

ECONOMIC ANALYSIS

Portugal: after the positive surprise in 4Q14, the recovery continues earlier this year

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The recovery gained traction in 4Q14, thanks to the increase in exports

- Throughout the fourth quarter, the Portuguese economy registered growth of 0.5% QoQ, higher than the expected 0.3% QoQ and accelerating from 0.3% QoQ in 3Q14. This time growth was due to the performance of net external demand, with exports growing strongly, while imports increased at a more moderate rate, unlike the previous quarter which relied more on domestic demand (Figure 1). According to the available indicators, in the last few months the highest-growing exports have been those targeted at non-EU markets in particular. Private-sector consumption moderated its growth (to 0.2% from 1.4% QoQ) and investment shrank (-0.1% QoQ), after a surge in the previous quarter (2.5% QoQ).

With the data available for 1Q15, our MICA-BBVA model forecasts that recovery will continue at a similar pace to 4Q14, with growth of 0.4%-0.5% QoQ.

The start-of-year indicators are more pitched towards a recovery in domestic demand

- So far in 1Q15, the European Commission's economic sentiment indicator (ESI) has moderated slightly but remains at pre-crisis levels (Figure 3). By sub-indexes, confidence has fallen again in the services sector, but recovered in industry and continues to make progress in households.
- This latter figure is reflected in the increase in January retails sales, after sliding in 4Q14, and in industrial production (Figures 5 and 6), although this remains below the average for the previous quarter. After hearty growth since last October (+4% QoQ in 4Q14), there has been a significant reduction in goods exports, as heralded by the moderation in manufacturing orders from abroad (Figures 7 and 8).
- The Portuguese labour market has experienced a rapid fall in unemployment (-1.7pp in the last twelve months), due mainly to job creation (five quarters in a row), although at a slower rate in 4Q14 (0.7% YoY after 1.9% YoY). The final months of the year, however, showed a slight increase in the unemployment rate, although the positive figure for January leads us to think that this was a temporary interruption in the trend. On the other hand, labour costs in the private sector have fallen again (-2.9% YoY in 4Q14 after -1.2% YoY), particularly in their wage component (-2.9% YoY), while in the public sector labour costs plummeted by 15.5% YoY, because of the base effect of the Christmas bonus, which was paid in the last quarter of 2013, but not in 2014 (Figures 11 and 12).
- The fall in headline inflation (HICP) moderated in February, coming in at -0.1% YoY (-0.4% YoY in January), mainly thanks to a more modest reduction in the prices of energy products (Figures 13 and 14), but also because of the increase in services inflation, which has taken core inflation to 0.4% YoY (0.3% YoY in January).

The 2014 deficit was lower than expected

- The fiscal correction was greater than expected in 2014, with a deficit estimated at around 3.8% of GDP (excluding temporary measures), beating the 4% target. This solid performance was due mainly to the reduction in fiscal spending (-1.4%), against a forecast of a 0.9% increase, because of a better cyclical improvement than expected (improvement in domestic demand and positive performance of unemployment).
- The first 2015 budgetary execution reading shows a decline in revenues from January 2014, mainly due to lower tax collection, on direct taxes above all, whereas the spending items are virtually unchanged (Figures 15 and 16). The deficit target for 2015 is 2.7% of GDP.

Portugal

National accounts: 0.5% QoQ growth in 4Q14

The increase in quarterly GDP is mainly accounted for by a solid recovery in net external demand, the result of robust growth in exports and a fall in imports. Private consumption, however, has decelerated.

Figure 1
GDP (% QoQ) and contribution by components (pp)*

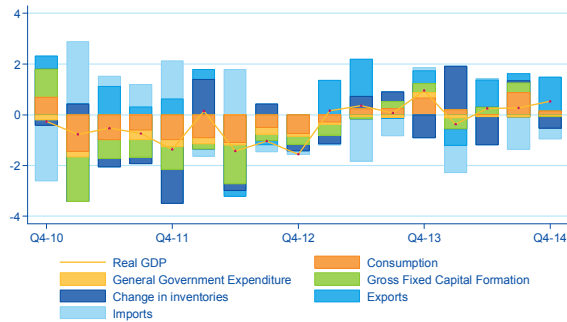
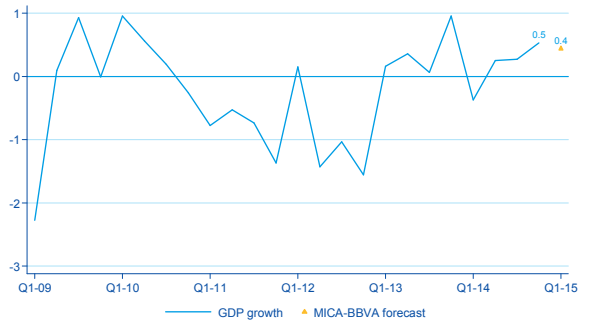


Figure 2
MICA-BBVA: GDP growth (% QoQ) and forecasts *



Confidence: the economic sentiment index remains high at the beginning of 1Q15

According to the ESI, business confidence stayed at pre-crisis levels in February. Industry and consumer confidence continued to perform positively, while there was a moderation of confidence in services, although it remained high.

Figure 3
Confidence (ESI) and coincident activity indicator *

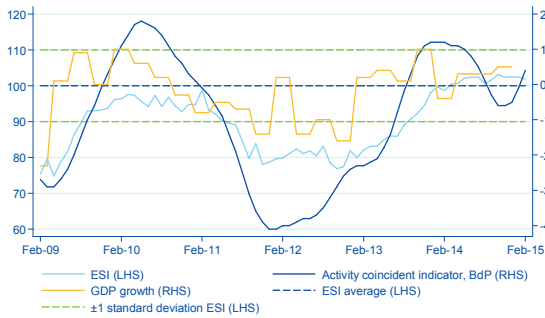
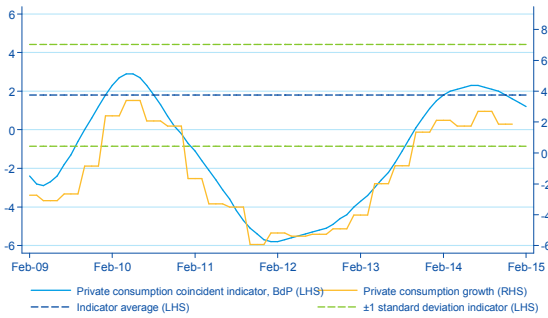


Figure 4
Coincident consumption indicator and private consumption (% YoY)*



Activity: industrial production and retail sales increase in January

Industrial production recovered in January, but was well below the 4Q14 average (-0.4% from 4Q14). Retail trade has surged +5.2% so far this quarter from last (-2.4% QoQ in 4Q14).

Figure 5
Industrial production (% YoY) and confidence*

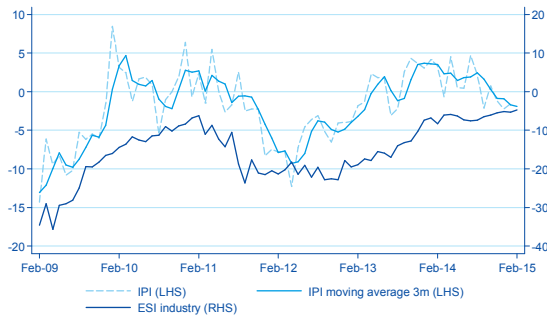
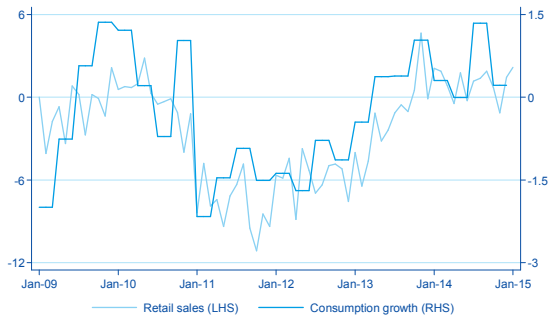


Figure 6
Retail sales (% YoY) and private consumption (% QoQ)*



* Source: Haver Analytics and BBVA Research

Foreign sector: a considerable reduction in goods exports after the growth registered since October

Goods exports fell by 6.1% MoM in January: so far this quarter they are 5.7% below their 4Q14 average. On the other hand, services exports (particularly tourism) continue to grow.

Figure 7
Exports and imports (% YoY, 3pMA)*



Figure 8
Exports (% YoY) and export orders *

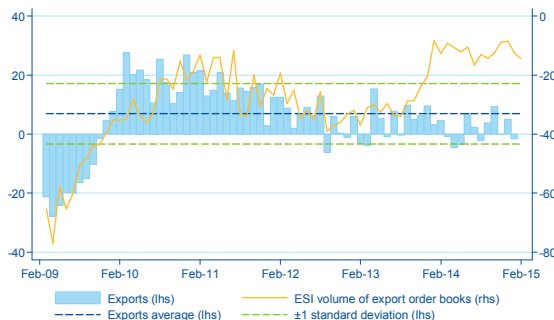


Figure 9
International trade by destination (% YoY)* sa %*

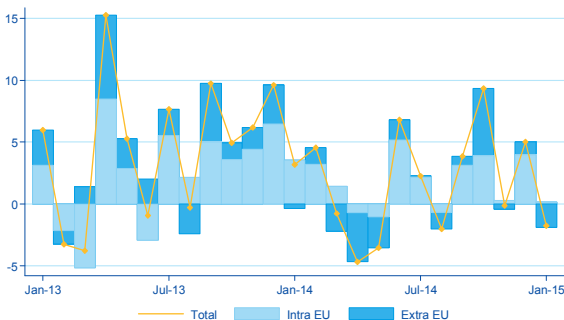
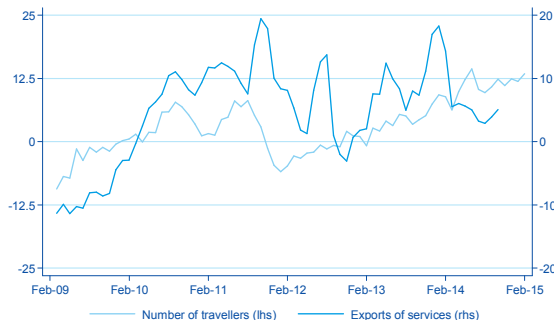


Figure 10
Tourism and services exports (% YoY, 3pMA)*



Labour market: the reduction in unemployment moderates

The labour market has reduced its unemployment (-1.7% over the last 12 months), mainly as a result of job creation (five consecutive quarters), although at a slower rate in 4Q14 (0.7% YoY after 1.9% YoY). Private-sector salaries have shrunk again (-2.9% YoY, following -1.2% YoY in 3Q14).

Figure 11
Unemployment rate (%) and employment expectations*

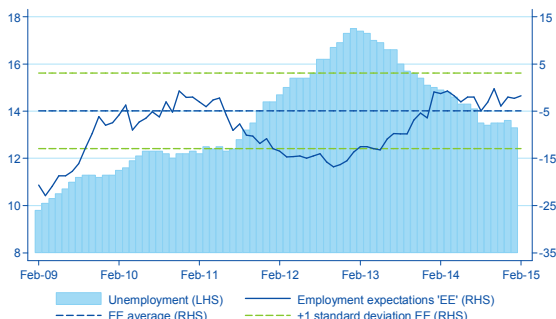
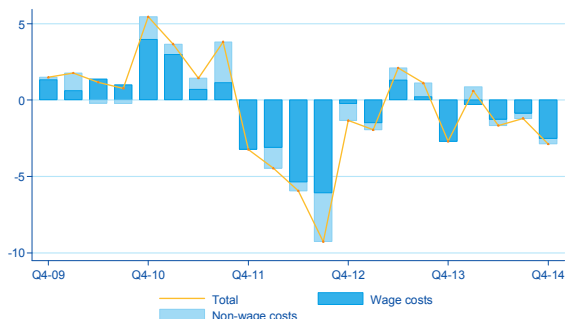


Figure 12
Labour costs in the business sector (% YoY)*



* Sources: Haver Analytics and BBVA Research

Prices: the fall in inflation tapers slightly in February

The fall in headline inflation (HICP) has flattened, standing at -0.1% YoY in February due to the moderation in the fall in prices of energy products. Higher prices in services have raised core inflation to +0.4% YoY.

Figure 13
Inflation rate, headline and core (%YoY)*

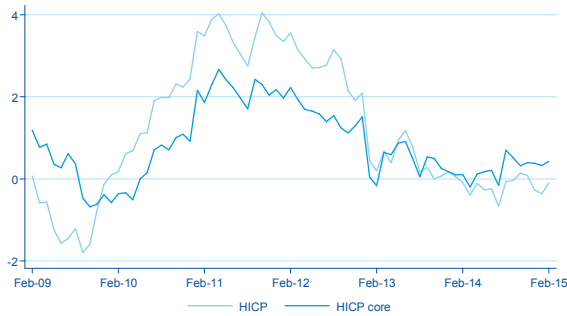
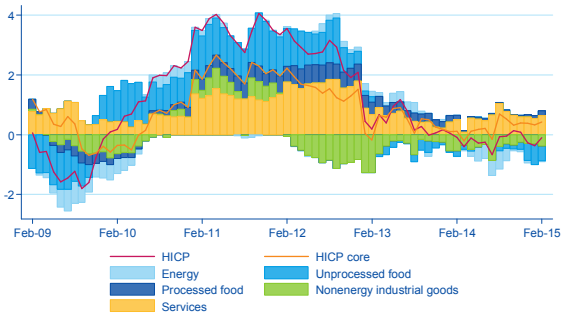


Figure 14
Inflation by components (contribution by %)*



Public sector: fiscal accounts, in line with the budget target

Despite lower-than-expected revenues, the reduction in fiscal spending (-1.4%) because of the improvement in domestic demand and the positive performance of unemployment mean that the deficit target of 4% of GDP will be met and surpassed: +3.8% in 2014.

Figure 15
Government expenditure (comparison with the previous year)*

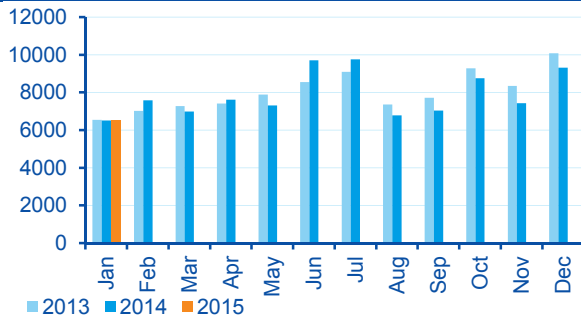


Figure 16
Government revenue (comparison with the previous year)*

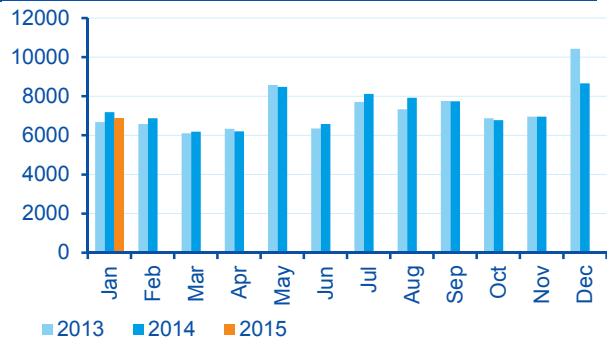


Figure 17
Public and private debt (% of GDP)

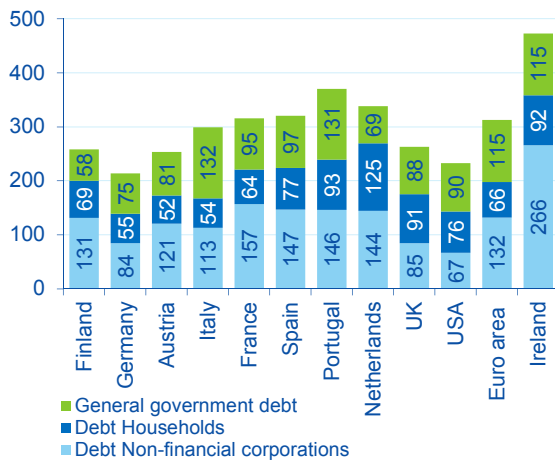
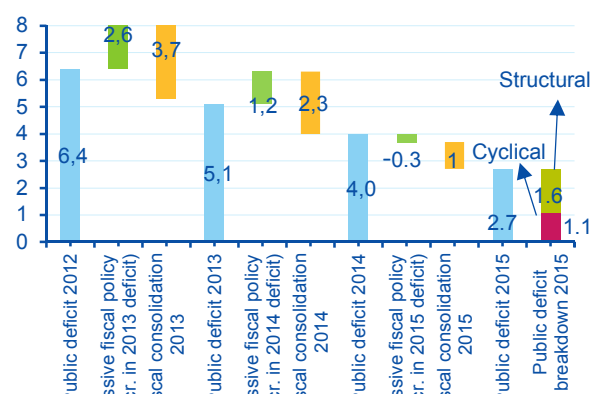


Figure 18
Breakdown of fiscal deficit (cyclical and structural)*



* Sources: Haver Analytics and BBVA Research

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