Executive summary

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DECENT WORK IN PORTUGAL 2008–18

From crisis to recovery

Executive summary

This report has been prepared following consultations with the Ministry of Labour, Solidarity and Social Security (MTSSS) of Portugal with the objective of reviewing the country's economic and labour market situation since 2008 and examining future prospects. It follows a previous ILO report, *Tackling the Jobs Crisis in Portugal,* prepared in 2013, and updates its findings and recommendations in view of the recent developments in Portugal and the European Union until the end of 2017.

The report highlights three distinctive features that helped Portugal through a tough adjustment process, and towards swift economic and labour market recovery

Following the financial and sovereign debt crises, Portugal went through a difficult process of adjustment and recovery common to other economies in the Eurozone. The implications for the labour market were severe. It took almost ten years to restore a consistent period of economic growth and reach employment levels approaching those prevailing before the global financial crisis.

First, the country was already on its own adjustment path before the crisis. A series of policies had gradually been implemented that helped fostering business restructuring towards the tradable sectors, including measures to reform the public sector, enhance the quality of infrastructure, support integration in global production chains, rapidly increase the education attainment of citizens and reform the training system. As external economic and financial conditions improved, the economy was ready to restart.

Second, the Portuguese experience does not support the conventional notion that adjustment can be accelerated and international competitiveness rapidly regained simply by means of reducing labour costs and making the labour market more flexible. More effective in the case of Portugal appear to have been broader measures to improve the business environment, ensure access to credit, improve the capability of the public administration, fine-tune tax and fiscal incentives, actively and wisely manage the public budget, and the preservation of the level of minimum wages, thus avoiding a sudden drop in domestic demand.

Third, while the scope of reforms and the fiscal targets of the financial assistance programme in 2011–14 were determined externally, the successive policy packages were discussed and adopted at national level, with the engagement of the social partners. This was a factor behind success in the most recent years. For one, it contributed to addressing the attention to the social costs of fiscal consolidation and the importance of supporting incomes and wages to boost economic growth. It is the view of this report that social dialogue – though not always resulting in unanimous consensus– was a primary vehicle to tailor policy changes to the needs and circumstances of the country and ensure buy-in.

The effective application of relevant International Labour Standards has also contributed to the achievement of the primary objective of the various policy initiatives reviewed by this report, which were aimed at combining the pursuit of sound macroeconomic goals and fiscal consolidation with the creation and protection of decent jobs, while addressing the needs of the most vulnerable.

Portugal has progressively regained financial and fiscal stability. But in spite of economic and employment recovery, there remain concerns about the quality of jobs generated and the need to further strengthen the production base to enhance external resilience. The two objectives are not incompatible. As suggested in the ILO report on Portugal presented in 2013, a coherent policy mix that focuses on decent work can help unlock a virtuous circle of improved social cohesion, productive upgrading and the generation of decent jobs.

Key findings and policy considerations

A solid economic recovery is underpinned by thriving exports, shrinking debt and improved access to finance

Ten years since the burst of the global financial crisis, the country's economic recovery is on solid ground, as reflected by sound GDP growth and a return of employment to pre-crisis levels. A consistent pattern of economic growth has been restored; exports are thriving and the country has regained access to the international financial market; external debt is gradually being reduced; private sector investments are gradually picking up; and some fiscal space is opening up that could be used parsimoniously to address bottlenecks to economic growth and to sustain social cohesion.

Overall, the rebound of the economy has benefitted from the relative diversification of exports that have been a main driver for the recent growth, as well as gains in the efficiency of public expenditure and changes in business regulations.

Income support and other demand-driving measures can fuel more GDP growth

There has also been a policy shift to a more accommodative fiscal stance, in the effort to maintain a balance between, on the one hand, a credible commitment to fiscal consolidation and gradual public debt reduction and, on the other hand, the need to support incomes, domestic demand, job-rich recovery and investment. Significant growth in 2016–18 is benefitting from some pick-up in domestic demand and especially investment – a welcome development that would fuel further increases in GDP.

External and domestic developments have contributed to boosting labour demand. Labour supply has been in a good position to capitalize on the new employment opportunities. Educational attainment of the Portuguese has increased significantly over the course of the last decade, and there are almost as many women as men in the labour force. The result has been a significant increase in employment that has recovered lost ground reaching 4.8 million by end-2017, while the number of unemployed has declined to levels last seen in 2003.

Despite rising employment, job quality and wages remain low

There remain however concerns with the quality of jobs. Labour market segmentation is widespread, with large numbers of temporary jobs. Stable and secure jobs are especially rationed for the younger cohorts, in spite of their growing educational attainments. Wages have remained nearly stagnant in real terms and are low relative to EU averages, although consistent increases in the minimum wage have contributed to a slight decline in inequality.

Areas that would require attention in the future include the level of gross fixed capital formation. The availability of credit has started increasing and the cost of credit has been decreasing as interest rates for non-financial firms have been reduced. Business credit in 2017 grew for the first time since 2011, but most firms still appear hesitant to borrow for investment purposes.

Future efforts should amplify Portugal's competitive edge and explore space for fiscal expansion

Some need for fiscal prudence remains, to ensure that public debt follows a downward trend over the medium and long run. Over-reacting financial markets might lead to higher yields on Portuguese debt, should conditions for a turbulent re-pricing of risk in the Eurozone arise again.

The road ahead rests on strengthening the country's competitive position, while ensuring opportunities for secure and well-remunerated jobs for all, backed by adequate social protection measures. In the short run, any space for fiscal expansion should be explored. Attempts to reduce the external debt should not compromise public investment, whose rate was 1.8 per cent of GDP in 2017 – a low level by historical standards. Public spending for investment could help crowd in private productive investment.

Aligning wages to productivity gains could broaden the recovery, but investments and diversification are also key

In addition, the conditions for collective bargaining should be fully restored in order to adjust wages after years of stagnation and align them to long-term growth in productivity. This might stimulate domestic demand and broaden the recovery. It might have an impact on price competitiveness of Portuguese exports, if productivity gains are ignored, but its effects could be absorbed as shown by the experience of the past decade. Portugal should not lock itself into price competition with new EU entrants and Asia. Wage pressures might indeed provide an incentive for firms to invest in technical progress and innovation. This is particularly relevant for Portugal, which suffers from a low level of capital per worker compared to other European economies.

As suggested in the ILO report in 2013, investment promotion, reforms in the business environment and financial support measures should be couched in a focused growth strategy aiming at diversifying, innovating and getting closer to the technological frontier in medium-high tech goods and services in higher value-added markets, such as ICT, upgraded tourism, agricultural niches and greener industries. Public and private efforts should continue to be combined to improve financial support to enterprises, as well skills development, business support services, promotion of clusters and value chain upgrading.

The case of Portugal suggests that EU macroeconomic policy should move beyond a one-size-fits-all approach

Developments in the Eurozone significantly affect trends in the country. The adjustment experience of Portugal offers ground to reflect on ways the European Union could in the future better shelter its members from financial and economic storms, e.g. by calibrating EU monetary policy to the needs of all countries, by broadening the scope of financial stabilization instruments, and by revising the conditionality attached to those instruments, especially as it concerns changes in labour market regulations.

MoU-induced employment protection reforms were unnecessary in a labour market with sufficient flexibility and already-high rates of temporary contract work

Portugal adopted several employment protection legislation (EPL) reforms in line with the Memorandum of Understanding (MoU) signed in 2011 between the Portuguese Government and its international partners.[1] These reforms were also reiterated in a tripartite agreement in January 2012.[2] An explicit goal of the reforms was "to tackle labour market segmentation, foster job creation, and ease the transition of workers across occupations, firms, and sectors".

The list of the reforms prescribed by the MoU concerned the alignment of severance payments of open-ended contracts with those of fixed-term contracts; general reduction of severance payments; and altering valid grounds for dismissals. In addition, several other measures were undertaken,

1. The European Commission (EC), the European Central Bank (ECB) and the International Monetary Fund (IMF).
2. Not all trade unions signed the agreement.

including transitory additional renewals of temporary contracts, a decrease of the end-of-contract indemnity, and extension of the total duration of very short-term contracts.

Contractual labour market segmentation has been a long-standing feature of the Portuguese labour market. Temporary contracts disproportionately affect younger workers (15–24) and their use has risen from less than 40 per cent in 2000 to more than 60 per cent by the early 2010s for this age group, where the figure has remained since. This has in part contributed to the near-5 per cent increase in the share of temporary contracts in total wage employment in the last 20 years. In most cases – and in contrast with other countries – temporary contracts are largely involuntary.

At the onset of the latest global economic recession, the legal framework favoured the use of temporary contracts, a situation that was reinforced by the reforms introduced between 2011 and 2013. Further ease of the use of temporary contracts was accompanied by a decrease of employment protection for permanent workers without leading to a change in the share of temporary workers among employees. Thus, adjustment reforms reduced protections without benefit to employment or the labour market.

Segmentation continues to raise both equity and efficiency concerns. The equity concerns stem from the fact that workers in different contracts face different working conditions, including penalties in terms of earnings, skill development, and prospects for temporary workers. Efficiency is also compromised, because temporary workers receive lower on-the-job training, and their high turnover does not favour skill and in-house knowledge accumulation, thus reducing overall productivity.

Future policies should include incentives to convert temporary contracts to permanent ones and ensure equality of treatment across contracts

While recognizing the validity of recent efforts, further policy measures to deal with labour market segmentation should aim at addressing its three key features: the high share of (involuntary) temporary employment; low transitions to permanent contracts; and unequal working conditions across contracts. Such measures can include placing stricter limits on the use of temporary contracts and ensuring compliance with such regulations. The tripartite agreement for the labour law amendments reached at the time of writing this report, and approved by the Parliament, takes steps in this direction. Enterprises can be encouraged to convert temporary contracts into permanent ones through various incentives, including in the area of training to be provided to temporary workers. Measures should also ensure equality of treatment and working conditions, eliminate incentives to use temporary contracts with the single aim of saving on labour costs, provide enough tools to enterprises to ensure internal rather than external flexibility, and stimulate responses through social dialogue that include temporary workers.

After deregulatory amendments, working hours – already high by EU standards – increased without improving employment opportunities

The regulation of working hours, working time arrangements, rest periods and holidays has been a central issue in the legal amendments that have taken place since 2008. This includes the reforms introduced during the adjustment period, whose aim was to increase working hour flexibility to improve employment opportunities and the economy overall. The experience of Portugal, however, provides little evidence that this deregulation worked. This may be in part due to the fact that the country's Labour Code already provided employers and workers with working time flexibility.

The amendments introduced under the MoU covered the expansion of flexible working time arrangements – including time banking, the reduction of overtime pay by 50 per cent and the elimination of compensatory rest periods for overtime hours. They were accompanied by a tripartite social dialogue agreement in 2012 that included the elimination of four national holidays and the elimination of extra annual holiday time ("bridge days"). Subsequently, some amendments were challenged in the Constitutional Court, which emphasized they could not be imposed on collective agreements in force without breaching the fundamental right to collective bargaining, therefore leaving some more favourable clauses from collective agreements in force.

With lower overtime pay and stagnant wages, these longer hours often mean more work for less money

Average numbers of usual weekly working hours increased on average by one hour – between 2009 and 2016 – and more so for women – even though Portugal already stood in the top quarter within the EU. The share of workers working overtime also increased and continues to rise. After a sharp increase, time-related under-employment started to decline as from 2015, with a declining share of part-timers who would prefer to work full time. This would suggest that there has been some improvement in options for employees working part-time hours. However, the increase in hours and the stagnation of monthly wages effectively reduced the hourly pay of workers.

Regulating working time in concert with wages and other aspects of employment may help workers and employers achieve optimal flexibility

The decision of the courts on the interplay between reforms and collective agreements implies that the best way forward is to articulate policies through social dialogue. While some of the reforms are still in force, others have recently been changed or reverted back to their pre-crisis formulation (e.g. the reintroduction of four public holidays, and discussions for time banking to be again subject to collective bargaining). More generally, working time should be seen as one of the elements of employment and should be regulated in conjunction with other aspects of employment, including wages, which in their totality can contribute the necessary flexibility desired by both workers and employers. Enforcement of any regulatory measures will be crucial to both workers and employers, while collective bargaining can also play a central role.

These considerations are particularly important in view of unfolding policy debates around the future of work and the impact of technology on workers and employers. The recent regulatory initiative in telework places Portugal at the vanguard of countries recognizing the need to balance the positive and negative impacts that technology can have on workers and employers. The recent resolution by the Portuguese Parliament on “on-call” work, with implications for the “right to disconnect”, could be an important measure to help facilitate work-life balance for workers.

Labour inspections fell as adjustment reforms reduced resources while making labour laws more complex

Labour law enforcement in Portugal falls under the mandate of a single institution, the Authority for Working Conditions (ACT), under the Ministry of Labour, Solidarity and Security. The Labour Code of 2009 and its successive amendments that introduced flexibility related to contractual forms, organization of work and enlarged liability schemes also increased the legal complexity for enforcement mechanisms. Many of the new legal institutes required stronger efforts to build legal cases, thereby slowing the enforcement capacity of ACT.

The reforms under the adjustment programme further increased the complexity of labour law, while decreasing inspection resources (e.g. pay cuts, a freeze on career progression and a reduced number inspectors). The result – lower staff motivation and a reduced capacity of ACT to effectively play its role of regulator, as ACT is forced to focus increasingly on individual requests with a limited effect on the regulated environment.

From 2011 to 2014 the number of inspections dropped significantly, as did the rate of proactive inspections and the number of legal and technical advice given by ACT. Part of this drop is explained by a change in the methodology used to register inspections, but it is also the result of the tough fiscal consolidation choices the Government chose to make. The efficiency was further hindered by the incompatibility of the internal electronic system with data sources of other State regulatory agencies, e.g. to produce automated reports or management scoreboards. Application of the recent law (42/2016) that authorized the inter-connection of data between the State Tax Authority, Social Security and ACT is a step in the right direction in this regard, and could be the foundation for more analytical components of an integrated IT system.

Traditional enforcement can be enhanced by strategic compliance planning and new legal tools, and some steps have recently been taken in the right direction

Consequently, all issues discussed in this report call for more effective law enforcement. An important step would be to implement strategic compliance planning rather than the single use of the traditional enforcement, educational and communication approaches. Improvements in this regard are expected, as ACT has been slowly increasing its human resource capacity since 2015, even if staff numbers still remain below what would be desirable. New legal tools may also have an impact on compliance, such as the recent competence for direct action in the recognition of employment relationships, established by Law No. 63/2013. Moreover, it is important to continue recruiting qualified staff and sustain staff motivation through additional training and capacity development investments, as well as transparent career progression incentives. Lastly, even if data does not reveal immediate outcomes, concerns have been raised on the capacity of labour courts to receive new cases referred by inspectors – an issue that would have to be addressed to increase efficiency and effectiveness of the overall enforcement mechanism of the Labour Code.

Active labour market policies – from job creation to training and public employment services – are a crucial factor behind Portugal's labour market recovery since 2013

In line with the policy recommendations advanced by the ILO in its 2013 study, renewed emphasis on active labour market policies (ALMPs) has substantially contributed to the labour market recovery observed in Portugal since 2013. In particular, direct and indirect support to job creation has strengthened employment growth, while reforms aimed to improve the delivery of public employment services have contributed to activating (and profiling) unemployed individuals more effectively, and training measures (especially those provided for a longer duration) have increased participants' employment probabilities.

However, large numbers of the newly created jobs were of a temporary nature, and only modestly benefitted young NEETs and long-term unemployed. This was due to the relatively loose targeting of ALMPs on the most vulnerable labour market segments, as well as to the design of employment incentive schemes, which aimed at supporting job creation regardless of its quality. Recent efforts to improve targeting of ALMPs and their impact on permanent hiring should continue.

Future ALMPs should enhance effectiveness and target more disadvantaged workers, including young people and the long-term unemployed

Latest policy efforts have significantly contributed to addressing some of the limitation in the design of previous ALMPs, while enhancing their inclusiveness. For instance, the current employment incentive schemes (*Contrato Emprego*), introduced in 2017, promotes the creation of permanent employment by restricting the use of temporary contracts only to particular categories of disadvantaged workers, such as long-term unemployed. Further, the 2017 training initiative (*Qualifica)* more closely targets low-skilled individuals, while strengthening work-related training components. In addition, the 2016 reform of the Public Employment Service (PES), has improved the quality of the services offered by providing a more personalized support to the unemployed.

While recent policy initiatives introduced in the country in the area of ALMPs go in the right direction of improving the targeting, delivery and inclusiveness of ALMPs, there is still room for improvement. First, it would be important to strengthen the institutional capacity of the Public Employment Service (PES) by reducing caseload per career manager, and improve its ability to monitor long-term sustainability of the placements done via the different ALMPs. Second, with around one third of young NEET not registered with the PES, it is key to introduce stronger outreach services (e.g. job fairs, social media campaigns, direct engagement with communities, etc.) to enhance youth engagement with PES. Finally, as economic conditions improve, it is important to take this opportunity to rebalance the existing ALMP policy framework, by reallocating part of the expenditure in employment incentives to finance other, more adapted ALMPs, such as stronger start-up incentives schemes for the unemployed. Important steps in this direction have been taken through the introduction of a new integrated strategy to entrepreneurship support (*Startup Portugal*) in 2016.

The minimum wage, a key labour market intervention in Portugal, has helped reduce income inequality

While wages picked up before the crisis, they sharply fell during 2010–13 and levelled off just slightly above pre-crisis levels. Real average wages were about 3 per cent higher in 2016 than in 2007. Portugal had a similar labour share to other European countries until 2009, but saw a steep decline between 2009 and 2015 when labour productivity increased more rapidly than wages. Although the decline in the labour share bottomed out in 2015, it remains well below its level of the early 2000s, and also below the level of various other European countries, suggesting some possible scope for sustainable and carefully considered wage increases in the future. Meanwhile, average wages remain low in comparison to the EU (approx. €900, compared to €2,000 in the EU as a whole), explaining at least in part why so many of its young people have sought work in other countries. While inequality in Portugal is comparatively high, both wage and income inequality have declined in recent years. The decline in wage inequality can be explained by two simultaneous factors: the drop in the wages of the top 10 per cent during the last few years, as well as the increase in the wages of low-paid workers helped by Portugal's minimum wage policy.

The minimum wage is an important labour market intervention in Portugal, which has contributed to increasing the wages of low-paid workers and reducing wage inequality. Setting an adequate level of minimum wage has implications both for inequality and poverty. In Portugal, almost one-fifth of all wage earners earn about the minimum; another fifth of wage earners earn no more than 25 per cent more than the minimum. This demonstrates the important role of the minimum wage, which not only benefits young workers but also more experienced and older workers, as well as many women – who make up about 61 per cent of minimum wage earners. While the minimum wage is low in absolute terms compared to other European countries, it is relatively high compared to the median wage in Portugal, but relatively similar compared to the average wage, which is partially a reflection of relatively high, albeit declining income inequality. Considering these complexities, it would be important to regularly and rigorously monitor the effects of the minimum wage on employment, and particularly on youth employment.

Future policies should focus on closing the gender gap and boosting wages through education and skills enhancement

Statistics of the gender pay gap show that it has slightly decreased in the past decade, but remains high, with men earning approximately 19 per cent more than women. This gender pay gap has been attributed to a mix of factors, including the fact that women workers tend to work in firms and jobs that pay less, and to lack of equal access to top jobs – the so-called glass ceiling. Further measures could thus be taken to reduce the gender pay gap. Overcoming unequal pay across groups requires sustained effort at various levels and through a wide range of policy approaches, including combatting gender-based stereotypes about women's roles and aspirations, strengthening policies on maternity and paternity as well as parental leave, and advocacy for better sharing of family responsibilities. Equal pay at the enterprise level also requires job evaluation methods free from gender bias.

Sustained attention to access to education, and policies to increase the skills of the labour force – particularly those at the bottom of the distribution – would also contribute to higher wages. An important source of income inequality is the high incidence of unemployment of vulnerable populations and the resulting downward pressure on wages for low-skilled workers.

Social dialogue has been key to Portugal's successful recovery but the culture of collective bargaining must be revitalized to ensure inclusive growth

Commendably, social dialogue was heavily relied upon prior, during, and after the crisis period. While full consensus often proved elusive, social partners were consulted on most decisions. Where decisions were made unilaterally, or against interests of unions and/or employers, conflict and push-back resulted. The freezing of collective bargaining at sectoral level during the MoU period, however, ensured that this policy instrument could not be used by workers and employers to respond to the crisis.

Collective agreements generally continue to provide terms and conditions that are equal to or only slightly higher than legal minima, in particular with regard to wages. The content of most collective agreements, with some important recent exceptions, appears largely unchanged when comparing the pre- to post-crisis periods. This points to a need to revitalize the culture of bargaining, and to make agreements more dynamic and reflective of current labour market challenges, including subject areas beyond wages and working hours. The June 2018 tripartite agreement could mark an important milestone in rebuilding a stronger culture of collective bargaining.

The goal of the MoU and subsequent legislation to decentralize collective bargaining from the sectorial level to the enterprise level was not achieved. The predominance of sectorial level bargaining coupled with the use of extension mechanism results in high collective bargaining coverage (over 85 per cent in 2016), an outcome largely supported by unions and employers' organizations. However, relatively low union membership figures (less than 9 per cent in the private sector) may raise issues of representativeness and "free rider" problems (i.e. workers benefit from agreements without joining a union or paying union dues).

Changes in criteria for extensions of collective agreements since 2014 have had a positive effect on the number of agreements and number of workers covered, though neither has yet reached 2008 levels. The total number of new agreements dropped from 296 in 2008 to 94 in 2013, and has recovered to 208 in 2017, while total collective bargaining coverage by new agreements has swung from nearly 1.9 million workers to 241,000 workers, before increasing to 821,000. It is clear that the changes in legislation and extension criteria had a direct impact on the number of agreements and workers covered, even though the gap between pre- and post-crisis coverage remains large.

The extension of collective agreements is a key policy tool to promote collective bargaining and enhances its role in reducing inequality and fostering inclusiveness. Therefore, it would be desirable to maintain a system of extensions, while monitoring the impacts of the criteria adopted in June 2017.

Lastly, minimum wages have become an increasingly important influence on average levels of wages across the economy. Therefore, it should be explored how collective bargaining at different levels can be better used to link wages with productivity growth at both the sectoral and enterprise level. This can help to avoid a low wage trap, and instead lead to a virtuous cycle of increased productivity growth, leading to increased wage growth and domestic consumption, which, when combined with higher levels of skills and capital investment, leads in turn to higher productivity growth.

About this report

The report is organized as follows. Chapter 1 focuses on economic trends and demand patterns. Chapter 2 examines developments in the labour market from the last decade till end 2017. Chapter 3 reviews legal and regulatory changes that were implemented as part of the 2011 adjustment programme agreed with the European Commission (EC), the European Central Bank (ECB) and the International Monetary Fund (IMF) – or in response to it – in the areas of employment protection and regulation of contracts, hours of work, and labour inspection. Chapter 4 provides an overview of recent reforms in the area of active labour market policies (ALMPs), discusses their effectiveness in improving labour market and social conditions, and proposes a number of policy options going forward. Chapter 5 examines trends in wages and looks at issues of inequality, poverty and the gender gap. Chapter 6 focuses on legal and policy changes in collective bargaining. Each chapter includes empirical and analytical findings and concludes by highlighting key challenges and policy considerations.

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