PORTUGAL

SOME FISCAL LEEWAY TO SUPPORT THE RECOVERY

Despite managing well the epidemic, Portugal has experienced a severe economic shock in Q2. Real GDP plunged by 13.9%, pulled down by sharp falls in goods and services exports (-36.1% q/q) and private sector consumption (-14.0% q/q). Investment dropped (8.9% q/q). The country has been heavily impacted by the collapse in tourism inflows and foreign activity, particularly in Spain. External factors could also hamper the recovery, particularly given the surge in new Covid-19 cases in Spain. Nevertheless, the improvement in public finances operated in recent years should translate into a government deficit for 2020 smaller than in other European countries – around 7.0% of GDP according to government estimates. This provides relatively more leeway to support the recovery.

Despite the easing of lockdown measures, many difficulties have persisted this summer. The UK's government decision to impose – between 10 July and 20 August– a quarantine period for travellers returning from Portugal has caused further downward pressures on the tourism sector. In July, arrivals were nearly two-thirds below their 2019 levels[1]. The same quarantine measure was reintroduced on 10 September. In addition, the resurgence of Covid-19 cases in Spain may indirectly impact Portugal's economic recovery – until the end of this year at least – due to the trade connectivity between the two countries[2].

Unsurprisingly, the impact of the lockdown measures on the labour market has been strong: employment fell 3.8% between January and July. The jobless rate climbed above 8% in July (8.1%) –its highest level since October 2017– while the youth unemployment rate (15-24 years old) rose to 26.3%. However, the labour market was already losing momentum well before the Covid-19 outbreak. The annual growth in employment had been slowing since 2018, reflecting the weakening in new job offers (see Chart 2).

The effects of the current crisis on the public finances should also be put into context. The country has improved its budgetary position over the past decade and posted a surplus of 0.2% of GDP in 2019. The public deficit will be substantial this year, but should remain close to the level recorded in 2010[3]. The government deficit in 2020 is thus likely to be smaller – relative to GDP – than in Spain or France. These two countries were still running large structural budget deficits prior to the pandemic.

That said, Portugal's government debt remains the third highest in Europe, behind Greece and Italy. As a share of GDP, public debt climbed to 127.2% in Q2. The European Commission now forecasts that the government debt-to-GDP ratio will hit 131.6% in 2020, before falling back to 124.4% in 2021, as growth rebounds.

Lastly, deflationary pressures are building, reflecting the protracted decline in demand. The core CPI (excluding processed foods and energy) fell by 0.4% over the last six months (August-February).

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GROWTH AND INFLATION (%)

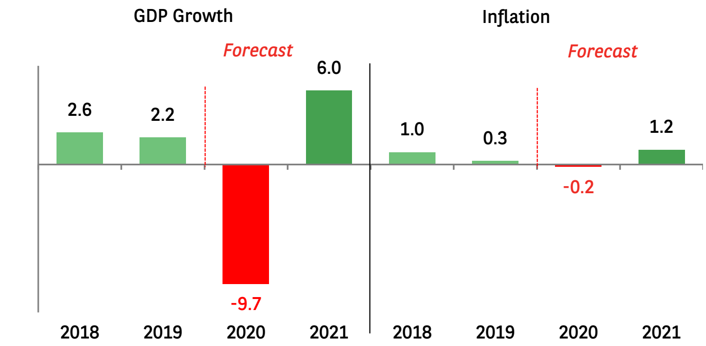

CHART 1 SOURCE: EUROPEAN COMMISSION, BNP PARIBAS

NEW JOB OFFERS

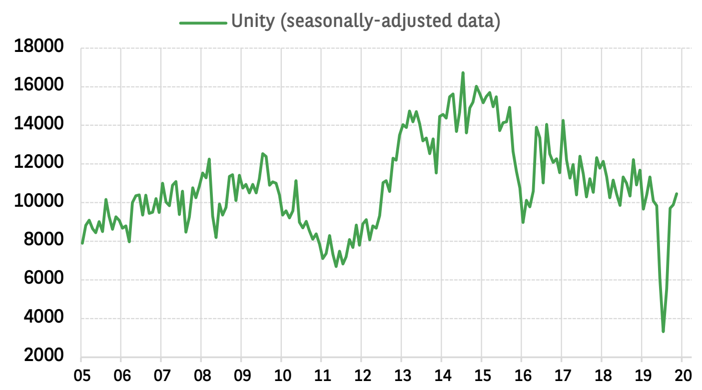

CHART 2 SOURCE: NATIONAL STATISTICS, BNP PARIBAS

1 According to Portugal's national statistical office (INE), the number of overnight hotel stays was 1.024 million in July 2020, down from 2.849 million in July 2019.
2 Spain accounts for approximately a quarter of Portuguese goods exports..
3 Between January and July 2020, the central government's deficit was EUR8.48 billion, compared with EUR8.90 billion in the same period in 2010.