Portugal

Conselho das Finanças Públicas
Portuguese Public Finance Council

Country note, July 2019

Key messages:

- **The Portuguese economy seems to have entered a period of slower growth after the fast recovery up to 2017, slowing down to 2.1% in 2018 and to around 1.7% in the following years**
- **Fiscal deficit in 2018 reached 0.5% and is expected to further decrease if policy stance is kept**
- **Further fiscal consolidation is necessary to achieve the medium-term objective of a null structural balance**
- **The major policy goal of gross debt ratio reduction has been achieved by the Government**

Macroeconomic outlook

After the strong GDP growth in 2017 and the slowdown in 2018, the outlook for 2019 is positive but further slowing, with growth around 1.7%, on the back of domestic demand. CFP has endorsed the MoF's forecast for 2019 but has not endorsed the forecast for the remaining Stability Programme (SP) horizon, signaling that it was neither the most probable scenario nor a more prudent one as required by the Budgetary Framework Law. The fiscal deficit reduction effort has persisted. Also, a financial market friendly orientation focused on debt reduction and budget balance control, committed to EC rules, supported confidence. Yet, still high external (public and private) debt levels make the economy sensitive to the significant geopolitical risks that remain in the background. All forecasters 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. The reduction of unemployment rate has been a major positive trait of recent economic developments that seems to be slowing down, with a possible negative effect on economic sentiment and on consumers and business confidence.

Short-term fiscal outlook

The General Government deficit official target for 2019 set in the SP is 0.2% of GDP; in March, under a no-policy change assumption CFP projected 0,3%. The primary surplus is forecasted by the Government to reach 3.1% of GDP in 2019 and 3.3% in 2020. For 2020 the Government plans a surplus of 0.3% of GDP. The lower expected growth makes it harder to achieve such goals that will require an unchanged fiscal policy stance, with a strong focus on expenditure control and on debt reduction to avoid any slippages.

Medium-term fiscal outlook

The Medium-Term Objective is now a structural budget balance of 0.0%, which the Government expects to achieve in 2020, according to the latest SP. The structural balance in 2019 is currently estimated at -0.1% of GDP in the SP (-0.7% according to CFP). Given the high public debt, the main fiscal challenge is to keep 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 SP primary surpluses and economic growth will be the main drivers behind the projected debt ratio decline.

There are budgetary pressures arising from civil servants' compensation of employees, intermediate consumption and reinvestment needs, after years of historical low investment expenditure. The social security expenditures may also pose some changes after a period of containment below nominal GDP growth rate. Even if expenditure control would be achievable in the short-term, long term mounting effects require structural changes that enhance public expenditure efficiency.

Fiscal framework and national fiscal rules

The implementation of the new Budget Framework Law adopted in September 2015 remains a challenge. Due to be to be implemented in 3 years' time it is still delayed even after being postponed by a year. Delays are also observable in the implementation of the essential 2015 public accounting standards reform towards an accrual system based on IPSAS.

Chart 1: GDP growth forecast assessment

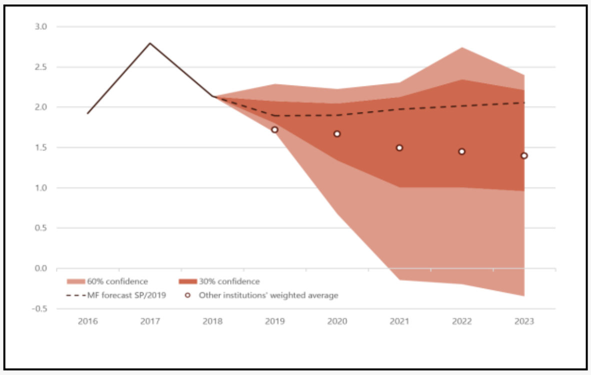
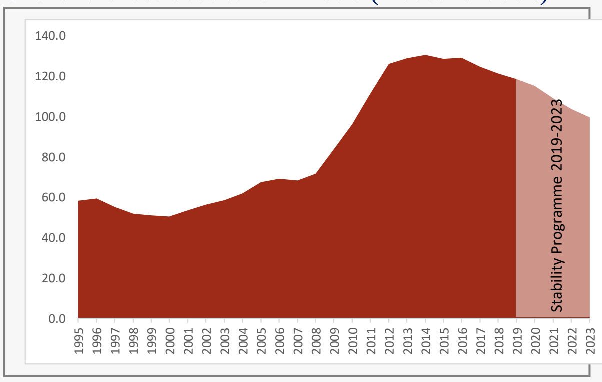


Chart 2: Gross debt-to-GDP ratio (Maastricht def.)



Key indicator forecast

		2018 p	2019 e	2020 f	2021 f	2022 f	2023
Real GDP growth rate (MoF)	[% y-to-y]	2.1	1.9	1.9	2.0	2.0	2.1
Real GDP growth rate (CFP)			1.6	1.6	1.5	1.5	1.4
Output Gap- MoF	[% of PGDP]	0.7	0.7	0.5	0.5	0.6	0.6
Output Gap- CFP	[% of PGDP]	1.4	1.1	0.8	0.6	0.5	0.3
GG balance - MoF.	[% of GDP]	-0.5	-0.2	0.3	0.9	0.7	0.8
GG balance - CFP	[% of GDP]		-0.3	-0.1	0.4	-0.1	-0.1
GG debt - MoF	[% of GDP]	121.5	118.6	115.2	109	103.7	99.6
GG debt - CFP	[% of GDP]		117.9	115.7	110.8	107.4	104.1
GG structural balance - MoF	[% of PGDP]	-0.6	-0.1	0.2	0.3	0.3	0.3
GG structural balance - CFP	[% of PGDP]	-0.8	-0.7	-0.5	-0.4	-0.3	-0.3

Sources:
2018- *Portugal Statistics; Bank of Portugal; EC*
2019-2023 *PT Ministry of Finance - Stability Program for 2019-2023, April 2019*
2018-2023 PT CFP - Report no. 02/2019: Public Finance: Position and Constraints 2018-2022 (no policy change projections), March 2019
p- provisional
e – estimate
f *– forecast*
Confidence interval for real GDP growth based on 1998- 2018 MoF Stability

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