Portugal

Caught up by the crisis

After what proved to be a rather mild slowdown, Portugal's GDP growth ended up in the upper range of expectations at 2.2% in 2019. The Covid-19 pandemic will surely erase the country's enviable performances as whole segments of the economy come to a standstill and the country sinks into a major recession in the weeks ahead. Similarly to its European counterparts, the Costa government is steadily implementing a series of measures to preserve the economic system during the crisis and safeguard the country's capacity to recover.

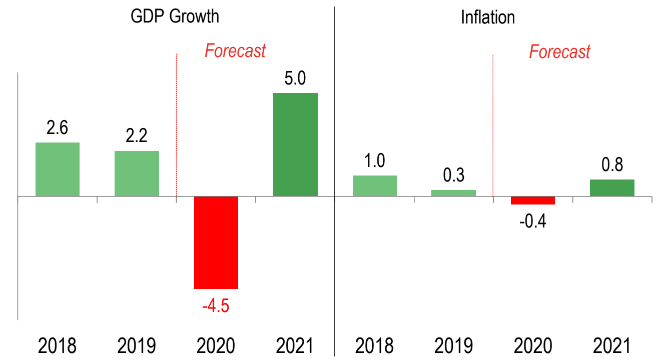
Portugal was already in the midst of a gradual but firm economic slowdown when it was caught up by the Covid-19 epidemic. Although the Q4 2019 rebound in GDP came as a surprise (+0.7% q/q after +0.3% in Q3), the mediocre quality of its components confirmed that the economy was running out of steam, (the first signs of which had appeared last fall), and that the business climate was deteriorating. Supported by a strong rebound in exports (which is sure to be short lived), the fourth quarter was marked by the stagnation of private consumption, a downturn in investment and massive destocking, which only amplified the slowing of domestic demand, a trend that gradually set in over the course of last year.

The coronavirus epidemic hit Portugal somewhat belatedly. At the end of March, the situation was not nearly as disastrous as in the neighbouring countries (Spain, France and Italy). The crisis is nonetheless poised to intensify in the weeks ahead, although the lag has given the Lisbon government some precious time to make a few early decisions. After closing schools and certain public spaces, the government declared a countrywide state of emergency effective 20 March, imposing confinement measures that are virtually identical to those in France. Portugal closed its borders with Spain, one of the epicentres of the epidemic, except for merchandise transport and cross-border workers. All air, sea and river travels were suspended.

Like the other European economies, Portugal will now have to prepare for a major recession in the months ahead. The downturn will apparently be concentrated in the second quarter, followed by a rebound, although for the moment, it is hard to foresee its timing or size. At this stage, rather than serving as veritable forecasts, our estimates mainly provide an idea of the order of magnitude. In Q2, we can expect the economy to contract by at least 10% q/q, which would bring the decline in full-year 2020 GDP to between 4% and 5%. We should expect coronavirus confinement measures to be accompanied by a major decline in the volume of services, especially personal care, retailing, and hotel and food services. The impact will not be as severe in other sectors of activity, like corporate services, construction and industry, although it will still be strong. Portugal has two other weaknesses: the heavy weighting of tourism and international goods transport. The epidemic could have a major, lasting impact on international tourism and travel, the weight of which has more than doubled over the past 10 years and now accounts for over 8% of GDP.

In addition to expenditures linked directly to the health crisis, the government has set up a series of measures to mitigate as best as possible the impact of shutting down businesses on employment and corporate solvency, in order to be prepared for the recovery. Portugal's economic fabric can be characterised by the high density of small and mid-sized companies, which means it must be particularly careful to minimize the destruction of productive capacity.

1- GDP Growth and inflation
(Y/Y, %)



Source: National Statistics, BNP Paribas

For the moment the government's economic support plan is built around four vectors: 1) vast measures to subsidise partial unemployment, which enable workers to preserve up to two thirds of their wages in the hardest hit sectors; 2) deferred tax payments and social security contributions; 3) a moratorium on capital and interest payments for certain bank loans to households (residential) and companies; and 4) corporate credit lines provided by banks with state guarantees. Initially estimated at EUR 9.2 bn (including EUR 3 bn in state guarantees), the cost of these and any additional measures will certainly rise in the weeks ahead.

Although Portugal still has a very high public debt ratio of just under 120% of GDP, the country is entering the crisis with solid public finances. In 2019, it ended up reporting a fiscal surplus of 0.2% of GDP, which it was not targeting until 2020. The fiscal manoeuvring room that Portugal has built up so diligently in recent years is about to pay off.

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