Portugal

Conselho das Finanças Públicas
Portuguese Public Finance Council

Country note, January 2018

Key messages:

- **The Portuguese economy keeps its recovery momentum and will likely grow above 2% in 2018**
- **Fiscal deficit in 2017 is expected to reach 1.4% of GDP in 2017 and will decline further in 2018**
- **Further fiscal consolidation is necessary to achieve the medium-term objective of a structural surplus**
- **Reduction of the gross debt ratio is the major policy goal that has been assumed as such by the Government**
- **Adoption of IPSAS and implementation of the new budget framework law keep being key issues**

Macroeconomic outlook

After the marked GDP growth since the second half of 2016, the outlook for 2018 is positive, with growth above 2%, on the back of net external demand (led by tourism) and public and private investment, according to recent forecasts. CFP has endorsed the MoF's forecast for 2018. The change in fiscal policy, towards a more financial markets friendly orientation focused on debt reduction and budget balance control, framed in a commitment to EC rules, supported consumer, business and investor confidence. Yet, significant geopolitical risks remaining in the background must be considered due the still very high external debt level. With the exception of OECD's, all other known forecasters assume a deceleration from 2018 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 2017 is 1.4% of GDP; in September, under a no-policy change assumption CFP projected the same figure (1.6% excluding one-offs). The primary surplus is forecasted by the Government to reach 2.5% of GDP in 2017 and 2.6% in 2018. In June 2017, the Council of the European Union abrogated the Excessive Deficit Procedure (opened in 2009). Consequently, Portugal is now under the preventive arm of the Stability and Growth Pact.

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 2021, according to the latest Stability Programme. The structural deficit in 2017 is currently estimated at 1.8% of GDP in the DBP and at 1.4% in 2018. According to the SGP rules it will have to be reduced at an annual pace of 0.6 p.p. of GDP. The EC projected that it will remain at 1.8% in both years.

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

Portugal focused for a long time on the annual dimension of fiscal policy, disregarding current decisions medium term implications. This led to tax instability and to a pro-cyclical fiscal stance, which were both detrimental to confidence levels and to growth. To change this, Portugal adopted in September 2015 a new Budget Framework Law (BFL), to be implemented in 3 years' time. The law envisages new procedures to design and implement fiscal policy. The change aims to effectively integrate fiscal policy in a medium term economic policy framework, and promotes a modern and efficient public financial management, reinforcing accountability. A public accounting standards reform towards an accrual system based on IPSAS was also legislated in late 2015, and is being implemented, although with some delay.

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

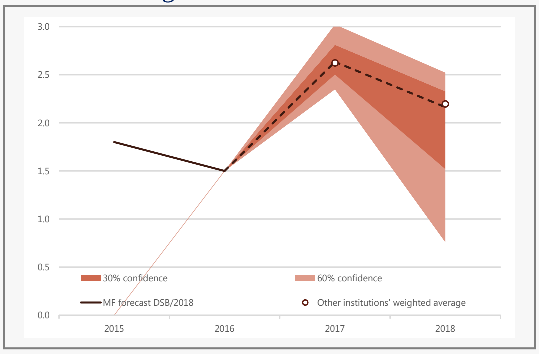
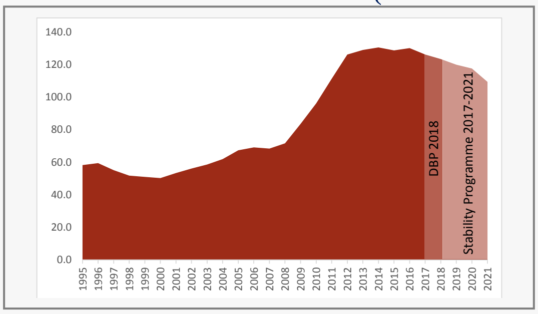


Chart 2: Gross debt-to-GDP ratio (Maastricht def.)



Key indicator forecast

		2016	2017 f	2018 f	2019 f	2020 f	2021 f
Real GDP growth rate (MoF)	[% y-to-y]	1.5	2.6	2.2	2.0	2.1	2.2
Real GDP growth rate (EC)	[% y-to-y]		2.6	2.1			
Output Gap- MoF	[% of PGDP]	-0.9	0.5	1.3	0.4	0.8	1.1
Output Gap- EC	[% of PGDP]		0.4	1.1			
GG balance - MoF.	[% of GDP]	-2.0	-1.4	-1.0	-0.3	0.4	1.3
GG balance - EC	[% of GDP]		-1.4	-1.1			
GG debt - MoF	[% of GDP]	130.1	126.2	123.5	120.0	117.6	109.4
GG debt - EC	[% of GDP]		126.4	124.1			
GG structural balance - MoF	[% of PGDP]	-2.0	-1.8	-1.4	-0.5	0.0	0.3
GG structural balance - EC	[% of PGDP]		-1.8	-1.8			

Sources:
2016 *- Portugal Statistics; Bank of Portugal; EC*
2017-2018 *PT 2018 DBP*
2019-2021 *PT Ministry of Finance - Stability Program for 2017-2021, April 2017*
EC *- COMMISSION STAFF WORKING DOCUMENT, Analysis of the draft budgetary plan of Portugal*
f – forecast
Confidence interval for real GDP growth based on 1998- 2016 MoF Stability Programme's forecast

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