Contraditório think-tank

Briefing

Portugal's exit strategy | Luís Faria

We were told that good times don't last forever. But nowadays in Portugal people are questioning if the same applies to bad ones. After a lost decade of sluggish growth Portugal badly needs a fiscal consolidation strategy based on credible reforms that would boost productivity and promote robust growth. Since the late 90's Portugal has accumulated a blend of growth unfriendly policies: a procyclical fiscal policy and profligacy in public expenditures, one of the most regulated economies of the OECD, excessive taxation, a rigid labour market and an economic development based on low skilled work force. This set of policies has hampered the country's competitiveness and Portugal has successively missed the opportunity to overcome the causes of Portugal's anaemic growth instead of its symptoms. The scenario reveals cheerless future perspectives but it doesn't have to be necessarily so. What are the reforms that Portugal could implement in order to credibly and decisively leave behind a decade of growth rates below 1% on average?

The rigidity of labour market created a two-tier labour market with protected jobs for some and insecure jobs or unemployment for the rest, the latter mainly affecting the youngest and the least educated. Portugal has one of the most protective labour market regulations, but paradoxically is one of the EU countries where workers most feel insecure about losing their jobs. A more flexible labour market would mitigate this highly segmented market. Portugal has an unemployment rate of 11% and one of the highest long-term unemployment rates in the EU: 4.3% of total active population is unemployed for 12 or more months. A feeble economy and paltry job creation leaves a narrow scope for measures aimed at promoting higher labour mobility. However, increasing social benefits policy efficiency and implementing effective training policies would not necessarily put at risk fiscal consolidation.

The gloomy scenario of education results in Portugal is worrying. According to last available data, Portugal exhibits one of the highest percentage rate of the population aged 18 to 24 not in education or training within the EU (31.2% in 2009) and only 29.9% of total population aged 25 to 64 had completed at least upper secondary education in 2009. Studies in economics of education demonstrate the critical impact of teaching quality in students' results. Nonetheless, all the attempted reforms to implement a new teacher's evaluation regime have so far faced a hefty resistance from powerful unions on the streets or opposition parties at the parliament. To address its education system deficiencies Portugal should urgently improve teaching quality and give schools and families more autonomy and freedom to choose.

Portugal must decisively promote strong competition policies that would bring positive and significant impacts to the Portuguese economy. That would enhance the necessary adjustment to a more competitive international environment and would substantially increase income and employment levels. Moreover, regulatory and administrative burden constitutes a huge hindrance to the entry of innovative newcomers in the market, foreign direct investment inflows and efficiency gains. It is also crucial to remove government special voting rights in private business activities and eliminate administered prices in services. A more competitive tax policy would also contribute to boost growth. Nevertheless, it would simultaneously inflame Germany and France accusations of "fiscal dumping", but for some reason Ireland vehemently rejected the idea of raising its corporate-tax rate. However, a more competitive tax policy complemented by inevitable government expense cuts wouldn't put fiscal consolidation at risk, as common sense may suggest. Countries with low corporate-tax rate yield proportionally bigger revenues than most other countries. There are few alternatives left, if any, for Portugal to boost its competitiveness.

At a time when political campaign already erupted in Portugal, some voices started preaching the virtues of some particular sectors or clusters as if they were the holy grail. New practices should emerge by trial and error, by private and non-profit sectors that must commit to ongoing experimentation and facing the harshness of a free market, not by a set of prescriptions defined by bureaucrats. In countries with poor practices and misconceived programs, such ideas can easily become a white elephant. It is time to stop poorly conceived projects based on popular ideas that only help fattening opportunists. However, Portugal's next government should assume its responsibility encouraging innovation. How? If Portugal wants to promote best practices and robust growth, the role of the government should be to remain sector neutral and to unleash entrepreneurial energies instead of protecting "national champions" and prophetic ideas with taxpayers' money. Government should get out of the way by reducing red tape and market barriers, to look out for market distortions and over-regulation that can be stripped away. Entrepreneurial activity should be encouraged by removing obstacles across the board and not by tempting centralized industrial planning. Portugal's next government urgently needs to change this deeply entrenched culture. That is an extremely difficult task, but countries like Chile and Ireland achieved it in less than a generation. Portugal is no different.

Portugal needs to create the environment to promote long-term growth and to decisively keep the murky perspectives off Portugal's outlook. Structural reforms and pro-growth policies would constitute a big leap forward in that direction. Hopefully, when the time comes Portugal will still have risk-takers who know what world they're living in.

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