Portugal

Country note, July 2018

Key messages:

- **The Portuguese economy recovery seems to slow down but still likely to grow above 2% in 2018 and close to 2% in 2019**
- **Fiscal deficit is expected to reach 0.7% of GDP in 2018 and will decline further in 2019**
- **Further fiscal consolidation is necessary to achieve the medium-term objective of a structural surplus**
- **Reduction of the gross debt ratio as the major policy goal has been confirmed as such by the Government**

Macroeconomic outlook

After the exceptional GDP growth in 2017, the outlook for 2018 is positive but slowing, with growth around 2,2%, on the back of net external demand (led by tourism) and private investment, according to recent forecasts. CFP has endorsed the MoF's forecast for 2018 but signaled downside risks to the 2019-2021 forecast. The fiscal deficit reduction effort has persisted. This financial market friendly orientation focused on debt reduction and budget balance control, framed in the commitment to EC rules supported consumer, business and investor confidence. Yet, the still high external (public and private) debt levels make the economy sensitive to the significant geopolitical risks that remain in the background. All forecasters, apart from the OECD, assume a deceleration in GDP growth from 2019 onwards derived either from a level effect and/or a lack of evidence of structural reform impetus.

Short-term fiscal outlook

The General Government deficit official target for 2018 set in the Stability Programme is 0.7% of GDP (revised down from 1.1%); in March, under a no-policy change assumption CFP projected the same figure. The primary surplus is forecasted by the Government to reach 2.5% of GDP in 2018 and 2.6% in 2018.

Medium-term fiscal outlook

The Medium-Term Objective is a structural budget balance surplus of 0.25% GDP, which the Government expects to achieve in 2020, according to the latest Stability Programme. The structural deficit in 2018 is currently estimated at 0.8% of GDP in the DBP and at 0.4% in 2019. According to the SGP rules it will have to be reduced at an annual pace of 0.6 p.p. of GDP.

Given the high public debt, the main fiscal challenge is to put the debt ratio on a clear declining trend. This is important to secure market confidence that will further ease the fiscal consolidation efforts. According to the latest Stability Programme primary surpluses and economic growth will be the main drivers behind the projected decline of the debt ratio.

Fiscal framework and national fiscal rules

The implementation of the new Budget Framework Law adopted in September 2015 is still a challenge. Due to be to be implemented in 3 years' time it will likely be postponed by at least a year. Delays are also observable in the implementation of the essential public accounting standards reform towards an accrual system based on IPSAS, also legislated in late 2015.

CFP is of the opinion that the full implementation of fiscal framework improvements is crucial to an effective medium-term planning of fiscal policy that paves the way to a more sustainable growth.

Chart 1: GDP growth forecast assessment

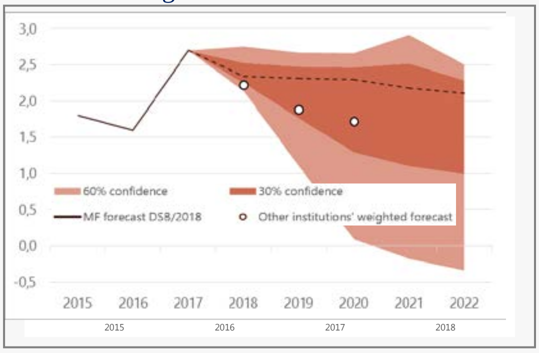
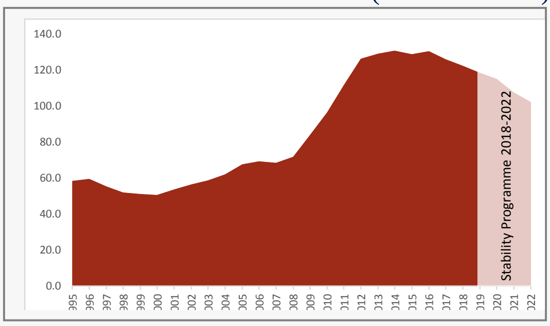


Chart 2: Gross debt-to-GDP ratio (Maastricht def.)



Key indicator forecast

		2017	2018 f	2019 f	2020 f	2021 f	2022 f
Real GDP growth rate (MoF)	[% y-to-y]	2.7	2.3	2.3	2.3	2.2	2.1
Real GDP growth rate (CFP)			2.2	1.9	1.7	1.7	1.6
Output Gap- MoF	[% of PGDP]	0.2	0.7	0.7	0.8	0.9	0.8
Output Gap- CFP	[% of PGDP]	0.4	0.8	0.7	0.7	0.7	0.6
GG balance - MoF.	[% of GDP]	-3.0	-0.7	-0.2	0.7	1.4	1.3
GG balance - CFP	[% of GDP]		-0.7	-0.3	0.1	0.8	0.6
GG debt - MoF	[% of GDP]	125.7	122.2	118.4	114.9	107.3	102.0
GG debt - CFP	[% of GDP]		123.0	119.4	116.4	109.9	106.0
GG structural balance - MoF	[% of PGDP]	-1.0	-0.6	-0.4	0.3	0.6	0.9
GG structural balance - CFP	[% of PGDP]	-1.2	-1.2	-0.6	-0.3	0.0	0.4

Note: excluding the impact of CGD recapitalization CG balance in 2017 was -0.9.

Sources:
__2017__- Portugal Statistics; Bank of Portugal; EC
__2018-2022__ PT Ministry of Finance - Stability Program for 2018-2022, April 2018
__2018-2022__ PT CFP - Report no. 02/2018: Public Finance: Position and Constraints 2018-2022 (no policy change projections), March 2018
f – forecast
Confidence interval for real GDP growth based on 1998- 2017 MoF Stability Programme's forecast errors.

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