

CHAPTER I

INTRODUCTION

A. Background

This thesis attempts to investigate the intervention of Troika¹ in Portugal financial crisis by conducting the Schema of structural Adjustment Program. Here the writer analysis Portugal government's decision to exit from the troika schema of Structural Adjustment Program, There must be certain factors why Portugal Government given policy about the exit from Troika schema.

The biggest economic crisis is currently attacking in the Eurozone countries, which are experiencing a decline and causing of the financial crisis. Portugal is one of the European Union member state and also a Eurozone country experiencing a financial crisis and receiving the financial assistance of the IMF and EU (Troika) after Greece and Ireland. Portugal is now experiencing the worst recession since the early 1970s. The unemployment rate reaches over 15% and the financial balance of the Portuguese government experiences bankruptcy as a result of too much state budget deficit reaching 12% and also has the debt ratio reaching 108% of GDP US \$ 248.98 billion in 2011. On the other hand, the EU Monetary Authority has

¹ Troika originally refers to the Russian word for a carriage with three horses, but can be used to describe any type of collaboration of three. But In the context of the European crisis, the Troika is the collaboration or corporatin of the three institutions that includes: the European Commission (EC), the European Central Bank (ECB), and the International Monetary Fund (IMF). Basically, what the Troika does is monitoring countries in severe economic trouble that are receiving financial loans provided for by the EU and the IMF. These loans, although they have a lower interest rate than the ones on the capital market, are hardly meant to help the economies of suffering countries to recover. Troika watch. "what is troika" <http://www.troikawatch.net/what-is-the-troika/> access October,08 2015

arranged that the debt ratio in the euro zone countries should not be above 60% of GDP and a deficit in each country should not be above 3% of GDP.² This condition that led to the financial crisis and the impact on the country's banking crisis. The result of economic decline in Portugal cause an increase in unemployment, tax, wage cuts, the revocation of pensions, financial crisis also cause Portugal suffer great lost of affordable market access at the time of bond payment..

In addition, the fall of Portugal's economy and liquidity crisis in the banking system affect the decrease in the exchange rate against foreign currencies Euro. Portugal's economy collapse is a spiral, which means one factor influence in other factors. It shows that the balance of domestic (household level), the balance sheet of companies / banks (corporate level), and the balance of government (country level) relate to each other. This will cause damage to the balance of banking and government.

The various policies have been issued by the Portuguese government to tackle the financial crisis. One of them is asking for financial assistance to IMF and the European Union. Since Portugal is one of the European Union member state and also a Eurozone country. a delay in resolving the debt crisis in Eurozone country especially in Portugal is able to drag economic recession not only in Europe, but also worldwide. Therefore European Union as a regional organization in stabilizing the economy in the member states with international financial

²Government Annual Surplus or Deficit. <http://www.bbc.co.uk/news/business-13366011>, diakses tanggal 16 Oktober 2015, Pukul : 22.04 WIB

institutions like the International Monetary Fund (IMF) adopted stringent austerity measures and economic reforms.

In resolving the economic crisis, International Monetary Fund (IMF) as an international financial institution established under the Bretton Woods System in 1944, provides loans to countries which are experiencing severe economic problems, such as Mexico experiencing financial difficulties in the 1980s and when the economic and monetary crisis hit Southeast Asia in 1997. In economic crisis in the Eurozone, IMF was involved in providing assistance by lending money to European countries in crisis. The target of IMF in resolving the crisis in European countries are reducing deficits and restructuring state finances which are in crisis.³ In resolving the crisis in the European Union countries, IMF corporates with the institutions of the European Union such as European Commission, and European Central Bank and a corporation called TROIKA. Basically TROIKA is monitoring countries in severe economic problems that are receiving financial loans provided for by the EU and the IMF.⁴ These loans, although they have a lower interest rate than the ones on the capital market, are hardly meant to help the economies of suffering countries to recover.⁵

The effort of Troika to overcome the economic crisis in Portugal b giving financial assistance amount 78 billion euro in 2011. After Portugal government made a formal request to Troika for financial assistance, Troika gave a financial

³Chibber, K. (2015, October 5). "Who are the troika that Greece depends on?" Retrieved from www.bbc.com: <http://www.bbc.com/news/business-15149626>

⁴Troika watch. "what is troika" <http://www.troikawatch.net/what-is-the-troika/> access 07, October 2015

⁵ ibid

assistance program, Structural Adjustment Program (SAP)⁶, in which Portugal government should implement this program. The program concerns four separate areas: [1]. Fiscal policy aimed at reducing public debt and deficit; [2] structural reform to streamline the public sector; [3] financial and cooperate sector policies aimed at protecting the financial system amidst deleveraging; and [4] structural reform to enhance competitiveness and rebalance growth from the non-tradable to the tradable sector.⁷ This program is requested by Troika to Portugal to receive financial assistance. This requirement is given to ensure that the assistance given by Troika used in accordance with the objectives of the Troika. The purpose of SAPs is to reduce fiscal imbalances in countries that receive assistance by making these countries become more market - oriented and concentrate on trade and production, so as to improve the economy quickly.⁸

After receiving a conditional loan from IMF and EU in dealing with financial crisis, the finance minister Gaspar Vistor to made sure that the government had raised income taxes on average, from 9.8% to 13.2%. Gaspar also announced cutting state spending by 2.7 billion euros. It impacted on the reduction of 2 percent of the 600,000 public sector workers. This policy to make savings by reducing the state budget, it is to comply with the standard deficit from Eurozone

⁶ Structural Adjustment Programmes (SAPs) are economic policies for developing countries that have been promoted by the World Bank and International Monetary Fund (IMF) since the early 1980s by the provision of loans conditional on the adoption of such policies. Source; who.com Structural Adjustment Programmes (SAPs) <http://www.who.int/trade/glossary/story084/en/> access March 2, 2016

⁷Pisani-Ferry, J., Wolff, G. B., & Sapir, A. (2013). EU-IMF assistance to euro area countries: an early assessment. Bruegel Blueprint [No. 19?], 16 May 2013.

⁸Greenberg, James B. A Political Ecology of Structural-Adjustment Policies: The Case of the Dominican Republic. Culture & Agriculture. 1983. Hlm. 85-93

average, that is maximum of 3% of Gross Domestic Product (GDP). According to an economist, quoted by Reuters news, agency of the government's austerity program that included a reduction in retirement benefits, the taxation of financial transactions and the increase in property taxes - could push Portugal into recession cycle as experienced by Greece.

Three years after Portugal was forced to impose austerity and re-structural program in exchange for a €78bn bailout package, the intervention of Troika got resistance from the public and also had an impact on the political in Portugal government. The citizens felt the country's social system was left in shambles. In an effort to balance the Portuguese budget, the government cut spending to wages, pensions, health care and education.⁹ Finally in May 17,2014 Portugal decided to exit from its three-year 78-billion-euro bailout this month without a precautionary credit line, as the country returns to growth after years of painful austerity and unpopular reforms. Portuguese decision to exit from schema Troika was made in the meeting of the cabinet after it passed the bailout end audit by experts EU - IMF. This decision closes an important part of a bailout of 78 billion euros for the three-year rescue, as stated by Portugal Prime Minister;

⁹euroviews Troika policy in Portugal: a trilogy of austerity, sorrow and social upheaval
<http://www.euroviews.eu/2014/2014/04/30/troika-policy-in-portugal-a-trilogy-of-austerity-sorrow-and-social-upheaval/#sthash.sDfgFfp6.oGTWkBoT.dpuf> access March 11, 2016

“The government has decided to exit the assistance program without turning to any kind of precautionary program,” (Prime Minister Pedro Passos Coelho)¹⁰

Pedro said, flanked by his entire government which met on Sunday to make the decision.¹¹ In addition, after the exit of a schema Troika, Portugal decision makers still impose the latest round of heavy steps to keep finances and try to be self-financing in the bond market without a safety net.

Here the writer wants to analyze the intervention of Troika to give financial assistance to Portugal financial crisis by conducting financial assistance program called Structural Adjustment Program (SAP). However Portugal decided to exit from the Troika scheme program in 2014 and rejected the further bailout. While the debt ratio that owned by Portugal are still rising and the growth of the economy has not fully recovered. Therefore here the author more focuses on the analysis the reason why the Portugal exit the Troika schema SAP and reject the bailout again.

B. Research Question

From the background that is explained before, the formula of the research question is “Why did the Portugal exit from the Troika bailout schema?”

¹⁰Reuters news may 2014 “Portugal decides on 'clean exit' from bailout”
<http://www.reuters.com/article/us-portugal-bailout-idUSBREA4309H20140504>access February 5, 2016
17:40

¹¹Ibid.,

C. Theoretical framework

Theory Two-Level Game

To answer the formulation of the problem above, the writer uses the theory in analyzing the formulation of the problem. The theory is the work describes what is happening, explaining what happened and may also foresee the possibility of recurrence in the future,¹² while the concept is an abstraction that represents an object.¹³

Portuguese government policy by asking the help of the Troika in dealing with the financial crisis, received pressure from the public resistance that ultimately made the decision to exit the schema troika. Problems exit of Portugal to the Troika's schema can be studied by the theory of policymaking Two-level game by Robert Putnam Two-level game (Robert Putnam)

Robert Putnam introduces a metaphor: "two-level game" to understand the relationship of domestic politics and International relations played by the decision maker. These decision makers could be president, the leader of the coalition parties, the finance minister, or prime minister called chief negotiators.

In the book of Diplomacy and Domestic Politics: The Logic of Two-Level Game, Putnam describes that there are domestic factors influencing the foreign policy of a country, and Putnam exemplifies how important of seeing domestic factors in foreign economic policy

¹²Mohtar Mas' oed, Ilmu Hubungan Internasional Disiplinan Metodologi, jakarta, LP3ES, 1990 p 185

¹³ Ibid., p 93

“The main purpose of all strategies of foreign economy policy is to make domestic policies compatible with the international political economy.” (Robert Putnam)¹⁴

An important point of this is where the "central decision-makers" (state) should pay attention simultaneously between domestic and international pressure. The position of government or decision maker is in the second game. Across the table sat on the international foreign colleagues, and on its side sat diplomats and other international advisers. Around the domestic table behind him sat notable figures of the party and parliament, statesman for domestic agencies, representatives of major interest groups, and his own political advisors. A simple description of "two-level game" is, a policy decision that sits in between two board games, which is one domestic and one international.

The metaphor of domestic-international reaction;¹⁵

1. In the national level, there is a process in which domestic groups fight for their interests by pressuring the government to adopt policies favorable. Politicians seek strength by means of a coalition between groups.
2. In the international level, there is a process in which the government of maximizing its ability to satisfy pressure groups before, and to minimize losses of foreign relations. So, the task of the government or the decision

¹⁴R. D. Putnam, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, *International Organization*, Vol. 42, No. 3 (Summer, 1988), pp432-433

¹⁵ *Ibid.*, R. D. Putnam, *Diplomacy and Domestic Politics*:

makers here is to secure the country in the international field, and to secure his political future in the country.

Based on the research question, the writer analysis the case by using the theory of two-level game by Robert Putnam, the case is Portugal financial crisis in which the government try to search assistance to get out from the crisis, by negotiating with EU and the IMF (Troika). However, there are disagreements from the society on the Government ways taken in the Troika intervention to this economic crisis, due to economic policies that rely heavily on foreign capital and debt funds and conditions that occur with increasing unemployment in Portugal. In this two-level game theory, the writer sees that the government should be able to play a "two-level game 'in foreign policy. At the domestic level, the government should be able to realize aspirations and accommodate domestic needs. While at the international level, the government should try to meet domestic needs as well as to minimize the consequences that could have an impact on the country.

“The politics of many international negotiations can usefully beconceived as a two level game. At naional level, domestic rous pursuetheir interest by pressuring the government to adopt favorable policies,and politicians seek power by conructing coalition among those groups.At the international level, national governments seek to maximize their own ability to satisfy domestic pressures, while minimizing the adverseconsequences of foreign developments.”(Robert Putnam)¹⁶

¹⁶Ibid., R. D. Putnam, pp. 435-442

Here, Putnam states about how to run the two-way relationship. A decision maker (head of state) should be able to run two games, namely domestic and international, and win both of which are the result of the Two-level game.¹⁷ In the theory, there are two concepts, namely;¹⁸The first is acceptability Set (platforms reception) is a level of agreement that can be reached and won by decision makers / negotiator. The result at the the concept is a temporary agreement (signed). And the second is a win-set. Its an agreement that has been reached and are considered by negotiators (already gaining from the negotiation process). This concept will measure why the Portuguese decided to exit from Troika's schema and whether the government succeedin running the two-level game. the conceptual win-set in the decision made by the Government Portugal to the Troika. Where the head of government that represent nations, or a representative of labor or management, or the party leader in the multi-party coalition, or the finance minister who negotiated with the IMF team, or the leader of the council-Senate conference committee, or leaders of ethnic groups in a democratic society.

¹⁷ Ibid.,

¹⁸ N. Pamuji, & H. Rais, PolitikKerjasamaInternasional: SebuahPengantar, Institute of International Studies: UniversitasGadjahMada, Yogyakarta, 2011, pp.33-41

D. Hypothesis

The Portugal exited from the Troika schema Structural Adjustment Program in 2014. Because; first, the economic growth in Portugal was improve since the implement of bailout program, so that Portugal financially able to disbursements in Troika, and second, there are political pressure from the society to exit from the schema bailout.

E. Purpose of Research

According to the research question above, this research proposal has certain purposes there are;

1. To know the cause of the economic crisis in European countries, especially Portugal
2. To Know how the Portugal government to overcome the financial crisis
3. To investigate the reason why of Portugal exited from the Troika's Schema

F. Coverage of Research

In coverage of the study the writer focused on intervention of Troika in portugal financial crisis on 2011-2014. The purpose of research coverage is intended to make is easer to analyze and morefocuse in the writing

G. Methodology of Research

a. Type of research

Here the writer uses explanation method, because through the research the author wants to explain why Portugal drcided to exit from the Troika's schema in resolving the financial crisis in 2011-2014

b. Method of collecting data

In collecting data the author uses library research which means that the source will come from books and journals to get some theories related to this study case and to make the hypothesis.

c. Method of analysis data

In analyzing data the author uses qualitative which means that the author used second data as the source of the research.

H. Systematical Writing

The systematic writing of this research is arranged as follow: in first chapter contains background, research question, purpose of research, theoretical framework, hypothesis, method of research, and systematical writing. Second chapter Contains about Portugal financial crisis, in this will be explain short profile of the Portugal country, the economic condition in Portugal before experiencing the debt crisis, and also Portugal and Troika's relations. Third, Contains about the troika efforts to overcome Portugal financial crisis the intervention of Troika in Portugal financial crisis, in this chapter will discuss Structural Adjustment Program that conduct by Troika and analysis the involvement of Portugal government in negotiation agreement of Structural Adjustment Program. Four, contains about the decision of Portugal to leave from the schema of troika, in here the author will mention the hypothesis where decision to exit from Troika's schema with involving actors bureaucracy and interest groups are pressing the government to leave the schema troika. And last is conclusion.