Portugal: growth slows in 2Q17

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The growth rate of the Portuguese economy in 2Q17 decelerated to reach 0.3% QoQ[1], in line with the BBVA Research estimate (0.4% QoQ) and below that seen in 1Q17 (1.0% QoQ).

Based on data so far available, BBVA Research estimates that growth in 3Q17 will be around 0.5% QoQ, recovering part of the slowdown in 2Q17 but below the levels seen at the end of 2016 and the beginning of 2017 (see Figure 2). This would be the result of the return to growth on the part of private consumption and exports, and in spite of any corrections that may occur in investment after the sharp increase seen over the past few quarters. **The above would be consistent with a growth forecast for the whole of 2017 of 2.6% and of 2.3% for 2018.**

Contribution of domestic demand to growth with investment progressing at pace and fall in private consumption

Domestic demand contributed 0.8 pp to quarterly growth in 2Q17, higher than in 1Q17 (0.6 pp)**. Private consumption registered a variation of -0.2% QoQ (1.5% YoY),** which represents the first decline since the beginning of 2013. The exhaustion of tailwinds that have favoured the Portuguese economy or the historically low levels of the savings rate would be some of the factors behind the adjustment.

For its part, **public consumption continues to show little variation** (-0.1% QoQ, -0.9% YoY), consistent with the process of adjusting the public deficit.

Therefore, the main reason for the improvement in domestic demand is linked to the increase in quarterly terms of investment, whose growth in 2Q17 (6.0% QoQ; 9.3% YoY) reversed the stagnation of the previous quarter (0.0% QoQ; 7.7% YoY) and contributed 1pp to the quarterly GDP growth. Thus, with a contribution of 0.2 pp, Gross Fixed Capital Formation (GFCF) recorded its fifth consecutive quarter of growth (1.1% QoQ and 10.3% YoY in 2Q17 vs. 2.8% QoQ and 9.6% YoY in 1Q17). Investment in transport equipment was the item that contributed most to this contribution (0.4 pp to GDP growth in 2Q17), while construction drained almost 0.3 pp. Despite the positive figures, most of the investment support to GDP growth during this quarter was due to changes in inventories (0.8 pp).

[1]: Seasonally and working-day adjusted (SWDA) data. All quarterly (QoQ) and monthly (MoM) changes in this document are calculated on the basis of SWDA data.

Exports fall, unlike imports

Net external demand, after contributing 0.4 pp to quarterly growth in 1Q17, contributed negatively to GDP growth in 2Q17 (-0.5 pp). On the export side, the adjustment (-0.2% QoQ) brought about by the fall in the sale of goods abroad (-0.8% QoQ, after growing by 3% QoQ in 1Q17) and the slowdown in services (1.6% QoQ vs. 2.6% QoQ in 1Q17). The decrease in exports was accompanied by an increase in imports (0.7% QoQ), as a result of increases in purchases of goods (1.1% QoQ) and the decline in services (-1.7% QoQ). Nonetheless, this growth, as compared to that for the same quarter of the previous year, reveals the rise of both exports and imports in recent months. Thus, after growing by 9.5% YoY in 1Q17, sales to abroad did so again by 8.2% YoY in 2Q17, with a particularly positive evolution in the export of services. For their part, imports have maintained the growth rates of late 2016 and early 2017 of above 7.5% YoY, correcting the low growth seen in the middle of 2016.

The pace of employment is maintained during 2Q17

Data published for 2Q17 increase employment growth to 0.9% QoQ (3.2% YoY), matching the evolution seen at the beginning of the year. Jobs in the services sector linked to tourism have been the main driver of employment in Portugal. Although to a lesser extent, industry and construction also contributed to the advance.

3Q17: growth could stabilise at around 0.5% QoQ

The known data for the third quarter of the year, referring to July, point to a stabilisation of growth in rates close to 0.5% QoQ during 3Q17, albeit with a change in composition with respect to 2Q17. Consumption and exports will recover dynamism, while investment could correct some of the momentum.

On the one hand, retail sales slowed their records down slightly in July compared to the past few months. However, both the indicator that measures consumer confidence and the Coincident Indicators of Activity and Consumption[2] of that same month maintain the trend of improvement already seen throughout 2Q17. Thus, and given the fall seen during 2Q17, a slight uptick in private consumption is foreseeable during 3Q17, which, although it would correct part of the adjustment of the previous quarter, would not reach the growth seen in 4Q16 and 1Q17. Going forward, the sharp rise in consumption, especially during the course of 2016, the fall in household saving levels and the depletion of factors that have recently favoured Portugal, suggest a **slowdown of private consumption contributions to GDP growth in the coming quarters.** In any case, it is expected that this process will occur gradually given the maintenance of lax financing conditions and the progressive withdrawal of stimuli by the European Central Bank.

On the other hand, and although 2Q17 registers have been positive in terms of investment, the Industrial Confidence Indicator prepared by the European Commission shows somewhat less favourable figures in July and August, a sign of the embryonic nature of the recovery. This, together with a lower contribution of inventories, would lead to a less intense advance in investment during 3Q17 than that seen in 2Q17. However, **international perceptions continue to**

[2]: Indicators published by Banco de Portugal, summarising the most significant information on the country's economic activity and consumption.

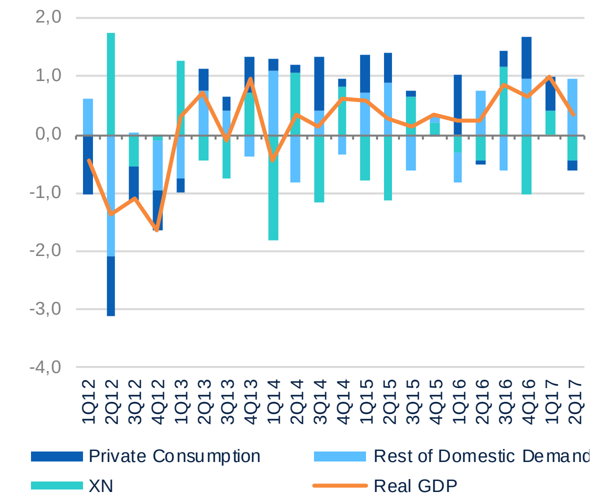
improve and this is reflected in the recent upward revision of Moody's rating outlook for Portugal, from stable to positive.

With respect to the Portuguese external sector, and despite the weak evolution shown between April and June, **exports are expected to maintain the positive momentum shown at the end of 2016 and early in 2017** and to continue contributing to growth in 3Q17. The improvement in forecasts for global growth and especially regarding Europe and Spain will continue to support the country's growth. **In addition, competitive gains coupled with the ongoing instability of some destinations that compete with Portugal will continue to attract tourism**. In fact, travellers coming into Portugal rose again between March and June with average monthly increases above 10% YoY. Finally, and as expected during 2Q17, the sluggishness of imports that had been seen was partly reversed and it is hoped that this behaviour will continue over the coming quarters. This would reduce the contribution of the external sector to GDP growth, or even make it negative.

Finally, **the monthly employment data continues to be positive.** Specifically, after an average monthly growth of close to 3.2% YoY (0.2% MoM) between April and June, employment in July increased by 2.7% YoY (0.3% MoM).

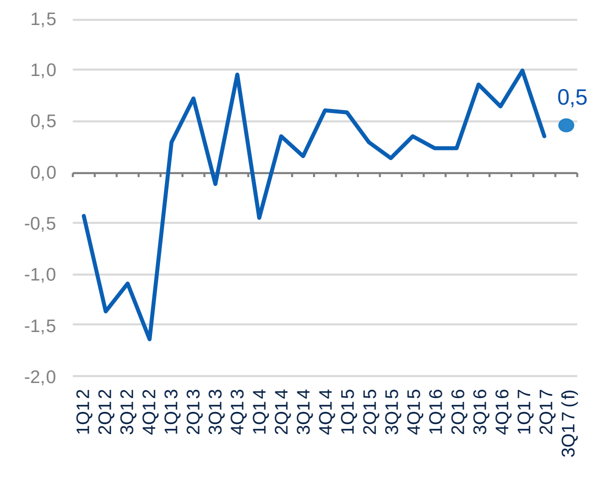
Main indicators of activity

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



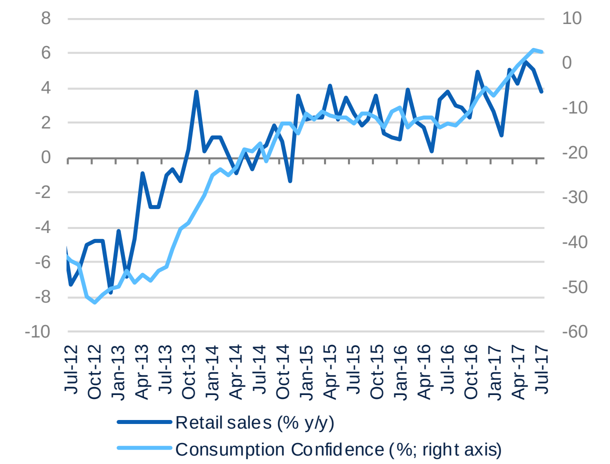
Source: BBVA Research based on INE

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



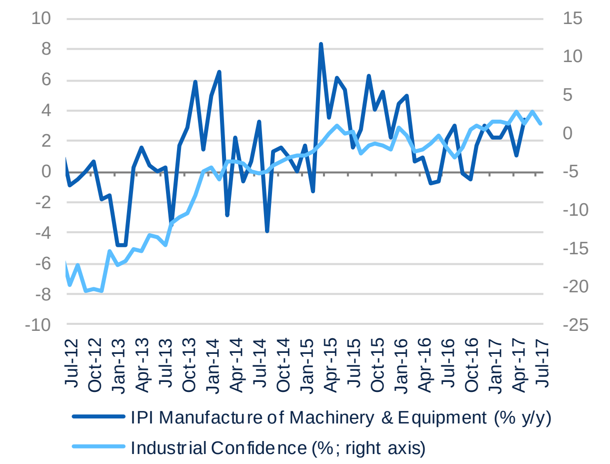
Source: BBVA Research based on INE

Figure 3 Indicators associated with consumption



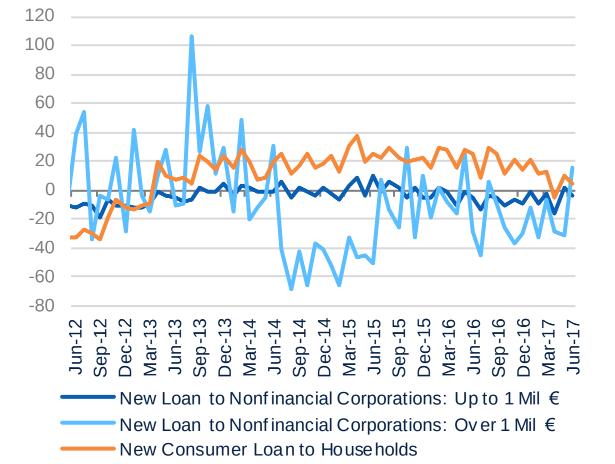
Source: BBVA Research based on INE

Figure 4 Indicators associated with industry



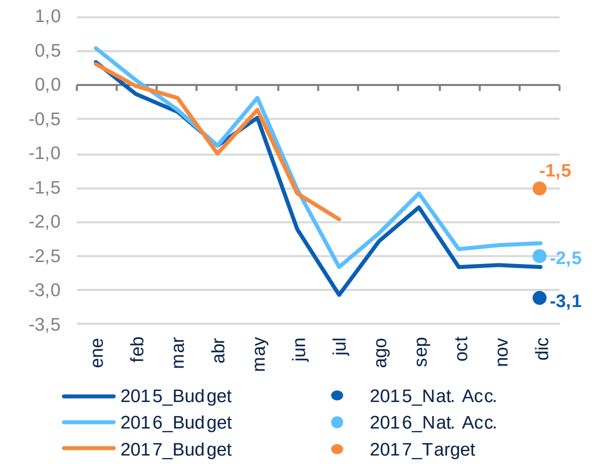
Source: BBVA Research based on INE

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



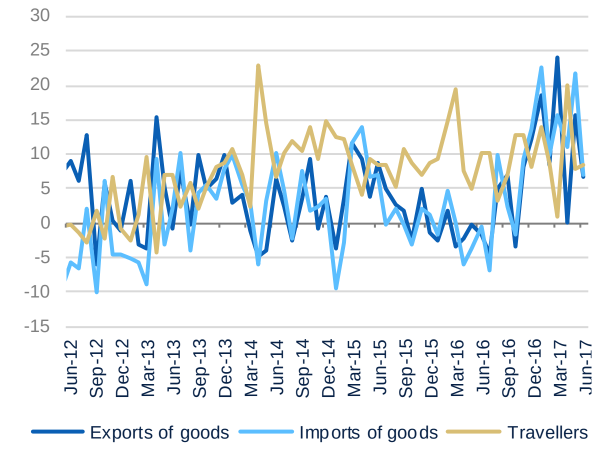
Source: BBVA Research based on BdP

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



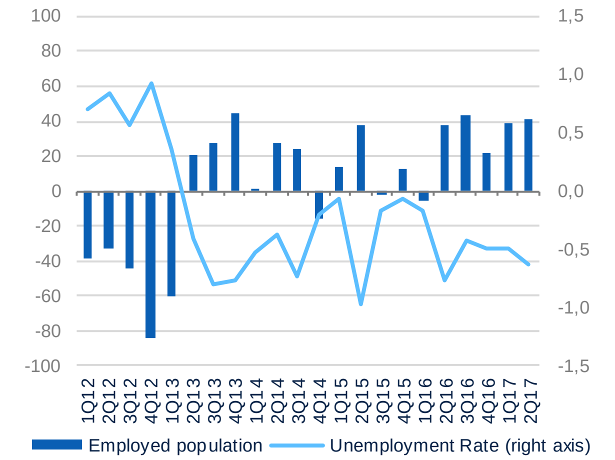
Source: BBVA Research based on BdP

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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