

ECONOMIC WATCH

GDP growth will continue to remain sound in 1Q18

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Portugal saw out 2017 with the highest growth in GDP recorded since 2001, 2.7% YoY, following the acceleration observed in the second half of the year. According to official figures, the increase in activity in 4T17 was 0.7% QoQ (0.3 pp above the BBVA Research forecast), largely due to the upturn in exports (see Figure 1). Over the course of the year we saw a marked increase in internal demand, especially in private consumption and investment, which registered average quarterly contributions of 0.3% to the growth of the economy.

The estimate of BBVA Research based on the monthly indicators available to date points towards **the GDP increasing in 1Q18 in the region of 0.7% QoQ SWDA¹, which maintains forecasts for the whole of 2018 and 2019 at 2.3% and 1.8% respectively** (see Figure 2).

At an external level, the main factors behind these forecasts include **higher-than-expected growth from the UEM, together with increasingly synchronised global recovery²**, which would offset the potential loss of competitiveness that would be seen with slightly higher oil prices. **We also forecast that support for monetary policy will continue, with normalisation expected to take place gradually**, ensuring an environment of low interest rates over the coming two years.

Internally, positive highlights include lessened uncertainty about economic policy and an expected increase in public consumption, following the discipline shown by the government in recent years in meeting its commitments. Similarly, **while private consumption would remain robust, its rate of growth would level off**, following the marked increases seen in previous quarters. **Lastly, despite the expected recovery in exports, external demand will continue to drain growth** because of the increase in imports driven by the improvement in investment and private consumption.

1: All variations expressed in QoQ or MoM terms are calculated based on Seasonally and Working Day Adjusted (SWDA) data.

2: See BBVA Research, Global Economic Outlook, January 2018, available in Spanish at: <https://www.bbvarresearch.com/wp-content/uploads/2018/01/1801-Situacion-Global.pdf>

Private consumption and investment were the components that made the greatest increase to the growth of the Portuguese economy in 2017

Domestic demand contributed with 2.9 pp to Portuguese GDP growth in 2017, the greatest contribution over the past 17 years.

Improved consumer confidence, as well as the positive figures regarding the labour market and access to household credit, meant that **private consumption registered growth of 1.7% YoY compared to 2016** despite the correction observed in the final quarter of 2017 (0.3% QoQ from the figure of 1.4% QoQ of 3Q17).

Public consumption, however, still has not shown significant variations with 0.1% QoQ in 4Q17, which means growth of 0.1% YoY for the whole of the year (0.6% in 2016), consistent with the process of adjustment of the public deficit. Also, according to budget implementation figures, the accumulated deficit was in the region of 1.4% of GDP, which means a reduction of 0.6 pp against the deficit of 2016 (see Figure 6) and fulfilment of the target set for the year as a whole (1.5% of GDP).

On the other hand, investment grew by 8.4% YoY in 2017, significantly above the increase observed in 2016 (0.8% YoY), which represents the highest rate in the last five years, even with the weakness observed in the final quarter of the year (-0.4% QoQ). The increased investment in machinery and equipment (+16% YoY in 2017), and construction would have contributed to this growth.

Lastly, **new business credit operations continued to reduce the heavy adjustments seen at the beginning of 2017**. Similarly, transactions under €1 million fell in December 2017 by -2.3 YoY (compared with -8.7% in December 2016), while those over €1 million increased by 40% YoY in Dec-17 (-30% YoY Dec-16) (see Figure 5).

The increase in imports offset the healthy performance of sales abroad

Net external demand reduced growth in the Portuguese economy in 2017, -0.2 pp (0.0 pp in 2016), even while in 4Q17 it contributed 0.6 pp to GDP growth. Imports counteracted the positive performance of the export sector by growing in 2017, in line with exports, some +7.9% YoY with regard to 2016. On the other hand, inward tourism posted a significant hike in the final quarter, 6.7% QoQ SWDA and for 2017 as a whole, growth of +8.6% in respect to the previous year.

Portugal in 4Q17 recorded its lowest unemployment rate since 2008

The higher growth in 2017 was reflected in the favourable growth in employment and enabled Portugal to close out December 2017 with its lowest unemployment rate of the past thirteen years (8.0%), becoming the third-largest recorded decrease among EU28 countries, just behind Greece and Croatia according to Eurostat. **Also, in 4Q17, Portugal posted unemployment figures of 8.1% QoQ, 9.4 pp less than the maximum level recorded in 2013 and the workforce in employment grew to 4.8 million persons, 3.3% higher than in 2016**. The sectors of services and industry, construction, energy and water were once again the main drivers of employment in Portugal, **just as they had been in 2016**.

1Q18: growth could stabilise at around 0.7% QoQ

The most recent monthly indicators confirm the trends in consumption and investment, signalling that the Portuguese economy will grow by around 0.7% QoQ in 1Q18, making it possible to maintain GDP growth forecasts for the whole of 2018 and 2019 at 2.3% and 1.8% respectively.

Retail sales continued their positive trend in January (5.4% YoY) in line with figures for 2017 as a whole, albeit with a slight decrease (-0.5% MoM). In turn, consumer confidence and the Coincident Indicator for Private Consumption continued to slow their growth (see Figure 3). This would be in line with the expectations already pointed out in previous outlooks that pointed precisely to a slowdown in the contributions of private consumption to GDP growth in the coming quarters.

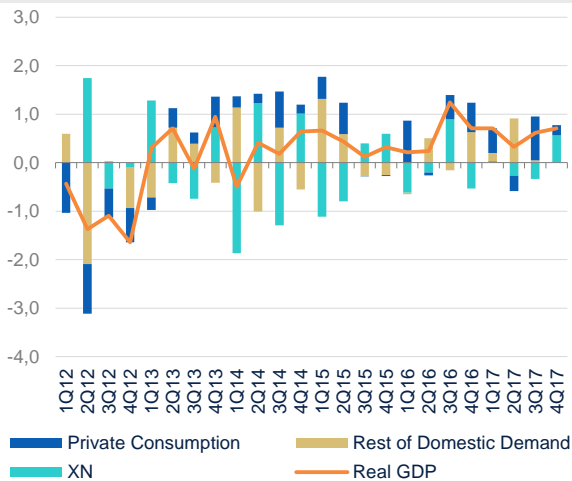
On the other hand, **the Industrial Production Index increased by 2.5% MoM in January**, while the Industrial Confidence Indicator prepared by the EU Commission stood at 2.6% in February of this year (3.3% in Dec-17).

In terms of the **sale of goods abroad**, they grew in January by 17.4% MoM (9.6% YoY), after falling in December 2017 by 21.9% MoM causing stagnation in year-on-year growth. Vehicles, aircraft, ships and other forms of transport, as well as machinery and electrical equipment were the main items producing this increase. Imports on the other hand grew by 10.1% MoM in January of this year (12.4% YoY).

Finally, **monthly employment data remains positive although they decelerated slightly.** Specifically, following average monthly growth figures around 0.3% MoM in 2017, the January employment figure, despite being positive, was a mere 0.04% MoM (3.6% YoY) and the unemployment rate fell by 0.1 pp to reach 7.9%.

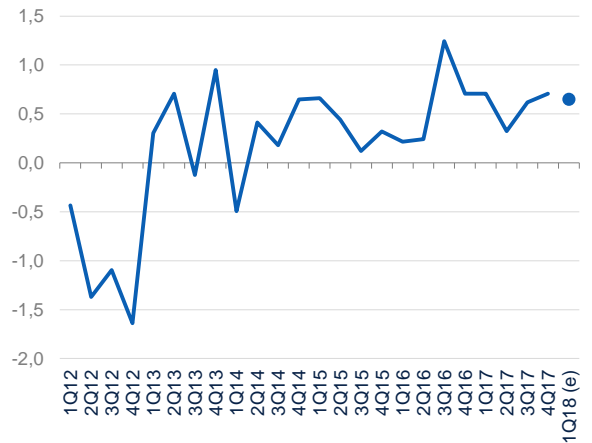
Main indicators of activity

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



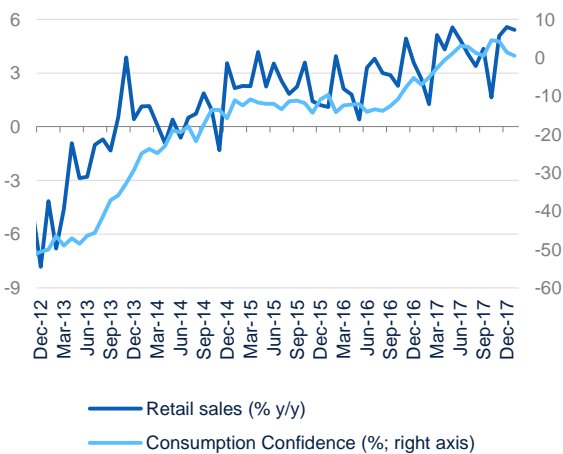
Source: BBVA Research based on INE data

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



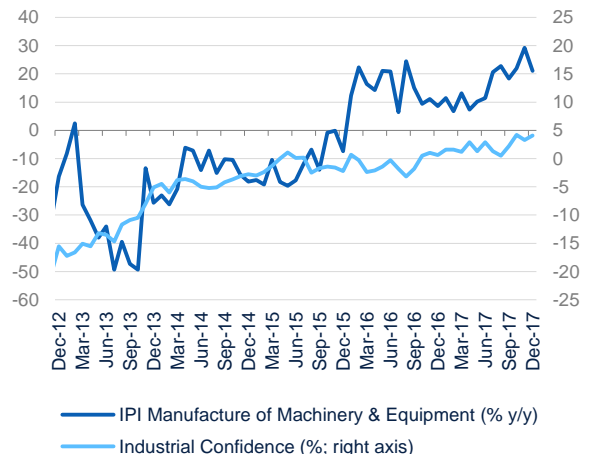
Source: BBVA Research based on INE data

Figure 3 Indicators associated with consumption



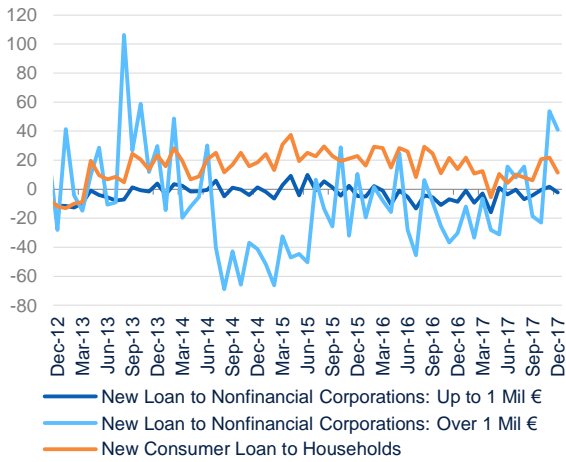
Source: BBVA Research based on INE data

Figure 4 Indicators associated with industry



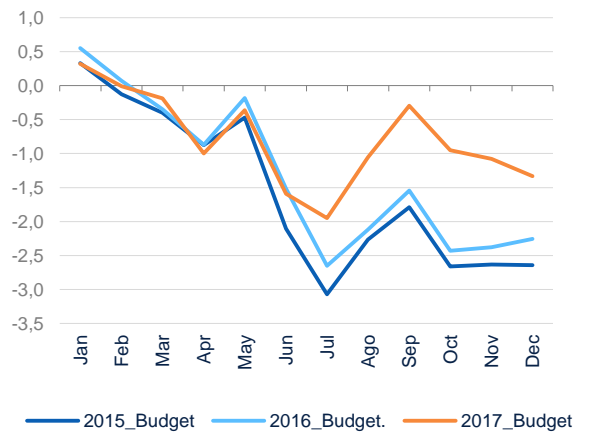
Source: BBVA Research based on INE data

Figure 5 New household and business credit (% YoY)



Source: BBVA Research based on INE data

Figure 6 Fiscal Deficit: Budget implementation (% GDP, without including financial sector aid)



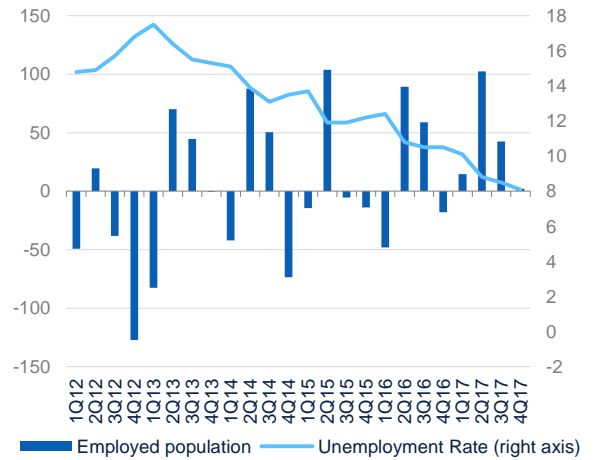
Source: BBVA Research based on INE data

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



Source: BBVA Research based on INE data

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



Source: BBVA Research based on INE data

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