Portugal's Soares welcomes IMF austerity demands

by Mary Goldstein

Portugal, under the government of Socialist Party Prime Minister Mario Soares, has become the first OECD country to accept IMF shock treatment as the price for loans to repay its foreign debt. The accord, reached with the IMF in early August after three weeks of negotiation, carries conditionalities on a par with those demanded of Brazil, Mexico, or Argentina.

But unlike the big Ibero-American debtors, who are moving steadily toward formation of a debtors' cartel to jointly confront the IMF, the Soares government welcomed the IMF with open arms. In fact, Mario Soares's campaign platform in last spring's elections was austerity, austerity, and more austerity. Immediately after the elections, his government announced a stiff austerity plan in line with what the IMF would require for its $480 million, three-tranche standby credit. Portuguese negotiators were nonetheless reportedly surprised when the IMF announced that the Soares plan was not rigorous enough.

Portugal's foreign debt reached $14.2 billion in April, a whopping 58 percent of GDP (gross domestic product), one of the highest ratios in the world. Its debt service ratio is 27 percent. The country's financing needs this year are high; 28 percent of total foreign debt is short-term and matures this year. This means principal payments of $1.3 billion, and $1.4 billion in interest payments due over the next five months. The country has been shut out of international credit markets since at least the beginning of this year, able to raise only $700 million in short-term credits from the Bank for International Settlements (BIS), using its gold reserves as collateral. Last March, Portugal was forced to sell 30 tons of gold to repay the BIS.

Shock therapy

The program laid out by the IMF is literal shock therapy. The foreign debt must be held to $14.6 billion this year, and to $16 billion in 1984. Balance of payments deficit of current account, which reached $4.6 billion in 1982, must be cut to $2 billion this year, and further reduced to $1.25 billion in 1984. The budget deficit, 12 percent of GDP in 1982, must be reduced to 8 percent of GDP this year and 6.5 percent in 1984 (the IMF demanded 6 percent for 1984, but Portugal resisted on this point). Against a 3 percent growth rate in 1982, the IMF requires *negative* 1 percent growth in 1984; the Soares government had projected 0 percent growth. Real wages will be cut by 4 percent.

Portuguese negotiators have good reason to be nervous. The IMF program is a prescription for social upheaval in Portugal, a country with massive unemployment and a low standard of living, whose major union federation is controlled by the Portuguese Communist Party.

Portuguese Finance Minister Ernani Lopes quickly went into action following the IMF accord. He declared an immediate 2 percent increase in interest rates on deposits and a 2.5 percent increase on interest rates on loans. Rates for 90-day loans have now hit 29.5 percent, while five-year loans carry rates of 32.5 percent. Inflation is currently estimated at 20 percent annual rate. Lopes further announced new direct and indirect taxes for this year, and a continuation of the 1 percent monthly "crawling peg" devaluations. These latest measures follow big cuts in subsidies and price hikes of more than 20 percent on fertilizers, milk, bread, and sugar carried out last June, as well as hefty price increases for petrol, utilities, and public transport.

The biggest "shock" will be felt in the public sector. Last June, before the IMF deal, the government froze planned investments of $1 billion, subject to review by a "permanent working group." Ernani Lopes told northern businessmen in early August that the government will make no new investments, and that programmed investments will be cut in part or totally, meaning a halt to projects already underway. "We will try to avoid it," he said, "but it's possible that we may have to do it."

The large and inefficient state sector, the SEE—Sector Empresarial del Estado—which employs some 209,000 workers, will be sharply cut back and large sections put up for "reprivatization." The SEE "excess workforce" is estimated at 50-100,000, a full 25-50 percent. Unemployment in Portugal is already extremely high: 1 million of an active population of 4.5 million, about 25 percent, are unemployed or underemployed.

To facilitate mass layoffs, the government is preparing a "lay-off law," which would allow job cuts by companies in severe economic straits. Under present law, workers cannot be fired or laid off. Under the new law, workers could be laid off for up to two years, during which they could receive up to 60 percent of their salary and their normal "welfare" benefits; during this time, they cannot take another job, or they will be "fired" and lose all benefits. The company is responsible for meeting the 60 percent payment (defined as minimally minimum wage, maximally three times minimum wage), but the government will cut the cost in half if necessary.