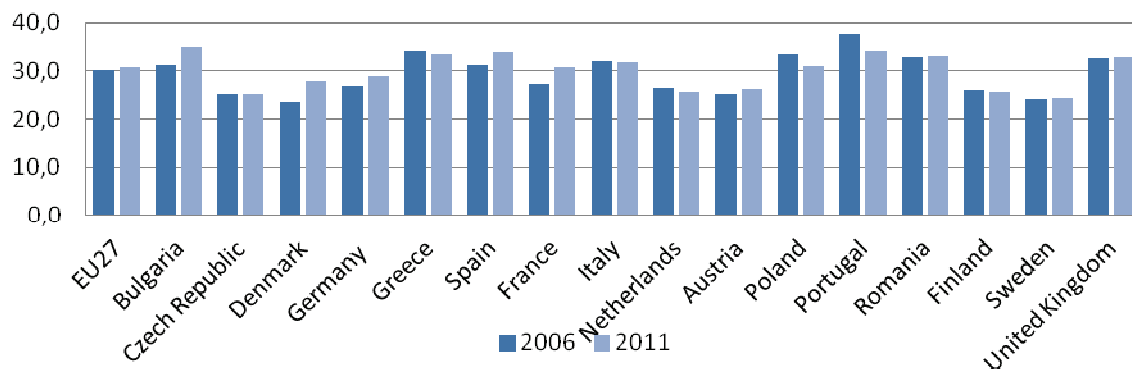


Figure 8.8 Gini coefficient of equivalised disposable income, Portugal and selected EU countries, 2006 and 2011

Note: Equivalised disposable income: total income of a household, after tax and other deductions, available for spending or saving, divided by number of household members converted into equalised adults; household members are equalised by weighting each according to their age, using the so-called modified OECD equivalence scale. Source: EUROSTAT, SILC [ilc\_di12]

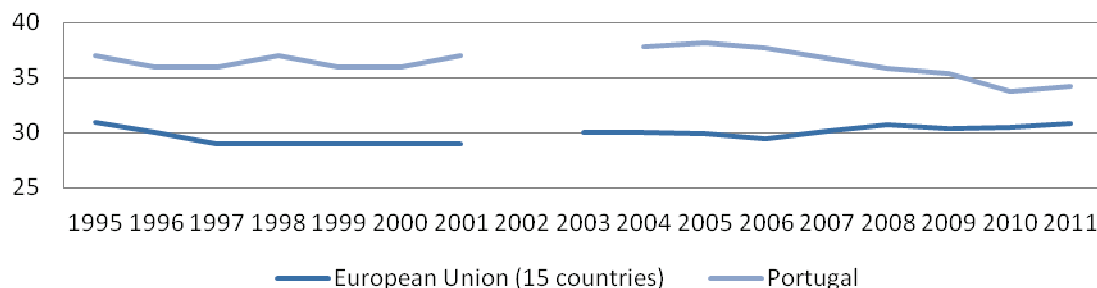


Figure 8.9 Evolution of the Gini coefficient of equivalised disposable income, Portugal, 1995–2011

Source: EUROSTAT, SILC [ilc\_di12]

on poverty risk: ‘single person with dependent children’, ‘one adult 65 years or over’ and especially ‘two adults with three or more dependent children’ households are much more exposed to poverty risks than other household structures (the at-risk-of-poverty rate in

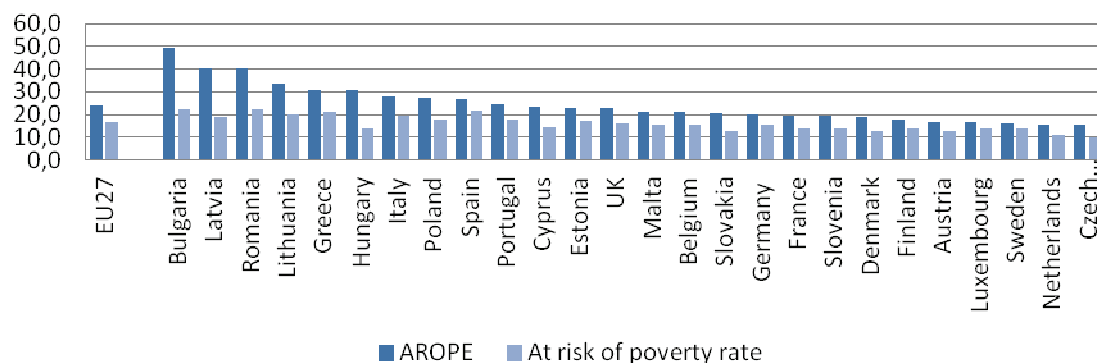


Figure 8.10 At-risk-of-poverty and at-risk-of-poverty or social exclusion (AROPE) rates, Portugal and selected EU countries, 2011 (%)

Source: EUROSTAT, SILC [ilc\_di12], [ilc\_peps01]

Table 8.3 *Poverty indicators, Portugal, 2008–2011 (%)*

	At-risk-of-poverty rate* after social transfers	At-risk-of-poverty or social exclusion** after social transfers
2008	18.5	26.0
2009	17.9	24.9
2010	17.9	25.3
2011	18.0	24.4

Notes:

\* The at-risk-of-poverty rate is the share of people with an equivalised disposable income (after social transfers) below the at-risk-of-poverty threshold, which is set at 60 per cent of the national median equivalised disposable income after social transfers (EUROSTAT).

\*\* ‘At risk of poverty or social exclusion’ (AROPE) refers to the situation of people either at risk of poverty or severely materially deprived or living in a household with a very low work intensity. The AROPE rate, the share of the total population which is at risk of poverty or social exclusion, is the headline indicator for monitoring the EU 2020 Strategy poverty target (EUROSTAT).

Source: EUROSTAT, SILC [ilc\_di12], [ilc\_peps01]

2011 was 27.9 per cent, 30.1 per cent and 34.5 per cent, respectively, compared with a total rate of 18 per cent).<sup>43</sup>

Finally, it is important to stress the importance of education as poverty-preventing: the risk of poverty reduces with the level of education and the education of the parents has an important effect on children’s poverty risk.

### 3.6 The Weakening of Traditional Portuguese Family Support

Pension cuts, even if progressive, are also hard to understand, especially as a persistent means of adjustment. It constitutes a sort of circle that closes up always with the same people inside. In the previous section we showed the impact on inequalities. At the same time, the family networks that traditionally provided an important buffer for Portuguese families in difficulties seem to have been disrupted. As more and more members rely on labour market incomes the difficulties of young people who are increasingly having problems entering the labour market, can less and less be supported by their parents (more and more squeezed by unemployment, wage cuts and tax increases) or by grandparents (pension cuts). At the same time, increasing unemployment, reductions in family income and uncertainty with regard to the future are compromising other long-term decisions of families. Among them and of the utmost importance is the decision to have children, which is crucial for intergenerational solidarity and the sustainability of social security.

### 3.7 Increased Distrust in the European Union

A growing feeling of mistrust towards EU institutions is also emerging. The same European institutions that co-financed Portuguese investments in infrastructure – among other things – are now blaming Portugal for having made these investments. The same EU institutions that recommended that Portugal increase service sector employment and reduce primary employment are now advising that unproductive employment in services is too high. The same European institutions that insisted on measures to fight poverty and social exclusion are now telling the country that cutting wages and social security provisions is

43 EUROSTAT [ilc\_li03].

essential even if Portugal ranks amongst the more unequal EU countries. The EU is starting to be seen as a very fragmented institution and a contradictory project, not dealing consistently with citizens' problems. Not ignoring the national responsibilities and weaknesses that led to the present situation, this is surely also a European problem, implying a European sharing of the costs and a comprehensive strategy to solve the sovereign debt crisis?

#### 4. CASE STUDIES: ILLUSTRATING THE EFFECTS OF THE CHANGES IN THE PORTUGUESE IMPLEMENTATION OF THE EUROPEAN SOCIAL MODEL

##### 4.1 Case Study 1: ESM Changes: Shrinking the Middle Class in Portugal?

###### 4.1.1 Introduction

One of the major discussions of the ongoing crisis concerns its effects on the middle class, the major supporter of democratic regimes. Despite the important discussions on the concrete meaning of the concept 'middle class' it generally refers either to intermediate income groups or to groups of the population that anticipate upward social mobility as an attainable goal. In Portugal, as previously mentioned, austerity packages have been implemented in a context of increasing structural unemployment and have been associated with a process of social, political and institutional instability. Instability can bring (in fact is bringing) increasing feelings of mistrust and lack of expectations with regard to the possibility of attaining a better future. This can compromise economic and social improvement but can also damage democracy itself.

###### 4.1.2 A Context of Inequality from a Comparative Perspective

Portugal is a very unequal country in international terms, whether compared with other EU member states or OECD countries.

A general comparison of the current (2011) income distribution in Portugal and the EU27 average shows the particularity of the Portuguese case: Portugal has a more polarised income distribution compared with the EU27 average (Figure 8.11). This polarization is characterised by:

- a higher income concentration in the top deciles in Portugal (decile 9: 14.7 per cent of income in the EU27 and 15.0 per cent in Portugal; and especially decile 10: 24.0 per cent and 27.2 per cent of income in the EU27 and in Portugal, respectively);
- a similar share of income, in Portugal and the EU27 average, of the lowest decile (2.9 per cent of total income);
- a lower income share for intermediate deciles in Portugal.

Portugal's situation is particularly unfavourable also by OECD standards. In a recent ranking of OECD countries according to inequality of household disposable income Portugal was included in the group of countries with higher income inequality, together with Chile, Israel, Mexico, Turkey and the USA.<sup>44</sup>

<sup>44</sup> OECD (2012), 'Reducing income inequality while boosting economic growth: Can it be done?', in *Economic Policy Reforms 2012. Going for growth*.

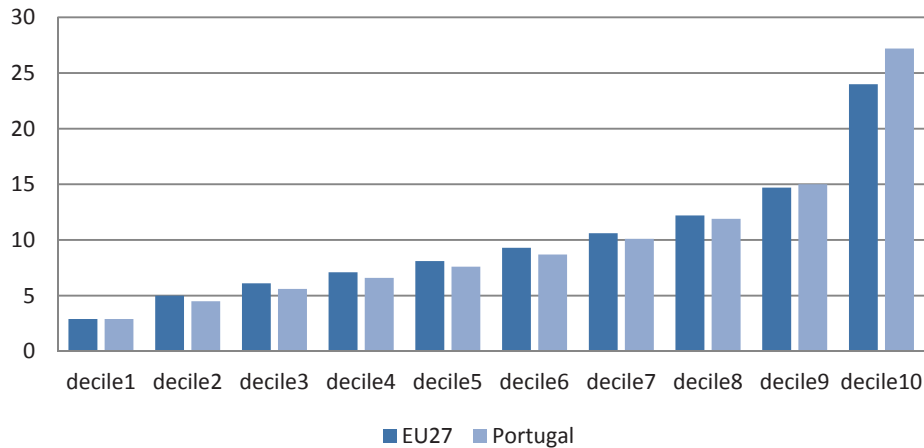


Figure 8.11 Income distribution, EU27 and Portugal, 2011

Source: EUROSTAT, SILC [ilc\_di01]

#### 4.1.3 Increased Inequalities in the Most Recent Period

The evolution of income distribution (Figure 8.12) in the past decade deserves comment:

- In the 2000s the income share of the top decile declined. However, in 2012 this share was higher than in 2011. Portugal remains the EU country with the highest share of income in the top decile (27.3 per cent in 2012).
- The share of the lowest deciles (1 and 2) does not show drastic changes in recent years.
- Deciles 3 to 8 (that, in a strictly income quantified way, can represent the middle class as they refer to the 60 per cent of the population) with an intermediate income (meaning that they do not belong either to the 20 per cent that have the lowest income nor to the 20 per cent with the highest income) appear to be maintaining their share of income in the austerity period.

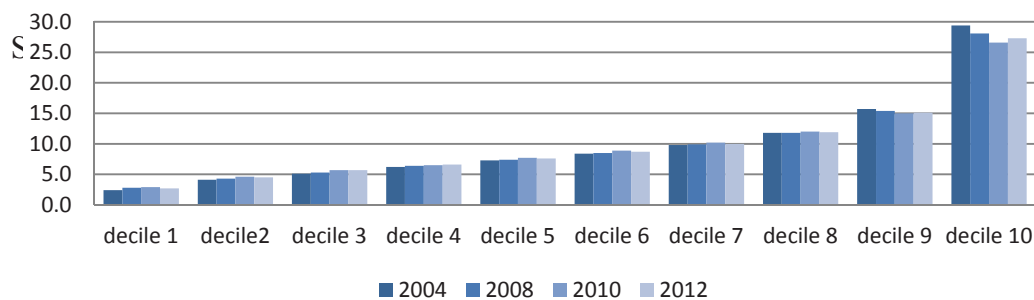


Figure 8.12 Distribution of equalised income by decile, Portugal, 2004–2012

Source: Author’s elaboration of Eurostat data.



Figure 8.13 Share of national equivalised income of different income groups, Portugal, 2004–2012 (%)

Source: EUROSTAT, SILC [ilc\_di01]

Looking in more detail at the recent evolution of income share by main income groups (low income: deciles 1 and 2, medium income: deciles 3 to 8, high income: deciles 9 and 10) we can obtain a clearer picture of the effects of recent austerity policy (Figure 8.13A and 13B).

The contrasted effects of austerity policy show up very clearly:

- Low income groups have a very low share of Portuguese income. However, the evolution of this share has varied significantly in recent years: consistently increasing until 2010 and decreasing afterwards.
- Medium income groups shared a higher percentage of income until 2010. After that, the income share of medium income groups remained almost unchanged.
- High income groups have also maintained a similar share of global income since 2010 (in fact it has increased slightly) after a period in which their share of total income fell.

#### 4.1.4 Public Sector Employees a Prominent and Representative Middle Class Group

It is also worth stressing that public sector workers in almost every country – and certainly in Portugal – tend to be prominent representatives of the middle class. The prestige of public service since the time of the autocratic regime (difficult to enter but offering conditions of stability and career progression) has been reinforced since the 1974 revolution. The need for new services specially linked to the enlargement of the social functions of the state (education, health, social security) increased public employment. As the new activities needed a large amount of highly qualified employees, a large number of high qualified workers entered the public sector and in doing so reinforced its social status.

As argued in the first part of the paper the PSM is mainly an outcome of the mid-1970s. This has created a substantial job creation dynamic, absorbing a large number of the highly educated (namely in the education and health care systems). This means that the increase in the level of education of the Portuguese population has gone together with an expansion of the social functions of the state. Public servants represent an important component of the Portuguese middle class and thus cuts targeted at them represent a serious blow to the middle class.

#### *4.1.5 Specific Effects of Austerity on the Middle Class in Portugal*

How have the austerity measures affected income distribution in Portugal? How did they affect the middle class? Existing estimates show an average reduction of 6.3 per cent in household income as one of the main outcomes of austerity policies in the country. The major contributors to this reduction are cuts in public pensions and public sector pay (net of contributions and taxes), as well as means-tested social security benefits.<sup>45</sup>

The design and intensity of the different austerity packages have led to different effects on income distribution. Avram et al. (2013) conclude that in Portugal austerity policies have affected income distribution by means of an ‘inverted U-shape effect’, meaning that middle income groups contributed relatively less compared with low and high income groups. According to the conclusions of the study austerity in Portugal involves a high income cut for the bottom decile (higher than 5 per cent). The following deciles (from the second to the sixth) have experienced a similar decrease of around 4 per cent. The higher deciles faced a marked progressive income cut (around 5 per cent, 6 per cent, 8 per cent and 9 per cent, respectively, for the seventh, eighth, ninth and tenth deciles).

In that same study an evaluation is made of the measures responsible for this outcome in the various countries. In Portugal cuts in public wages have been the more clearly income-progressive cuts (especially applying to middle and top percentiles).

In Portugal, cuts in public wages are shown to be the most progressive measure, representing cuts in the middle and top percentiles. Public pension cuts are also generally income progressive in their design but had some particular effects compared with public wage cuts in that they affect all deciles, even the lowest. Their impact is relatively similar in the first four deciles, increases for deciles 5, 6 and 7 and increases again for the upper three deciles. Cuts in social security benefits (other than pensions) show a regressive effect on income profile: although affecting all deciles it affected lower more than higher incomes. With regard to measures on income tax and worker’s contributions they also had a transversal effect (with the exception of the top and bottom deciles) and particularly the middle deciles. As the authors report, ‘in the case of Portugal, this effect [the inverted U-shaped effect] is due to a combination of progressive effects from cuts in public wages and pensions and regressive effects from the reduction of the (real) value of means-tested social assistance’ (Avram et al. 2013: 16).

#### **Beyond the income cuts and tax increases: low disposable income**

In the analysis of the austerity policies’ effects in Portugal it is necessary to keep in mind that median disposable income is very low in Portugal according to EU standards. A simple look at Figure 8.14 gives us the dimensions of the income gap between Portugal and its EU partners.

This needs to be kept in mind. Austerity in Portugal is hurting very low incomes by EU standards.

45 Avram S., Figari F., Levynti C., Levy H., Navicke J., Matsaganis M., Militaru E., Paulus A., Rastrigina O. and Sutherland H. (2012), ‘The Distributional Effects of Fiscal Consolidation in Nine EU countries’, Research Note 01/2012, European Commission, December, 2012.



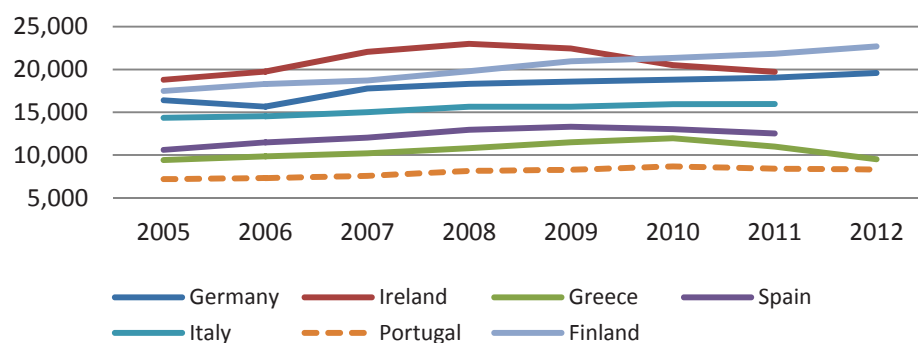


Figure 8.14 Median income, Portugal and selected EU countries, 2005–2012 (euros)

Source: EUROSTAT, SILC [ilc\_di03]

### Increased homogeneity within income groups

Looking in more detail at the data on median income and at the cut-off values that separate the different deciles additional information can be obtained (Table 8.4). In 2009 and 2010 the increase of median income corresponded to particularly high increases in the income boundaries of lower income deciles (2009) and lower and medium deciles (2010). In 2011 and 2012 the reduction of the median income went together with a particularly strong decrease in the income boundaries of the lowest incomes (decile 1 in 2011 and 2012), intermediate deciles (decile 4, 6 7 and 8 in 2012) and also decile 9 in this last year. This can be read as a sign of lower income diversity within these income groups. Considering the cumulative effect of 2011 and 2012, the income groups in which income diversity has decreased the most are deciles 1, 6 and 7 (by 6, 5.2 and 4.9 percentage points, respectively).

Table 8.4 Annual growth rate of cut-off income, Portugal, 2009–2012 (%)

	2009	2010	2011	2012
Decile 1	2.9	5.5	-3.4	-2.6
Decile 2	4.5	4.9	-2.0	-0.3
Decile 3	4.0	3.4	-1.7	-1.1
Decile 4	2.3	3.4	-1.5	-1.8
Decile 5	1.7	4.8	-3.1	-1.0
Decile 6	0.8	6.0	-3.8	-1.4
Decile 7	1.8	4.6	-2.4	-2.5
Decile 8	-1.3	2.3	-1.8	-1.5
Decile 9	-1.5	3.0	-2.7	-1.7
Median equivalised net income	1.7	4.8	-3.1	-1.0

Source: SILC [ilc\_di01]

### Lack of Upward Mobility

There is also evidence of lower mobility throughout the austerity period. This is visible in the EU27 as a whole but is more intense in Portugal: the percentage of the population

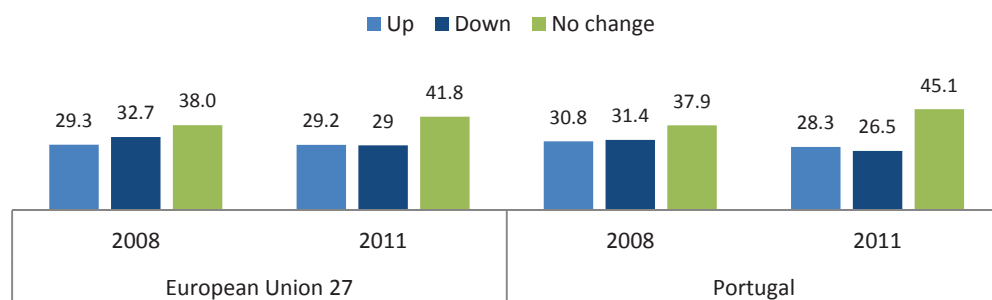


Figure 8.15 Transitions of income by decile, EU27 and Portugal, 2008 and 2011

Source: EUROSTAT, SILC [ilc\_di30]

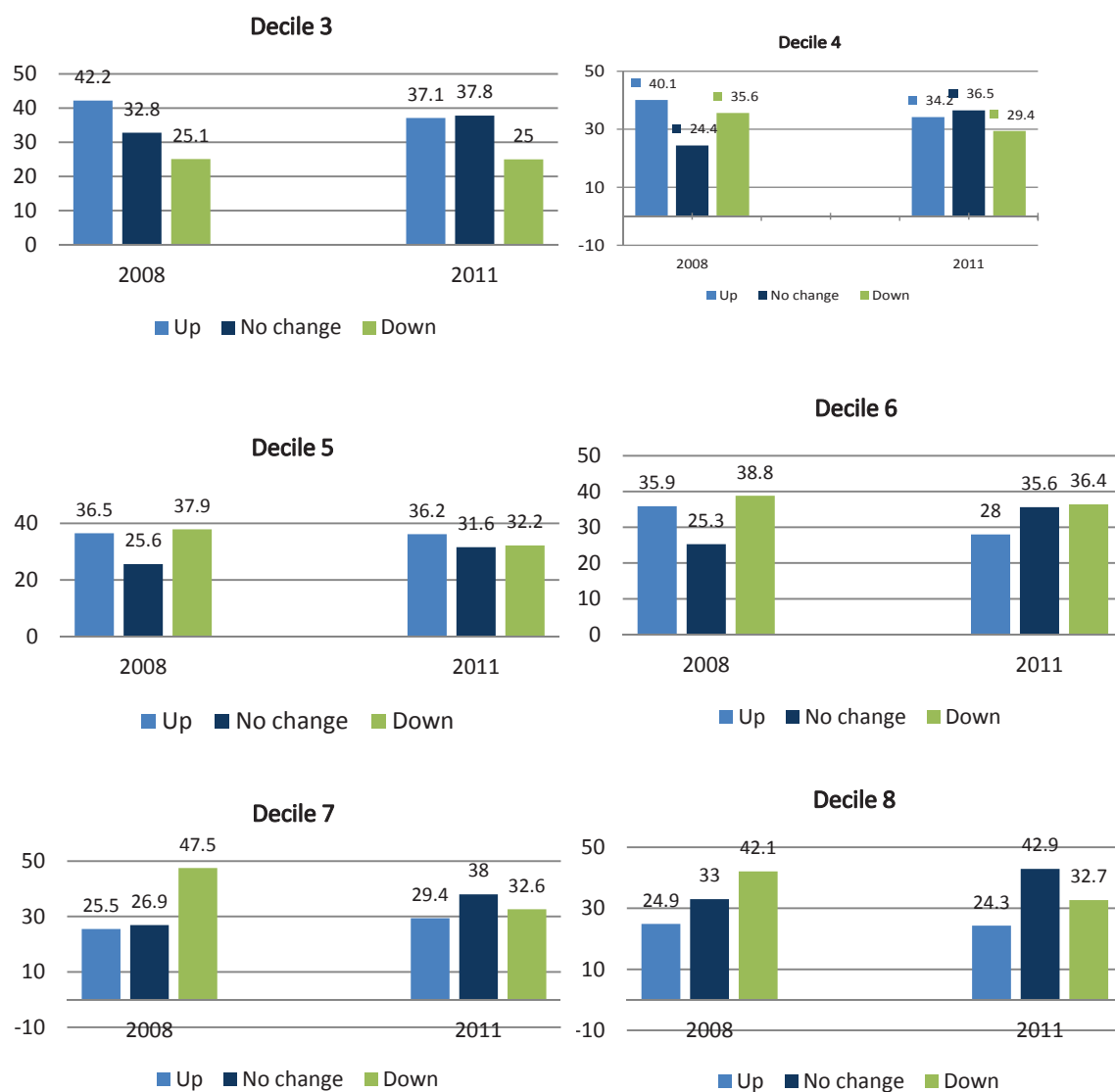


Figure 8.16 Transitions of income by decile, Portugal, 2008 and 2011 (intermediate deciles)

Source: EUROSTAT, SILC [ilc\_di30]

remaining in the same income decile group (no change in Figure 8.14) increased by 3.8 percentage points in the EU27 and 7.2 percentage points in Portugal in 2008–2011.

Increased immobility characterises all income deciles, particularly the intermediate ones (Figure 8.16). In deciles 3 to 8 mobility was high in 2008 (percentage of no change ranging between 24.4% and 33%, low behind the national average, 37.9%) and higher mobility corresponded to the middle deciles 4, 5, 6 and 7. Precisely these are the deciles where immobility has increased most: 12.1 pp, 11.1 pp and 10.3 pp respectively for decile 4, decile 7 and decile 6. This means less opportunities to progress especially among the employees who belong to the middle income groups and so to the middle class.

### **Mass unemployment putting in question upward mobility**

Portugal has a very high education deficit, ranking at the bottom among EU countries with regard to the percentage of 25–64 year-olds who have completed at least upper secondary education (in 2012 this percentage was 37.6 in Portugal and 74.2 in the EU27).<sup>46</sup> However, the recent evolution (as described in Case Study 2) has been fairly striking: the same percentage was as low as 20.2 in 2001.

The increase in unemployment among the highly educated has been undermining the upward mobility path that high education traditionally enabled. Education has historically been, in all European countries, an important means of promoting upward social mobility. Lower-income families aiming at improving the economic and social conditions of their young people found education an effective and secure investment, enabling them to enter more qualified jobs. This defines a strategy of upward mobility that is a main factor in the development of a middle class.

The emergence of structural unemployment in Portugal has challenged this mobility in two ways: (i) increasing unemployment reduces family income (as do wage cuts, social security benefit cuts and tax increases) and so diminishes the household's ability to finance education and (ii) increasing and very high unemployment rates among the highly educated (the third highest in the EU in 2012 and almost three times that of 2002)<sup>47</sup> makes investment in education, paradoxically, too risky in Portugal.

#### *4.1.6 Concluding Remarks*

According to the above information and the previously presented recent trends in the Portuguese labour market we can argue that austerity policies are hitting the middle classes hard, namely because:

- The unemployment rate is affecting the population as a whole. It is true that it has started to hurt a number of sectors in particular but it has been extending to other sectors, including services and is currently hitting the public sector. The existence of a high unemployment rate for university graduates, which has risen to an unprecedented level,<sup>48</sup> is one element clearly narrowing upward social mobility (in 2012 the unemployment rate stood at 15.7 per cent and was as high as 11.9 per cent among those with tertiary education).<sup>49</sup>
- Austerity has strongly reduced family income and affected social mobility mainly in the middle income groups.

46 EUROSTAT, edat\_[lfse\_08]

47 EUROSTAT, [lfsa\_urgaed]

48 However, it is important to stress that this rate still ranks well below the unemployment rate of less educated groups.

49 EUROSTAT, [lfsa\_urgaed]

- Austerity also affected the income distribution within quintiles introducing less income diversity mainly in the very low and medium income groups;
- Austerity measures are significantly concentrated on the public sector: cuts in wages and pensions and promotion freezes have been implemented since 2010. Public servants, a core group of the middle class, have so been losing monetary power due to tax increases but also because of cuts targeted on them.
- Associated with this loss of income but also with a political discourse centred on the idea that the ‘privileges’ of the public sector are one of the main causes of Portugal’s current problems is that public sector workers are also losing social status. This has become particularly evident in the case of teachers, who consider the political speeches of recent ministers of education as an attack on their professional ethics. They complain that it affects how students and parents relate to them. One result of this is an increasing lack of motivation in state schools.
- Recent changes have increased the working time of public sector workers and have introduced measures aimed at allowing lay-offs in the public sector.

The Portuguese middle class (whether represented by those with an intermediate level of income or by one of its core groups, such as public sector workers) appears to be constrained by the recent changes. Under pressure from the risk of unemployment, they face, if employed, wage cuts, social security cuts, tax increases, low probability of upward social mobility and possibly a decline in social status.

The existing lack of trust and uncertainty about the future do not represent an optimistic future. This is fatal for the middle classes because it hampers expectations of social mobility. And as democratic regimes rely on middle classes a moment can arrive where democracy can be in danger, in Portugal and in Europe.

## **4.2 Case Study 2: Dismantling of ESM Putting Portugal’s Future Skills Endowment at Risk**

### *4.2.1 Introduction*

The ESM’s labour dimension in Portugal is strongly conditioned by the structurally low level of qualifications. Stocks versus flows is a metaphor we use to describe how the recent improvements in secondary and tertiary education enrolment rates, the significant fall in the drop-out rate and the strong increase in the number of PhDs (used here as a proxy of advanced human resources) have not yet succeeded in inverting the structural low average performance of the Portuguese economy regarding skills.

The improvements observed in the past two decades and a half are globally the effect of public policies: first, mass participation in basic and secondary education; more recently, the fight against dropping-out and failure, essentially driven by the generalization of vocational education (double certification of education and training courses, vocational courses, apprenticeship) and science policy. In the majority of these public policies the role of the ESF cofunding has been very strong, playing a systemic role in their intensification.

In this context of persistent low levels of education, the penalizing effects of the crisis and of disproportionate austerity measures have risked blunting the contribution of public policies. The results already obtained can only eradicate the structural problem of low skills in the medium term with a continuous improvement in flows. Interrupting these improvements is to compromise the sustainability of the needed structural change.

#### 4.2.2 Recent Improvements in Access to Education

The magnitude of flows can be illustrated by the evolution of the number of students enrolled in secondary education (Figure 8.17) and of gross enrolment rates in secondary and tertiary education (Figure 8.18).

There was a strong increase in the number of students enrolled in secondary education at least until 1996. Stabilization of the number of students enrolled in general (non-vocational) courses began some years before and following a period of significant decline has been stabilizing again recently. In the past ten years, a significant number of students have been absorbed by a diverse set of vocational options, including technological courses, (dual) apprenticeships, double certification (education and training) vocational courses and, more recently, level 3 vocational courses in regular schools.

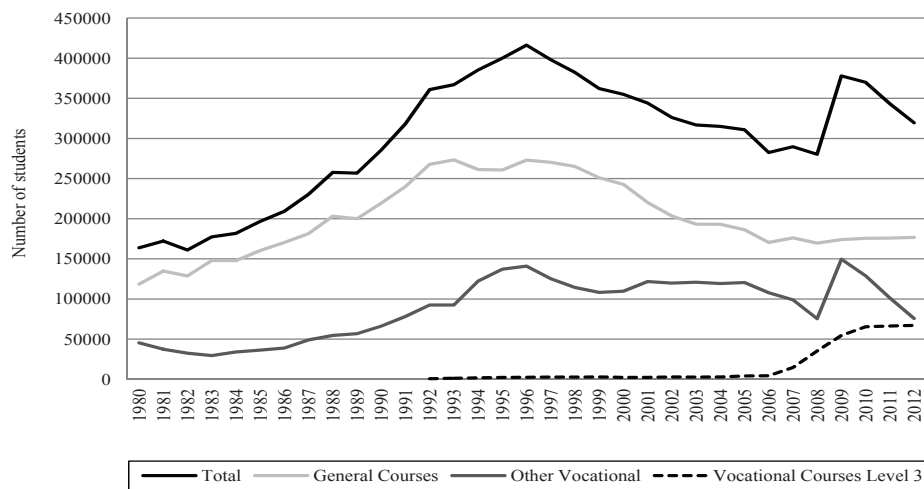


Figure 8.17 Evolution of the number of students enrolled in secondary education, general and vocational courses, Portugal, 1980–2012

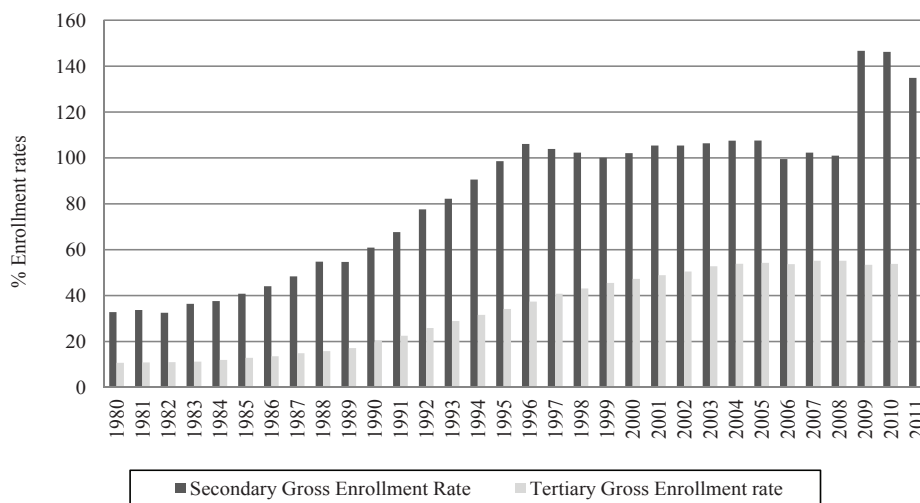


Figure 8.18 Evolution of secondary and tertiary enrolment rates, Portugal, 1980–2012

Source: PORDATA figures on education (both graphs).

The evolution of secondary gross enrolment rates is also striking, mainly in the period from 1980 to 1996. It has since stabilised. The peaks of the past few years have a number of explanations: on one hand, secondary vocational courses managed to recover youngsters already out of the system; on the other hand, as *gross* enrolment rates the numerator includes students in secondary courses who are not of normal secondary age. Tertiary enrolment rates also reveal a stable rising trend, although slower than in secondary education.

The impressive positive evolution of flows has not managed to counterbalance Portugal’s very poor skills endowment. One of the outcomes of this non-conformity between stocks and flows is an emerging dualism.

In a recent study published by CEDEFOP,<sup>50</sup> the limitations of the skills endowment of the Portuguese economy are clearly shown. Comparing the incidence of medium and high qualifications in the labour force in 2010 with the projected change in percentage points by 2020, Portugal is the only country classified as a ‘low level, low change country’: only 30 per cent of the labour force had, in 2010, medium or high qualifications and the estimated change by 2020 is by only 6 percentage points.

It is also worth analysing the ranking of Portuguese regions regarding the incidence of low qualifications,<sup>51</sup> as measured by the percentage of people with at most pre-primary, primary or lower secondary education in the population aged over 15. Amongst the ten worst EU regions as regards these indicators are five Portuguese regions, including Lisbon. For example, Lisbon ranked second in the group of the ten worst performing regions, at 64.5 per cent with at most pre-primary, primary or lower secondary education compared with only 10.4 per cent in the best performing EU region (Prague).

Looking at the skills indicator ‘number of people with tertiary education (levels 5–6 ISCED 1997) as a percentage of the population aged 15 and over’, two Portuguese regions are among the ten EU worst performing regions.

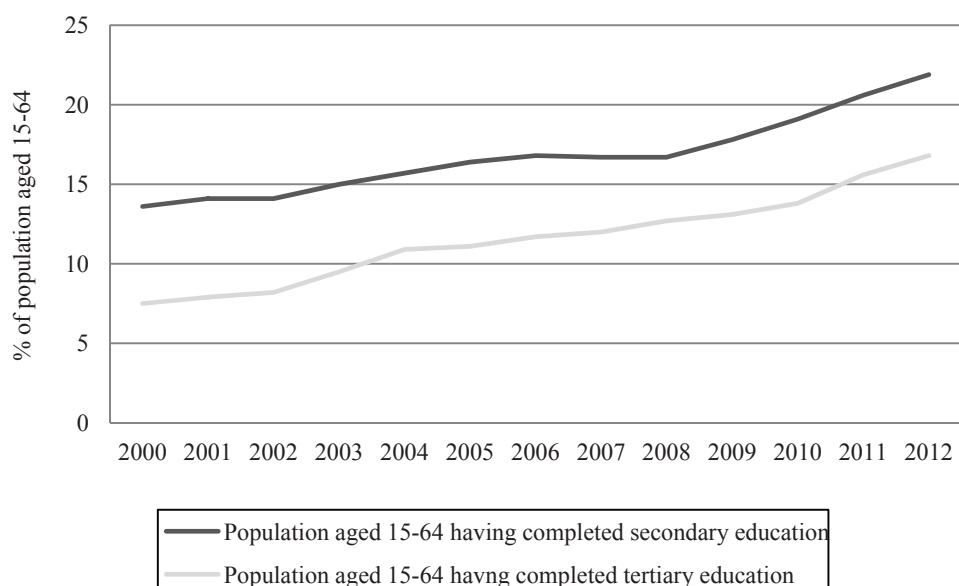


Figure 8.19 Population aged 15–64 who have completed secondary and tertiary education, Portugal, 2000–2012

Source: PORDATA, INE – Annual Estimations of Population and Employment Survey; series break in 2011.

50 CEDEFOP (2010), *Skills supply and demand in Europe – Medium Term Forecast up to 2020*, Tessaioniki

51 European Commission (2013), ‘Mind the Gap – Education Inequality across EU Regions’, NESSE (Network of Experts in Social Sciences of Education and Training).

Notwithstanding the weakness shown by these figures, the EU Innovation Scoreboard 2011 refers to complementary and contradictory signs of skills endowment. The human resources dimension of the EU Innovation Scoreboard depicts the Portuguese economy as contradictory. Regarding the ‘new doctorates’ indicator, Portugal performs relatively well compared with the EU27 (above the EU average). However, as regards the indicators ‘population aged 30–34 having completed tertiary education’ and ‘youth aged 20–24 with an upper secondary level education’ Portugal ranks 30 per cent and 26 per cent, respectively, below the EU average. The high increase in the number of doctorates is also strongly correlated with the impressive positive change regarding international scientific co-publications.

Figure 8.19 (previous page) clearly shows the slowly increasing trend of Portuguese population aged 15 and 64 who have completed secondary and tertiary education, as well as their low levels at the beginning of the decade.

#### *4.2.3 Improvements before the Crisis with ESF Support*

Before the crisis (and with substantial help from the structural funds), a considerable number of public policy instruments targeted at achieving sustainable inclusive modernization of Portuguese society were launched.

##### **The objective of ‘inclusive modernization’**

The fight against dropping-out, the technological and physical improvement of school buildings and infrastructure and the development of vocational education have been the main drivers of so-called inclusive modernization. The rationale has been to foster the modernization of firms to match the continuous improvement of skills flows and to ensure that, by means of training courses, the low skilled unemployed (essentially in construction and low wage sectors) can be redirected to other sectors. There have been encouraging results even if the matching in terms of employability between these two drivers of change is far from complete.

##### **Vocational education and training the key**

On the skills front, the strong impulse of vocational education and training courses has probably been the most important policy measure because it has managed to motivate the return to school of people who had abandoned it and to prevent the dropping-out of youngsters still in school, but facing a high risk of leaving it before gaining qualifications. Regarding basic education, double certification education and training courses have been the dominant approach. Concerning secondary education, vocational courses (*cursos profissionais*) offered by regular schools have prevailed. The apprenticeship system has a long tradition in Portugal and is the only dual modality involving work in the classroom and on-the-job training. Public investment in the modernization of basic and secondary schools, the most quantitative effort partially supported by the ESF, has contributed to this process.

##### **Concrete results on school drop-out rate**

The falling trend of the school drop-out rate from 2000 to 2012 (Figure 8.20) is a good example of ‘stocks versus flows’.

A clear falling trend, particularly for women, is visible and in 2012 was close to the established goal of 10 per cent for early school-leavers. But the really striking figure is the 50 per cent drop-out incidence among men at the beginning of the decade. It illustrates

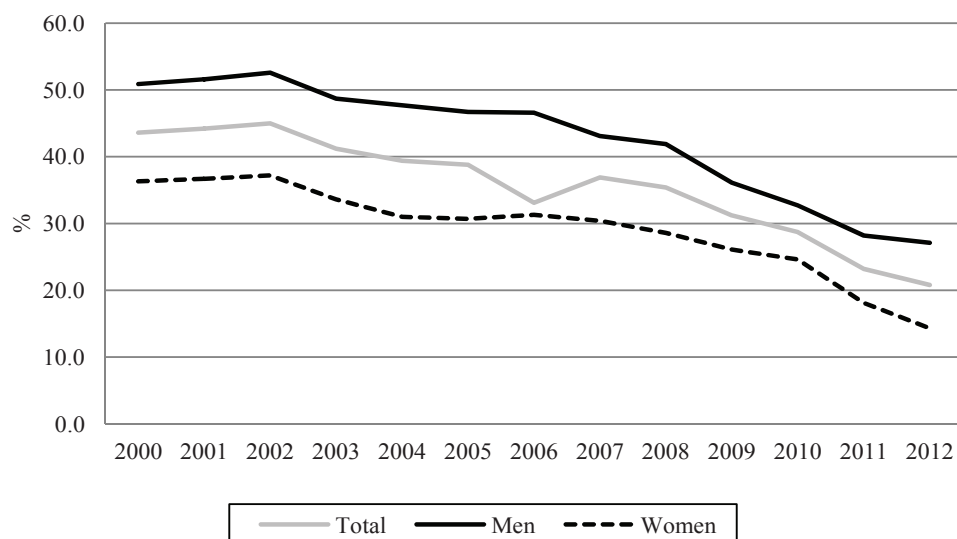


Figure 8.20 School drop-out rate, Portugal, 2000–2012

Note: 2000 begins a new series; 2011 – break of series. Source: PORDATA.

how problematic this phenomenon was. However, in 2000 the most powerful factor determining dropping-out of school was the high probability of entering the labour market early. The capacity of the Portuguese economy to create unskilled and low paid jobs was very high. A model focused on low paid jobs seems to have developed because of the joint interest of employers and low skilled youngsters so that that some matching took place. However, this context has been changing throughout the decade. The capacity to create this type of job seems to have little future because of the structural change due to globalization and affecting low paid jobs. Available data on unemployment clearly show the low education level of unemployed people registered in public employment services (employment centres) and training centres (Figures 8.21 and 8.22).

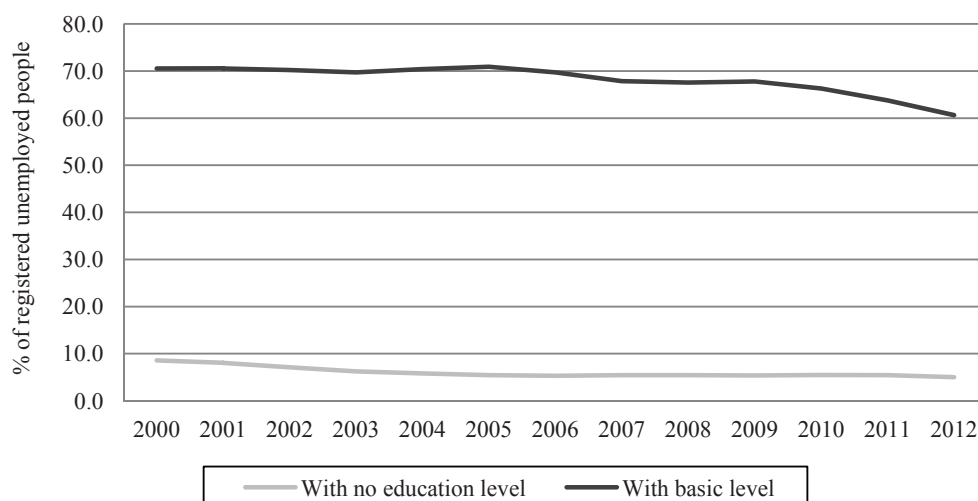


Figure 8.21 Unemployed people registered in public employment services and training centres with no education or with basic education, Portugal, 2000–2012

Note: 2000 begins a new series; 2011 – break of series. Source: PORDATA.



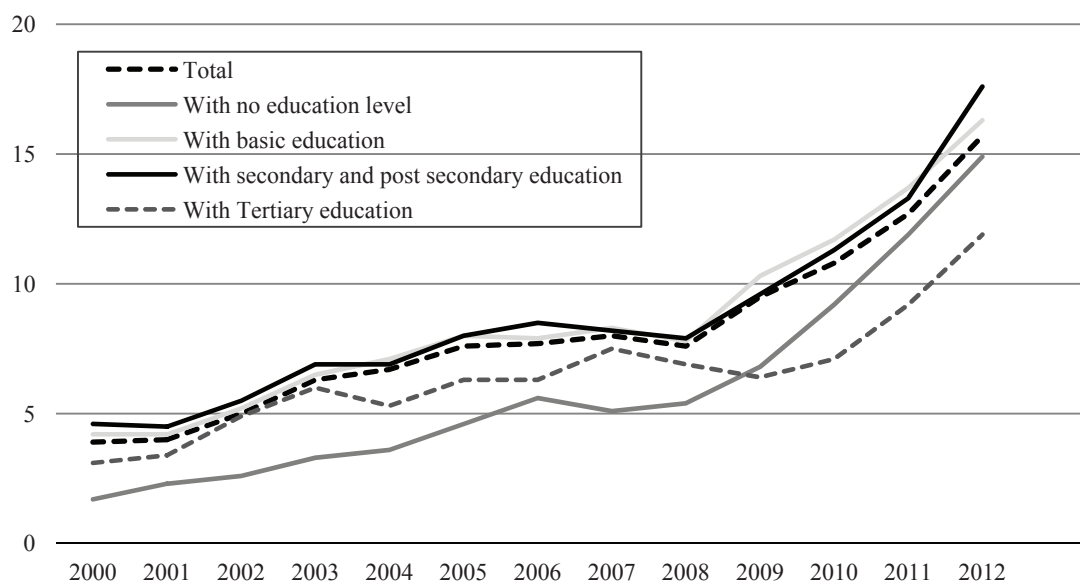


Figure 8.22 Unemployment rate by level of education, Portugal, 2000–2012

Note: 2011 – break series.

Source: PORDATA, using data from Employment Statistics Surveys.

#### A lower probability of low educated workers (re)entering the labour market

The high percentage of the unemployed with no qualifications or only a basic education among the unemployed is a penalizing factor for ambitious structural change in the Portuguese economy and for their reintegration for the reintegration of those unemployed into the labour market. It is true that unemployment rates for those with secondary and tertiary education has also increased dramatically in the post 2007/2008 years. But the probability of being reintegrated is much higher for this last group. By contrast, the non-educated are strongly dependent on the re-emergence of activities on the ‘old model’ (construction and basic retail) which are precisely those most affected by the deleveraging of non-tradable sectors and by the decline in credit operations. The need of a ‘social buffer’ or ‘shock absorber’ is crucial in order to avoid exit from the labour market becoming an irreversible situation for these population groups.

#### 4.2.4 Concluding Remarks

In this problematic context, the policy instruments to fight school dropping-out and failure (focused on young people with a higher propensity to be involved in these processes) and to increase the level of qualifications of low educated unemployed people (mainly focused on adults) turn out to be crucial dimensions of the ESM in Portugal. The relevance of these dimensions is, on one hand, a question of democratic values: the need to minimise the inequality of opportunities between population groups. But these dimensions are also relevant in instrumental terms: successful structural change in the Portuguese economy will be facilitated by more balanced qualifications between population groups.

However, the development of skills and education could be undermined by the abrupt fiscal consolidation driven by the bailout of the Portuguese economy and the conditionality imposed by the Troika. The education and training system is now facing the challenge of integrating young people with higher risk of not completing regular or vocational

education. Additionally, compulsory education increased to 12 years. Consequently, the system is under the pressure of working with more problematic publics in terms of attitudes and motivation to learn. In this difficult context of progression of the education and training system, the effects of austerity are worsening the working conditions in schools and leading the most experienced teachers to leave the system.

After some promising years of good flows concerning enrolment rates, falling school drop-outs and dissemination of vocational education and training modalities in basic and secondary education, the system is under pressure from qualitative developments: the needs to work with young people at risk of dropping-out, to attract people already outside the system, to control retention rates and to prepare teachers in regular schools to adapt themselves to vocational modalities, all these qualitative developments are resource- and time-consuming. Schools and other educational bodies can hardly manage to cope with these new challenges in a context of doubts, troubles and uncertainty induced by severe and blind fiscal consolidation.

## 5. CONCLUSIONS

The example of Portugal illustrates particularly well the combined effects and risks of the financial crisis and of the austerity measures implemented as the bailout adjustment.

First, the international financial crisis hit the Portuguese economy in a period of strong structural change determined by globalization and the anaemic growth of GDP and productivity, which by itself generated substantial job destruction in poorly performing firms. Demand for social protection was very strong in that period and a number of pillars of the ESM in Portugal were involved in efficiency and sustainability-led changes, including social security and the national health system.

Then came the financial crisis and the fiscal stimulus initially recommended (but quickly abandoned) by the European Commission. The vulnerability of the Portuguese economy and of the public accounts to the debt sovereign crisis was very high due to the combination of high and increasing public and private debt, low growth prospects and competitiveness challenges. The bailout austerity measures and the abrupt consolidation of public accounts significantly reinforced the deterioration of social conditions and unemployment figures which were already in place due to structural change in the Portuguese economy and the impact of the financial crisis.

The first lesson to be learned from the Portuguese bailout and associated measures is that one cannot ignore the stage of development of an economy subject to intervention. The demand for social protection was already very high when the memorandum of understanding was signed and austerity measures began to be imposed. The ESM pillars were significantly weakened when demand for social protection was rising and structural unemployment strongly increased, definitively inverting a long period of procyclical unemployment. The high levels of structural unemployment mean that the probability of re-accessing the labour market is very low at least for a large group of low-skilled people. Dismantling the recent and vulnerable dimensions of the ESM in Portugal in such a context will have very high social costs that will not be easy to compensate in the near future. In that context all the progress made in adapting the ESM to modern times and low economic growth prospects which were under way through efficiency and sustainability-led reforms risk being lost. Some of these reforms had been approved within the social dialogue between trade unions and employers but the austerity measures contributed to suspending that favourable social climate. Of course we can say that the competitiveness

problems of the Portuguese economy would definitively lead to the destruction of a significant number of jobs even if the financial and sovereign debt crisis did not exist. Social protection would in any case be crucial in helping Portuguese society to solve that problem. What has happened in fact has been the deterioration of social protection precisely when it was most needed.

The second lesson is that one should be particularly aware of the dynamic negative effects generated by austerity. It is false that after implementing the austerity agenda everything will be ready for a recovery of the trajectory of growth and change. Austerity measures removed the rationale from the adjustment efforts that the Portuguese economy was already making before the crisis, transforming them into a ragbag of expenditure cuts with no strategic goal. There is a high risk that blind austerity measures will generate negative dynamic effects in the long term, penalising growth potential (many people will not return to the labour market) and leading families to inefficient allocation of resources (for example not investing in education). Internal nominal devaluation and the pressure to reduce wages also risk reducing firms' incentives to innovate and to recruit more qualified workers.

The third lesson concerns the risks of regression of social dialogue as a crucial element of democracy in Western advanced societies. The capital of trust between social partners risks being destroyed not because of conflicts between trade unions (at least the moderate UGT) and employers' representatives, but on the contrary due to the lack of trust in government decisions. This is a very harmful effect in a country facing a competitiveness problem that cannot be solved without long-term compromises. Social dialogue is the right institutional space to build that compromise and blind austerity is undermining it. Social dialogue is also a powerful instrument for spreading understanding of the need for austerity when needed and consequently for obtaining acceptance of it without the risk of social disputes, distrust in politics and institutions and threats to democracy.

The fourth lesson is that blind austerity measures are undermining the social cohesion that the Portuguese economy needs to complete the structural change that was under way even before the 2008 financial crisis. The eradication of the competitiveness gap of the Portuguese economy, building a more knowledge-intensive and technology-based specialization profile and reducing the weight of non-traded goods and infrastructure in the Portuguese growth model is a very tough process that cannot be completed by eroding social cohesion. The strong increase in structural unemployment needs a solid base of social protection and not its disintegration. It's true that unemployment benefits can be more efficient in avoiding the risks of voluntary unemployment often emerging in low-wage contexts as observed in Portugal. However, the number of unemployed people not receiving any kind of social protection and the number of couples in which both the man and the woman are unemployed is now out of control. Besides this, Portuguese society is blocked in terms of upward social mobility, as we demonstrated in the first case study. The cuts of public servants' wages, pensions and social benefits in general, the interruption of career progression in public administration and the strong increase in taxes (direct and indirect) are now hindering social mobility. Uncertainty and the increasing number of unemployed young graduates are now pushing a large amount of skilled young people to emigration, provoking a huge fall in human capital in Portugal and a negative return on public investments in education in the past two decades. In this context, families and individuals are now revising their investments in education. Portuguese society, after a long period of low investment by families in education, was beginning to change. The risks of suspension or regression of this investment are now very high, which also contributes to blocking upward social mobility and undermining trust in democracy.

All these lessons cannot be interpreted as a sign that Portuguese society rejects, without understanding, the need to consolidate the public accounts. The high levels of public and private debt (families and firms) are well understood by the public, which is not unaware that deleveraging can be painful. But five years after the 2008 financial crash, two and a half of them under a bailout agreement, the negative effects of austerity are now well perceived as a burden that so far has not brought about a sustained consolidation of the public accounts. In fact, there is no historical example of simultaneous deleveraging and correction of balance sheets of firms, families and governments without painful and unnecessary recession costs. The fiscal consolidation of a small euro-zone economy cannot be achieved independently of a solution for the euro zone as a whole. It is doubly difficult to achieve such consolidation in a period of anaemic growth prospects for the EU. Notwithstanding the resilience of Portuguese exports in an unfavourable context, a fall in the public debt/GDP ratio requires a more favourable context for Portuguese exports to EU markets. Portuguese public opinion in general and the social dialogue partners in particular are beginning to perceive the painful adjustment costs imposed by austerity as in vain and not leading to a sound recovery.

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Table 8.5 *ESM elements in Portugal – Main changes and objectives/drivers in the pre-Troika austerity period*

	<b>Main developments/ changes and dates</b>	<b>Main objectives</b>
<i>Workers' rights</i>	The Labour Code was revised in 2009 namely introducing: i) more flexible working time arrangements; ii) simplification of the dismissal procedures; iii) new measures promoting the reconciliation of work and family life namely related to parental leave; iv) new incentives for firms to promote secure jobs; v) the prevention of illegal work.	To make the labour market more flexible and more job-creation friendly
<b>Social protection</b>		
<i>Pensions and other social security allowances</i>	<p><b>2010:</b> Introduction of the obligatory means-tested (income) mechanism to calculate social allowances</p> <p><b>2010:</b> Freezing of most of the social security allowances (in the non-contributory regime).</p> <p><b>2010:</b> Reduction of the total expenditure in the non-contributory system; 20% cut in the total expenditure on grounds of Minimum Income; Cut of the extraordinary increase of 25% in Child allowances (introduced in 2009) for low income families and extinction of child allowance for high income families</p> <p><b>2010 to apply in 2011:</b> pensions freeze</p>	To ensure the sustainability of the pensions system and to reduce public spending
<i>Unemployment benefits</i>	<p><b>2010:</b> adoption of transitory measures increasing the unemployment pay for families with dependent children having both members of the couple unemployed; The same applies to single parent families.</p> <p><b>2010:</b> change in the relation of the value of the previous net wage and the amount of the benefit (100% to 75%);</p> <p><b>2010:</b> Reduction of the wage offer that the unemployed are obliged to accept</p> <p><b>2010:</b> Possibility of accumulating partial unemployment benefit and part-time employment</p>	To reduce public spending to rationalize social expenditure, to promote social justice and to create incentives for more active job search. Social Partners could not reach an agreement on this issue.
<b>Social dialogue</b>		
<i>Tripartite consultations/pacts</i>	Social Partners and Social Dialogue had an important role on the revision of the labour Code. A Tripartite Agreement for a new System for Labour Regulation, Employment Policy and Social Protection" was signed in June 2008 by the four Employers' Confederations, One of the two Workers' Confederations and the Government, which was the basis of the revision.	Very important role as a means of promoting social peace and trust amongst the participants. This revision was a process that started in 2005 involving studies and a large negotiation process.
<b>Public sector</b>		
<i>Cuts (employment and wages)</i>	<b>2010:</b> 5% cut in the wages of political staff (President, Prime Minister and all the other public heads) and managers of state owned firms.	Reduction of the public deficit with two main objectives: i) to support the financial credibility of the country needed to ensure its regular financing and ii) the sustainability of social policy

Table 8.5 *ESM elements in Portugal – Main changes and objectives/drivers in the pre-Troika austerity period (cont.)*

	Main developments/ changes and dates	Main objectives
	<b>Public sector</b>	
<i>Cuts (employment and wages)</i>	<p><b>2010:</b> Cut in the amount of extra pay (on grounds of transportation, overtime). Impossibility to accumulate a public wage and a public pension.</p> <p><b>2010:</b> Freeze of new hiring to the public sector and reduction of the public employment</p> <p><b>2010:</b> 1% increase in the public sector workers' contribution to Social Security (the rate is now in line with the private sector).</p> <p><b>2010</b> to apply in 2011: Cut of 5% in Public wages. The measure was designed in a progressive form: i) it applies only to those that have a monthly pay higher than 1500€; ii) progressive design of the cut (3.5% to 10%);</p>	
<i>Hire/fire rules</i>	<b>2010:</b> Stricter application of the rule 1 hire for 2 leaves.	Reduction of the public deficit
<i>Flexibility</i>	<b>2010 to apply in 2011:</b> Freezing of promotions in the public service;	
	<b>Wages &amp; living standards: minimum wage, equality, etc.</b>	
<i>Minimum wage</i>	<p><b>2010:</b> Minimum wage increase (from 450€ in 2009 to 475€)</p> <p><b>2010 to apply in 2011:</b> Increase to 485€</p>	To prevent additional employment cuts
	<b>Regional cohesion</b>	
	<p>No relevant changes at this level, excepted the local reorganization of municipalities; the announced reduction of the number of municipalities has not been implemented and only the fusion/association of parishes (at sub-municipal level) has been achieved; the influence of Structural Funds has been relevant to inhibit the fall of regional cohesion; besides this, there is empirical evidence that inter-regional asymmetries in Portugal tend to fall in recession times, increasing on the contrary in expansionary periods.</p>	
<i>Tax policy</i>	<p><b>2010:</b> Creation of a new 45% tax bracket for higher incomes (higher than 150 thousand €)</p> <p><b>2010:</b> Introduction of pay in the previously not paid highways</p> <p><b>2010:</b> Increase by 1 p.p. in each of the three VAT tax brackets that became, respectively, 6%, 13% and 21%;</p> <p><b>2010:</b> Increase of 1 and 1.5 p.p.(for lower and higher incomes) in the income tax rates; complementary taxes of firms</p> <p><b>2010:</b> Increase in the fees to be paid to access some public services namely Justice.</p> <p><b>2010 to apply in 2011:</b> - Increase of the higher (normal) VAT rate in 2p.p. - Cut in the deductions to income tax</p>	
<i>Social expenditure</i>	<b>2010:</b> To reduce expenditure in the Health System by a more efficient management.	

Table 8.6 *ESM elements in Portugal – Main changes and objectives under the Memorandum*

	Main developments/ changes and dates	Main objectives
<p><i>Workers' rights (right to strike, etc.)</i></p>	<p style="text-align: center;"><b>Workers' rights and working conditions</b></p> <p>The Labour Code was revised in <b>2012</b>  The main changes relate to:  - Simplification of firing procedures;  - Cut in overtime pay;  - Working time arrangements  - Reduction of severance pay  - Reduction of holidays  It was implemented in <b>August 2012</b> following Social Dialogue. In September 2013 the Constitutional Court declared the unconstitutionality of some of its dispositions related to firing procedures (considered as not complying with Employment Security as stated in the Constitution) and Collective Bargaining (considered as not complying with the right to Collective Bargaining as stated in the Constitution)  <b>2013:</b> Cut of 4 holidays;  <b>2013:</b> Cut of the possibility of having 3 extra holidays as a productivity bonus in the private sector</p>	<p>To make the labour market more flexible and more job-creation friendly</p>
<p><i>Pensions</i></p>	<p style="text-align: center;"><b>Social protection</b></p> <p><b>2012:</b>  - All public pensions were frozen.  - An extra tax on pensions was introduced for pensions higher than 1500 euros a month and varying according to level from 3.5 to 10%);  <b>2012:</b> Increased limitation on early retirement (retirement age kept at 65 years and 30 working years, extended to public sector workers). Additional penalties for pre-retirement situations. Over-taxation of pensions (higher than 1350 euros a month) to be paid as an extra solidarity measure (the constitutionality of this measure was causing a big debate)  <b>2012:</b> suspends 13th and 14th pension pay (the Constitutional Court declared this measure unconstitutional but admitted it in 2012 as an exceptional measure related to the deepness of the crisis);  <b>2012:</b> freezes pensions, except for low pensions  <b>2013:</b> Cut of 14th month pay for public pensioners (this measure was declared unconstitutional by the Constitutional Court and so suspended)</p>	<p>To ensure the sustainability of the pensions system and reduce public spending</p>



Table 8.6 *ESM elements in Portugal – Main changes and objectives under the Memorandum (cont.)*

	<b>Main developments/ changes and dates</b>	<b>Main objectives</b>
<i>Social security</i>	<p><b>2010-2012:</b> freeze the nominal 2009 value of the social benefit index (SBI) which is the base for most social benefits.</p> <p><b>2012:</b> Cut in illness pay</p>	To reduce public spending.
<i>Unemployment benefits</i>	<p><b>2012:</b> reduce unemployment benefit amount and duration but also reduces minimum contribution period.</p>	To reduce public spending and to create incentives for more active job search.
<i>Social allocations</i>		To reduce public spending.
<b>Social dialogue</b>		
<i>Tripartite consultations/pacts</i>	<p>Important agreement but clearly less importance attached to social dialogue</p>	Important at the formal level (as a way of ensuring social peace) but hard to achieve.
<b>Public sector</b>		
<i>Privatization</i>	To continue the privatization programme	Improve the efficiency of the system
<i>Cuts (employment and wages)</i>	<p><b>2012:</b></p> <ul style="list-style-type: none"> <li>- Cut of the 13th and 14th month pay (the Constitutional Court declared this measure unconstitutional but admitted it in 2012 as an exceptional measure related to the deepness of the crisis);</li> <li>- lay off of at least 2% of public sector workers</li> </ul> <p><b>2013:</b> Cut of 14th month pay for public workers (this measure was declared unconstitutional by the Constitutional Court and so suspended)</p> <p><b>2013:</b> Increase of the working time to 40h/week</p>	Reduction of the public deficit
<i>Employment</i>	<b>2013:</b> Increase in working time: implementation of 40 hours/Week	
<i>Hire/fire rules</i>	<b>2013:</b> more dispositions aimed at the mobility of employees	To increase recruitment and employment
<b>Wages and living standards: minimum wage, equality, etc.</b>		
<i>Minimum wage</i>	<p><b>2012:</b> Minimum wage kept its value of 2011: 485 Euros (14 months a year). This value was maintained in 2012 at the level of 2011 (since 1982 it had increased yearly). This is currently one of the main discussions within Social Dialogue bodies.</p>	To prevent additional employment cuts

Table 8.6 *ESM elements in Portugal – Main changes and objectives under the Memorandum (cont.)*

	<b>Main developments/ changes and dates</b>	<b>Main objectives</b>
	<b>Public services</b>	
<i>Health care</i>	<p><b>2011</b> on: reduction of the price of medicines</p> <p><b>2012:</b> increase of moderation rates paid in the use of SNS services and reduction of the number of exemptions.</p>	To reduce public spending.
	<b>Regional cohesion</b>	
<i>Tax policy</i>	<p>No relevant changes except fusions of parishes and reorganization of some public services in inner and less developed areas</p> <p><b>2011-2012:</b> Creation of a new income tax applying to all employees and pensioners (3.5%)</p> <p><b>2012:</b> increased tax rate on capital income</p> <p><b>2012:</b> change social insurance contributions of self-employed workers</p> <p><b>2012:</b> Increase of the income tax (in 2.5%) for higher incomes (more than 153 300 €)</p> <p><b>2012:</b> More goods included in the higher VAT bracket</p>	
<i>Social expenditure</i>	A much slower increase in Portugal than in the average OECD country	Budgetary purposes

