Portugal: growth forecast for 2017 and 2018 raised

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Available data point to a stabilisation of GDP growth during 2Q17 at around 0.5% QoQ, SWDA[1] (see Figure 2). This estimate is likely to be the result of the continued growth of private consumption and the positive contribution of both the construction sector and tourism. This is despite a less positive behaviour of exports of goods and an uptick in the growth of imports. The trend shown by activity indicators together with the positive surprise in 1Q17 and the maintenance of conditions that will support the continuation of the recovery, **led to a raising of the growth forecast for Portugal's GDP to 2.6% in 2017 and to 2.3% in 2018**.

Consumption still shows no signs of slowing down

After slight moderation in **retail sales** during the first quarter of 2017 (3.0% YoY), the data for April and May **again show an acceleration** of growth and, on average, registered increases of around 4.7% YoY. **This same evolution was observed in vehicle registrations**, which, after an average monthly growth of 4.2% YoY between January and March, accelerated their progress to 15.8% on average in April and May. The **coincident indicator of private consumption**[2] **continued to improve**, recording a growth of 2.7% YoY in April and May, compared to an average of 2.5% in the first three months of the year. **Along the same lines is the evolution of consumer confidence**[3]**, which reached the highest level since its creation (see Chart 3).**

Investment, for its part, continues to show no clear signs of recovery. After the sluggishness of late 2016, **the known data for the Industrial Production Index (IPI) for machinery and equipment accelerated its growth** in the first quarter of the year (to 2.5% YoY on average between January and March). From this point of view, and as has been observed in other indicators of consumption or foreign trade, the month of April was weaker (1.0% YoY), while May recovered its momentum (3.3% YoY). **Industrial confidence remains optimistic**, around the levels observed in recent months (see Figure 4). In any case, the lack of traction of gross capital formation expenditure could be one of the reasons why new corporate financing operations continue to show declines in YoY terms (see Figure 5).

On the **residential investment side, the signals extracted from both supply and demand indicators show that the recovery is ongoing in the sector**. Specifically, housing building permits that were showing strong progress in the first three months of the year (monthly average close to 50% YoY) are expected to have slowed in April and May, although they are expected to have maintained a positive tone, with average growth of 7.3% YoY during these two

[1]: All variations expressed in QoQ or MoM terms are calculated on Seasonally and Working Day Adjusted data (SWDA).
[2]: Indicator published by Banco de Portugal, summarising the most significant information on the country's private consumption.
[3]: It measures the difference between the percentages of positive and negative responses regarding consumer confidence collected in surveys conducted by the National Statistics Institute.

months. This trend is repeated in mortgage loans to households which, after a sharp increase in 1Q17 (with a January-March average of nearly 50% YoY) have slowed down, although they were still growing above 30% YoY in April.

Exports stumble in April and reversal of low growth in imports

After the good results achieved by the foreign sector at the beginning of 2017, the information on the second quarter seems to correct part of the advance. Thus, **exports in April hardly changed compared to the same month of the previous year, although they recovered their growth trend in May (15.4% YoY).** In addition, **sales abroad were offset by the increase in imports** (11.4% YoY in April and 22.4% YoY in May).

Meanwhile, **the Portuguese tourism sector continues to show great strength** and after the increase of around 8% YoY (in the average of the first three months of the year), travellers arriving in the country have grown again above 15% YoY in the April and May average (see Figure 7).

Job creation is stagnating

Following the upward trend shown between January and March (with an average monthly growth of 1.1% YoY), **employment rose again in April (1.3% YoY) and May (1.1% YoY)**. In monthly terms it represents an advance in April (0.3% MoM) and fall in May (-0.1% MoM). The number of **employed persons therefore remained above 4.6 million people, which means that they have recovered something more than 50% of the employment destroyed between 2008 and 2012** (when the low point of recent years occurred). The unemployment rate stood at 9.4% in May, 0.4 pp lower than in March.

Improvement in forecasts

Information learned in the second quarter of the year, together with the strong increase in 1Q17 (1% QoQ) and improved fundamentals, led BBVA Research to raise Portugal's GDP growth forecast to 2.6% in 2017 and 2.3% in 2018 (from the previous 1.7% for both years).

In particular, the international environment is improving thanks to the **acceleration of world growth**. The good tone of world trade and positive growth forecasts for Europe and Spain, recently revised upwards by BBVA Research[4], will continue supporting the sales of Portuguese goods and services abroad. To this we should combine the reduction of **political uncertainty in Europe**, partly as a result of the results of the elections in France.

On the other hand, the factors that have driven the demand for Portuguese tourism services have been maintained. In particular, competitiveness gains, together with the perception of insecurity in some of the competing destinations for the national tourism sector, will continue to redirect the flow of visitors to Portugal. Additionally, the recent evolution of oil prices points to an annual average below what was expected 3 months ago and still 40% below 2014 levels. This should benefit the Portuguese economy, more so if the fall in prices is due to an increased supply in the fuel market, rather than a decrease in global demand.

[4] For further details see 3Q17 Spain Outlook available in: https://www.bbvaresearch.com/wp-content/uploads/2017/07/Spain_Outlook_3T17.pdf

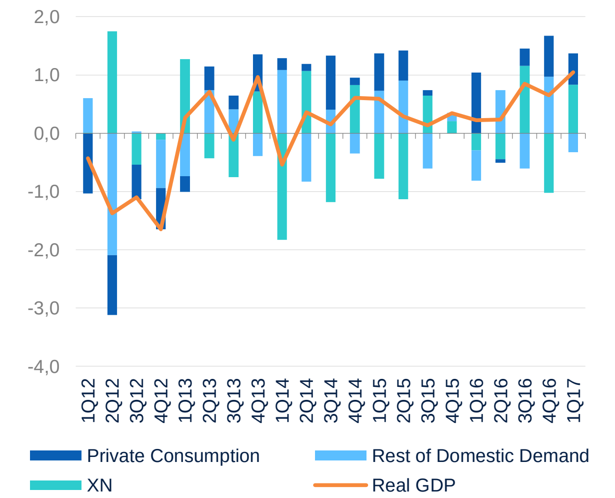
Both the evolution of activity in the euro area and the outlook for inflation confirm the expectation that benchmark interest rates will remain at historic lows in the coming months. In any case, once the probability of a deflation scenario is eliminated, the ECB is expected to start gradually withdrawing the stimuli currently in place from 2018 onwards. This maintenance of **lax financing conditions should support the continuation of the deleveraging process of the public and private sectors, as well as greater access to solvent demand**

Regarding the **tone of fiscal policy, it is expected to remain neutral**. **If the control on spending which has been observed so far is maintained, compliance with the deficit target is feasible.**

Finally, **uncertainty about economic policy has been on the decline**, as shown by the different confidence indicators. In any case, the imbalances still present in the Portuguese economy make it **necessary to implement reforms** that improve the functioning of the markets for goods and services, and promote a more intense and equitable recovery.

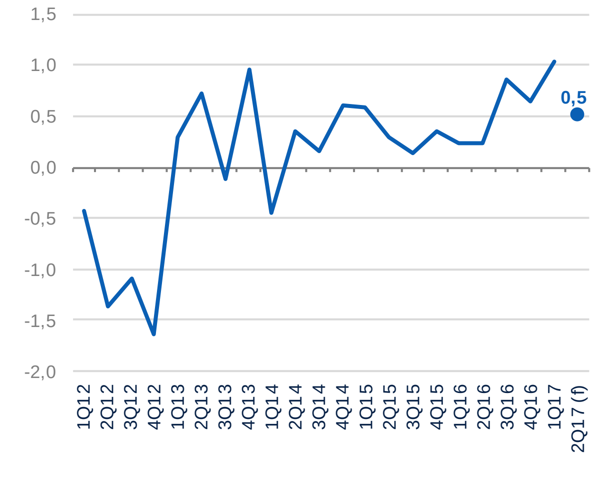
Main indicators of activity

Figure 1 GDP (% QoQ) and contributions by component (pp)



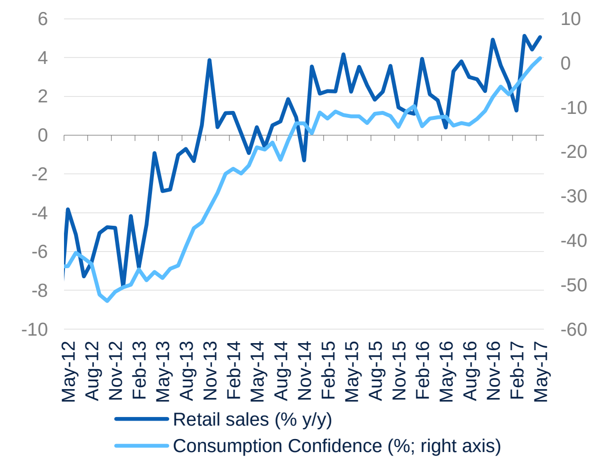
Source: BBVA Research based on INE

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



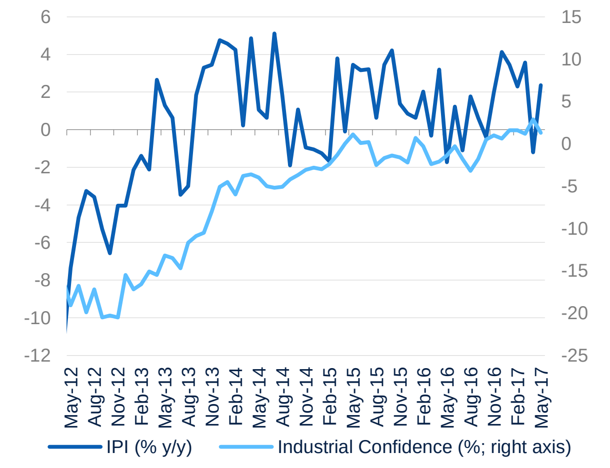
Source: BBVA Research based on INE

Figure 3 Indicators associated with consumption



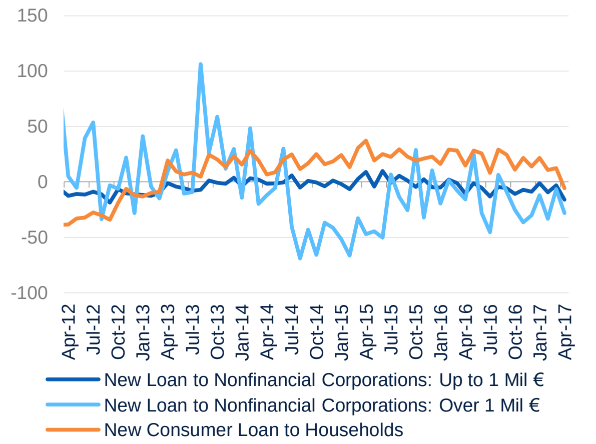
Source: BBVA Research based on INE

Figure 4 Indicators associated with industry



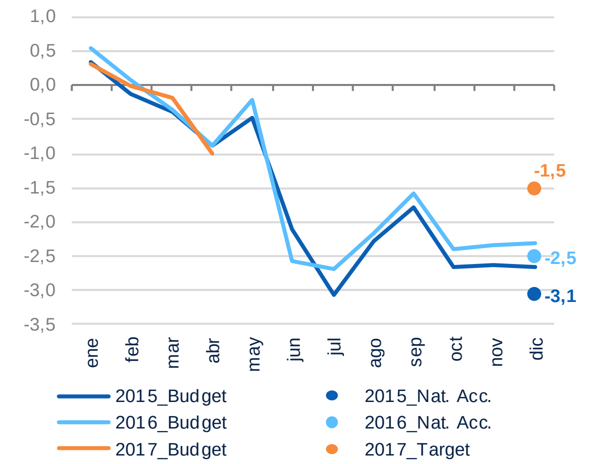
Source: BBVA Research based on INE

Figure 5 New loan to nonfinancial corporations and households (% YoY)



Source: BBVA Research based on BdP

Figure 6 Fiscal Deficit: Budgetary execution and National Accounts (% GDP, Not including injections to the financial sector.)

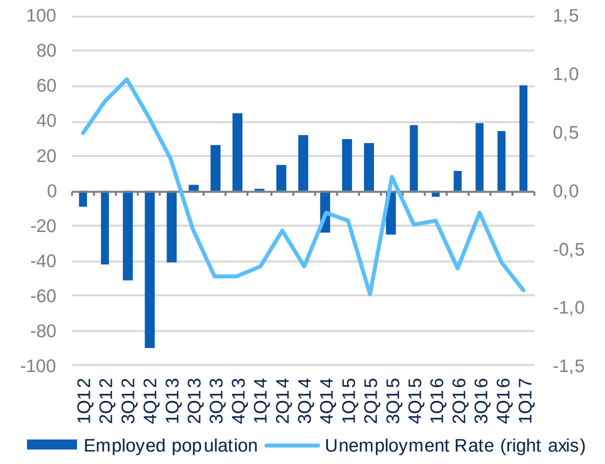


Source: BBVA Research based on BdP

Figure 7 Indicators associated with the external sector (% YoY)

Source: BBVA Research based on INE

Figure 8 Population employed (quarterly change in thousands of persons) and unemployment rate (quarterly change in pp)



Source: BBVA Research based on INE

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