



## Product specialisation and global competition: Portugal's path to crisis

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Abstract

A widely held view in economics and comparative capitalism states that the crisis in the eurozone was a crisis of labour cost competitiveness. This view maintains that a divergence in Unit Labour Costs engendered a cleavage between the euro area’s core and periphery. Critics have disputed this and drawn attention to product and export specialisation, along with global competition, rather than intra-European competition. To make progress on this agenda, this article focuses on structures of production as a source of crisis vulnerability. It advances the notion that specific counties have unique forms of articulation within global capitalism, and that this matters to understanding crises. Focusing on the Portuguese case, it asks if competition from China and other low-wage economies caused an erosion of manufacturing and a resulting deterioration of the external accounts. It concludes that Portugal’s current account deficit developed in the context of deindustrialisation and industrial recomposition followed by a generalised stagnation in virtually all manufacturing sectors. By stressing changing industrial patterns, the article provides a more concrete analysis of production than most accounts of the crisis in the eurozone.

Wordcount: 7951

**Keywords:** eurozone, European integration; core-periphery; crisis; current account imbalances; financialisation; deindustrialisation; product specialisation; competition; unit labour costs

## 1. Introduction

The Global Financial Crisis (GFC) may have been global in scope, but its manifestations varied according to individual countries' articulation within the world economy. Major channels of transmission included trade and financial flows (Akyüz and Paolo 2017; Ghosh 2009). Portugal was vulnerable due to large payment imbalances and was first hit when the banks faced difficulties in accessing finance on international wholesales markets from 2008 (Bank of Portugal 2009; Lagoa et al. 2014; p.102; Jurek and Marszalek 2014, p.21). The initial phase of crisis management witnessed counter-cyclical policies and generous transfers to finance under the European Union's (EU) coordination (Costa and Castro Caldas 2014). Subsequently, the GFC mutated into a 'sovereign debt crisis' (McNally 2021), and the Portuguese state was next to be shut out of international financial markets. A political crisis intertwined with fierce pressure from domestic and international financial institutions, and Portugal became the third eurozone country to request a bailout from the 'Troika' of the International Monetary Fund (IMF), European Commission (EC) and European Central Bank (ECB) in April 2011. The bailout was conditional on a structural adjustment programme which deepened austerity and opened the door to an unprecedented neoliberal restructuring. The programme interfered with health, education, housing, state-owned enterprises, the labour market, social protection, and the legal system (Costa and Castro Caldas 2014; Hermann 2014; Hespanha et al. 2014; Author 2021). After a recovery with almost 2% growth in 2010, Portugal fell back into recession and returned to growth only in 2014 (World Bank 2020a).

It is now widely agreed that peripheral eurozone countries' vulnerability stemmed from their large current account deficits and dependence on capital inflows. This made them vulnerable

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to a ‘sudden stop’. Consequently, scholars in economics and comparative capitalism (CC) have devoted their attention to explaining how these imbalances developed. A commonly held view in economics states that the imbalances resulted from a divergence in Unit Labour Costs (ULC) between core and peripheral countries (Blanchard 2007; ECB 2012; IMF 2011; Arestis et al. 2013; Pérez-Caldentey and Vernengo 2012; Lapavitsas 2019; Lapavitsas et al. 2012). The varieties of capitalism (VoC) approach replicate this view but focuses on institutional factors (Hall 2012; 2014; 2018) whilst the growth model perspective sees ULCs as a determinant of export performance either in general or among *some* countries (Baccaro and Pontussen 2016; Baccaro and Tober 2021; Stockhammer 2016). A different, albeit partly overlapping view maintains that the crisis (and indeed the failure to resolve it) are results of the eurozone’s ‘flawed institutional design’ (Arestis and Sawyer, 2011; Arestis et al., 2013; Botta 2014; De Grauwe 2010; Lavoie 2015). The institutional design view has provided critical insights into the EMU’s inadequate crisis management; yet, it is not the focus of the present paper, since it has already been critically interrogated with reference to the Portuguese case (Author 2021). Whilst the political and methodological differences between mainstream and heterodox interpretations should not be understated, Storm and Naastepad (2015a, pp.959, 965) have pointed out that analyses from both strands in economics share a logic that revolves around ULC (hereafter referred to as the ULC view). The ULC view has underpinned painful labour market reforms imposed by the Troika, as well as labour legislation that national governments are currently introducing in the name of “competitiveness”, within a post-bailout context.

In our view, there is still scope for a much greater sensitivity to singularity when accounting for crisis vulnerabilities. Much of the literature in economics and CC focuses on what crisis ridden countries had in common. In the search for commonalities, unique historic and economic factors are often ignored. This article shows that detailed empirical case-based

research can provide insights that challenge the dominant crisis diagnosis (and indeed the solutions that follow). Although the eurozone crisis started over a decade ago, it is crucial to gain a more refined understanding of its causes. The imbalances that made peripheral countries vulnerable could re-emerge, and moreover, the efforts to build back from the Covid-19 pandemic need to be informed by a context specific understanding of trade, global competition and industrial development.

The article shows that production matters to understanding the crisis in the eurozone. In international political economy it is widely known that ‘globalisation’ has been constituted by a new division of labour engendered by an expansion of world trade and internationalisation of production driven by global value chains and production networks (Charnock and Starosta 2016; Oatley 2019; McGrew 2018). Yet, the *global* economy does not provide the main context for most analyses of the euro crisis. This article draws attention to the interaction between Portugal’s pattern of product specialisation and the country’s place within the global division of labour. It is inspired by studies that approach European integration and the crisis from a historical materialist perspective (Bieler et al. 2019; Poulantzas 1978; Romão 1982; Serfati 2016). Its main contribution is to build on the literature that rejects the ULC view (Storm and Naastepad 2015a; Felipe and Kumar 2011). This approach holds that ULCs were largely irrelevant and that the eurozone’s periphery’s main vulnerability was its product specialisation and competition from China. This approach has highlighted the centrality of production. Yet it is based on aggregate indexes for product specialisation. This is a crucial starting point, but it is necessary to complement their findings with more detailed qualitative analysis of structures of production and their interaction with competitive dynamics in the world economy, based on case study research.

This article provides a single case study of the Portuguese case. Some of the questions that guide the analysis are: What does Portugal produce and export? Which countries compete in

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these sectors? Did Portugal’s export specialisation and exposure to competition from China and low-wage economies cause the imbalances? The article draws on trade data from the United Nations Statistical Division (UNSD) Commodity Trade (UN Comtrade) database which is available through World Integrated Trade Solution (WITS) and on production data from Eurostat and OECD. The data shows that Portugal’s traditional low-tech industries were indeed in decline in the 2000s, faced with competition from China and Central and Eastern Europe. In fact, these industries were in decline already in the 1990s, but initially, their decline was accompanied by a rise of other manufacturing sectors. While the article rejects the ULC view, wage differentials across countries played a role in the Portuguese path towards crisis. The article concludes that Portugal’s trade deficit must be understood in the context of deindustrialisation and industrial recomposition followed by a generalised stagnation in virtually all manufacturing sectors.

The article is structured as follows. Section two reviews the dominant interpretations of the crisis in the eurozone. Section three presents a series of critiques of the ULC view of the eurozone’s imbalances. Section four presents a case study of Portugal with a focus on the structure of production, exports and competition. Section five concludes.

**2. Unit Labour Costs in theory and practice**

ULCs can be defined as the ratio of a worker’s total compensation to labour productivity, or as the total labour costs per output produced. Labour costs includes not only wages, but also fringe benefits, severance pay, wages in kind, social security, pension contributions and life insurance (Felipe and Kumar 2014, p.491; Frumkin 2006, p.251; OECD 2021). Productivity refers to the number of units produced, e.g. pencils, litres of milk, or cars. At firm level, ULCs can be derived by dividing total labour costs by the number of outputs produced. For

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3 firms, ULCs are important since labour costs represent a significant part of production costs.  
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5 Savings made can be channelled into investments or more dividends may be transferred to  
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7 shareholders (Yamarone 2017, pp. 253-255). At the national level, many products are  
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9 produced, and it is impossible to derive ULCs by dividing labour costs on the number of  
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11 outputs (carrots, pencils etc). Therefore, at the aggregate level, output refers to the economy's  
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13 value added. ULCs are calculated as the ratio of labour compensation to real GDP. ULC data  
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15 usually shows the percentage change from the previous year, and it tends to be expressed  
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17 with reference to a base year. In discussions about competitiveness, authors often refer to  
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19 relative ULC (RULC) where the ULCs of a given country are divided by the ULCs in a base  
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21 country (often Germany) (Felipe and Kumar 2014, p.483-491; Frumkin 2006, pp.251-252;  
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23 OECD 2007; Powell 2013, p.65).

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29 When the eurozone crisis hit Greece, fiscal profligacy and national policy errors were seen as  
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31 the main cause of the turmoil. Mainstream institutions were concerned with problems in the  
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33 public sector, and the public deficit and debt were heavily scrutinised (European Commission  
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35 2010; IMF 2009). The focus on states that had 'spent beyond their means' has been a  
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37 powerful narrative and in the context of the Covid-19 pandemic, fiscal prudence has  
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39 continued to be a source of tension among EMU members (Khan 2020). It provided the  
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41 theoretical foundation for austerity, and for the eurozone's tightening grip on member  
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43 countries' fiscal policy in the aftermath of the GFC. As the eurozone crisis evolved within  
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45 and beyond Greece and spread to countries with fiscal surpluses prior to 2007-8 (i.e. Spain  
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47 and Ireland), private sector competitiveness figured with increasing prominence. The Twin-  
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49 Deficit-Hypothesis focuses on the parallel existence of large budget deficits and current  
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51 account imbalances (Mavroudeas and Paitaridis 2015). In this diagnosis, ULCs are central.  
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53 For example, an ECB paper (2012, p.5) identifies that '[t]he onset of the financial crisis in  
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55 2008 has highlighted the problems of diverging external imbalances within ...[EMU] and the  
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role of persistent losses in competitiveness'. The problem was that wages rose faster than productivity, translating into higher ULCs (ECB 2012, p.6).

A focus on ULC spans mainstream and heterodox literature in economics and CC. Storm and Naastepad (2015a, p.959) point out how '[t]he dominant view both on the mainstream right and on the left, holds that the eurozone crisis is a crisis of labor-cost competitiveness—with trade imbalances ... being driven by divergences in relative unit labor costs ... between surplus and deficit countries'. In the Portuguese case, this view was advanced before the GFC. Blanchard (2007, p.4) argued that from the mid-1990s, a weakening competitiveness (defined as 'the inverse of unit labor costs relative to those in in the euro area') damaged the current account. A boom in private consumption and investment was accompanied by nominal wage increases and these exceeded productivity growth. Consequently, ULCs rose. The boom turned into stagnation in the early 2000s, but RULC continued to increase (Blanchard 2007, pp.4-6). Blanchard proposed that the way to correct the imbalances is through 'competitive disinflation' – a period where high unemployment leads to a decline in RULCs and an improved current account position. He held that 'a decrease in nominal wages sounds exotic, but it is the same in essence as a successful devaluation'. He warned that the adjustment would be 'long and painful' (Blanchard 2007, pp. 7, 13, 20). At the domestic policy level, the finance minister who negotiated Portugal's entry into the ERM in 1992, Jorge Braga de Macedo, subscribes to the Twin-Deficit-Hypothesis:

The entry level is always difficult ... The idea of getting a different [exchange rate] level was not realistic. What is correct, however, is that once you enter, you need appropriate policies with respect to wages and budgets. The opposite happened. Wages increased in Portugal far more than in any other country in the eurozone (Interview, Braga de Macedo 2014).<sup>i</sup>

In practice, the mainstream's ULC crisis diagnosis had powerful consequences in the world of labour. It provided the theoretical foundation for the strategy of internal devaluation. The



Portuguese structural adjustment programme included an ambitious set of labour market policies. The MoU froze the minimum wage at €485 per month, and a striking attempt to dismantle the system of collective bargaining was justified in the name of external competitiveness (IMF 2011).

Post-Keynesian and Marxist analyses have made tremendous contributions to the field; by scrutinising the trade and financial relationships between the core and peripheral eurozone countries they have overcome methodological nationalism. They have advanced a relational account of the crisis. They have dismissed the fiscal profligacy thesis and seek to explain the current account imbalances between the eurozone's core and the periphery (Arestis et al. 2013; Botta 2014; Bibow 2013; Cesaratto 2015, Blankenberg et al. 2013; Lapavitsas et al. 2012; 2019; Pérez-Caldentey and Vernengo 2012). Yet, many of them share the analytical focus that has justified internal devaluation, namely the focus on ULCs. Post-Keynesians and Marxists have different emphasis (a 'mercantilist' project pursued by the core, versus world money, imperialism and class) but share important similarities. In both accounts, the trade surpluses of the core and the deficits of the periphery are two sides of the same story. Regarding Portugal, Reis (2014) states as follows:

Portugal was one of the peripheral economies which, since the preparation for the euro, registered a prolonged stagnation, with continuous current account deficits, leading to a high external indebtedness. Peripheral deficits are linked to the surpluses of the core and these fuel the corresponding financial capital's recycling processes through credit to deficit countries (Reis 2014, p.12).

In the heterodox variation of the ULC view, the euro is at the heart of the imbalances. It was the 'original sin' that led to the crisis (Cesaratto 2015, p.152) because it fixed the exchange rate (Arestis et al. 2013, p.24). Peripheral countries entered at a high exchange rate and lost competitiveness from the onset (Lapavitsas et al. 2010, p.6). Subsequently, they were left

with no scope for devaluation except through internal deflation (Arestis et al. 2013, p.24). Post-Keynesians hold that the euro was established in the context of a ‘neo-mercantilist’ or export-led-growth strategy pursued by core countries (Cesaratto 2015; Bellofiore, Garibaldi and Halevi 2011; Pérez-Caldentey and Vernengo 2012; Stockhammer 2016). It was based on a policy of wage moderation where ULCs in the core were kept constant to enhance competitiveness. In the periphery ULCs increased, and the net result was a real exchange appreciation (Pérez-Caldentey and Vernengo 2012). Bibow (2013, p.360) states that the current account imbalances ‘ultimately go back to competitive wage restraint on Germany’s part since the late 1990s’. Similarly, Lapavistas et al. (2010, pp.326-337) maintain that the EMU was a race-to-the bottom with regards to wages and labour conditions, and that this race was won by Germany.

CC literature has much in common with heterodox economics and also tries to explain the current account imbalances. Many CC scholars have a similar view of competitiveness in the context of monetary integration to that of heterodox economics and see the crisis as one of external price – and indeed labour cost competitiveness (Hall 2012; 2014; 2018; Hancké 2013; Stockhammer 2016). In the traditional VoC view, coordinated market economies such as Germany compete on quality and skills rather than price (Hall and Soskice 2001, p.42). Its more recent formulations however, attribute importance to price and labour costs when accounting for export success and failure. The coordinated wage bargaining system stands out as a guarantor of wage repression and hence falling or stagnant ULCs in the North. The South on the other hand, lost the capacity to devalue, and its “fractious” union movement precluded wage discipline. Thus, due to their respective institutional arrangements, the EMU suited Northern economies’ export-led model but not the Southern demand-led growth model (Hall 2012; cf. Hancké 2013). The institutional setup also explains differences in skills regimes, vocational training, innovation and research (Hall 2012; 2014; 2018). The

Keynes and Kalecki inspired Growth Model perspective sees financialisation as a major factor behind the imbalances, but also attributes importance to ULCs when accounting for the complimentary relationship between demand-led and export-led growth models (Stockhammer 2016). Baccaro and Benassi (2017) hold that German exports are price sensitive, and some sectors increasingly so, but that overall export prices are more important than RULC. Recently, Baccaro and Tober (2021) have argued that wages determined export performance in the German case, but not in other countries. Still, higher wages in Germany might ‘rebalance’ the eurozone.

In sum, while the heterodoxy does not concur with savage wage cut, but instead propose deeper EMU integration and reform, wage increases in core countries, or that crisis ridden countries should break out of the EMU, a core element of their analysis tends to replicate mainstream accounts. ULCs or export prices stands out as a root cause of uneven competitiveness, and wage repression the sole cause of Germany’s competitiveness (Storm and Naastepad 2015a, p.965). While mainstream economics sees Germany as the example to be followed, the heterodoxy turns the problem upside down and sees it as the source of the periphery’s problems.

### 3. Bringing in the role of product specialisation

There are longstanding critiques of ULC as a measure of competitiveness (Felipe and Kumar 2011; 2014; Myant 2016). The critiques include methodological, historical and logical inconsistencies. Firstly, some have pointed to the problems with calculating ULCs at the aggregate level rather than firm level. Since the national economy produces many goods and services, aggregate ULCs are effectively a ‘unitless magnitude’ (Felipe and Kumar 2014). Second, the ULC argument does not focus on actual labour costs and production levels, but

rather the *rate of change* of the ratio between the two. Usually, the period analysed goes back to the mid-1990s, thus the historical trajectory of the current account and its relationship to ULC remain unexplained. Third, historical evidence shows that following World War Two, countries with the strongest reduction in price competitiveness were those whose market share increased the most (Felipe and Kumar 2014, p.498). This puts into question the use of ULC as a proxy for competitiveness. Fourth, the ULC argument assumes that labour costs are the only costs that determine export competitiveness. As noted by Storm and Naastepad (2015a, p.966) ‘[w]hat matters in international competition is the ‘gross output price’ of a product or service—the full (national accounts) price, which includes the costs of intermediate inputs and labor as well as a profit margin’. In this vein, Felipe and Kumar (2011, p.27) propose that ULC should be complemented by a measure of unit capital costs (UCC), since profits can also be at the detriment of competitiveness. In twelve eurozone countries, Portugal included, UCC increased faster than ULC. Storm and Naastepad (2015a, p.966) show that exports from Southern European economies are not sensitive to RULC, which ‘did not affect trade balances of Greece and Portugal in a statistically significant manner’ (cf. Storm and Naastepad 2015b; Storm and Naastepad 2015c, p.845). RULC account for 0.7% of the Spanish trade deficit and 7.9% of the Italian. The authors conclude that ‘[t]he bottom line is that RULCs are basically irrelevant’ (Storm and Naastepad 2015a, p.966).

Fifth, the ULC argument rests on the assumption that peripheral countries are in direct competition with Germany. As Smith (2016, p.88) says, the imperative that peripheral countries must resort to savage wage cuts rests on the false premise that Germany is Greece’s, and other peripheral countries’ ‘principal rival’. In the heterodox contributions to the debate, this assumption stems from the affirmation that the core’s surpluses and the periphery’s deficits are of similar size. This appears convincing at the level of the eurozone as a whole,

but it bypasses individual countries' specific trading patterns. In the Portuguese case, this poses a problem since the most important trading partner is Spain, another 'peripheral' country. Growth in trade with Spain was the main development as far as trade is concerned after EEC membership in 1986. From having represented 4% of exports and 7% of imports in 1985, this share reached 28% and 31% respectively in 2008 (INE 2016a; INE 2016b). Following the ULC logic, it would be more appropriate to conclude that Spain is Portugal's main competitor.

Sixth, in assuming that peripheral countries are in direct competition with Germany, the ULC argument tends to ignore the question of product specialisation. Focusing on ULCs in the aggregate, mainstream and heterodox interpretations in economics disregard the fact that different countries provide different products to the global market and therefore compete on different markets. It should however be noted that important contributions to the VoC and Growth Models perspectives are not oblivious to export specialisation. Questioning the ULC view, Felipe and Kumar (2011) maintain that Portugal and Greece do not compete with Germany, but with China, because their specialisation profiles are similar. They compare the complexity of the export baskets from peripheral eurozone countries with those from German. Complexity is defined based on a combination of diversity and ubiquity. They conclude that German exports are the second most complex in the world, and the second most diverse. Among the world's ten most complex products Germany controls a significant share. In contrast, Portugal ranks as 53<sup>rd</sup>, which is close to Greece (52<sup>nd</sup>) and China (51<sup>st</sup>) (Abdon, Bacate, Felipe and Kumar 2010; Felipe and Kumar 2011, p.10). On this basis, they suggest that it is precisely the product specialisation that is the source of trouble:

We believe that this is where the real problem of the peripheral countries lies. Their lack of competitiveness vis-à-vis Germany is not due to the fact that they are expensive (their wage rates are substantially lower), or that labor productivity has not increased. The problem is that they are

stuck at middle levels of technology and they are caught in a trap. Reducing wages would not solve the problem (Filipe and Kumar 2011, pp.11).

This view is supported by Storm and Naastepad (2015a, p.968; 2015c, p.845) who hold that technological or non-price competitiveness is most important, not price competitiveness. They argue that export performance is determined by the composition of commodities for exportation and export destinations. While Germany’s export market share grew 0.45% on average between 1996 and 2007, this reflected an export orientation towards countries with high growth and an increasing specialisation in medium-tech products with a fast-growing market. Upper-market products with high to medium technology represent over half of exports and these are sold at high prices. In contrast, Portugal produces low-tech, and the destinations of Portuguese products are ‘saturated’. Of the hundred most complex products on the world market, Germany has a share of 18% whereas Portugal controls 0.04% (Felipe and Kumar 2011, p.29; Storm and Naastepad 2015a, p.969). Portugal, Greece and Italy lost global market shares between 1996 and 2007. This reflects an export specialisation which corresponds with that of China, which exposes them to competition. Portugal’s export specialisation has a 52% overlap with the Chinese, whilst Germany has 22% (Storm and Naastepad 2015a, pp.968-969). If China were the comparator, and the policy of internal devaluation were to be pursued with this in mind, it would mean even deeper wage cuts than what has been implemented with the Troika adjustment programmes (Smith 2016, p.90). However, this may be as meaningless as it is painful, if, as argued by Felipe and Kumar (2011, pp.27-28) even a 20-30% reduction in nominal wages would not be enough to compete with Chinese wages.

These arguments find support in the literature on Portuguese industrial policy (see Godinho and Mamede 2016; Mamede 2014; Mamede et al. 2014). This literature maintains that Portugal’s external accounts eroded over the last two decades and that this stems in part from

a specialisation profile which overlapped with that of China and Eastern European countries (Godinho and Mamede 2016, p.334; Mamede et al. 2014, p.251). Out of a group of 27 European economies, as of 2004, Portugal had the second highest correlation of revealed comparative advantage with Asian economies (Mamede 2014, pp.3-4). With the internationalisation of production and the adjustments to enter the EMU, Portugal's traditional sectors faced competitive pressures (Mamede et al. 2014, pp.253, 269). Godinho and Mamede (2016, p.334) speak of three competitive shocks: China's entry into the WTO, the EU's expansion to the East and the euro's appreciation vis-à-vis the dollar between 2001 and 2008. Consequently, value added in manufacturing stagnated between 2000 and 2008 whilst almost one in every five jobs were lost. Textiles and clothing were both in decline.

#### 4. The case of Portugal

The critiques of the ULC argument provide insights that counter the entire logic of much of the literature on the eurozone crisis. Their insights beg for a focus on patterns of product specialisation. The argument that peripheral eurozone countries are in competition with China rather than Germany (Felipe and Kumar 2011; Storm and Naastepad 2015a) is based on aggregate indicators for technological complexity. This is a crucial starting point. To advance this analysis, these findings would benefit from being complemented by a detailed analysis of structures of production, global competition and external imbalances, based on case study research. From the above reviews, it can be expected that Portugal's current account deficit reflects a product specialisation which overlapped with that of China and Eastern European economies. The 2000s were not only marked by the finalisation of the euro project, but also by China's entry into the WTO in 2001 and the EU's expansion to Central and Eastern Europe in 2004 and 2007. This included twelve new member countries (Cyprus, Czech republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Romania and



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Bulgaria). These events are usually not discussed in literature on the eurozone crisis. The evidence presented here corroborates the argument developed by Felipe and Kumar (2011) and Storm and Naastepad (2015a) but shows that the story is somewhat more intricate. Portugal's traditional low-tech export industries such as textiles and clothing were in decline in the 2000s, but their demise dates further back. Initially, their effect on the trade balance was mediated by the rise of medium-tech sectors. The novelty of the 2000s was not the erosion of the traditional sectors, but rather that virtually all sectors were in stagnation or freefall.

Before analysing Portugal's exports, some stylised facts concerning the payment imbalances are needed. First, the large current account deficit developed in the context of a transition from economic boom in the second half of the 1990s to stagnation in the 2000s. Between 1995 and 2000, the average growth rate was 4.1%, but this dropped below 0.9% between 2001 and 2005 (World Bank 2020a). In this regard, Portugal differed from Greece, Spain and Ireland where the crisis was preceded by high growth. The strong growth rates in Portugal were driven by a boom in construction, and the subsequent stagnation by its hollowing out. The EMU was not only associated with a fixed exchange rate regime, but also with financial liberalisation and large financial flow, and credit was directed towards housing and construction (Pinho 1997; Previdelli and Souza 2012; Rodrigue and Reis 2012). Second, Portugal witnessed a growing current account deficit from the mid-1990s. This was before other crisis ridden countries in the eurozone. By 2010, this had reached over 10% of GDP. Third, Portugal's trade deficit preceded the current account deficit. In fact, the external balance of goods and services was negative the entire period from 1970 to the GFC. This observation is relevant, since many accounts assume that the euro was what hampered competitiveness in the eurozone's periphery. From the mid-1980s, the trade deficit was



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3 accompanied by a growth of secondary income, largely consisting of personal transfers,  
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5 which helped keep the current account in balance (IMF 2016). Remittances accounted for  
6  
7 almost nine percent of GDP in the early 1980s but became negligible by the turn of the  
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9 millennium (World Bank 2020b). This means that Portuguese emigrants' income is part of  
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11 the balance of payment trajectory. This insight is usually left out of discussions about the  
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13 eurozone crisis. Fifth, Portugal's negative trade balance derives from an import growth which  
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15 exceeded export growth (World Bank 2020c). In the 1990s, this was mainly due to imports of  
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17 consumer goods, which increased as a share of total imports until 2002. The share of capital  
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19 goods also increased in the second half of the 1990s (WITS 2022a). The decade prior to  
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21 Portugal's EEC membership in 1986 had been one of rapid trade orientation, but in the early  
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23 1990s exports declined and stagnated thereafter (World Bank 2020c), thus contrasting with  
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25 the global trend towards trade expansion. One cannot speak of an erosion of export capacity –  
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27 due to ULCs or any other factor – but it is relevant to pose the question of why exports failed  
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29 to keep up with imports.  
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36 To assess the relationship between Portugal's export specialisation and the trade deficit, it is  
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38 necessary to decompose the general index of complexity. This paper uses UN Comtrade, the  
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40 largest repository of international trade data, and WITS, which comprises several databases  
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42 including UN Comtrade and the WTO's Integrated Trade Data Base.<sup>1</sup> From the UN  
43  
44 Comtrade database it can be observed that among Portuguese exports to the world, the most  
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46 important category from the 1960s was 'manufacture goods classified chiefly by material'.  
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48 This accounted for over 42% of exports of goods in 1965 (Figure 1). The category includes  
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50 Portugal's traditional export industries such as textiles, clothing and wood. Within this  
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52 category the most important subsectors were 'textile yarn, fabrics, made up articles' and  
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57 <sup>1</sup> UN Comtrade uses several nomenclatures, or classification principles that systematise commodities. The  
58 present paper draws on SITC, which records trade data back to 1962. SITC has several levels of product  
59 categories, as shown in Figure 1 and 2. It can be noted that the commodity classifications used by WITS and UN  
60 Comtrade are not identical.

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‘wood and cork manufactures’. ‘Non-metallic mineral manufacture’ was also significant (Figure 2). Data from WITS shows that by 1990, Portuguese exports continued to be heavily concentrated in the traditional sectors, notably textiles and clothing, footwear and wood. ‘Textiles and clothing’ represented 29% of export revenue whilst ‘footwear’ represented 8% and ‘wood’ 12% (WITS 2022b). Beyond the traditional export industries, ‘machinery and electrical equipment’ accounted for 13% of export revenue (WITS 2022b).

FIGURE 1

FIGURE 2

As expected, based on the arguments developed by Storm and Naastepad (2015a) and Felipe and Kumar (2011), Portugal’s export structure did represent a vulnerability, exposing the country to competition from China and Central and Eastern Europe. In 1992 ‘textiles and clothing’ were responsible for 29% of Chinas export revenue, ‘machinery and electrical equipment’ 14% and ‘footwear’ 6% (WITS 2022c). The rates were almost identical to those in Portugal. Textiles and clothing had thrived after Portugal joined EFTA in 1960 (Truett and Truett 2019). At that time, textile production was sustained by cotton production in the Portuguese colonies. In 1960, the colonies were the source of 82.7% of raw cotton imports, and the destination of 35.8% of cotton manufacturing exports (Anderson 1962). Subsequently, by the eve of colonial liberation, Portuguese textile and clothing produce was protected by the 1974 Multi Fibre Agreement (MFA) which imposed quotas on developing countries’

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3 exports to EEC countries (Fernandes and Tang 2020). Trade with Europe was progressively  
4 liberalised through EFTA, the EEC and the Single Market (Amador and Opromolla 2009). In  
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6 1994, the MFA was substituted by the WTO Agreement on Textile and Clothing (ATC). The  
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8 quotas were phased out and the sectors were fully integrated into the GATT/WTO system by  
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10 2005. The liberalisation exposed Portuguese producers to competition from China and other  
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12 low-wage countries (Fernandes and Tang 2020; Lains 2018; Rezazadeh and Carvalho 2018;  
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14 Schütz and Palan 2016; Truett and Truett 2020). The EU's expansion to Eastern and Central  
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16 Europe added to the low-wage competition, particularly from Bulgaria and Romania where  
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18 textiles and clothing production were important sources of export revenue (Amador and  
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20 Opromolla 2009). In these two countries, textiles and clothing represented 14% and 13% of  
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22 export revenue respectively (WITS 2022d; 2022e). Portuguese wages in the sector were low  
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24 compared to the EU average (45% in 2001) but in Bulgaria and Romania they were much  
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26 lower (6% and 9%) (Truett and Truett 2019). In parallel with the EU's expansion towards  
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28 Central and Eastern Europe, textiles and clothing lost importance as a source of Portugal's  
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30 export revenue. In 2003, this sector accounted for 16% of export revenue, but by 2008, it had  
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32 dropped to 10% (WITS 2022b). This suggests that Storm and Naastepad (2015a) and Felipe  
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34 and Kumar (2011) correctly identify export specialisation as a source of the imbalances.  
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45 Notwithstanding these findings, the tendency towards industrial decline in the traditional  
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47 sectors such as textiles and footwear dates further back than the 2000s. The contribution of  
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49 textiles and clothing to total export revenue was in freefall already from the early 1990s.  
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51 From having represented over 30% of export revenue in 1988, it had dropped to just over 23%  
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53 by 1995 (WITS 2022b). Portuguese footwear was in decline from the mid-1990s and its  
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55 contribution to total export revenue dropped from 10% in 1994 to 4% in 2007 (WITS 2022b).  
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57 In the words of the Association for Portuguese Textiles and Clothing (*Associação Têxtil e*  
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*Vestuário de Portugal*, ATP) the industry ‘faced several competitive shocks’ and a ‘continuous turmoil’ composed by several ‘succeeding crises’. These crises included the liberalisation of world trade between 1995 and 2005, China’s entry into the WTO and the EU’s enlargement to the East (*Associação Têxtil e Vestuário de Portugal*, ATP). The latter two events represented continuity rather than rupture.

It is essential to stress the dynamic aspect of Portuguese exports both before and during the growth of the current account deficit. In the 1990s, the traditional low-tech sectors were substituted by medium-tech exports. Despite the erosion of textiles and clothing, the share of manufacturing goods of total exports increased from 78% in 1988 to 83% in 1993 and remained stable until 2003 (WITS 2022f). Low wages had been a driver of industrial relocation towards Portugal in the 1970s (Poulantzas 1976), but by the early 1990s, the Iberian peninsula was ‘superseded by Central Eastern Europe in its function of low-wage periphery’ and many transnationals shut their plants in Spain and Portugal and moved their operations elsewhere (Serfati 2016, pp.266, 277). Despite this offshoring, there was no overall deindustrialisation of Portuguese exports. What took place was a change in the composition of manufacturing exports. Thus, we can speak of a *deindustrialisation* that was mediated by industrial *recomposition*. As the share of consumer goods in total exports declined from 64% to 54% between 1993 and 2003, the share of capital goods increased from 13% to 22% (WITS 2022f). The substitution of one manufacturing branch by another is not accounted for by the critiques of the ULC argument (Felipe and Kumar 2011; Storm and Naastepad 2015a), who do not analyse peripheral countries’ dynamic industrial trajectories. The data shows that ‘machinery and transport equipment’ came to overtake ‘textile and clothing’ as Portugal’s most significant export sector. From 1993 to 2003 this sectors’ contribution to total export revenue increased from 21% to 34% (WITS 2022f).

‘Transportation’ and ‘machinery and electrical equipment’ were also on the rise. The export capacity in machinery and transport equipment was largely driven by FDI in the automobile sector (Amador and Cabral 2008, p.100; Cabral 2004, p.80). In 1995 Ford and Volkswagen opened the automotive assembly plant AutoEuropa in Setúbal outside Lisbon. This occurred within a context of a spatial reorganisation of production by German automobile suppliers, as more producers began to relocate production to low-wage economies (Krzywdzinski 2014). Seen as ‘irrefutable evidence of Portugal’s convergence on more capital-intensive forms of accumulation’, AutoEuropa was the most important FDI project ever in Portugal (Bieler et al. 2019, p.812). However, Portugal’s insertion into this value chain was a subordinate one. The most capital-intensive components were imported from countries such as Germany, the UK and France. Product strategy, marketing and investment decisions were carried out in Germany and the USA (Bieler et al. 2019, p.812). With a ‘just in time’ production model (Correia 2000) AutoEuropa was responsible for 12% of exports and 2.1% of GDP just one year after its inauguration (Wise 2017). Thus, the industrial recomposition and the rise of these sectors made up for lost export revenue resulting from deindustrialisation in textiles and clothing.

Portugal’s crisis trajectory did however not end with a mere substitution of one manufacturing branch by another. From the early 2000s a new set of dynamics were at work. The turn of the millennium initiated a period of stagnation. The production volume in both construction and manufacturing decreased significantly. The OECD has records of the volume of manufacturing production in Portugal from 1955 onwards. The total manufacturing volume was almost consistently rising this entire period, until 2002, after which it was in a sharp decline. Using 2015 as a basis year, the volume produced at the peak in 2002 was 142% of what it was in 2015. In 1955 it was only 19% of the 2015 level, but by

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1980 it reached 83% and by 1990 123% (OECD 2020). In the construction sector, production reached a peak in the early 2000s and plummeted from 2003 (OECD 2019). This shift occurred within a transition from an investment surge in the second half of the 1990s to a slump in the 2000s (Mamede 2014). Gross fixed capital formation reached a peak at 28% of GDP in 2000 but dropped to 23% of GDP in 2008. From having been well above the euro area average, it dropped to average in the mid-2000s and far below thereafter (Eurostat 2017a). Although textiles and clothing deindustrialised prior to 2003, there had not been an overall decline in Portugal’s total manufacturing production. But from 2003 Portugal deindustrialised at the aggregate level. The decline was sharp between 2002 and 2009. Thus, in aggregate terms, deindustrialisation occurred from the early 2000s *until* the GFC.

The novelty in the first decade of the millennium was not deindustrialisation in the traditional export sectors, but rather that there was no new sector to make up for their demise. Eurostat’s index on manufacturing production volumes shows that Portugal’s entire manufacturing industry was in decline or stagnation in the 2000s (Table 1). The index distinguishes between twenty sectors and uses 2010 as a base year. Manufacturing production overall reached a peak in 2002, when the volume produced was 22% higher than in 2010. Some sectors saw a moderate increase, but it was much less pronounced than the decline in the main export sectors. Textiles and clothing were strong drivers of the general decline. In textiles the production volume was 62% higher in 2000 than in 2010. In ‘manufacture of wearing apparel’ the production volume dropped by about a third. These sectors, which still accounted for an important share of export earnings, were in a steep decline. Nonetheless, the demise of the medium tech sector that so far had replaced them as sources of export revenue, was even starker. In 2002 ‘manufacture of motor vehicles, trailers and semi-trailers’ produced at 280% of the 2010 level. The decline was almost consistent (Eurostat 2017b). This is likely to have been driven by a relocation of automobile production towards Eastern European economies

(Godinho and Mamede 2016). Indeed, Simonazzi, Ginzburg and Nocella (2013) maintain that an eastward orientation by German supply chains with consequent changes in trade flows was one of the causes behind the accumulation of external deficits in Southern European economies. ‘Manufacture of electrical equipment’ also saw a strong decline. In 2000 the production volume was 301.5% of what it would be ten years later (Eurostat 2017b). The trend is quite clear. The products that had gained prominence as sources of export revenue in the 1990s were now producing at very low levels. Reflecting the contraction in production, export data shows the same tendency. The share of manufacturing in total exports only started to decline after 2003, when it dropped from 86% to 76% in 2008 (Wits 2022c). From that point onwards, Portuguese exports deindustrialised.

#### TABLE 1

The empirical findings presented here pose theoretical challenges to the most widespread interpretations of the crisis in the eurozone and of core periphery relations there. These challenges have powerful ramifications in the realm of policy making. The simplest point that can be drawn out of the above discussion is that production matters to understanding the Portuguese crisis. Alongside the development of a large current account deficit unfolded a process of industrial decline. Thus, something else than a mere divergence of ULC vis-à-vis core EMU economies occurred. If production and industrial collapse matter to understanding the Portuguese crisis, similar processes might have played a role in crisis trajectories elsewhere in the eurozone. Notwithstanding this, most analyses have ignored or underappreciated country specific patterns of production. From the onset of the eurozone crisis, the “competitiveness problem” emerged as a major policy focus and a hegemonic



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discourse in European policy circles. Underpinning it was a narrow, cost centred and ULC centred notion of competitiveness. As highlighted by Miró (2021, p.712) this notion came to be “discursively articulated as an object of state action”. With such a general problem, no detailed examination of national industries was needed. The ULC story offered a simple problem and a simple solution. It was the perfect diagnosis for a one-size-fits-all approach to competitiveness which underpinned the structural adjustment programmes imposed on the eurozone’s periphery. An alternative approach to competitiveness would have focused on concrete sectors of production, industrial upgrading, and an active industrial policy. This was absent in all the memorandums of understanding. In fact, prominent proponents of internal devaluation explicitly rejected active industrial policy (Blanchard 2007).

In dissecting Portugal’s structure of production and pattern of export specialisation, the present analysis has offered an alternative account of trade imbalances. In doing so, it has added to the heterodox literature on the eurozone crisis. In taking a bird’s eye perspective on intra EU/EMU imbalances, this literature has too often missed out on country specific particularities, and like the mainstream, it has offered policy proposals based on a *general* crisis diagnosis. While some of the recent CC literature has paid more attention to export specialisation than the heterodox economics literature, some country specific details necessarily get lost in the focus on typologies. The analysis here has shown that Portugal did face competition, but this competition came from China and other low wage economies. It was specific to the type of products Portugal exports. The demise of the traditional sectors – notably textiles and clothing – reflected a gradual exposure to competition through liberalisation. This included China’s entry into the WTO, but it started before. The EU’s expansion to the East added to the competitive pressure. Portugal no longer served as a low-wage periphery, and Eastern European economies outcompeted Portuguese wages in the textile and clothing sector. That is, labour costs certainly played a role in Portugal’s industrial



trajectory, but international wage differentials between countries with similar export profiles were more important than aggregate RULCs. In scrutinising these dynamics, this paper has challenged the heterodox notion that peripheral eurozone countries were in direct competition with Germany and core EMU countries.

## 5. Conclusion

This article has advanced the notion that specific counties have unique forms of articulation within global capitalism, and that this matters to understanding crisis trajectories. It posed the question of what caused the crisis in Portugal. To answer this question, it critically interrogated the view that diverging ULC trajectories were the main cause of the imbalances that led up to the crisis in the eurozone. This is a common answer across strands in economics and CC. The article showed that the ULC view studies current account imbalances in the eurozone at an excessively aggregate level and relies on a single indicator to serve as a proxy for competitiveness. It assumes that Greece, Portugal, and Spain are all in direct competition with Germany and usually bypasses fundamental questions about what is produced and exported, or indeed whether production has collapsed altogether. It tends to avoid posing the question of whether eurozone countries play different roles in the global division of labour and therefore compete on different product markets. The ULC view does not investigate individual countries' productive structures and patterns of export specialisation. Despite this, various crisis diagnoses that focus on ULC have been popular – and they have informed radically different policy proposals, including attacks on wages, working conditions and trade unions in the eurozone's South, wage growth in the North, and peripheral countries' exit from the EMU.

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In providing a single case study of Portugal, the article made several methodological points. First, it insisted that singularity matters. A lack of sensitivity to context underpinned the strategy of internal devaluation, which followed a race-to-the-bottom logic. Heterodox economics has offered an alternative to the mainstream’s methodological nationalism, yet, in focusing on trade and financial flows, it often takes an intra-regional perspective. Single-case studies are well placed to shed light on the merits and limitations to crisis interpretations that take a bird’s eye perspective. Second, history matters to understanding the crisis. The literature usually looks at the development of macroeconomic imbalances from the mid-1990s or 2000. This study showed that many factors that shaped Portugal’s current account trajectory date much further back. This includes the trade deficit itself, remittances that helped keep the current account in balance and inwards FDI. A third methodological point concerns geography and space. The article approached the crisis in Portugal by looking at changing patterns of regional integration, global competition, and the geographical reorganisation of specific value chains.

Building on existing critiques of the ULC view, the article asked whether the real drivers of vulnerability were the country’s pattern of export specialisation and exposure to competition from China and other low-wage economies. It showed that behind the large current account deficit hides a trajectory of deindustrialisation and industrial recomposition, and subsequently, industrial decline. This reflected international competition that put pressure on specific sectors. The large current account deficit that preceded the crisis developed in the context of import growth without an equivalent export growth. At a time when world trade expanded exponentially, Portuguese exports stagnated. The trajectory in textiles and clothing were critical. This sector accounted for over 30% of exports in the late 1980s but embarked on a path of sustained decline. Portuguese textiles faced competition from Eastern European economies and China. In the 1990s the demise occurred alongside the rise of medium-tech

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3 exports. Portugal benefitted from the spatial reorganisation of automobile production.  
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5 However, also in this sector, a subsequent reorientation towards Eastern Europe appears to  
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7 have added to the pressure on trade. This, together with the longstanding erosion of textiles  
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9 and clothing and a hollowing out of industrial production more generally negatively affected  
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11 export revenue. The 2000s were marked by stagnation or contraction in almost all  
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13 manufacturing sectors. Deindustrialisation and dynamics of industrial recomposition were  
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15 crucial factors. In sum, production matters to understanding the crisis.  
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27 <sup>i</sup> Braga de Macedo stressed that he was speaking in a personal capacity and not on behalf of the Social  
28 Democratic Party (PSD) in Portugal.  
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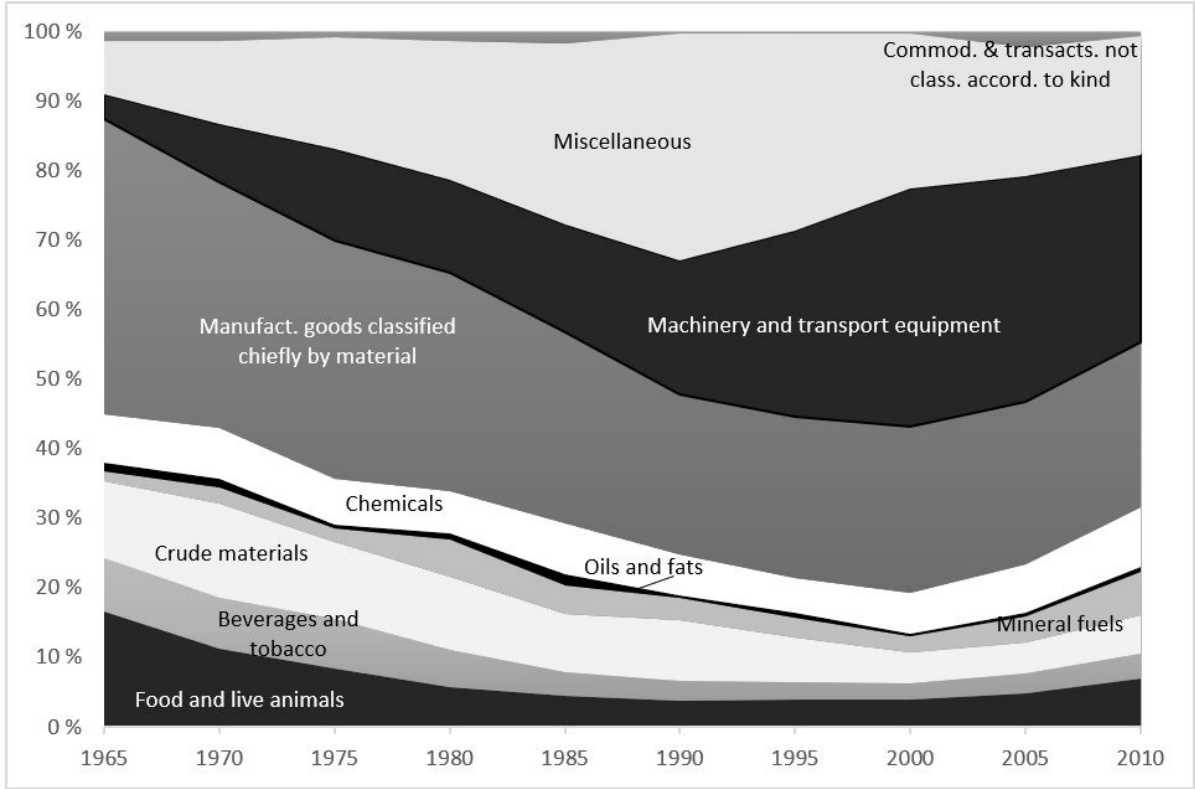
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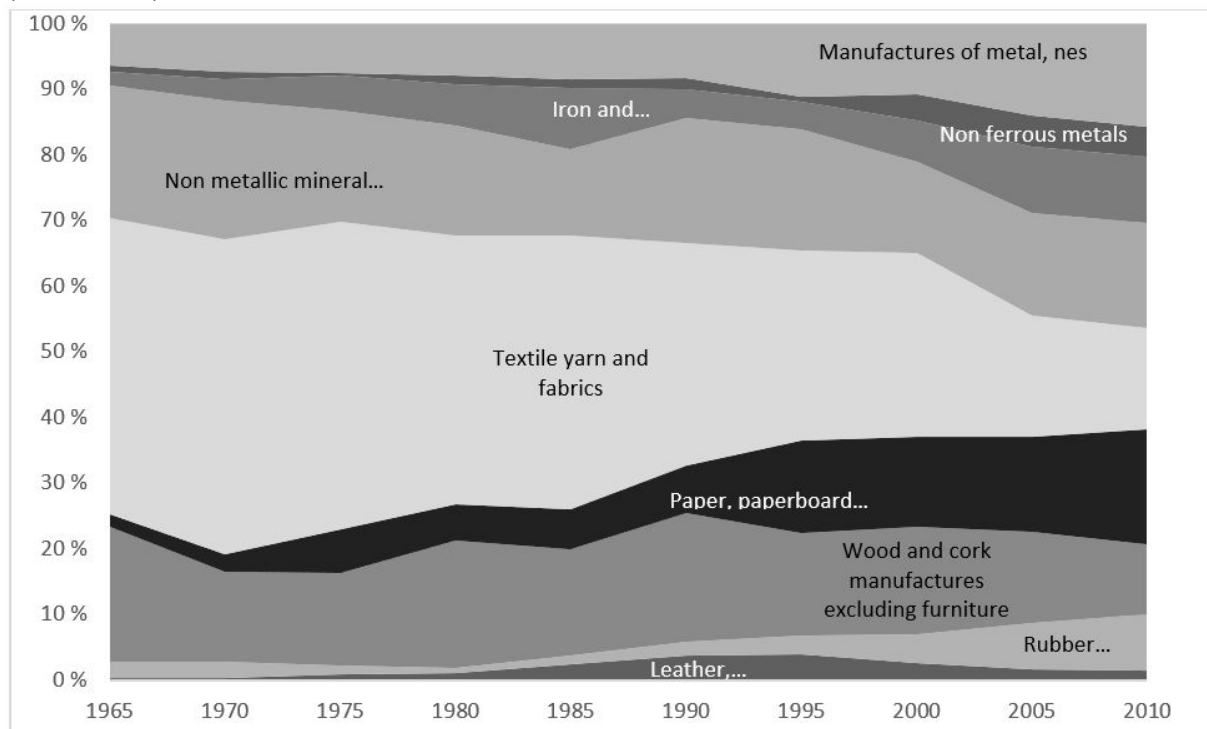
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Figure 1. Portuguese exports of goods to the world, by classification (1965-2010)



Notes: Full series names from the top are 1) Commodities & transactions not classified according to kind; 2) Miscellaneous manufactured articles; 3) Machinery and transport equipment; 4) Manufact goods classified chiefly by material; 5) Chemicals; 6) Animal and vegetable oils and fats; 7) Mineral fuels, lubricants and related materials; 8) Crude materials, inedible, except fuels; 9) Beverages and tobacco; 10) Food and live animals. The figure is based on trade values in US\$. Source: UN Comtrade. Classification SITC, Rev 1. Commodity codes 0-9.

**Figure 2. Portuguese exports of manufactured goods classified chiefly by material (1965-2010)**



Notes: Full series names from the top are: Manufactures of metals, n.e.s.; 2) Non-ferrous metals; 3) Iron and steel; 4) Non-metallic mineral manufactures, n.e.s.; 5) Textile yarn, fabrics, made up articles, etc.; 6) Paper, paperboard and manufactures thereof; 7) Wood and cork manufactures excluding furniture; 8) rubber manufactures, n.e.s., The figure is based on trade values in US\$. Source: UN COMTRADE. Classification SITC, Rev 1. Commodity codes 61-69.

Table 1. Production volume in manufacturing by industry (index, 2010: 100)

Industry	2000	2002	2004	2006	2008	2010	2012	2014	2016
Manufacturing	119.5	122.2	116.5	111.9	109.0	100.0	96.9	99.6	98.9
Textiles	162.2	158.8	144.0	120.8	104.0	100.0	95.1	102.5	95.3
Wearing apparel	146.9	141.4	128.1	118.3	109.3	100.0	98.4	110.5	99.0
Leather and related products						100.0	101.1	108.9	96.9
Wood and wooden products						100.0	111.9	112.3	118.7
Paper and paper products	59.3	86.7	90.9	90.9	92.7	100.0	107.9	109.4	109.5
Printing and recorded media	138.1	134.4	120.7	115.8	111.1	100.0	85.8	81.4	79.0
Coke and refined petroleum products	95.7	102.4	105.8	114.8	104.8				
Chemicals	84.5	96.0	103.7	103.3	98.1	100.0	88.4	94.6	93.7
Pharmaceuticals	110.6	101.6	97.9	96.7	105.8	100.0	100.3	108.6	128.9
Other non-metallic mineral products	131.1	132.7	128.0	121.8	117.8	100.0	100.0	91.3	87.9
Basic metals	68.6	67.0	68.2	76.2	81.1	100.0	97.6	103.5	116.8
Fabricated metal products	96.1	106.6	100.6	109.3	112.6	100.0	97.7	96.7	96.3
Computer, electronic and optical products	194.4	184.3	199.2	235.8		100.0	110.1	74.9	76.6
Electrical equipment	301.5	205.1	178.3	123.6	116.2	100.0	89.2	83.1	88.0
Machinery and equipment n.e.c.	119.2	119.4	110.0	106.7	106.1	100.0	100.7	102.6	107.1
Motor vehicles, trailers and semi-trailers	240.1	280.0	210.1	192.3	164.1	100.0	88.0	104.0	105.6
Other transport equipment						100.0	85.6	75.5	81.8
Furniture	113.0	127.3	140.4	124.5	117.0	100.0	97.4	96.6	82.4
Other manufacturing	151.2	227.7	193.2	167.6		100.0	92.9	94.2	91.5

Notes: Full series names are 1) Manufacture of textiles; 2) Manufacture of wearing apparel; 3) Manufacture of leather and related products; 4) Manufacture of wood and of products of wood and cork, except furniture; manufacture of articles of straw and plaiting materials; 5) Manufacture of paper and paper products; 6) Printing and reproduction of recorded media; 7) Manufacture of coke and refined petroleum products; 8) Manufacture of chemicals and chemical products; 9) Manufacture of basic pharmaceutical products and pharmaceutical preparations; 10) Manufacture of other non-metallic mineral products; 11) Manufacture of basic metals; 12) Manufacture of fabricated metal products, except machinery and equipment; 13) Manufacture of computer, electronic and optical products; 14) Manufacture of electrical equipment; 15) Manufacture of machinery and equipment n.e.c.; 16) Manufacture of motor vehicles, trailers and semi-trailers; Manufacture of other transport equipment; 17) Manufacture of furniture; 18) Other manufacturing. Source: Eurostat, volume index of production (2017).

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