Portugal in 2021: Structural factors point to a weak recovery

Portugal's economy faces a number of hurdles in 2021 to a swift recovery, notably the revival of the tourism sector. But the situation is not as grim as that in neighbouring Spain

Particular vulnerablilities

Even though the health crisis was less severe in Portugal than in other European countries, notably Italy and Spain, the economic impact of the first wave and corresponding lockdown measures was harsh. In the first half of 2020, economic activity dropped by 18% compared to pre-crisis levels, while neighbouring Spain, where the health crisis was one of the worst in Europe, lost about 22% of activity over the same period. Obviously, the economy recovered in the third quarter, but the resurgence of the pandemic in October and new containment measures make a double-dip recession more likely.

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The Portuguese economy has a number of characteristics that make it more vulnerable to both the initial shock of the pandemic and its aftermath. For starters, the country has a large tourism sector, which is impacted strongly by the crisis. In addition, Portugal ranks in the top five eurozone countries with the highest share of small companies (defined as companies with 0 to 9 employees). Smaller companies generally have limited financial, managerial and technological resources. It is, for example, more difficult for small firms to respond to the crisis with technological solutions such as telework. And the fiscal space of Portugal is also relatively low, as the government debt-to-GDP ratio stood at 117% last year.

These characteristics lead us to conclude that the Portuguese economy will need more time to recover from the 2020 recession compared to the eurozone average.

Interestingly, Spain also suffers from the same structural issues discussed above as Portugal. But we think that the situation in Portugal is less grim. First, the health crisis was not as severe compared to Spain. Second, even though Portugal has a similar share of vulnerable workers as its neighbour, the unemployment rate is much lower. Spain entered the crisis with an unemployment rate of 13.8%, while Portugal's was just 6.7%. Finally, even though the debt level is high and will increase sharply, the structural budget balance in 2019 calculated by the European Commission was lower than in Spain, which implies more fiscal space. On top of that, Portugal will receive grants worth more than 4% of GDP over the next two years from the European Next Generation EU fund.

The Portuguese economy in a nutshell

	2019	2020F	2021F	2022F
GDP growth (%)	2.2	-8.2	3.5	3.1
Headline CPI (%)	0.3	-0.3	0.2	1.2
Unemployment rate (%)	6.6	7.3	7.9	7.5
Budget balance as % of GDP	0.1	-7.1	-4.5	-3.5
Government debt as % of GDP	117.2	132.3	130.7	128.6

Source: Refinitiv Datastream, all forecasts ING estimates