ECONOMIC WATCH

Portugal: stable and relatively robust growth in 2Q15

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In 1Q15 there was strong private consumption and investment growth but exports stagnated

- Over the first quarter, the Portuguese economy registered QoQ growth of 0.4%, which was less than had been expected but stable with respect to 4Q14. This time growth was as a result of the performance of domestic demand, which contributed 1.4pp thanks to the rise in private consumption, and, above all, the surge in investment. Contrary to what had happened in the previous quarter, which hinged more on external demand (Figure 1), net exports were a drain on growth (-1pp) as imports soared while sales abroad fell off slightly. This drop in net exports was a common factor among most of the eurozone countries and comes at a time of a slowdown in world trade.

Indicators for 2Q15 suggest that growth should continue to be sustained by the recovery of domestic demand …

- So far in 2Q15, the European Commission's economic sentiment indicator (ESI) has improved notably and is settling at pre-crisis levels (Figure 3). By components, both manufacturing and services sector confidence are more buoyant, while household confidence has ebbed.
- The decline in consumer confidence is reflected in the fall in retail sales for April with respect to the previous quarter (-1.6%), when these flipped up by 3% QoQ, while industrial production is better (Figures 5 and 6) and stands above the first quarter average (at around 2%, after 0.6% QoQ in 1Q15). Turning to exports, after the sharp drop recorded in January, which led them to post a decrease of 2.6% QoQ for the first quarter, there was a notable recovery in April, as was signalled by the rise in manufacturing orders from abroad (Figures 7 and 8), in spite of the deceleration in certain emerging markets, especially Angola. This upturn could finally be evidence of the depreciation of the EUR and the consolidation of the recovery in the rest of the eurozone, although, on the other side of the equation, imports are also rising sharply, possibly to satisfy the improved domestic demand.
- The labour market experienced a brisk fall in unemployment over 2013 and 2014, which broke off in 4Q14. In the opening months of the year, the positive trend has sprung into life again and the unemployment rate has retreated by 0.6pp, reaching 13% in April, which is its lowest level in almost four years. The pattern displayed by the unemployment rate is mainly due to the sustained job creation (over six months in a row), which has picked up in 1Q15 relative to 4Q14 (1.5% YoY after 0.6% YoY). On the other hand, labour costs in the private sector have risen (4.5% YoY in 1Q15 after dropping back over three quarters), especially as regards their wage component (4.9% YoY), which is largely due to the base effect of the fall in 1Q14, while public sector labour costs have climbed by 3.4% YoY, partly because of the reinstatement of the wage cut in the civil service (Figures 11 and 12).
- In May, the acceleration by headline inflation (the HICP) was more pronounced than had been expected and amounted to 1% YoY (0.5% YoY in April), thanks mainly to a lower fall in energy product prices (Figure 13 and 14), though also to the considerable rise in non-processed food prices. The pick-up in services prices has taken the core index to 0.7% YoY (0.5% YoY in April).

… which should allow the recovery to progress at a stable and relatively robust pace

- According to the data available for 2Q15, our MICA-BBVA model forecasts that the recovery will continue at a rate on a par with that seen in 1Q15, with growth of around 0.5% QoQ[1]. Our scenario assumes that this growth rate stability will continue for the rest of the year, which should lead to an AAGR of around 2% for the year as a whole.

The deficit to April has come down

- Budget implementation to April reveals a deficit of EUR2.018bn, which is lower than that of EUR2.245bn recorded in April 2014 (Figures 15 and 16). This is mainly due to VAT collected and a drop in unemployment benefit payments, which more than offset the partial reversal of the wage reduction, and the increase in expenditure on infrastructure and servicing public debt interest. The government has forecast a fiscal deficit for the whole of 2015 of 2.7%, which is slightly above our estimates (Figure 18).

1: Given the volatility in this series, the MICA-BBVA model includes two factors, one which tracks the more stable component, and another which captures the high-frequency volatility. The more stable factor suggests quarterly GDP growth of around 0.5%, although the second factor indicates a risk on the upward side of around 0.1pp.

Portugal

National accounts: growth of 0.4% QoQ in 1Q15

QoQ GDP growth was mainly due to the solid recovery of domestic demand, with a pick-up in private consumption and an upturn in investment, while net exports were a drain on growth. For 2Q15 we predict a slight acceleration in growth (around 0.5% QoQ).

Figure 1
GDP (% QoQ) and breakdown by component (pp)*

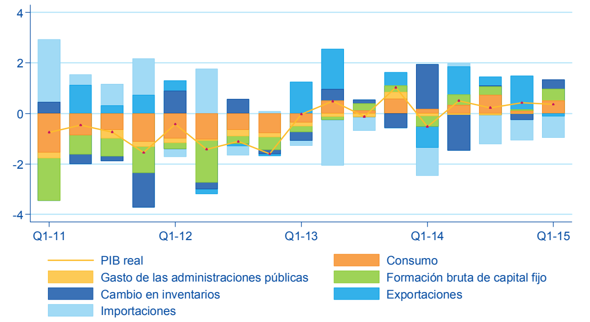
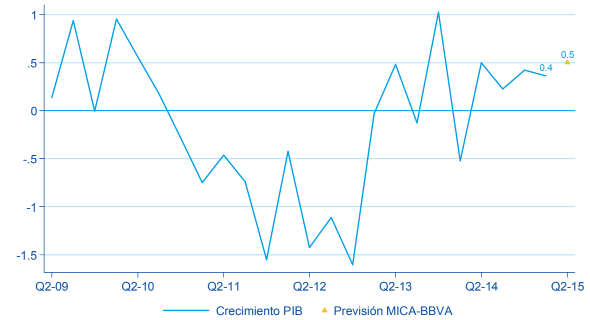


Figure 2
MICA-BBVA: GDP growth (% QoQ) and forecasts*



Confidence: the economic sentiment indicator is still at high levels in 2Q15

According to the ESI, business confidence held in at pre-crisis levels in May. Industry and the services sector continue to perform positively, while the consumer confidence has slipped back a little, although it remains at high levels.

Figure 3
Confidence (ESI) and coincident activity indicator*

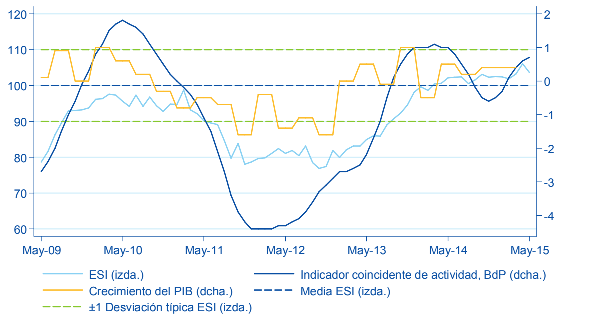
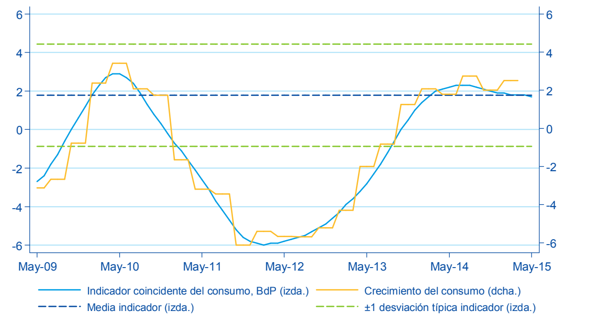


Figure 4
Coincident consumption indicator and private consumption (% YoY)*



Activity: industrial production rose and retail sales slipped back in April

Industrial production was up again in April and stands above the average for the previous quarter (2.1% over 1Q15). Retail trade so far this quarter is showing -1.6% with respect to 1Q15 (when it rose by 3% QoQ).

Figure 5
Industrial production (% YoY) and industrial confidence*

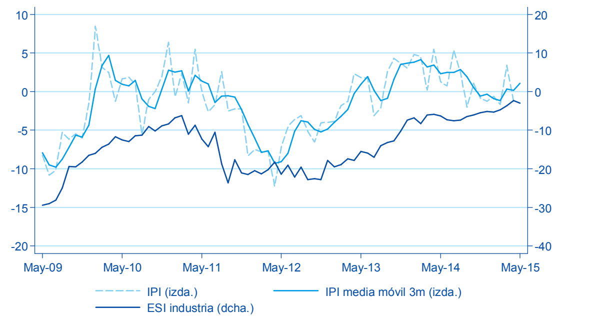
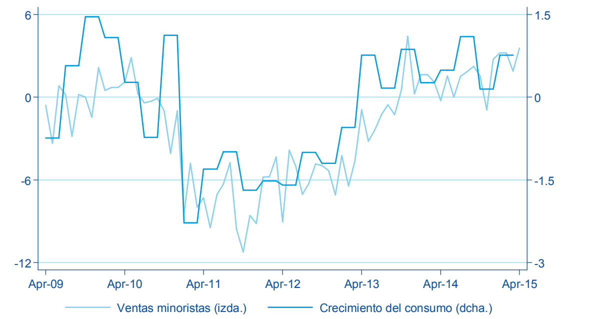


Figure 6
Retail sales (% YoY) and private consumption (% QoQ)*



* Source: HAVER and BBVA Research

External sector: a notable increase can be seen in goods imports at the start of 2Q15

Goods exports were down 0.4% MoM in April, but so far this quarter they are 3.2% above the average for 1Q15. On the other hand, imports bounced and rose 10.7% with respect to the previous quarter.

Figure 7
Exports and imports (% YoY, 3p moving average)*

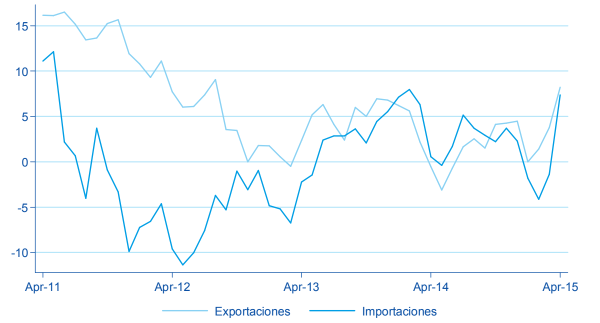


Figure 8
Exports (% YoY) and export orders*

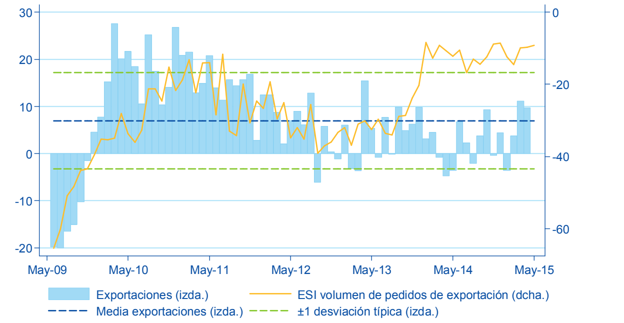


Figure 9
International trade by destination (% YoY, sa)*

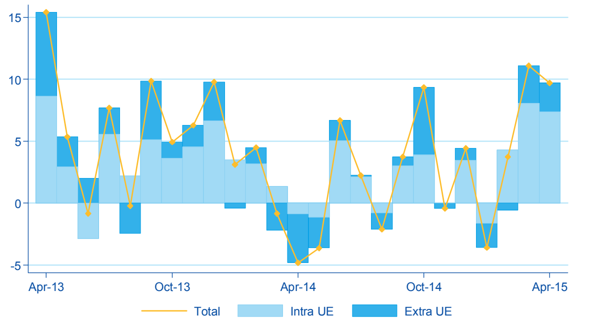
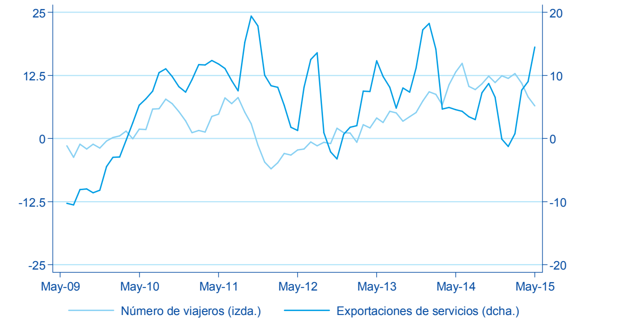


Figure 10
Tourism and services exp. (% YoY, 3p mov. av.*)



Labour market: the reduction in unemployment continues, underpinned by the increase in employment

The unemployment rate came down to 13% in April and job creation continued (six quarters in succession), which picked up in 1Q15 (1.5% YoY after 0.6% YoY). Private sector wages were up (4.9% YoY after -2.1% YoY in 4Q14).

Figure 11
Unemployment rate (%) and employment expectations*

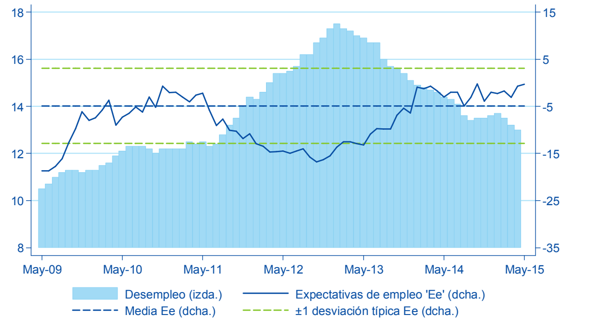
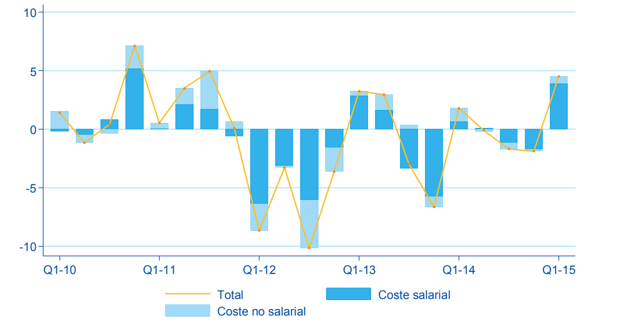


Figure 12
Labour costs in the business sector (% YoY)*



* Sources: HAVER and BBVA Research

Prices: inflation rose in May

The acceleration of headline inflation (HICP) to 1% YoY in May was due to more moderate falls in energy prices and the increase in foods and services prices. Core inflation rose 0.1pp to 0.7% YoY.

Figure 13
Inflation: headline and core (% YoY)*

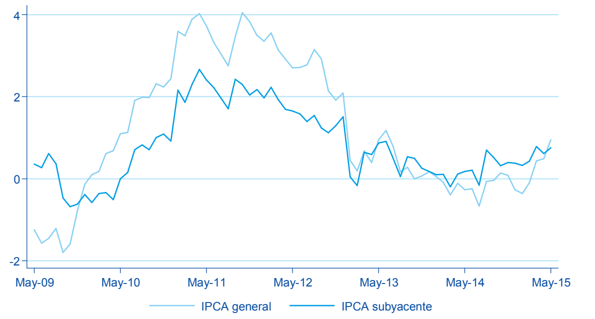
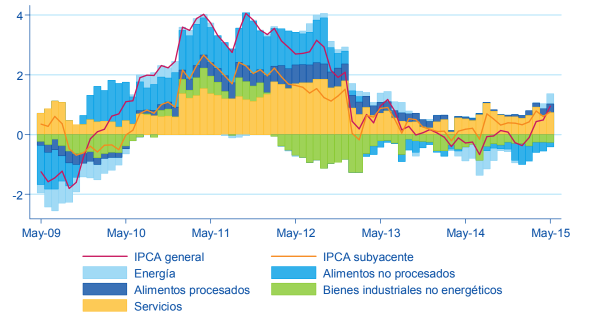


Figure 14
Inflation by component (contribution in %)*



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

The increase in fiscal revenues, especially from collections of indirect tax, more than offset the rise in expenditure. For the whole of 2015 we forecast a deficit of 2.5%.

Figure 15
Fiscal expenditure (compared to previous year)*

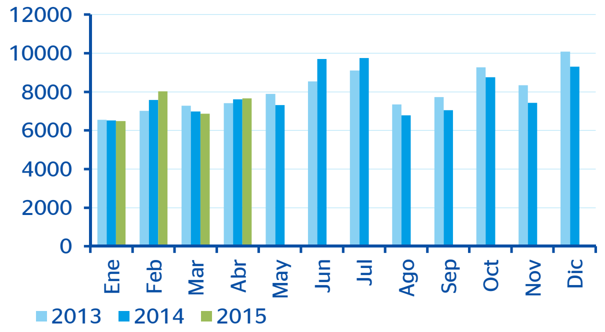


Figure 16
Fiscal revenues (compared to previous year)*

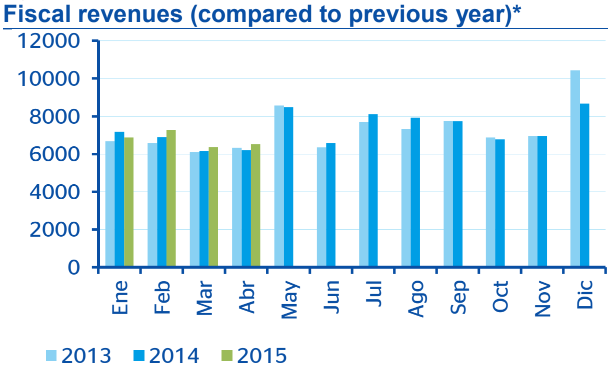


Figure 17
Public and private debt (% of GDP)*

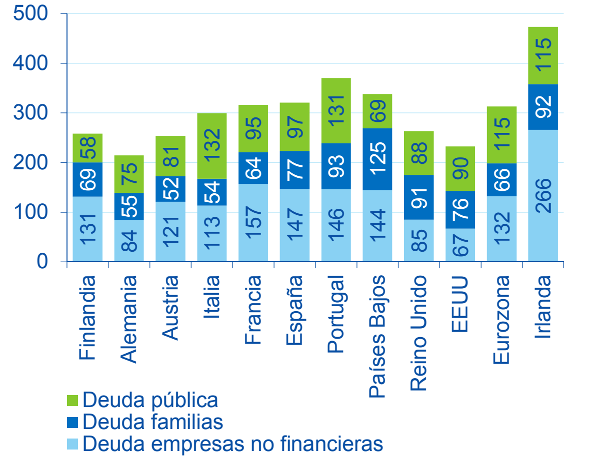
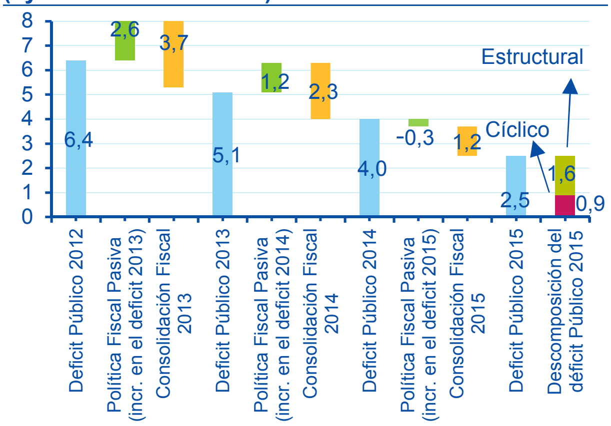


Figure 18
Decomposition of fiscal deficit (cyclical and structural)*



* Sources: HAVER and BBVA Research

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