

The Impact of the Fiscal Crisis on Greek and Portuguese Welfare States: Retrenchment before the Catch-up?

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Abstract

This article examines the impact of the ongoing (2008–13) economic crisis on Greek and Portuguese welfare state reforms in a comparative perspective with a particular focus on the public sector, labour markets and social protection. It is argued that the recent crisis caused ‘shock and awe’ in Greece and Portugal resulting in an unprecedented wave of cuts, tax rises and labour market reforms. In particular, public sector remuneration and jobs were cut, pensions were significantly curtailed and pension rights significantly restricted, successive tax hikes were implemented and welfare benefits became less generous and more conditional. It is argued that these reforms constitute a critical juncture and a considerable effort towards welfare retrenchment, which is which is implemented before converging with the more advanced welfare states of the EU15. Both countries appeared to be significantly more vulnerable to the crisis than the richer countries of Northern Europe (e.g. Germany, Austria, Sweden, Finland and the Netherlands) and their larger Southern counterparts (Italy and Spain). Yet, the latter had to implement similar measures, albeit in a less abrupt and extensive fashion. In other words, it may be that size is less important than economic and political power for coping with the effects of the current crisis.

Keywords

Financial crisis; Welfare state; Retrenchment; Southern-Europe; Greece; Portugal

Introduction

The integration of Europe’s Southern Periphery (Portugal, Ireland, Greece and Spain – known as the cohesion countries, or by the offensive acronym PIGS) into the EU has always been a controversial issue: on the one hand, some have highlighted the acute disparities between Europe’s periphery and core (cf. Rodriguez-Pose 2002). On the other hand, the literature emphasized the crucial link between EU membership and political, economic and social modernization (see Featherstone and Kazamias 2001). The recent financial crisis of 2007 and the subsequent sovereign debt crises in Greece, Ireland and

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Portugal put cohesion counties along with Italy at the centre of a borrowing cost upward spiral. Their ever-increasing borrowing costs and recourse to the EU and the International Monetary Fund (IMF) for financial support meant that they had to implement extensive fiscal consolidation measures to tackle their unsustainable borrowing levels and costs.

This article discusses the impact of the ongoing (2008–13) economic crisis on Greek and Portuguese welfare state reforms with a particular focus on the public sector, labour markets and social protection. The first part discusses briefly the literature on the characteristics of the Greek and Portuguese welfare states, arguing that despite disagreements between different schools of thought, there is a broad consensus that both welfare states are underdeveloped and weak – especially in comparison to those of the other members of the EU15.¹ The second part discusses the trajectories of the Greek and Portuguese welfare states until the financial crisis, arguing that despite considerable improvement, both Greece and Portugal caught up only partially with, and with much less generous provisions than, the rest of the EU15. The third part examines the impact of the financial crisis on the Greek and Portuguese welfare states, arguing that both countries implemented very similar reforms – especially after Portugal received a bail-out in April 2011 from the European Commission/European Central Bank/International Monetary Fund (EC/ECB/IMF), the so-called troika (that is, one year after the Greek one in May 2010): public sector remuneration and jobs were cut, pensions were significantly curtailed and pension rights significantly restricted, successive tax hikes were implemented and welfare benefits became less generous and more conditional.

It is argued that these reforms constitute a considerable effort towards welfare retrenchment (cf. Pierson 2000; Hemerijck 2002) which is implemented before converging with the more advanced welfare states of the EU15 (for an overview of the weaknesses of the Greek and Portuguese welfare states vis-à-vis those of the EU15 along with a detailed analysis of their efforts to converge with their richer counterparts, see Katrougalos and Lazaridis 2003; Arts and Gelissen 2002; Rhodes 1997). Both countries appeared to be significantly more vulnerable to the crisis than the richer countries of Northern Europe (e.g. Germany, Austria, Sweden, Finland and the Netherlands) and their larger Southern counterparts (Italy and Spain). Yet, the latter had to implement similar measures, albeit in a less abrupt and extensive fashion. In other words, it may be argued that it is not size but whether a country is part of the EU core or of the EU periphery in terms of economic and political power that matters for coping with the effects of the current crisis.

Greek and Portuguese Welfare States: The Poor Relative or a Distinct Model?

Greece and Portugal have similar socio-political backgrounds and welfare systems with common features. The literature on the features of Southern European welfare systems follows mainly three distinct approaches. The first one argues that Southern European welfare states are perceived as the underdeveloped/poor version of Esping-Andersen's (1990) Conservative or

corporatist model (cf. Katrougalos and Lazaridis 2003: 16–30). In contrast, the second approach argues that they share a set of distinctive features, which lead to a unique type of welfare model. Despite the numerous differences between these two schools, both agree that Southern European countries form a distinct group. Yet they disagree on whether their similarities result in a variety of Esping-Andersen's conservative type or a new model (for a detailed discussion of these schools' main propositions, see Arts and Gelissen 2002: 141–6). Lastly, the third approach understands Southern Europe as welfare societies, where social protection is provided by the family and social networks rather than the state (cf. Santos 1994; Marinakou 1998). Despite their differences, all these schools of thought agree on the weakness of the Southern European welfare states, which results in low employment rates, high poverty, high inequality, a strong division between labour market insiders and outsiders, limited redistribution and inefficient welfare spending (cf. Sapir 2006). Unavoidably, this leads to poor provision of effective services and low satisfaction from the 'customers' of the public sector: Greece and Portugal usually achieve the lowest scores in bureaucratic efficiency among the EU15 (Sotiropoulos 2004a; Van de Walle *et al.* 2008).

Furthermore, while neither country was classified by Hall and Soskice (2001: 21) in their original typology of Varieties of Capitalism (VoC), Greece and Portugal were later classified as two cases of a third VoC type called Mixed Market Economies (MMEs) (Molina and Rhodes 2007). The main characteristics of MMEs are (Kornelakis 2011: 55–6): considerable institutional stability combined with low institutional complementarities and clustering and mixed coordination that is both market and non-market. In MMEs the non-market element is provided mainly by the family given the absence of state intervention and the under-developed and inefficient welfare state (Molina and Rhodes 2007). Moreover, both Greece and Portugal can be considered as two countries, where institutional change is unlikely (Hall and Thelen 2009).

Nevertheless, EU entry in the 1980s constituted a turning point for both countries in terms of financial, cognitive and strategic resources (cf. Sotiropoulos 2004b, 2011; Zartaloudis 2011a). More specifically, both countries benefited considerably from EU structural funds (especially from the cohesion fund and the European Social Fund) that were vital to the financing of public services, public works and vocational training (cf. Sotiropoulos 2011; Zartaloudis 2011a). In addition, both countries developed a number of EU-inspired social policies, such as activation through Public Employment Services (Zartaloudis 2013a), gender equality policies (Zartaloudis 2011b) and in the case of Portugal a minimum income scheme (Zartaloudis 2011a). Moreover, in both countries pro-reform governments and actors (e.g. central bankers) used the Maastricht criteria for access to the Economic and Monetary Union (EMU) to help with the management of public finances and the promotion of unpopular reforms – especially labour market and pension reforms – throughout the 1990s and 2000s. This is despite Europeanization being considered as weak (cf. Featherstone 2003, 2005; Carrera *et al.* 2010; Blavoukos and Pagoulatos 2008). Furthermore, for both countries Europe has always been synonymous with higher living standards, a stronger welfare state

and an economic policy which enhances social solidarity (cf. Sotiropoulos 2011; Zartaloudis 2011a). Although this emphasis on Social Europe was common in other southern European countries like Spain and Italy, it is not found in other member states such as the Central and Eastern European Countries (where EU membership is not linked with social Europe but with human rights and protection from Russia), Scandinavian countries (where the EU is either neglected as irrelevant due to its weak social policy or feared as a threat due to the single market and the EMU) or some continental old members such as France (where domestic actors boast that there is no EU influence since their welfare state is the model for the EU and not vice-versa) (cf. the respective chapters of Graziano *et al.* 2011 on the usages of Europe on domestic employment friendly reforms).

Greek and Portuguese Welfare States before the Crisis: Towards Catch-up?

Besides the stabilization of their political systems (cf. Ioakimides 2001; Maravall 1997; Magone 2003), for both countries EU entry meant a path towards catching up with their developed EU partners of the core (cf. Guillen *et al.* 2003; Sakellaropoulos 2007). Although Europe has always been used by domestic actors for upgrading national welfare states (cf. Sotiropoulos 2004b, 2011; Zartaloudis 2011a, 2011b, 2013a), this process remained incomplete and somewhat uneven. In other words, despite considerable improvements in their welfare states, both Greece and Portugal caught up only partially with, and with much less generous provisions than, most EU15 countries. Hence, recent EU discourses blaming profligate southerners who have been living beyond their means (cf. Papadimitriou and Zartaloudis 2014 forthcoming) is only partially supported by empirical reality.

Greece

After the restoration of democracy in 1974, Greece maintained its long-standing model of statism – state intervention in economic and social activities – accompanied by clientelism, which marginalized any autonomous political expression of disadvantaged classes or groups (Diamandouros 1983). Moreover, trade unions were subordinate to political party and the pressure from civil society, the social partners and other societal actors for progressive redistribution was weak (Petmesidou 1991). Nonetheless, until the Greek dictatorship (1967–74), Greece's economic model was based on monetary and fiscal stability (Pagoulatos 2003). After 1974, however, monetary and fiscal stability were largely ignored by the post-dictatorship governments (Pagoulatos 2005). Hence, from 17.6 per cent of gross domestic product (GDP) in 1970, public debt increased to 28.3 per cent in 1981 and reached the level of 112 per cent in 1986 (Ioakimides 2001: 77). Additionally, the 1980s were characterized by government intervention that resulted in minimum wages that were not always in line with changes in productivity or levels of employment, but rather with the political promises and ideological convictions of the Pan-Hellenic Socialist Movement (Greek acronym: PASOK) governments

Table 1

Public deficit as a percentage of GDP

	1981	1988	1995	1997	1999	2000	2007	2009	2010	2011	2012
Greece	-11	-12.8	:	:	:	-3.7	-6.5	-15.8	-10.6	-9.5	-10.0
Portugal	-9.2	-6.1	-5.0	-3.4	-2.7	-2.9	-2.8	-10.1	-9.8	-5.6	-2.9
EU27	:	:	:	-2.7	-1.0	+0.6	-0.9	-6.9	-6.6	-4.4	-4.0
EU17	:	:	-7.2	-2.8	-1.5	-0.1	-0.7	-6.4	-6.2	-4.2	-3.7

Source: 1981 and 1988 data from Eurostat; Dornbusch and Draghi 1990: 2.

(Venieris 2006). This policy, however, had a negative effect on unemployment, which became an acute problem especially among the young and women (Katrougalos and Lazaridis 2003: 59) as the country's competitiveness declined considerably (Venieris 2006).

After the early 1990s, both PASOK and New Democracy (ND) governments implemented a number of privatizations and labour market reforms in order to achieve EMU entry by the late 1990s (cf. Pagoulatos 2005: 360), which trade unions opposed (cf. Featherstone 2003). Moreover, pay rises and generous pensions along with early retirement schemes continued unabated (Tsakalotos 1998: 121). Additionally, Greece had been traditionally plagued by low tax revenues, which had been consistently lower than the EU and the Organisation for Economic Co-operation and Development (OECD) average (Meghir *et al.* 2010: 10–13). The latter is not only related to public sector inefficiency and corruption, but also to the structure of the economy, as the country's unofficial sector is larger than the EU average and self-employment and/or family businesses are more common than in the rest of the EU (Katrougalos and Lazaridis 2003). Despite media coverage of public sector profligacy (cf. Featherstone 2011; Verney 2009), clientelism did not lead to an overstuffed public sector, but one plagued by persistently low efficiency despite gradual improvement during the period 1990–2000 (Afonso *et al.* 2005).

Moreover, Greece was one of few EU countries providing pay rises to public (and private) sector employees until 2008 (cf. Kapsalis 2011). Despite some very minor pension reforms (cf. Featherstone and Papadimitriou 2008), Greece continued to provide generous pensions to public sector employees along with various formulas for early retirement (Tsakalotos 1998: 121). Consequently, public sector personnel outlays (including pensions), despite a temporary slowdown in the mid-1990s, constitute the principal expenditure item in the budget (Papapetrou 2006: 451; OECD 2002). Additionally, although Greece faced a number of Excessive Deficit Procedures, high growth rates and the notorious 'Greek statistics', which systematically under-reported Greek debt and deficits,² allowed Greek governments to avoid electorally painful reforms that required the reduction of public expenditure (see tables 1 and 2).

As a result of the policies discussed above, Greece was plagued with persistently high public debt, deficits and sluggish growth during the 1980s (see

Table 2

Public debt as a percentage of GDP

	1981	1988	1995	2000	2007	2009	2010	2011	2012
Greece	28.8	73.6	97.0	103.4	107.4	129.3	148.3	170.3	156.9
Portugal	37.1	72.2	59.2	48.5	68.3	83.7	94.0	108.3	123.6
EU27	:	:	:	61.9	59.0	74.6	80.0	82.5	85.3
EU17	:	:	:	69.2	66.4	80.0	85.4	87.3	90.6

Source: 1981 and 1988 data from Eurostat; Dornbusch and Draghi 1990: 2.

Table 3

GDP per PPS compared to the EU27 average

	1996	2000	2004	2008	2009	2010	2011	2012
Greece	83	84 ^p	94 ^p	92 ^p	94 ^p	87 ^p	79 ^p	79 ^p
Portugal	77	80	85	83	84	82	82	81
EU17	115	115	113	109	108	108	108	108

Source: Eurostat.

Note: p = provisional value.

Table 4

Unemployment levels

	1995	2000	2007	2009	2010	2011	2012
Greece	:	11.2	8.3	9.5	12.0	17.9	24.5
Portugal	7.2	4.5 ¹	8.9	10.6	11.4	13.4 ²	16.4
EU27	:	8.8	7.2	9.0	9.7	9.7	10.6
EU17	10.5	8.7	7.6	9.6	10.1	10.2	11.4

Source: Eurostat.

Notes: 1 = estimated value; 2 = break in series.

table 5). Nonetheless, when fiscal consolidation was coupled with privatization after the early 1990s in order to achieve EMU entry, growth picked up and until 2007 Greece enjoyed a period of increasing prosperity, with high growth rates, decreasing unemployment rates and rising incomes (tables 3 and 4), which led to a 94 per cent of EU27 average GDP per capita in Purchasing Power Standards (PPS) (see table 3).

Table 5
Growth levels

	1996	2000	2007	2009	2010	2011	2012
Greece	2.4 ^p	3.5 ^p	3.0 ^p	-3.1 ^p	-4.9 ^p	-7.1 ^p	-6.4 ^p
Portugal	3.4	3.9	2.4	-2.9	1.9	-1.6	-3.2
EU27	1.8	3.9	3.2	-4.5	2.1	1.6	-0.4
EU17	:	3.8	3.0	-4.4	2.0	1.5	-0.6

Source: Eurostat.

Note: p = provisional value.

Portugal

Portugal witnessed a similar trend towards welfare expansion after the restoration of its democracy. By March 1975 military and civilian leftists were power and a 'revolutionary' period followed with the nationalization of major sectors of the economy (including banking, insurance, shipbuilding, air and road transport, cement and beer production) and the 'occupation' of the majority of the large farms in the south by their workforce. Although the 1976 elections marked the beginning of a new era of parliamentary democracy, political instability continued until 1986 when Portugal joined the European Community, as from 1975 to 1987 there were frequent changes of government. Unsurprisingly, public policy was very unstable until 1986, as governments tried to reconcile the conflicting objectives of social justice and fiscal stability. After the 1987 elections, coalition governments were replaced by a series of single-party majority governments (Social Democratic Party [Portuguese acronym: PSD]³ governments during 1987–95 and Socialist Party [Portuguese acronym: PS] governments during 1995–2002). The 1987–95 PSD governments – led by Prime Minister (PM) Cavaco Silva – initiated numerous generally successful and popular reforms aimed at encouraging private enterprise and improving public finances, with the help of generous EU funding. For instance, privatizations only became possible after the 1989 constitutional reform. EU accession and the prospect of the completion of the single market were key factors in promoting these changes (Hemerijck *et al.* 2002: 76). As a result of these pro-business measures, foreign investment grew enormously, contributing greatly to economic growth and higher employment. With the exception of a short break in 1992, Portugal witnessed steady economic expansion from 1993 to 2000 (OECD 2001: 10).

After the 1995 elections, PM Guterres headed fairly stable PS governments, which followed policies very similar to those of the PSD governments. For instance, in February 1996 Portugal approved a new privatisation⁴ programme for 1996–97, in which 22 companies were partly or completely privatised (EIU 1996: 13). Despite the PS governments' greater emphasis on social issues – especially on increasing social spending and on educational reform – economic policy throughout the 1990s was largely shaped by the

need to meet the Maastricht criteria (Hemerijck 2002). This bi-party consensus on the objective of early EMU entry facilitated the governments' efforts. While other EU member states' governments faced strong opposition to the austerity programmes that were intended to meet the criteria for EMU accession, protests remained fairly subdued in Portugal. Nonetheless, during 1995–2001 public spending grew on average by 8 per cent every year as thousands of new jobs were created in the public sector, a Guaranteed Minimum Income (GMI) scheme was introduced and hundreds of wider public sector bodies were created (EIU 2002: 19–20). Due to its narrow victory in the 2002 elections, the PSD formed a coalition government with the small Popular Party, a right-of-centre libertarian/conservative party. Although Portugal experienced its steepest economic recession in two decades during 2002–04, the PSD-PP government implemented a severely restrictive budgetary policy. Poor economic growth and relatively high unemployment rates continued throughout the 2000s. PM Sócrates' PS government of 2005–12 implemented a number of cuts and reforms in order to place the country's deficit under control and stimulate growth. However, Portugal did not escape the fate of Greece and requested a bail-out from the troika in April 2011, that is, one year after Greece did so in May 2010.

Welfare State Policy in an Era of Crisis: Abrupt Retrenchment

Greece and Portugal exhibited divergent reform records before the crisis. While Greece maintained a generous expansionary policy until 2008, Portugal implemented a number of cost-containment reforms. However, both countries have implemented very similar welfare reforms since the beginning of the crisis aiming to reduce public spending through a combination of cuts, tax rises and internal devaluation. In other words, both Greece and Portugal had to implement welfare retrenchment before catching up with the more advanced welfare states of the EU15.

Greece

Until 2008, Greece was providing generous pay rises in both the public and the private sector. It was only in March 2009 that the outgoing ND government implemented a pay freeze for public sector employees and pensioners with some concessions for those on low salaries and pensions that were intended to mute the reaction of the trade unions. Thus freezes were applied only to public sector (excluding state-owned corporations) employees earning more than €1,700 (gross) and pensioners receiving more than €1,100 (Tikos 2009). In an attempt to allay the opposition's concerns, the ND government provided some financial compensation (a tax free allowance of €500) for those earning up to €1,500 (gross) and receiving a monthly pension of up to €800. For those earning between €1,501 and €1,700 the allowance was €300 (Tikos 2009). Trade unions reacted angrily to the government's measures and held a mass strike in April 2009. Nonetheless, the government went ahead and

implemented the cuts. These were the last measures aiming to cut public spending until 2010 when Greece requested official support from the troika.

PASOK could not implement any fiscal consolidation measures and/or cuts when it took office, as this would have sharply contradicted its electoral manifesto. On the contrary, it even gave an extraordinary social solidarity benefit to two and a half million low income citizens in 2009 worth €1 billion (Kousta 2009; Express 2009). The dramatic revision of the Greek public finance statistics and the subsequent reform inertia of the Greek government – coupled with Greek and EU officials' public statements about Greece's dire financial situation – led to increasing uncertainty about Greece's membership of the EMU. Reform inertia came to an abrupt end on 15 March 2010 when, in a highly atypical fashion for post-authoritarian Greek politics, the PM announced significant cuts for public sector employees and (public and private sector) pensioners. According to PM George Papandreu, 'Europe' demanded these measures in exchange for its financial support through Eurozone and IMF loans (see Zartaloudis 2013b; Papadimitriou and Zartaloudis 2014 forthcoming).

The troika-Greece deals and the subsequent Memoranda of Understanding (MoUs) entailed the promotion of three main goals:

1. to eliminate fiscal imbalances by achieving fiscal surpluses;
2. to improve competitiveness;
3. to provide liquidity for Greece until its return to the financial markets.

Given the country's large fiscal imbalances when it requested official support (see tables 2 and 3 above), the MoUs initially focused on achieving fiscal consolidation by cutting public sector spending and increasing tax revenues. Greece implemented several rounds of public spending cuts including (cf. Commission of the European Communities 2010b, 2012): the reduction of public investment, a gradual abolishment of the so-called 13th and 14th salaries (Christmas, Easter and summer bonuses) for public sector workers, the establishment of a uniform system of public sector remuneration, the introduction of a pay ceiling for general government employees (starting from approximately €3,000 per month in 2010 and currently set at €1,900), the reduction of allowances by approximately 30 per cent, the introduction of a one per five hiring ratio in the public sector – meaning that only one employee could be hired only for every five who left – and the introduction of a labour reserve scheme whereby approximately 150,000 public sector workers would be fired or forced into early retirement. In November 2012, the newly elected coalition government implemented the latest austerity measures which included *inter alia*: the halving of all remuneration of local government officials, the further reduction of allowances for all public sector employees, the reduction of pay for all high-level bureaucrats and political personnel, the inclusion of more employees of the wider public sector in the common remuneration system and the further reduction of public sector employees paid via special arrangements (e.g. the judiciary and the army).

In addition, a series of pension cuts were implemented for all (public and private) pensioners: the 13th and 14th pensions were gradually abolished for

pensioners earning over €2,500 monthly and those below 60 years of age, all pension entitlements were frozen until 2014, pensioners earning more than €1,400 would pay an additional tax (constituting between 3 per cent to 9 per cent of their remuneration), the retirement age was increased to 67 years of age for all employees, many occupational funds providing more favourable conditions were merged with the main social security fund of the private sector – thus transforming the Bismarkian Greek pension system to a multi-pillar pension system with separate contributory and non-contributory elements (Matsaganis 2011). Moreover, in November 2012 most pensioners lost a great amount (25 per cent to 50 per cent on average) of the lump sum payment they received when they retired, and a regressive reduction of pension remuneration was implemented (5 per cent cut for pensions from €1,000 to €1,500 up to 25 per cent for pensions above €4,000).

The above cuts were combined with a series of tax rises. More specifically, in the first year of the MoU a number of indirect taxes were introduced along with the steep rise in Value Added Tax (VAT). Additionally, Greece gradually harmonized its ceiling for taxable income with the EU average as it had the most generous scheme (€12,000) in the OECD (Garello 2012). Moreover, all Greeks earning above a certain income had to pay an extra tax called Social Solidarity Tax, which would finance a cash benefit for the poorest Greeks. Furthermore, all home owners had to pay an additional property tax. Another key aspect of all MoUs was the reform of the tax collection system through a reduction of the number of agencies responsible for tax collection, the reduction of staff numbers and bureaucratic processes along with the modernization of the tax collection system. The latter aspect still remains to be seen in Greece and has proven to be the most difficult to implement (cf. Commission of the European Communities 2010b, 2012).

With regard to increasing competitiveness, Greece had to reduce its labour costs as it had previously given frequent pay rises above productivity since the early 1980s. For this purpose, Greek governments introduced a series of pay freezes in the private sector as well as a new framework of lower minimum salaries and lower pay levels than the national minimum for young workers. Furthermore, a series of labour market reforms were implemented aiming to promote flexibility of employment relations by allowing collective agreements at the local, sectoral and company levels even if their provisions are less favourable than those of the national-level agreements. A major change was also introduced in the setting of the national minimum wage through the latest austerity package (Law 4093/12 of November 2012) whereby the minimum wage will not be determined through collective bargaining between social partners but through governmental decrees after consultation with the social partners (cf. Lampousaki 2013).

Another key element of the MoUs was a requirement linked with a number of EU directives regarding the opening up of the so-called closed professions, as in Greece most professions (e.g. lawyers, pharmacists, taxi drivers and engineers) were heavily regulated with restrictions on entry, operation and service fees. Greece also had to implement a series of privatizations. However, little progress has been observed on this front thus far while the prospect of a

mass privatization programme has attracted fierce resistance from trade unions and opposition parties (cf. Zartaloudis 2013b).

Portugal

Contrary to Greece, Portugal embarked on welfare retrenchment in the early 2000s. More specifically, after 2002, PM Barroso's centre-right government implemented numerous cost-cutting measures: it closed 30 public organizations, froze the hiring of permanent public sector employees, froze pay rises for salaries above €1,000, announced that no temporary employment contracts in the public sector would be renewed (a measure that resulted in up to 50,000 redundancies), implemented a reorganization of existing public sector staff by allowing the horizontal interdepartmental transfer of employees and introduced – but failed to actually implement – an entirely new system of promotions based on individual performance evaluations (known as Integrated System of Performance Evaluation/SIADAP) (Stoleroff 2007; Lima 2008).

During 2005–09, the PS government enacted a series of harsh austerity measures, including tax increases and wide-ranging public administration reforms. The government targeted especially public-sector employees in order to meet its medium term stability programme projections of a gradual decrease of the general government deficit from 4.6 per cent of GDP in 2006 to 3.7 per cent in 2007 and 3 per cent in 2008. In a dramatic U-turn from its electoral promises of fiscal expansion, the PS government maintained the salary freeze for those earning more than €1,000 and also implemented a freeze on promotions and career advancement, raised fees and related charges for public services and increased the retirement age along with reducing pensions for public sector employees (EIU 2006: 6–7; Stoleroff 2007). Moreover, the PS government fully implemented the SIADAP system for public sector employees and closed 187 'overlapping' public entities (Lima and Naumann 2006). In 2008, the PS government was reported to have maintained the goal of making redundant around 75,000 public sector employees, even though the share of public employment in the overall workforce in Portugal was below the EU average. The PS justified this by emphasizing the higher than the EU average public sector personnel costs (14.6 per cent of GDP in Portugal, over 12 per cent at the EU) (Lima 2008). Lastly, the PS government transformed employment relationships for the employees in the police, the army and the judiciary by converting their contractual status into individual employment contracts. This meant that public sector employees could be easily transferred or fired due to poor performance and, hence, they were almost equated with private sector employees (Stoleroff 2007).

Despite increasing uncertainty in global financial markets due to the financial crisis, which began in 2006 when a number of small financial firms providing high-risk sub-prime mortgages collapsed and peaked with the collapse of the US investment bank Lehman Brothers in 2008 (cf. Eichengreen *et al.* 2012), Portugal provided a 2.9 per cent pay rise for all public sector workers in 2009. This measure contradicted the PS government's policy of wage moderation, which had been implemented since it took office in 2005. Although the government argued that the main reason for this U-turn was the

country's solid public finances, it appears that this one-off pay rise was related to the national, European and local elections of 2009. Tellingly, in 2010, despite the fierce opposition of the trade unions, the government implemented a pay freeze for public sector employees (maximum pay rise of 0.8 per cent in accordance with the inflation rate) (Lima 2010a). In addition, the government imposed stricter financial penalties for early retirement by increasing the annual cut of 4.5 per cent for each year before the legal age of retirement to 6 per cent (Lima 2010a). These measures sparked a series of trade union strikes and protests which, nonetheless, did not deter the government from enforcing the reforms (Lima 2010b). The next wave of cuts was implemented in May 2010, which brought an end to the measures implemented one year earlier by the PS government, such as more training and employment subsidies and extension of unemployment benefits to tackle the negative effects of the economic crisis (cf. Lima 2009, 2010c). Despite the fact that they were ferociously opposed by the trade unions, these measures were co-decided with the leader of the PSD Passos Coelho (Lima 2010b, 2010d).

In September 2010, the government introduced additional 'emergency' austerity measures as a result of continued market pressure and consecutive downgrades by major credit rating agencies. The PS minority government proposed the following measures for the 2011 state budget (Lima 2010c): an overall 5 per cent cut in core and wider public sector remuneration expenses resulting from a 3.5 per cent to 10 per cent cut to salaries over €1,500 per month and a freeze on all promotions, lower spending on pensions, allowances and social benefits and a freeze on public sector investment. The proposals also included public sector restructuring, which could result in redundancies and privatization of public corporations (cf. Lima 2011a).

In March 2011, in an attempt to avoid recourse to external financial assistance, the PS government proposed another austerity package (the fourth within a year) which included a series of cuts in welfare and health budgets along with a pension freeze. However, the Parliament rejected the bill and PM Sócrates was forced to resign. By May 2011, Portugal was following Greece and Ireland on the deeply unpopular path of requesting financial assistance from the troika. In October 2011, the PSD-PP government introduced an additional austerity plan for the 2012 budget, described by PM Coelho as 'the most difficult to close and implement in living memory' (Lima 2011b). The plan included the suspension of the 13th and 14th salary bonuses for public sector employees and pensioners earning over €1,000 a month for the duration of Portugal's bailout programme, while those earning between €485 and €1,000 a month would have one of their bonus salaries cut. According to some estimates, during 2010–11 public sector employees lost approximately 20 per cent of their income, with more losses for the high-paid staff (Lima 2011b). Beyond cuts in public sector remuneration, the budget included a series of extensive cuts in education, healthcare, social protection and public investment. It should be stressed that both measures (50 per cent cut on Christmas bonus for 2011 and the suspension of the Christmas and holiday bonuses afterwards) went beyond the troika's

requests, as the government promised during its electoral campaign that it would go much further than the MoU required it to (Lima 2011b). According to PM Coelho these measures were necessary because Portugal had to implement additional measures worth €3 billion to meet its budget deficit reduction goal for 2011.

The next wave of cuts was introduced by the 2013 budget which was passed on 27 November 2012. The latter abolished the holiday bonus of an extra salary for public sector employees while public sector pensioners were to receive only 10 per cent of it. In addition, 50,000 public sector jobs were to be cut (Lima 2013a). However, after the Constitutional Court rejected key cuts on grounds of fairness,⁵ the government increased the working hours of public servants from 35 to 40 on grounds of fairness, proposed the merging of their various supplementary bonuses into a single system, increased their health-care contributions by one per cent and reduced their annual leave from 25 to 22 days (Lima 2013b). In addition, it introduced stricter penalties for early retirees and cut the budgets of the Ministries of Education and of Social Security by €325 million and €299 million respectively.

As was the case in Greece, the above cuts were combined with a series of tax rises. In September 2010, the PS government increased VAT from 21 to 23 per cent. On 14 July 2011, barely a month after its election, a new PSD-PP government proposed an extraordinary tax of 50 per cent on any amount over the obligatory minimum wage of €485 in the Christmas bonus for all employees, pensioners and the self-employed. While employees and pensioners would have their bonus cut, the self-employed would have to pay an extra tax levy for the year 2011 (Lima 2011c). The next significant tax rise was included in the 2013 budget which was passed on 27 November 2012 and redefined the personal income tax rate bands and introduced an extra 3.5 per cent levy on all categories for the year 2013. These measures increased direct income taxation by 30 per cent on average. The most severely affected were the low-income earners who saw taxation of their earnings almost double as they were included in a new higher tax band (Lima 2013a). Moreover, the budget abolished numerous personal tax exemptions and introduced an additional 'extraordinary solidarity tax' of 3.5 per cent to 10 per cent on pensions above €1,350 a month (Lima 2013a). After the Constitutional Court rejected the latter measure (see also above), the government replaced it with a tax on all pensioners in order to ensure that the measure would not be judged unconstitutional (Lima 2013b).

As was the case in Greece, the MoU required Portugal to reduce its labour costs in order to boost its competitiveness. As a result, in November 2011 the PSD-PP government reached an agreement with the social partners to reduce severance pay for workers from 30 days to 20 days per year (Lima 2012a, 2012b). Moreover, the government extended normal working hours for all employees by two hours per day in order to cut overtime costs. As was the case in Greece, Portugal pushed for more firm-level collective agreements and even individual agreements between employers and employees. In addition, it abolished four public holidays and extended the concepts of unsuitability and extinction of work positions to facilitate individual dismissals (Lima 2012b).

Conclusion

The recent financial crisis posed an immense challenge for Greek and Portuguese public finances. Both countries implemented a series of reforms aiming towards welfare retrenchment (cf. Pierson 2000; Hemerijck 2002): public sector remuneration and jobs were cut, pensions were significantly curtailed and pension rights significantly restricted, successive tax hikes were implemented, welfare benefits became less generous and more conditional. Despite the better state of Portugal's public finances, both countries have so far implemented similar cuts. Nevertheless, Greece had to implement these cuts much earlier than Portugal. In addition, both countries are also plagued with high unemployment, recession and a seemingly endless process of decreasing living standards. It can, therefore, be argued that Greece and Portugal have entered a period of welfare retrenchment before being able to converge in terms of welfare provision with the core of EU15 (cf. Katrougalos and Lazaridis 2003). Tellingly, for both countries, EU and euro membership have been two celebrated achievements that were associated with an improvement in living and social standards and a Europeanization of their welfare states whereby the Greek and Portuguese people could enjoy similar social rights to the citizens of richer EU countries. Alas, both achievements are increasingly becoming associated with austerity – something unprecedented for both countries (cf. Sotiropoulos 2011; Zartaloudis 2011a).

Moreover, both countries appear to have been significantly more vulnerable to the crisis than the richer countries of Northern Europe (e.g. Germany, Austria, Sweden, Finland and the Netherlands) and their larger Southern counterparts (Italy and Spain). Yet, the latter had to implement similar measures, albeit in a less abrupt and extensive fashion. In other words, it may be argued that it is not size but whether a country is part of the EU core or of the EU periphery in terms of economic and political power that matters for coping with the effects of the current crisis. The fact that three out of four cohesion countries have been ousted from financial markets and they have required EU/IMF support raises complicated and unsettling questions about the ability of the EU to achieve convergence between rich and poor countries and renders its future direction uncertain (cf. Krugman 2011). Additionally, it demonstrates the multi-faceted failure of markets, national governments, and EU institutions to anticipate and deal with the crisis (Tsoukalis 2011: 26–8; Papadimitriou and Zartaloudis 2014 forthcoming). It remains to be seen whether the (painful and unpopular) reforms discussed in this article will help in overcoming the crisis or whether Europe's southern periphery will face more hardship in the future.

Acknowledgements

I would like thank Dr Richard Parry, Dr Waltraud Schelkle and Dr Kyriakos Moumoutzis for their support and advice when writing this article. I am also grateful to the reviewers for their insightful and helpful comments. Funding from the European Commission FP6 (Reconciling Work and Welfare in Europe' (RECWOWE) Research Network of Excellence – Contract No.

028339-2, 2006–2011), the Propondis and Bodossaki Foundations and the London School of Economics is gratefully acknowledged. Any errors are the author's responsibility.

Notes

1. EU15 is the group of countries belonging to the EU before the 2004 enlargement – namely: Germany, France, Italy, the Netherlands, Luxembourg, Belgium, the UK, Ireland, Denmark, Greece, Spain, Portugal, Austria, Sweden and Finland.
2. After a long period in which Greece was under the Excessive Deficit Procedure for its public deficit, Eurostat (Commission of the European Communities 2010a) published a damning report in which it stated that Greece remains the only country in the Eurozone that fails to provide the basic statistics necessary for the EMU, thus failing to meet the most fundamental – and at the same time basic – EU requirement for EMU.
3. Contrary to its name and the political tradition in all European countries, PSD is a centre right party.
4. Although privatization has also been driven by a broad political commitment to free enterprise and competition, EU-level liberalization measures have also been a key driver in this process (EIU 2002: 23).
5. The court argued that cutting the holiday bonus only for public sector employees was unconstitutional as the government targeted only one group of employees and not all Portuguese workers since the holiday bonus for private sector employees was not affected. The court also found the extension of the cut to pensioners unconstitutional and rejected the special levy on sickness allowance and unemployment benefit (Lima 2013b).

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