

18 January 2018  
Article

## Portugal: Riding the growth wave

Portugal's economy will grow more than 2% this year, helped by some mild fiscal stimulus. But with lingering bank issues, a spending splurge is unlikely

### Content

- Domestic demand drives growth
- Investment recovery and surprisingly strong employment
- Strong growth and fiscal adjustment at the heart of a two-notch upgrade
- Mild fiscal push to support GDP growth in 2018, but lingering bank issues suggest prudence

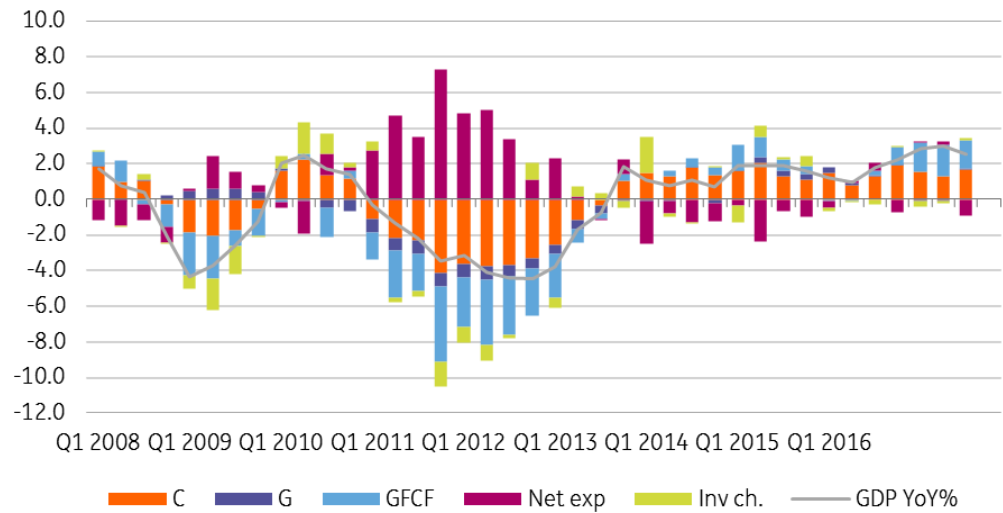
### Domestic demand drives growth

The Portuguese economy is still riding the growth wave with no sign of a slowdown. In 3Q17, private consumption (which added 1.7% to growth year-over-year) and gross fixed capital formation (which contributed 1.6% YoY) were confirmed as the main drivers of annual GDP growth. Despite a substantial export drive, net exports acted as a drag on growth (-0.9% YoY).

### Investment recovery and surprisingly strong employment

With capacity utilisation almost back to pre-crisis levels, a recovery in private investment was expected. The improvement in private consumption came somewhat as a surprise, however, though this was consistent with unexpectedly strong employment and recovering wage growth. Data on employment expectations suggests that this pattern might continue in the short run, but could soften over time, as the current high elasticity of employment to GDP looks unsustainable. The recent decline in productivity already signals some potential future strain in cost competitiveness.

### Domestic demand traction continued unabated (contribution to YoY GDP growth)

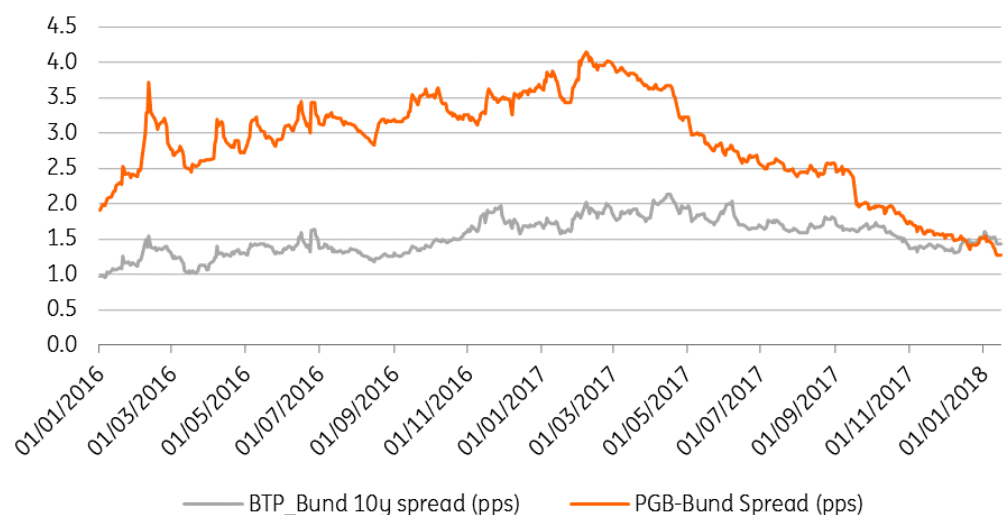


Source: Thomson Reuters

### Strong growth and fiscal adjustment at the heart of a two-notch upgrade

Above-potential GDP growth had a positive impact on fiscal data, putting the 1.5% deficit-to-GDP target for 2017 well within reach. The concurrent expected decline in the debt-to-GDP ratio was an additional piece of evidence that led Fitch to upgrade Portugal by two notches in December. We expect Portugal's fiscal stance to remain mildly expansionary in 2018, which should help the economy to grow slightly more than 2% over the whole year.

### Growth and adjustment mix did the magic: now 10y PGBs trade through Italian BTPs



Source: Thomson Reuters

### Mild fiscal push to support GDP growth in 2018, but lingering bank issues suggest prudence

Room for laxer fiscal policy remains limited, though. Despite the ongoing deleveraging and improved financial stability, Portuguese banks' balance sheets are still burdened by a heavy load of non-performing loans. Keeping some fiscal room for a rainy day could still be prudent. With the Portuguese finance minister Mário Centeno now heading the Eurogroup, the risk of Portugal

indulging in any fiscal splurge looks very small indeed.

**Paolo Pizzoli**

Senior Economist, EMU, Italy, Greece

+39 02 55226 2468

[paolo.pizzoli@ing.com](mailto:paolo.pizzoli@ing.com)

### **Disclaimer**

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("**ING**") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group NV and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. The producing legal entity ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is subject to limited regulation by the Financial Conduct Authority (FCA). ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.