Silvia Merisio

ADJUSTING THE ADJUSTMENT PROGRAMMES

INTERNATIONAL FINANCIAL ASSISTANCE DURING THE CRISIS: SHAPING THE IMF TEMPLATE TO FIT THE EURO AREA COUNTRIES

working paper

Centro Einaudi

N8 2014 ISSN 2036-1246

Laboratorio di Politica Comparata e Filosofia Pubblica

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International Financial Assistance During the Crisis: Shaping the IMF Template to Fit the Euro Area Countries

Centro Einaudi • Laboratorio di Politica Comparata e Filosofia Pubblica
with the support of Compagnia di San Paolo

Working Paper-LPF n. 8 • 2014

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The underlying idea is that implementing forms of "civilized" politics is desirable as well as feasible. And, as far as the Italian political system is concerned, it is also urgently needed, since the system appears to be poorly prepared to deal with the challenges emerging in many policy areas: from welfare state reform to the governance of immigration, from the selection criteria in education and in public administration to the regulation of ethically sensitive issues.

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Keywords

Washington Consensus, IMF, Troika, Euro area, bailout

ABSTRACT

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In the past few years, the Euro area member countries have embarked on an unprecedented effort aimed at tackling the challenges posed by the international financial crisis. For the first time, developed and open economies have tried to adjust within a monetary union. In May 2010 Greece became the first Eurozone country to receive official financial assistance from European institutions and the International Monetary Fund (IMF). Other three countries have followed suit, receiving extensive financial assistance programmes: Ireland in November 2010, Portugal in April 2011 and Cyprus in March 2013. It is argued that the conditions which the Eurozone's Economic Adjustment Programmes (EAPs) are enforcing are very similar to the IMF prescriptions, which were attached to the programmes implemented in Latin America in 1980s during the debt crisis and they recalled the policies that John Williamson identified with the "Washington Consensus". Furthermore, the EAPs imply the same approaches to the state: they are formulated in the middle of a deep economic turmoil for insolvent countries having no alternative than to accept International Financial Institutions (IFIs) assistance. What are the dynamics underpinning this policy choice? Why Eurozone member countries did not oppose this strategy? What relationship exists between national governments and the Troika? This paper addresses these questions by focusing on the case of Portugal.

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INTRODUCTION

In the past few years, the Euro area member countries have embarked on an unprecedented effort aimed at tackling the challenges posed by the international financial crisis. For the first time, developed and open economies have tried to adjust within a monetary union. In May 2010 Greece became the first Eurozone country to receive official financial assistance from European institutions and the International Monetary Fund (IMF). Other three countries have followed suit, receiving extensive financial assistance programmes: Ireland in November 2010, Portugal in April 2011 and Cyprus in March 2013.[1]

At the outset of the crisis, the European Union was not equipped with a crisis resolution mechanism, thus the principles and the modalities of financial assistance had to be gradually created in the midst of the economic turmoil. The result was the strengthening of the Stability and Growth Pact, the broadening of multilateral surveillance, the establishment of new treaties (Euro-Plus Pact, Fiscal Compact) and the creation of new instruments (European Financial Stability Facility, European Stability Mechanism among others). In this framework, the European Commission, the European Central Bank and the IMF also started a new form of cooperation, giving birth to the so-called "Troika". This tripartite organism has been charged with the task of coordinating the lending operations between the official lenders and the governments of recipient countries. The Troika is a unique institutional construction that involves an unprecedented degree of cooperation between regional and global financial institutions.

Financial assistance to Eurozone countries was provided following the IMF template: international/supranational institutions provide funding in exchange of

[1] The analysis focuses on the Euro area member states which agreed an Economic Adjustment Programme with the EU institutions. The case of Spain is out of the scope of the analysis as the financial assistance was provided for the recapitalization of financial institutions and the conditionality attached to the loan differed from the conditionality applied to the Economic Adjustment Programmes (DG ECFIN website).

policy reforms which address the economic and structural problems of the country. The conditionality attached to the Eurozone financial package was grounded on neoliberal principles, as the reforms encouraged fiscal austerity, internal devaluation and structural reforms as tools for increasing competitiveness while reducing the current account deficit. Although the four Eurozone's "programme countries" received different programmes tailored to their needs, the underlying philosophy appeared to be the same (Theodoropoulou and Watt 2011). It is argued that the conditions which the Eurozone's Economic Adjustment Programmes (EAPs) are enforcing are very similar to the IMF prescriptions, which were attached to the programmes implemented in Latin America in the 1980s during the debt crisis and they recalled the policies that John Williamson identified with the "Washington Consensus". Furthermore, the EAPs imply the same approaches to the state: they are formulated in the middle of a deep economic turmoil for insolvent countries having no alternative than to accept International Financial Institutions (IFIs) assistance. There are evident differences between the polities and the economies which were targeted in the IMF structural adjustment programmes and the Euro area member countries to which the EAPs are addressed. What is consistent, however, is the use of the policy tools: "conditional loans, used by international governmental organizations to promote a consistent list of economic policies" (Greer 2013, 5).

The Eurozone adjustment programmes implemented so far have already proved to be controversial. The EAPs brought deeply disappointing economic outcomes and social hardship notably in Greece and Portugal,[2] they have been subjected to continual renegotiation in terms of assistance (especially in Greece), and this has caused divisions within the Troika and among national governments (Pisani-Ferry et al. 2013). Moreover, the modes and the practices of implementation of the programmes, as well as the content of the policy conditionality and its similarities with the past IMF programmes, have attracted criticism. While the IMF programmes in Latin America have been acknowledged of being at least unsatisfying, leading to the elaboration of new approaches, the European institutions decided to revive the old Washington Consensus and to push it into peripheral countries. What are the dynamics underpinning this policy choice? Why Eurozone member countries did not oppose this strategy? What relationship exists between national governments and the Troika?

This paper aims to address the above questions by analysing the interplay between Troika conditionality and the domestic politics of EU countries, compared to previous IMF intervention in deficit countries. The main features of the IMF and Troika's assistance programmes are outlined in the first part of the research, which analyses the setting in which the programmes were elaborated, it identifies the main actors on the scene and presents the philosophy underlying the formulation of the financial assistance packages. A case study, Portugal, is presented in the

[2] Too little evidence is available for Cyprus.

second part, focusing on the dynamics of elaboration of the programme. The case of Portugal best represented the European programme countries as it received the third bailout in the Eurozone and the procedures and the modalities of the agreement had already been defined.

1. International financial assistance and conditionality

1.1. The IMF and the origins of international financial assistance programmes

The IMF was originally created in 1944 with a regulatory function in overseeing the system of fixed exchange rates and a financing function, providing credit for the settlement of short-term imbalances. With the collapse of the Bretton Woods system in 1971 and the introduction of a new system of flexible exchange rates, the regulatory function was no longer needed. Since then, the IMF primary fulfilled its mandate of providing financial assistance to countries which were struggling to survive in an increasingly globalized economy, thus gradually becoming the lender of first resort. In particular, this transformation of IMF's tasks was accompanied by the development of the practice of conditionality. Even though some elements of conditionality had been attached to Fund financing since the mid-1950s, conditionality became the keyword for IMF lending in the early 1970s, and then in the 1980s in a more intrusive manner[3] (De Vries 1987). The idea of conditionality refers to the policies a country is expected to implement in order to gain and secure access to resources of the Fund (Buira 2005). The macroeconomic conditions attached to the programmes were designed in order to restore the balance of payments and to tackle inflation problems, and usually involved restrictions on government's fiscal deficit as well as controls on the monetary policy. This practice of conditionality was tested and developed in Latin America during the 1970s, when the IMF provided extensive financial assistance in countries experiencing temporary difficulties of the balance of payments.

> In Latin America, the IMF began to lengthen its stand-by arrangements (SBAs) beyond six months, consequently making loans conditional on implementation of policy rather than just commitment to policy. Soon, SBAs were paid out in instalments (tranches) rather than as a single lump sum so that payment of the balance could be made conditional on prior performance. SBAs began to include consultation and review clauses to ensure that borrowers met with IMF staff, and binding conditions were added to the loan arrangements. (Babb and Carruthers 2008, 16).

Then, the debt crisis of the 1980s marked a turning point in the IMF history. The sudden reduction of private lending to developing countries plunged the majority of the latter in a severe debt crisis: by the end of 1984, 66 countries were forced to

[3] Nevertheless, conditionality was not foreseen in Keynes' original plan (except for the minimal financial conditions of payment schedules and interests) and it is not mentioned in IMF's original 1944 Articles of Agreement (De Vries 1987).

implement rigid adjustment programmes.[4] But the debt crisis was also threatening the main private banks and public creditors, which became highly dependent on the possibility of the IMF to reach a stabilization agreement with national governments. The IMF thus imposed itself as the crisis manager of the first order, starting then to interfere with the national political sovereignty of debtor countries (Altvater et al. 1987).

The old instruments used by the IMF to solve former liquidity squeezes were no longer suited to cope with such a crisis. Extremely high interest rates, hyperinflation, economic recession, a hostile international context and the high level of debt incurred by developing countries witnessed the impossibility to comply with their commitments and, at the same time, to enhance growth. Empowered by the new scarcity of resources and by its new role of crisis manager, the IMF reinforced the macroeconomic conditionality and made an unprecedented leap towards the structural conditionality. This is more intrusive than the macroeconomic conditionality, since it is broadly aimed at adjusting the overall architecture of the national economic and political system. This change is the result of increased emphasis placed by the Fund on economic growth as a policy objective, "with the recognition that rising growth on a sustainable basis requires strengthening the supply side through structural reforms" (IMF 2001). The basic idea was to lend to highly indebted countries, thus providing temporary cash relief, in order to give them the time necessary to restructure their economic system towards a more export-oriented one (Babb and Carruthers 2008). Yet in the 1980s, in the political context of the Reagan-Thatcher revolution, neoliberal ideas seemed the best solution to solve the problem of countries facing serious balance of payment problems and registering huge public deficits; for this reason they started to be channelled into the countries asking for loans. Supported by the United States, the International Financial Institutions (IFIs)[5] coordinated their actions to "promote market-liberalizing programs, including measures such as cutting deficits, raising taxes, cutting expenditure and privatization" (Stiglitz 2002, 12). These measures were aimed primarily at stopping demand by limiting credit expansion, reducing budget deficit and lowering real wages. Structural conditionality, in particular, provided "safeguards to the Fund to ensure that successive tranches of financing are delivered only if key policies are on track, and assurances to the country that it will continue to receive the Fund's financing provided that it continues to implement the policies envisaged" (IMF 2001).

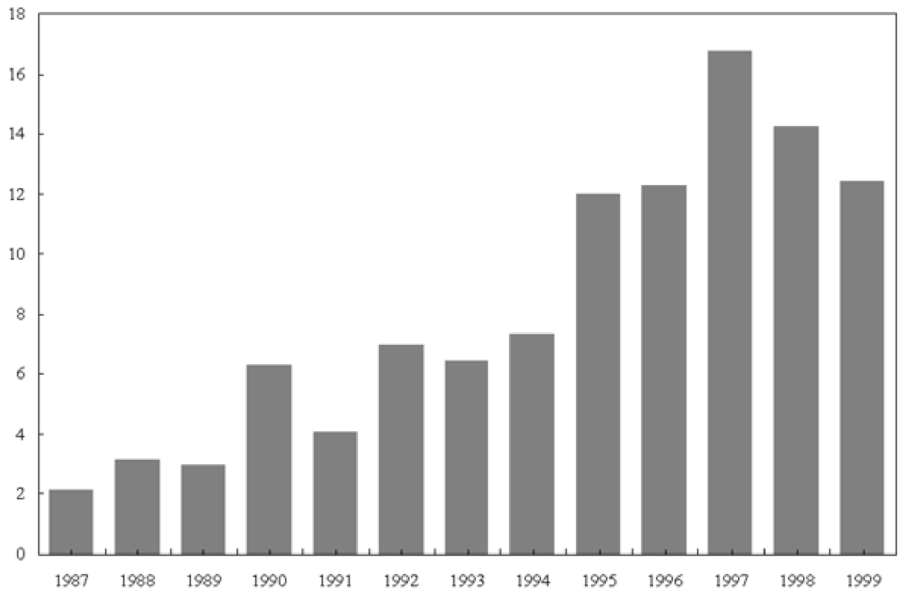
Following this expansion of conditionality, the tools used by the Fund to monitor and assess compliance increased exponentially: more complex and intrusive set of procedures, including periodical reviews, were established and the number of indicators such as performance criteria, prior actions and structural benchmarks

[4] For a more detailed analysis of the Latin American debt crisis see below.

[5] At the same time, other public organizations such as the World Bank started to emulate the IMF's concessional lending, setting up their own institutions.

proliferated as never before[6] (Boughton 2001). The number of structural policy commitments (prior actions, structural benchmarks, conditions for programme reviews and performance criteria) imposed by the Fund reached the peak during the Asian crisis in 1997, and the IMF justified it by stressing the fact that "while these countries had achieved impressive growth, serious financial sector vulnerabilities were at the root of their financial crises, so reforms aimed at addressing these vulnerabilities were key to the restoration of the confidence on a sustainable basis" (IMF 2001).

Figure 1 – **Average number of structural conditions per programme per year**



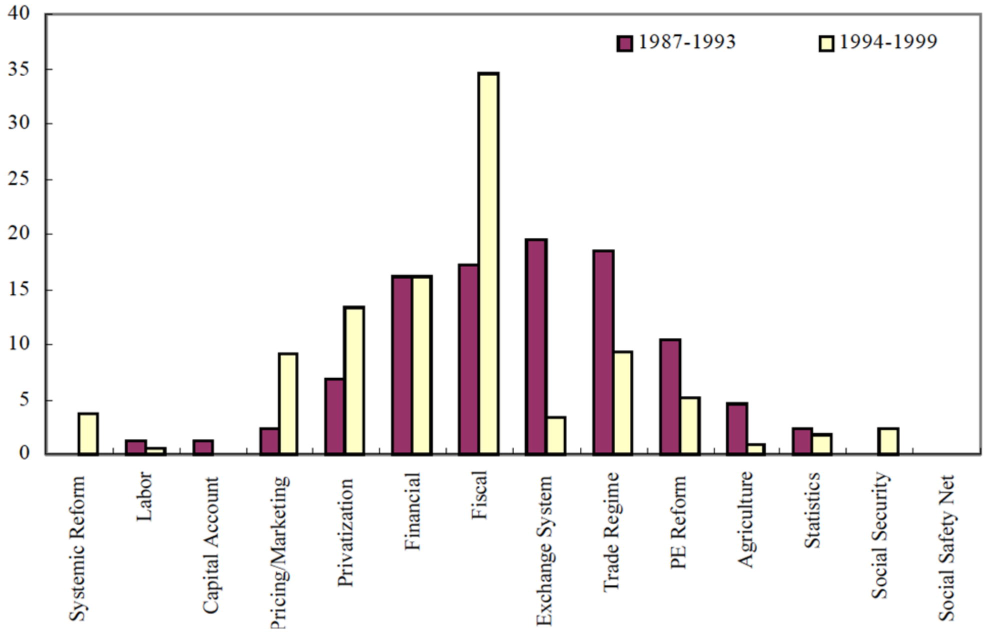
Total number of structural performance criteria for 1987-1993 include only PCs on approval or, in the case of ESAF arrangements, at the start of each annual programme.

Source: Buira 2005

Figure 1 shows the increasing number of structural conditions per programme per year, including all the structural performance criteria, prior actions, benchmarks and conditions for completion of review adjusted for difference of programme length. It can be noted that in the programmes of the 1980s the average number of structural conditions was 2, whereas it peaked in 1997 with 17 per programme

[6] Performance criteria are the oldest tools introduced in the 1950s. PC specifies either a quantitative target to be met or a policy action to be implemented by an agreed date for the country to be able to continue to draw on the IMF's financing (IMF 2002). "Prior actions are ex post instruments that require governments to implement reforms before becoming eligible to receive an IMF loan. Structural benchmarks are incremental steps toward reform that lack the formal legal status of performance criteria. These vehicles of policy reform were used much more frequently after the introduction of structural conditionality, and especially after the rise of governance reforms in IMF programs" (Babb and Carruthers 2008).

Figure 2 – **Structural performance criteria: sectoral distribution**



Total number of structural performance criteria, benchmarks, prior actions, and conditions for completion of review in stand-by, EFF, and SAF/ESAF/PRGF-supported programmes, adjusted for differences of programme length.

Source: Buira 2005

per year (Buira 2005). On the other hand, Figure 2 represents the sectoral distribution of the structural performance criteria included in the programmes agreed between 1987 and 1993 and those agreed during the conditionality boom of the late nineties. It is interesting to note that throughout the decade the focus of the reforms moved from macroeconomic adjustment to structural reforms: late nineties programmes are less concerned with trade regime, exchange system, but they include prescriptions about systemic reform and social security. Last but not least, none of those programmes include reforms regarding the implementation of social safety nets.

1.2. The "original" and the "augmented" Washington Consensus

As mentioned above, the renovated notion of conditionality coincided with a new market-mantra endorsed by the IMF at the end of the 1980s, as part of the neoliberal philosophy, which signalled that the Keynesian orientation that guided the IMF since its creation had been replaced by a radically different approach to economic development and stabilization. In the 1980s the New Right administration of Ronald Reagan and Margaret Thatcher embarked on a systematic and comprehensive project of fiscal retrenchment, financial and labour market deregulation, and erosion of the Keynesian assumptions that had underpinned post-war economic and social policy (King and Wood 1999). Subsequently, most countries embraced some version of neoliberal theory to tackle the debt crisis and adjusted at least some policies and practices accordingly; moreover, universities and think tanks advocated the neoliberal turn, same as corporate boards and key state institutions (treasury departments and central banks). Thus, under the Anglo-American pressure, neoliberal ideas became hegemonic and well entrenched in international financial institutions such as the IMF, the World Bank and the World Trade Organization, which started to push all countries to adopt neoliberal reforms (Harvey 2005). Neoliberal theories have proven exceptionally resilient in the last decades and they remain at the centre of political discourse. The main features of those prescriptions will be examined below, especially referring to the policies implemented in Latin America during the 1980s, also known as Washington Consensus.

The term Washington Consensus was coined by the economist John Williamson in a 1989 conference at the Institute for International Economics in Washington. The first usage was in the background paper for the conference *Latin American Adjustment: How Much Has Happened?* (Williamson 1990) with the task to "examine the extent to which the old ideas of development economics that had governed Latin American economic policy since the 1950s were being swept aside by the set of ideas that had long been accepted as appropriate within the OECD" (Williamson 2004). Williamson (1990) made a list of ten policy instruments "whose proper deployment Washington can muster a reasonable degree of consensus". For Washington he meant both the "political" Washington of the US Congress and the White House, and the "technocratic" Washington of international financial institutions, the IMF, the World Bank, US governmental agencies and the Federal Reserve Board. His list of economic policies would thus have had the consent of the major international financial institutions. Williamson's prescriptions were elaborated upon three policy priorities: reduction of state intervention in the economy, privatization and deregulation, commercial policy revision. Box 1 presents briefly the ten prescriptions which originated a large number of controversial interpretations.

The principles of the Washington Consensus remain at the heart of the conventional understanding of growth policies, even though they have been greatly revised and expanded in the following years. The term Washington Consensus is now identified with the set of policies that focus on privatization, liberalization and price stability, which has been implemented by international financial institutions in Latin America during the 1980s and early 1990s. The term is often used also as a synonym of neoliberalism or market fundamentalism because of the emphasis on liberalization and on the importance of a minimal state. Since the attested failure of this developing strategy in Latin America, a large number of leading economists and intellectuals started to reconsider the ideas underlying the Washington Consensus and the way in which they had been pushed by the IMF on the poor countries (Williamson 2004).

Box 1 • **Washington Consensus Prescriptions**

Fiscal Discipline. As Williamson (1990) pointed out, "there is very broad agreement in Washington that large and sustained fiscal deficits are a primary source of macroeconomic dislocation in the forms of inflation, payments deficits, and capital flight". A high budget deficit is considered as an element of policy failure. Fiscal discipline and the macroeconomic balance are therefore essential in developing countries.

Reordering Public Expenditures. The basic idea is to rationalize public expenditure and to eliminate inefficiencies. Subsidies, healthcare, education and public investment should be rationalized and made more efficient. State subsidies are targeted for reduction or preferably elimination. Education and health are subject to generalized cuts.

Tax Reform, Liberalizing Interest Rates, Competitive Exchange Rate. The idea is to enlarge tax bases and to have moderate marginal tax rates. Interest rates should be market-determined in order to avoid resource misallocation and should be positive in the sense that they can encourage savings and prevent capital flights but also moderate to avoid the explosion of big debt. The prescription about exchange rate is that they must be kept competitive. As Williamson (1990) underlined, "A competitive real exchange rate is the first essential element of an 'outward-oriented' economic policy, where the balance of payments constraint is overcome primarily by export growth rather than by import substitution. There is a very strongly held conviction in Washington that outward orientation and expanding exports are necessary for Latin American recovery". This point will be highly criticized with respect to its effect in Latin America together with the following one.

Trade Liberalization and Liberalization of Inward Foreign Direct Investment. The idea was that an outward-oriented economy should be supported by import liberalization in contrast with import licensing considered as the "worst form of protectionism" that impoverishes the economy. Economic restrictions were seen as the obstacle to development, whereas free trade could lead to a more competitive economies and a reduction in prices for consumers. The seventh point concerned the liberalization of FDIs in order to bring know-how, capitals and skills for producing new goods and also to export them.

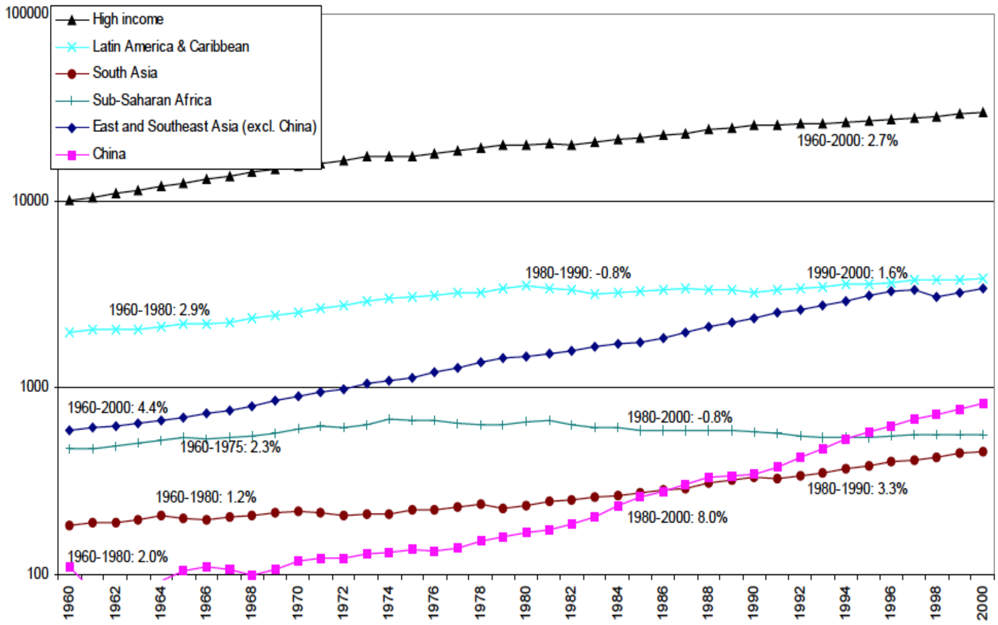
Privatization, Deregulation and Property Rights. The idea is that private enterprises can be managed more efficiently relative to state enterprises. Moreover, "privatization may help to relieve the pressure on the government budget, both in the short run by the revenue produced by the sale of the enterprise and in the longer run inasmuch as investment need no longer be financed by the government" (Williamson 1990). The ninth point deals with deregulation as another way to promote competition. And also as a tool to reduce corruption which was usually widespread in Latin America. The last prescription is intended to guarantee property rights in order to have the basis to promote capitalist economy.

Washington Consensus policies have been applied for more than two decades in diverse contexts such as Africa, Latin America and Asia, as well as in the formerly socialist countries in Eastern Europe and Central Asia. There were usually two major stages of intervention: the first focused on macroeconomic stability and structural adjustment programmes, the second included objectives such as improving institutions, reducing corruption or dealing with infrastructure inefficiency (Naím 2000). One of the main causes of the failure of the IMF programmes in all those areas is found in the market fundamentalist approach. Most notably, Joseph Stiglitz, chief economist at the World Bank from 1997 to 2000, argued that markets by themselves do not produce efficient outcomes when information is imperfect and markets are incomplete, which is true in developed countries and especially in developing countries. Moreover, historical experience also showed little evidence on the belief that markets, by themselves, would lead to rapid economic development. The IMF had an overly optimistic view of the functioning of the market, while considering the government more part of the problem than the solution of it. Furthermore, Washington Consensus policies often had a pessimistic view of the nature and the capability of all governments without considering country specific situations. The IMF tried to elaborate a one-size-fits-all approach to solve the crisis in different countries excluding the national government from the policy elaboration and implementation process and relying on the markets by themselves (Stiglitz 2002).

According to that view, the effect of policy measures in the short run could be ignored if in the long run they would make the country better off, any adverse short run impact was considered as the necessary pain that was part of the process. Moreover, the bargaining power was strongly biased toward the IMF relative to the country asking for loans and grants, because unless the IMF approved the country's economic policy there would be no debt relief and this gave the IMF a high leverage. The imbalance of power between the IMF and the "client" countries inevitably created tensions between the two, but the resistance of the organization during negotiations and the conditionality policy often exacerbated the situation (Stiglitz 2002). Serra and Stiglitz (2008, 78) have also argued that sometimes the IMF "simply used the opportunity that the crisis gave it to push its political agenda" in order to encourage liberalization or to call for more independency of the central bank, focusing on inflation. Additionally, these policies have been implemented through an opaque process of negotiations, resorting in little accountability to the population of the country they affected. There is little transparency in the decision-making process of the IMF, which should be a public institution and consequently a problem of legitimacy is raised (Babb and Carruthers 2008). The policy of the IMF are decided through a shareholder model that awards majority rule to the rich developed members that finance it and bestows the leading role to the US government. Consequently, Gould (2006) argued that IMF policies respond to the interest of third parties that provide financing for the lending to the developing countries and who use IMF arrangements for signalling that the country is safe for investment.

The Washington Consensus is considered so large a failure because it failed to acknowledge the developing process of countries, and because the scope of its objective was too narrow and it missed issues that should have been taken into account in the developing process. It has been estimated that Latin America's total external debt climbed from $231 billion in 1980 to approximately $417.5 billion in 1990; debt service accounted for 34 percent of exports in 1980 and 42 percent in 1990 (after a decade of export promotion)[7] and real GDP per capita declined in 1981, 1982, 1983, 1988 and 1989 and showed a cumulative decline of 5-10 percent in the course of the decade.[8]

Figure 3 – **GDP per capita by country groupings (1995 US$)**



Source: Rodrik 2008

As shown in Figure 3, Latin America's growth rate remained significantly below its level in the previous decade (–0.8 percent). On the contrary, China and East-Asian countries, where the policies implemented differed significantly from the Washington Consensus, exhibit positive growth rate since the early 1960s (Rodrik 2008). Social justice was also challenged by Washington Consensus policies: painful sacrifices have been inflicted upon the people of Latin America, especially on the working classes. In 1987 UNICEF published the report *Adjustment with a Human Face* denouncing the disastrous impact that the first wave of IMF's structural adjustment programme was having in Latin America and African countries and calling for new policies directed towards protecting "social and economic sectors

[7] Inter-American Dialogue (1989, esp. 3-4).
[8] Figures vary slightly by source, see Smith 1991.

that were essential to the survival of the poor, through the introduction of social protection programs" (Lopes 2011).

Nevertheless, it was just at the end of the 1990s, in conjunction with the Asian crisis, and then in 2004, with the Barcelona Development Agenda, that Williamson's original list started to be expanded in favour of a more comprehensive set of reforms. Table 1 summarizes the core principles of the "original" Washington Consensus and of the "augmented" Washington Consensus. To the thinking of international financial institutions and their economists, it was necessary to add a number of prescriptions (so called, second-generation reforms) having a more institutional target and restoring the role of the state.

Table 1 – **The main characteristics of Washington Consensus and "augmented" Washington Consensus**

Washington Consensus (Williamson 1990)	**"Augmented" Washington Consensus (additions to the original 10)**
1. Fiscal discipline	11. Corporate governance
2. Reorientation of public expenditures	12. Anticorruption
3. Tax reform	13. Flexible labour markets
4. Interest rate liberalization	14. Adherence to WTO disciplines
5. Unified and competitive exchange rates	15. Adherence to international financial codes and standards
6. Trade liberalization	16. "Prudent" capital-account opening
7. Openness to direct foreign investment	17. Nonintermediate exchange rate regimes
8. Privatization	18. Independent central banks/inflation targeting
9. Deregulation	19. Social safety nets
10. Secure property rights	20. Targeted poverty reduction

Source: Rodrik 2008

The second-generation reforms constitute an attempt to cope with the failures of the Washington Consensus as applied in Latin America preserving the core ideas of the concept. The new agenda was not addressed directly to one particular context (as it was for the Latin America prescriptions in the 1980s) and it should not be considered as a universal paradigm. There was growing consent on the extent to which economic adjustments might be inadequate if not supported by appropriate institutional transformation ranging from bureaucracies to labour markets. In 1998 Joseph Stiglitz, the Senior Vice President and Chief Economist at the World Bank, claimed that there was an emerging "post-Washington Consensus" (Stiglitz 1998, 33). Acknowledging the success of East Asian development, Stiglitz argued that, "while macro-stabilization policies are necessary, there is a need for less distorted, more competitive, more efficient marketplace" (p. 2) and this must be complemented by effective regulation and competition policies. Stiglitz criticized the fact that the Washington Consensus prescriptions underestimated the importance of building human capital and transferring technology in order to achieve long-term development. In the East Asian economies, for example, where governments played a role in providing universal education, the transformation from agrarian to industrializing economies was extremely rapid. The main argument is that "left to itself, the market will tend to underprovide human capital. It is very difficult to borrow against the prospects of future earnings since human capital cannot be collateralized. These difficulties are especially severe for poorer families. The government thus plays an important role in providing public education, making education more affordable, and enhancing access to funding" (Stiglitz 1998, 23). Furthermore, investments in Research & Development should be increased as it is estimated that they provide high individual and social returns.[9] A high number of concerns were also raised with regard to financial liberalization, which may lead to crisis and volatility, when a regulatory framework is not adequately designed. Finally, in response to the complaint that the original Washington Consensus responded inadequately to the Latin American crisis, the policy framework was augmented with a focus on the concept of "ownership". This means that in order to achieve a sustainable development and to avoid social and political turmoil in developing countries, national governments must claim the ownership of the policies that are implemented.

Although the core principles of the Washington Consensus as outlined by Williamson in 1990 were questioned and criticized in several occasions, they have proven remarkably resilient.[10] This neoliberal philosophy remains at the heart of today's conventional thinking of a desirable policy framework for economic growth. In the following paragraphs I will argue that EU's recent lending policies amount to a European rescue of the Washington Consensus (Lutz and Kranke 2014): the EU and the IMF came back under a new form of cooperation to push for orthodox measures inspired by neoliberal theories in return for loans to the Eurozone peripheral countries.

2. THE EUROZONE CRISIS

2.1. From the global crisis to the Euro crisis

The strategy followed by the EU institutions and member states in trying to cope with financial troubles has to be analysed in the light of the global economic context. The economic crisis which started in 2007 led the EU countries to experience the most severe economic contraction since the 1930s. The effects of the contraction were amplified as they were affected by a large global economic and financial collapse affecting most of the countries at the same time. Thus at

[9] Individual returns accounts for 20-30 percent and social returns 50 percent or higher in industrialized countries (Stiglitz 1998).

[10] For an analysis of the reasons of this resilience see Schmidt and Thatcher 2013.

the end of 2008, 25 of the 27 members of the EU were in recession. The global financial crisis had immediate and severe implications for the Eurozone: peripheral countries accumulated current account deficits and indebtedness levels rose either for households or for corporations (Lapavitsas 2012). At the same time, a great pressure was put on workers' salaries and conditions across the periphery. In 2008, after the collapse of Lehman Brothers, the European Central Bank engaged in extensive liquidity provision, allowing banks to adjust their balance sheet. The result was a credit shortage and accelerated recession across the Eurozone, including the periphery. Under these conditions, several countries, both from the core and the periphery of the Eurozone, started to seek additional funds in financial markets. As the recession hit, tax revenues decreased causing a decline in public revenues, while public expenditures rose due to the recapitalization of banks in many countries. Accelerated public borrowing was caused by the crisis and subsequently by speculation in financial markets, as it happened in Greece (Lapavitsas 2012).

In November 2008 the European Commission formulated a plan envisaging a fiscal stimulus of €200 billion in 2009 and 2010 equivalent to 1.5 percent of its GDP (see European Commission website). However, the rate of economic contraction accelerated in the following months, proving that the EU had underestimated the magnitude of the crisis (Bermeo and Pontusson 2012). In the spring of 2009, the EU resisted to the pressures coming from US and OECD to approve a further fiscal stimulus, even if the economy was still contracting. That resistance can be explained by the difficulty for the 27 members to agree on a change in policy in the midst of the economic crisis as well as by the limited budget capacity of the EU. Moreover, the institutional mechanism surrounding the Euro has been an essential part of the crisis.

In early 2010 the economy was slightly recovering, with exports improving more than anticipated and public expenditures supporting investment and household incomes, when the Eurozone sovereign debt crisis exploded. In February, the magnitude of Greek problems became clear and yields of ten-year Greek bonds reached a peak of 7 percent. On 11 February 2010, the informal meeting of the Heads of State and Government stated that the priority was to preserve financial stability in the Euro area as a whole. With a clear reference to Greece, this represented a message for financial markets as well as for member countries, which were opposing any bailout. The following month the Heads of State and Government confirmed that the strategy to follow included severe national austerity to pursue fiscal consolidation and to alleviate market pressure. The efforts undertaken by the Greek Government were not enough to restore market confidence and at the European Council of 25 March it became clear that Greece would need a bailout. European member states declared their willingness to participate in bilateral loans as part of a package involving the financing of the International Monetary Fund. The loans would be unanimously decided, subject to strong conditionality, and they would not be provided at the average interest rate or at a more favourable rate, in order to avoid moral hazard. The aim was to allow the country to return to market financing as soon as possible (Lourtie 2011, 19). An agreement was reached on 3 May 2010, according to which Greece would have its external financing needs covered until 2013 with a sum of 110€ billion provided by the Euro area and by the IMF (Theodoropolou and Watt 2011). The fact that the disbursement of the loan was dependent on the willingness of the member states, most of them sceptical about the bailout, and the increasing popular discontent in Greece led the Greek 10-years bond interest rates to peak above 12 percent on Friday, 7 May. On the same day an extraordinary meeting of the EU Heads of State and Government was held in Brussels: they agreed on the creation of the European Financial Stability Mechanism (EFSM) and the European Financial Stability Facility (EFSF), accounting for 750€ billion, of which one third from the IMF. Meanwhile, peripheral countries such as Spain and Portugal were trying to resist market pressures by endorsing the austerity mantra.

A short period of relative calm followed until concerns about the Irish banking system started to upset financial markets. The situation was aggravated by the joint Franco-German statement about an "adequate participation of the private creditors" in sharing the burden of the crisis, on 18 October 2010 (*ibidem*, 22). As a consequence, interest rates skyrocketed in Ireland and Portugal and kept growing. It was then evident that the fate of the country did not rely exclusively on domestic policy but it was shaped by the actions of the other members and of international markets. Finally, an agreement was reached on 22 November to provide financial assistance to Ireland through a 85€ billion package, with conditionality reforms attached. A few days later the Eurogroup institutionalised the future European Stability Mechanism (ESM) as a permanent mechanism for crisis resolution.

Once Greece and Ireland had been put under the Troika surveillance and a crisis resolution mechanism had been implemented, the whole Eurozone was looking at Portugal as the next in the pipeline. In the months following November 2010, the Portuguese Government tried to avoid international assistance, anticipating strong austerity measures. Then, in March 2011, an internal political crisis prevented the implementation of the announced reforms and led to the resignation of the government.[11] The caretaker government finally decided to ask for international financial assistance from the European Union and the IMF the following month. The result was the extension of financial support to Portugal under a conditionality agreement (Memorandum of Understanding on Specific Economic Policy Conditionality – MoU) issued by ECOFIN Ministers on 8 April 2011. A 78€ billion loan was agreed and provided in equal parts by the EFSF, the ESM and the IMF over three years. Table 2 summarizes the most significant events that led the three programme countries toward the bailout.

[11] The steps which led to the Portuguese bailout will be described in section 4.

Table 2 – **Crisis timeline: its causes and effects**

Timeline	Main steps
October 2008	**United States** • Global financial crisis • Lehman Brothers bankruptcy • PT vs. DE bond spread widens. But less than Greek, Italian and Irish bond spreads
January 2010	**Greece** • Greek deficit swells • Uncertainty as to Greek figures
4 February 2010	**European Union** • EU HSG meeting proclaims coordinated action to safeguard financial stability in **Euro area** • Bond yields peek in peripheral countries. Pressure lowers in February and March
April 2010	**European Union** • European scepticism to bailout mechanism • Need for unanimous agreement, including national Parliaments **Greece** • More austerity in Greece, which demands for financial help
7 May 2010	**European Union** • EU HSG meeting agrees EFSF/EFSM • Spain and Portugal signal austerity at home
September 2010	**Ireland** • Concerns with Irish banking sector • Ireland bails out Anglo-Irish
October 2010	**European Union** • Franco-German(18 October) + European Council (29 October) decision to include private sector in future crisis mechanism **Ireland** • Magnitude of Irish debt swells • European news on private sector involvement put pressure in peripheral countries. Bond yields increase
28 November 2010	**European Union** • Eurogroup clarifies private sector involvement. Separation between solvent and insolvent countries • Short period of calm • Portugal is seen as the next in line for financial assistance
April 2011	78€ billion loan is agreed for Portugal

HSG = Head of State and Government

Source: Lourtie 2011, 29-30, Table 4

As it can be observed, the main features of the crisis in the four programme countries appear to be approximately the same, namely large-scale of capital outflows, vulnerability of sovereigns borrowing in a currency of which they have no command, no control over nominal exchange rate, which implies a longer adjustment process, and financing of the balance of payments by Eurosystem liquidity. The response of the peripheral countries consisted in pursuing internal devaluation with respect to other countries (Germany in particular), through cuts in wages and public expenditures. These policy choices increased the already existing cleavage between the core and the peripheral countries. The crisis thus revealed two phenomena: a sharp shrinking of the policy space for the peripheral countries as a result of monetary unification and a push in a neo-liberal direction for the whole Euro area (Armingeon and Baccaro 2012). As it will be shown in the next paragraphs, this strategy was enforced through the use of the conditionality attached to the bailout packages, and, indirectly, through relatively high interest rates on sovereign debt (Lane 2012). These packages were elaborated by the so-called Troika, the tripartite organism composed by the EU institutions and the IMF, to which the implementation of the programmes has been entrusted.

3. THE TROIKA AND THE MEMORANDUM OF UNDERSTANDING

3.1. The Troika

The IMF and the EU institutions experimented the first form of cooperation shortly after the peak of the global financial crisis, when Central and Eastern EU countries asked for financial assistance. In October 2008 Hungary requested a Stand-By Arrangement (SBA) from the IMF, after discussing it with the European institutions. Thus, with the consent of the EU, the IMF set up a financial assistance programme for Hungary, which combined the lending expertise of the IMF with the regional interests of the Union, constituting the first example of cooperation between the two organizations. Subsequently, in December 2008, another joint EU-IMF programme was elaborated for Latvia and, in March 2009, a 13€ billion loan was provided to Romania by the IMF in agreement with the EU and other international institutions. On this occasion the EU, in collaboration with the IMF, started to set up the guidelines for providing financial assistance in Europe. At that time, the possibility of extending this kind of programme to Euro area members was not taken into consideration. Nevertheless, with the aggravating of the crisis, the European Union and the IMF embarked on an unprecedented form of cooperation providing for the first time financial assistance within a monetary union:

> The Troika formally originated from a decision of the heads of state and government in the Euro area taken on 25 March, 2010 regarding the Greek economic situation. On that occasion the Eurozone member states affirmed their willingness to contribute coordinated bilateral loans to Greece as part of a package involving "substantial IMF financing and a majority of European financing"[12] and to set out the conditions for the loans. A few days later, the Eurogroup announced that "the Commission, in liaison

[12] Statement by the Heads of State and Government of the Euro area, 25 March 2010.

> with the ECB" would start working on a joint programme "with the IMF and the Greek authorities"[13] and on 19 April the first Troika mission started negotiations in Greece. (Pisani-Ferry et al. 2013, 19)

The Troika programmes follow the same template for the Irish, Portuguese and Cypriot bailouts and they are modelled on the IMF standard. Once a country has asked for financial assistance, a preliminary work starts within the concerned unit in the IMF and in the European Commission. Within the IMF, the area department, in accordance with the Strategy Policy and Review Department, prepares a document (Policy Note), which assesses the economic and political situation of the country in question and sets out the guidelines to be followed. Once the Policy Note has received the approval of the responsible units, it can be transmitted to the ad hoc mission team, which effectively participate in negotiations.[14] At the same time, within the EC, the Directorate General of the Economic and Financial Affairs (DG ECFIN) is responsible for drawing up an early assessment of the main problems of the country (Policy Brief), whereas the policy guidelines emerge from previous internal debates and Ministers meetings.[15] Those assessments are exchanged and discussed within the two organizations and constitute the basis for the negotiations with the authorities are held jointly by the Troika officers (coming from IMF, DG ECFIN and ECB). The negotiations with national authorities are carried out in the borrowing countries and involve members of the government, representatives of opposition parties and consultations with social partners. The result is the "Letter of Intent" outlining broad intentions and a "Memorandum of Economic and Financial Policies" (MEFP) that defines the policy strategy, the planned policy actions and determines the "benchmarks". An additional Memorandum of Understanding on specific economic policy conditionality (MoU) is drawn up, which contains very detailed structural measures that the country has to implement in order to receive further tranches of the loans, and represents the basis for the EFSF/ESM financial assistance decision.[16] Once the programme has been agreed upon, the financial assistance is formally granted and the loans are provided by the IMF and the ESM. The recipient countries enter in separate agreement with the IMF and the ESM, which set out their lending terms. The implementation of the programme and the fulfilment of the stated objective are assessed by the Troika on a quarterly basis: at each stage two different reports are drawn up, one by the IMF and one by the EC, while the Letter of Intent and the associated MoU are updated and revised. The ECB does not publish any report as it is stated to work "in liaison" with the EC. Table 3 provides an overview of the Financial Assistance Programmes agreed with Greece, Ireland and Portugal. In the next section, one of the principal documents negotiated and produced by the Troika, a Memorandum of Understanding, will be analysed with reference to the IMF structural adjustment programmes described above.

[13] Statement on support to Greece provided by the Euro area member states, 11 April 2010.
[14] Information provided by an IMF Senior Officer during an interview, 19 June 2013.
[15] Information provided by DG ECFIN Head of Unit during an interview, 11 June 2013.
[16] European Stability Mechanism (ESM) replaced the EFSF since its creation in October 2012.

Table 3 – **Overview of the Financial Assistance Programmes in Greece, Ireland and Portugal**

	Greece		Ireland	Portugal
	1st Programme	2nd Programme		
Date	May 2010 until June 2013	March 2012 until end 2014	December 2010 until end 2013	May 2011 until mid-2014
Size	€110 bn	€164.5 bn	€85 bn	€78bn
Nature	IMF: SBA EA: Greek Loan facility	IMF: part of EFF €28 bn arrangement EA: EFSF	IMF: EFF EA: EFSF EU: EFSM Bilateral Ireland	IMF: EFF EA: EFSF EU: EFSM
Contributors	IMF: €30 Pooled bilateral from EA (€80 bn)	IMF (€19.8bn) EFSF (€144.7 bn)	IMF (€22.5 bn) EFSF (€22.5 bn) EFSM (€22.5 bn) UK (€3.8 bn) Sweden (€0.6 bn) Denmark (€0.4 bn) Ireland: Treasury and National Pension Reserve Fund (€17.5 bn)	IMF (€26 bn) EFSF (€26 bn) EFSM (€26 bn)

SBA: Stand-By Arrangement • EFF: Extended Fund Facility • EFSF: European Financial Stability Facility • EFSM: European Financial Stabilization Mechanism (Pisani-Ferry et al. 2013).

Source: DG ECFIN

3.2. The Portuguese Memorandum of Understanding

The case of Portugal, the third member state to receive a bailout, is analysed here because it best represents the European programme countries. In fact, by the time Portugal came to receive financial assistance the procedures and the modalities of the agreement had already been defined.

The stated objective of the Economic Adjustment Programme for Portugal was "to restore market confidence and to raise the potential of our economy to generate socially balanced growth and employment" (Letter of Intent, May 2011). In order to achieve this goal Portugal, in agreement with the Troika, would set up a "strategy [that] envisions bold and upfront structural reforms to improve competitiveness, an ambitious but credible pace of fiscal adjustment, and measures to ensure a stable and dynamic financial system." Among the broad set of measures that are listed in the EAP it is possible to find common elements with the IMF structural adjustment programme presented before. In particular, several prescriptions summarized by the Washington Consensus can be easily recognised in the document, including: (1) fiscal policy adjustment, (2) reordering public expenditure, Box 2 • **The first Memorandum for Portugal (2011)**

1. Fiscal discipline: reform of fiscal policy that involves reforming taxes to produce revenue and steer economic activity while reducing government expenditure. Reduction of government deficit to a level below 5.9 percent of GDP based on projection as of 2011, 4.5 percent of GDP in 2012 and 3 percent of GDP in 2013. [In spite of tight spending controls and favourable one-off factors, the deficit targets of 4.5 percent of GDP in 2012 and 3 percent of GDP in 2013 are no longer achievable (Seventh Review 2013)].

2. Cuts in public expenditure: **i)** reduce the number of public services and of civil servants; **ii)** reduction in subsidies to private producers of goods and services; **iii)** lower public sector wage bill (limit staff admissions and freeze wages) and a lower and shorter term for unemployment benefits, suspend application of pensions indexation rules and freeze pensions (a special contribution on pensions above 1,500 euros in 2012); **iv)** control costs in health sector and in the area of education and reduce the cost in state owned enterprises.

3. Tax reform: reduction of corporate tax deduction and special regimes (ending the reduced rate for small enterprises); reduction of personal income tax benefits and deductions; changes in property taxation to raise revenue; raise VAT revenues.

4. Trade liberalization in this case is more related to sectoral reform that involves specific recommendations on sectors such as health or transport, implying market promotion. In all the cases the programmes are promoting domestic markets and a smaller state. It is interesting to note that the healthcare sector is subjected to very detailed reform programme, which addresses quite technical items including the development of clinical practice guidelines. On the other hand, the labour-market reforms are left very general and unspecified, such as "Reform employment protection legislation to tackle labour market segmentation" (MoU 2011), revision of the unemployment insurance system (shorter and lower benefits), strengthen social safety nets. Easing rule on employee dismissal, increasing flexibility on working time, more firm-level union bargaining and exemptions to sectoral bargaining agreements); and promoting active labour market policies in order to encourage the jobless into work [erased after] sector (EDP, REN).

5. Privatization (Portuguese state owned enterprises are identified as a major drain on the budget), TAP airlines, the postal service and some nationalized finance companies, energy sector (EDP, REN).

6. Financial sector reform, including better regulation and market-determined interest rates. In this case this also meant various level of subsidy and public assumption of financial sector losses.

(3) tax reform, (4) liberalization, which is in this case more related to sectoral reform within the country, (5) privatization of the state-owned enterprises, (6) reform of the financial sector, including regulation of the financial enterprises and market-determined interest rates. The Washington Consensus prescriptions concerning unified and competitive exchange rates and openness to FDIs are already

incorporated in the EU, whereas even if trade liberalization was partly achieved by many different EU laws, EAPs contain many different liberalization programmes. The main features of the EAP for Portugal are summarized in Box 2.

As it can be observed, the Memorandum of Understanding of Portugal contains several traditional remedies typical of the IMF adjustment programmes. The same remedies were also suggested to Ireland and Greece[17] despite their structural differences: the tendency is to call for labour market liberalization, firm-level wage setting, more flexible and deregulated labour market, and liberalization of energy and transport sectors. Privatization is always suggested when there are important state-owned enterprises, notably in the transport and public services. The sector of education receives low consideration, whereas healthcare has very detailed reform strategies and the local government is mentioned for unspecified cuts. In all countries the reforms aim to set up facilities to rescue and monitor private banks (Greer 2013). Moreover, the recipients of the loans, the programme countries, can operate in a narrow policy space: their actions are constrained by the fact that they have lost access to private bond market and they are no more able to finance themselves.

Both IMF programmes and EAPs foresee two stages of intervention: the first is focused on macroeconomic stability and adjustment reform, the second is aimed at reducing structural inefficiencies. Absolute priority is given, in both contexts, to fiscal adjustment and restoration of the balance of payments. As far as the structural reforms are concerned, the EAPs include a higher number of conditions aimed to address specific structural weaknesses (in the Portuguese MoU a whole section is devoted to the judicial system), whereas the IMF adjustment programmes in the 1980s omitted reforms regarding the strategies of legal or public management improvement and there was neither concern for the social impact of the adjustment nor for attentiveness to local context. However, even if the EAPs included more structural reforms than the previous programmes, it was still largely focused on fiscal consolidation reforms (Pereira and Wemans 2012). All the EAPs seem to endorse this market fundamentalist approach, the same that was identified by Joseph Stiglitz as one of the main causes of the failure of the IMF programmes at the end of the 1990s. The European economic elites focused on the primary surplus obtained by cutting public expenditure or increasing taxes. The European leaders seem therefore to have ignored the wide debate about the austerity and the IMF programmes in Latin America (see Stiglitz 2002, Rodrik 2008, Serra and Stiglitz 2008).

Despite the similarities in the content of the adjustment programmes, it is necessary to investigate the dynamics underpinning the negotiations on the elaboration of the assistance package in the Eurozone to understand the reasons of European's policy choices.

[17] The case of Cyprus is atypical due to the small size of the economy and to the fact that the economy is focused on the services sector.

4. THE PORTUGUESE ADJUSTMENT IN THE SPOTLIGHT

4.1. Institutional framework and actors

In the light of the analysis conducted so far, the adjustment programmes can be regarded as the setting in which international institutions and national governments negotiate over the access to funding in exchange of policy reforms; therefore, interactions between the various actors occur in a complex web of economic and political interests at both international and domestic level (Pop-Eleches 2008).

In the institutional framework of IMF programmes, such as those implemented in Latin America, several external factors affected the interaction between the Fund and national authorities. In particular, the IMF action was tied to its role of lender of last resort and overseer of international economic stability and, at the same time, it was also influenced by the specific economic and geopolitical interests of its larger shareholder countries. National governments in Latin America had to take their decisions considering the international and domestic economic situation and keeping into account the internal political opposition and the bureaucratic constraints on the range of feasible economic policy options.

On the other hand, the Eurozone's adjustment programmes are elaborated within a much more complex framework, namely a full-fledged currency union, and are implemented by a heterogeneous team of international officials belonging to three different organizations. The possible policy options are limited in this kind of framework and the high degree of interdependence between the economies results in additional concerns about the elaboration of the programmes for a Euro area country. Moreover, European institutions act on behalf of the member states, which provide also part of the funding to the peripheral countries. Finally, the relationship between the Troika and national governments is complex in terms of bargaining power, as the recipients of loans are among the richest countries in the world.

In this context, the Troika can be considered as the intermediary between national governments and the major lending institution, the European Stability Mechanism (ESM), even if many other actors interfere. National governments asking for financial assistance negotiate the conditions for having access to the loan with the tripartite organism, composed by two communitarian institutions, the European Commission (EC) and the European Central Bank (ECB), and the IMF, which is supposed to be the neutral entity in the cooperation. The Troika is in charge of the formulation and the implementation of the programmes, but it is neither a decision-making organ nor a lending institution (Pisani-Ferry et al. 2013). The funding is provided by both the ESM and the IMF and, in some cases, through bilateral loans approved by EU member countries, while policy guidelines are set by the European Commission in agreement with the IMF (#DG ECFIN Structural, #DG ECFIN Portugal, #IMF Senior Officer). Additionally, the ESM is not a technocratic institution but an intergovernmental organization, involving finance ministers, heads of state and governments and national parliaments. In this way the decision-making process for the Eurozone programmes results in a more fragmented and highly politicized procedure. Moreover, the tripartite nature of the Troika raises a number of concerns about the effectiveness and the legitimacy of the cooperation. The EU institutions involved in the cooperation face a potential conflict of interests between the policies implemented by the Troika and the ones established within the framework of the European Union, on the basis of the treaties and the procedures. As it has been said, the European Commission acts in the Troika as the agent of the Eurogroup, which decides whether to provide financial assistance or not and monitors the lending activities through the ESM. This is in sharp contrast with the normal role of the Commission, which is an independent principal charged with the task to preserve the stability of the Union (Pisani-Ferry et al. 2013). The role of the European Central Bank in the Troika is difficult to assess, as it does not publish any reports about its involvement in the programmes. The ECB does not participate in the lending but it relies on its own instruments to alleviate the programme countries' financial problems, providing liquidity to the banking system and supporting the activity of the European Commission. Also, the role of the ECB in the cooperation raises a few concerns relatively to its mandate. Firstly, its involvement in the programmes for peripheral countries might influence the activity of the Bank, distracting it from its mandate to maintain price stability in the Euro area as a whole. The ECB might be tempted to deviate from its price stability objective in order to help to improve the budgetary sustainability in a given programme country, or it might be biased towards fiscal consolidation because of its focus on price stability.

The presence of the IMF in the cooperation complicates the decision-making process of the Troika. Contrary to its previous experiences, the Fund is a minority lender in the Troika and it is playing a junior role. Its participation has raised several concerns about whether IMF's junior position in the Troika has reduced its ability to conduct its role objectively; diverse stances have emerged within the Fund questioning the approach taken in the elaboration of the programmes (see Spiegel and Harding 2013) and criticizing EU institutions' policy strategy (#IMF Senior Officer, #FT journalist).

In addition, the three organizations composing the Troika have very limited democratic accountability: the European Central Bank, shielded from politics, accountable to central banks and bound by strict treaty limitations; the IMF, that is formally accountable to its shareholder governments; and the European Commission, closer to European voters, but still only indirectly accountable to governments and the European Parliament (#Portuguese Minister, Lourtie 2011).

This complex framework has significantly affected the formulation and the implementation of the adjustment packages for peripheral countries. The fact that a crisis-resolution mechanism had to be created in the middle of the economic crisis, the high degree of politicization of the process and the diverse stance standing within the Troika might have led from the initial uncertainty in the policy strategy to the choice of rescuing the neoliberal theories of the Washington Consensus and to promote them through the adjustment programmes. New instruments had to be elaborated in a short time frame in order to avoid negative spill-overs in the whole area, and the complex EU institutional setting was not prepared to elaborate a fresh approach to the creation of lending programmes. The rigid financial rules contained in the Stability and Growth Pact (SGP) did not leave much space for the development of new and perhaps even creative approaches to handle financial crises (Lutz and Kranke 2014). The EU's overarching concern was to maintain the stability of the Euro area and the political nature of the Union could not be detached from its members' interests. Therefore the most straightforward solution to the fiscal imbalances of the peripheral countries was offered from an ideological point of view by the old market mantra of the Washington Consensus. This neoliberal philosophy has proven remarkably resilient over time; its general principles allowed it to adapt and to resist challenges. Moreover, the strength of the neoliberal ideas in the policy debate and policy discourse made them suitable for the purposes of the EU institutions, which had to find an underlying paradigm for the newly created adjustment programmes. Then, the debates over a response to the Euro crisis was centred on neoliberal policies, because the crisis was depicted as due to the profligacy of peripheral countries and their "excessive" state debt required austerity measures and reduction in public spending[18] (*ibidem*).

For these reasons the Eurozone core countries and their leaders, Merkel and Sarkozy above all, started to advocate severe austerity measures in order to cope with the crisis (#Portuguese Minister, #IMF Senior Officer). Indeed, this rhetoric worked and resulted effective to spread the old-new Washington Consensus throughout Europe: the apparent "good sense" of the neoliberal prescriptions provided cognitive power and normative resonance in policy debates and political discourse.[19] As a consequence, EU countries, including peripheral countries, embraced the neoliberal ideas and accepted with various degree of compliance the resorting policy prescriptions. Then the implementation of the neoliberal prescriptions in the framework of the adjustment programmes was delegated to the EU bureaucracies (#Pedro Adao e Silva, #Portuguese Minister, DG ECFIN Structural), which enjoyed some discretionary power in formulating and implementing policies. In a sense, senior unelected EC and ECB officers have also contributed to produce and enforce the neoliberal policy ideas and agendas. This has been most evident "through their membership in the epistemic communities and advocacy coalitions formed to promote financial market liberalization, competition policy, and liberalization of services in the Single Market, as well as to push the austerity agenda for the EMU over time" (Schmidt and Thatcher 2013, 416).

[18] See Jones in Schmidt and Thatcher 2013.

[19] For instance, "Keynesian policies of supporting demand through fiscal policy face 'common sense' claims that states cannot continue to spend more than they earn" (Schmidt and Thatcher 2013).

The result was that first-lender EU institutions insisted to apply orthodox austerity measures into peripheral countries, whereas the IMF staff appeared to be more lenient in the conditions and underlined the importance of structural measures. This can be explained by the fact that over the years the IMF has revised its approach and adjusted its lending policies, after several negative experiences (such as the Latin American one), whereas the lack of expertise of the EU can be one of the reasons explaining the European policy strategy (Lutz and Kranke 2014, #Portuguese Minister, #IMF Senior Officer, #David Dinis). Nevertheless, there were obviously additional external factors that pushed the EU to embrace the values of the Washington Consensus. In particular, EU institutions had to face strong pressure from market actors with high stakes in the troubled region, which were worried about the risk of negative spill-overs (Lutz and Kranke 2014).

4.2. Dynamics of interactions

The picture outlined above results from the available literature and the few newspaper articles dealing with the interactions between national governments and Troika. Indeed interaction dynamics are difficult to disentangle, as the initiation and the negotiations of the programmes were not conducted openly. This opacity in the decision-making process may provide a misleading perception of the relationship between EU member countries and the Troika, which fully explains the reasons of the policy strategy pursued. It seems unlikely that industrialized and developed countries such as Ireland, Portugal and Greece could have accepted the Troika's prescriptions without exploiting the bargaining power, which resorts from their membership in the monetary union and the leverage at their disposal in the complex framework of the Euro area. Further information collected during interviews by several EC officers, a former Portuguese Minister, an IMF officer, a few scholars and David Dinis, the coauthor of the book *Resgatados*, which retraces the negotiations of the bailout, provided essential insights to understanding the dynamics which has led to the Portuguese bailout.

The missing information regarded the process of negotiation which preceded the formal request of financial assistance by the Portuguese government in April 2011. In this period, the Portuguese socialist government had the possibility to bargain with the EU actors, exploring possible alternatives to the bailout. The beginning of the "informal" negotiations coincided with the approval of the first Greek bailout, when countries such as Portugal, Spain and Italy were asked to implement the first austerity measures by the Eurogroup in May 2010 (Lourtie 2011, #David Dinis). At that time the economic crisis was rapidly spreading all over Europe and negative spill-overs were affecting several countries in the Euro area. Portugal managed to respond quickly to the Eurogroup's requests and to approve the first tough set of austerity measures a few days after the meeting, with the consent of the major opposition party. These measures helped to relax financial markets for a couple of months, and a period of relative calm followed. However, negative signals for Portugal were coming from international organizations, such as the IMF, whose director, Dominique Strauss-Kahn, expressed to Portuguese Prime Minister

José Socrates his concerns about the economic situation of Portugal,[20] and from the ECOFIN meeting and the Eurogroup, where European leaders started to push for a Portuguese bailout. In this period the Portuguese Government, and the Prime Minister above all, was trying to resist his partners' requests in an everlasting negotiation game. Every time external factors and spill-overs increased pressure on Portugal, the Government negotiated a pack of reforms in order to relax international concerns (#Portuguese Minister, #NovaEconomicsClub).

The problem was that after the bailout of Ireland in November 2010, Portugal was seen as the next in the pipeline and the whole international community was monitoring its economic situation. In January 2011 the Portuguese situation was getting worse and worse and the bonds could not be sold on international markets at a reasonable price. At this point it was clear that the Eurozone economic crisis was sharply aggravating and that the measures taken by the EU institutions could not keep the contagion effect under control. It was thus necessary to take frontloading measures to cope with the difficult Portuguese situation, but the possibility of a bailout could imply other negative spill-over effects and foster the spreading of the economic crisis (#DG ECFIN Portugal, #Portuguese Minister). These considerations, coupled with the resistance of the Portuguese Prime Minister, led the EU institutions to envisage the possibility of a "shadow" programme (#DG ECFIN Portugal, #David Dinis), by which the European Commission and the European Central Bank could assess the Portuguese economic imbalances, formulate a comprehensive programme of reforms in agreement with the Government and make national authorities fully accountable for this, avoiding the backlash of a formal bailout. Consequently, a few EC and ECB officers were sent to Lisbon to assess the national budget, the financial system as well as structural imbalances.

During negotiations, the bargaining power of the Portuguese Prime Minister *vis-à-vis* the Commission team was high due to the secrecy of the negotiations themselves: the Portuguese Prime Minister was in the position to veto several proposals and to push for specific reforms, as the introduction of Active Labour Market Policies in the Memorandum, or preventing low income earners (below 1,500 euros) to be subject to cuts in salaries, or limiting the privatizations (against the Troika proposals) (#Portuguese Minister, David Dinis). An agreement could be reached after three weeks of negotiations only with the direct intervention of the German Chancellor Angela Merkel, and, indirectly, of the President of the Commission Manuel Barroso (who was the intermediary between Angela Merkel and José Socrates) (#David Dinis). The German Chancellor ensured full support to Socrates' Government during the European Council, in order to rule out the

[20] David Dinis reports a conversation in July 2010 between Dominique Strauss-Kahn and Socrates. The Portuguese Prime Minister had asked to the director of the Fund to visit Lisbon in order to give a positive signal to the markets. However Strauss-Kahn refused the invitation explaining that it was a shared view that Portugal would not be able to regain market confidence and it would end up asking a bailout (Dinis and Coelho 2012).

possibility of a bailout, in exchange of his compliance with the Commission's team proposals. The programme contained also a non-written secret part, which consisted in a guarantee of financial help by the ECB with the aim to stop the climbing of debt. This was the type of safeguard that Socrates was waiting for (Dinis and Coelho 2012). Then the Government announced the agreed programme under the name of "Programa de Estabilidade e Crescimento" (PEC IV) and officially presented it at the European Council of 11th of March 2011. The European Council approved it, but this time the centre-right party Partido Social Democrata (PSD) of Pedro Passos Coelho refused to give its support[21]. Indeed, with the aggravating of the crisis Passos Coelho had, on the one hand, to respond to the pressure coming from its political party, and on the other hand to face the requests of the government.

With the presentation of the PEC, this political tension culminated. As the consensus basis of the Socrates Government had shrunk since the elections in 2009, due to the unpopular measures that it was proposing and implementing, the PSD foresaw the chance to gain broad political support in case of elections, and decided to withdraw its support to the Government. Then, the PEC IV was submitted to the approval of the Parliament, which rejected it, and Socrates' Government resigned. Nevertheless, José Socrates was still opposing the possibility of a bailout, even though the economic and political situation of the country did not leave much room for alternatives. At this point it seems that also the Commissioner Barroso, aware of the economic and financial troubles of his country, turned to push for a bailout. The intention to start a process of request of financial assistance was finally revealed by Texeira dos Santos, the Finance Minister, during a TV interview in April 2011 (Dinis and Coelho 2012, #Portuguese Minister). Then the IMF entered the negotiations within the Troika and the first official mission to Lisbon occurred in April 2011. The PEC IV constituted the basis for the agreement (being already the result of a process of negotiation with the EU institutions) and it was revised under the suggestion of the IMF team and extended over a three-year period.

However, this first programme has been criticized since it presented several gaps in the provisions of measures: the general targets were set, but no specific measures regarding how to reach them were included. Therefore, what was presented as Socrates Government's victory can also be considered the result of a quick negotiation process among many different actors (#David Dinis, #DG ECFIN Portugal).

On 5 July 2011 Pedro Passos Coelho became the Prime Minister and Vitor Gaspar, a former ECB officer, was appointed Finance Minister. This Government inherited the hard task of implementing the programmes and revising it in accordance with the Troika. After nine revisions and renegotiations of the

[21] Since 2009 Socrates Government had a minority support in Parliament and subsequently refused to form a coalition with the other left-wing parties.

agreement, the outcomes have been acknowledged to be quite unsatisfying[22] (Wise and Fontanella-Khan 2013). The Memorandum had to be adjusted mainly in relation to the fiscal consolidation part, partly because the recession worsened after 2011 and the country did not respond to the programme as the Troika expected. Moreover, domestic demand fell much more than expected, while exports performed better and total GDP was weaker. Less tax revenues than expected could be actually collected and the impact of retrenchment measures on the labour market and employment was surprisingly negative (#DG ECFIN Portugal, #Pedro Adao e Silva, #NovaEconomicsClub, #DG Employment).

It is interesting to notice that the first reforms implemented in the framework of the adjustment programmes did not encounter a sharp opposition from the social partners. This was probably due to the effective rhetoric discourse about the fact that Portugal has lived above its limits for long time and perhaps the Government was able to use the catalytic effect of the economic crisis to forge a consensus (#Portuguese Minister, #DG Employment). Nevertheless, the neoliberal reforms have not proven resilience in Portugal; two years after the agreement of the programme, the political support to the Government sharply decreased and the protagonist of the reform programme, Vitor Gaspar, had to resign in June 2013.[23] This situation further underlines the limit of the policy prescriptions of the Troika and the importance of the political consensus underpinning reforms (#Portuguese Minister, #Calca). Whereas Portugal became the "pupil" of the Troika and its Finance Minister was praised by the international lenders, he was also seen by many Portuguese as the face of deeply unpopular austerity measures.

Table 4 provides a timeline of interactions between the Portuguese Government and the other actors from May 2010 to April 2011, also suggesting some links between these interactions and the conditional approach by the European and International institutions.

The table shows that since the approval of the first bailout to Greece the interactions between the Portuguese Government, the EU institutions and member countries have gradually intensified, following the aggravating of the crisis. In particular, the Portuguese Prime Minister, José Socrates, found himself plunged in a complex web of interactions among the European Council, the Eurogroup, the EU member states and the European Commission, the European Central Bank and the IMF. In the period between May 2010 and the early 2011, the interactions occurred mainly within the European Council and bilaterally between Portugal and other EU member countries. Each time that the international pressure on Portugal increased, Socrates' Government—long with the consent of the main opposition party—either approved a new reform package or signalled austerity by approving tougher targets in the state budget.

[22] For a detailed assessment of the Programme for Portugal see Pisani-Ferry et al. 2013.

[23] In November 2011, 22 percent of Portuguese trusted the Government, whereas in May 2011 the trust in the Government in lowered to 10 percent (Eurobarometer).

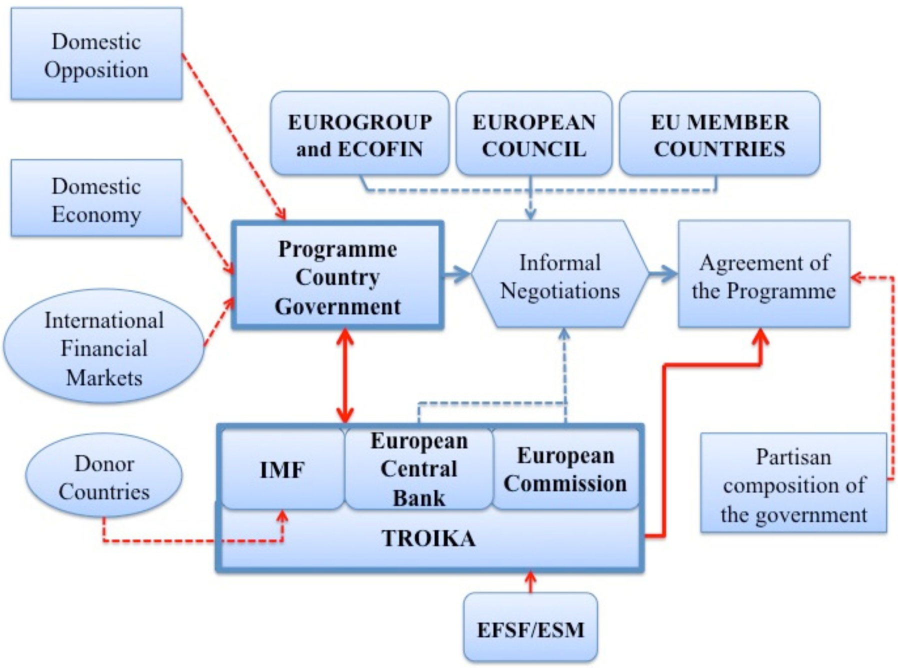
Table 4 • **Timeline of informal interactions leading to the approval of the programme for Portugal**

	Background factors	Informal interaction	Portuguese move	Effects
May 2010	Greek bailout	EU member countries invite Portugal and Spain to implement austerity measures	Portuguese Government approves PEC II	Period of apparent relative calm. Portuguese bonds' rates decrease
November 2010	Ireland request of a bailout		Approval of the budget for 2011 (the toughest in 30 years)	Portugal is seen as the next in line
December 2010	High market pressure	Core member states push for Portuguese bailout	Severe austerity measures implemented in Portugal	Portugal is given more time
January 2011		Secret trip of a Portuguese delegation to Berlin and Paris	Possibility of consultation between Portugal and EU institutions	Last chance for Portugal to avoid the bailout
February 2011		Meeting between Barroso and the Portuguese Prime Minister in Lisbon	Agreement on expenditure side measures (further cut of 0.8 percent of GDP)	A shadow programme is envisaged for Portugal instead of an official one
		Eurogroup meeting. Meeting between Socrates and Merkel	Socrates' declaration: willingness to take any necessary measure to avoid a bailout	
February-March 2011		EC and ECB teams in Lisbon. Tough negotiations. Socrates is received by Merkel in Berlin	Socrates directing the negotiations and resisting to the agreement	Socrates agrees to the three issues he was opposing in exchange of full support by Germany at the EU Council
March 2011		European Council. The shadow programme (PEC IV) is approved	Passos Coelho withdraws its support	Request of financial assistance
April-May 2011	International pressure to reach quickly an agreement to stabilize the Euro area	Troika in Lisbon for the negotiations	PEC IV is the basis for the Memorandum. Socrates Government resists and puts some safeguards	The programme does not include detailed measures. Safeguards on the expenditure cuts and labour reforms

Sources: Dinis and Coelho 2012, Lourtie 2011, Interviews

When pressure became unsustainable, after the Irish bailout, the EU institutions started to elaborate the shadow programme. Consequently, from January to March 2011, this large number of informal meetings led to the approval of the PEC IV. In this period José Socrates was able to use the leverage at his disposal to orient the negotiations and to put safeguards in the programme (see above). Finally, when the PEC IV was rejected in the Parliament, the Portuguese Government was pressured to ask for an official bailout. From that moment, the negotiations became public and the interactions occurred mainly at a formal level. After the 2011 elections, the change of Government and the endorsement of the neoliberal theories by the political elites weakened the substance of these interactions. The lack of sharp contrasts between the positions of the national Government and the Troika changed the nature of the interactions; convergent views between the two main actors smoothed the conflicts, thus resulting in an easier bargaining process.

Figure 4 • **Eurozone adjustment programmes: actors and interactions**



To conclude, Figure 4 provides a summary of the main findings concerning the dynamics of the elaboration of the programmes. The rectangles in bold at the centre of the figure identify the official actors involved in the negotiations: the programme country and the Troika. The other actors taking part (formally or informally) to the decision-making process are represented by the rounded rectangles, whereas the squares and the circles stand for the external and internal variables which affected the agreement of the programme. Different arrows denote the different nature of the interactions occurring among the actors: the red arrows represent the official interactions and the blue-dotted lines arrows represent the informal ones. The red-dotted arrows identify the influence of the external and internal variables on the choices of the actors. The figure also shows that the process of agreement of the programme for Portugal included an intermediate stage constituted by the informal negotiations, which was not foreseen in previous IMF programmes. Whereas there are external and internal variables (Domestic Opposition, Domestic Economy, International Financial Markets and Donor Countries) which interfered in the process of negotiations, Portugal was able to benefit of this informal stage and elaborate a "shadow programme" in order to cope with its economic imbalances. In this way, the country received a preferential treatment from EU institutions, which gave the Socrates' Government a last chance to avoid a formal bailout.

CONCLUSIONS

The comparison between IMF's financial assistance programmes and Eurozone rescue packages has proven to be useful for understanding the key elements of the programmes adopted during the recent sovereign crisis in Europe. It has been observed that Eurozone programmes are modelled on the IMF template and follow the same technical steps for the formulation and implementation. Indeed, the EAPs are the conditions on loans, overseen by the IMF, ECB and European Commission. Rigid conditions were considered necessary to avoid moral hazard, thus the loans had to be accompanied by a comprehensive set of reforms aimed at changing countries' economic trajectory and eliminating structural weaknesses. Moreover, Williamson's prescriptions remained valid for the Eurozone countries.

The implementation of this kind of reforms testified the remarkable resilience of the neoliberal prescriptions of the Washington Consensus. In 2010 what Williamson identified with "Washington" was represented by the core EU countries led by Germany, which started to promote these recipes and to channel them into the peripheral countries with the policy tool of the conditional lending. This new/old Consensus has been institutionalized at two levels: within the Troika technical team enforcing neo-liberal measures in the programme countries and within the governments which agreed to adopt the measures. About the resilience of Washington Consensus, Sarah Babb (2012) argues that when international organizations are involved in a specific context, they play a role in the diffusion of paradigms: "At the national level, the paradigms are brought to the power through the domestic political processes that institutionalize particular goals and policy practices within government bureaucracies. Yet, influencing the outcome of these domestic processes are organizations with transnational power and with paradigms of their own, which shape governments' behaviour" (p. 274).

As presented above, the economic adjustment programmes are the result of a complex interaction process between international and domestic political actors and conditions. The Eurozone programmes are unprecedented for the nature of the problems that they addressed—i.e. open and mature economies adjusting within a monetary union—and for the form of cooperation which is in charge of the adjustment. In this setting the Eurozone programme countries have enjoyed significant bargaining power *vis-à-vis* the lending institutions. The formulation of the programmes was affected by the strong interdependence of economies belonging to a monetary union and, thus, by the concerns regarding the stability of the whole Euro area. Moreover, the tripartite nature of Troika, directly accountable to the member states, made negotiations over the programme even more complex. As it has been stated, the opacity of the interactions between the main actors in Europe may lead to a misleading perception of the dynamics underpinning the agreement on financial assistance packages. Further analysis revealed that national governments, or at least the Portuguese Government, had the possibility to bargain (formally or informally) with the Troika the conditions for its bailout.

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