CATÓLICA-LISBON **Forecasting Lab** | NECEP

Executive Summary

Taking into account recent developments, in particular the good performance of the Portuguese economy in the first quarter, the NECEP projects **GDP growth of 2.7% in 2017**, an upward revision of 0.3 percentage points (pp) from the April estimate. This forecast is involved in a **considerable degree of uncertainty** due to the combination of calendar effects, high deflators and significant changes in inventories that blur the first quarter data. Thus, it is difficult to extract unequivocal signals from it. The projection results from the cumulative effect of three **favourable factors**: the stronger growth in the euro zone, the lagged effects of last year's fiscal policy and the clear signs of cyclical recovery of the Portuguese economy. If NECEP estimate materializes, it will be the strongest GDP growth since the year 2000, surpassing the 2.5% observed in 2007.

The second quarter maintains, qualitatively, the recovery of the Portuguese economy. However, the abovementioned effects make it difficult to quantify the **quarter over quarter GDP growth**. The best estimate of the NECEP for this rate is **0.7%** (**3.3% year-on-year**), but a hiccup in the data is possible. Even with slightly weaker growth, the strong dynamics of the Portuguese economy should be consistent with our GDP annual growth forecast.

In fact, the Portuguese economy seems to be going through a period of unambiguous cyclical recovery, now also visible in **investment**. The quarterly GDP output may return to 2010 levels by the end of this year. However, the investment is still about 30% below the levels of that year, so it will be necessary to observe a stronger and longer sequence of growth in this aggregate to assess the strength of the current recovery.

The updated **public finance** data suggests the maintenance of the structural balance in 2017. An improved outlook of the economy leads the **headline deficit** projection to be **2.1%** of the GDP against the Government's target of 1.5% assumed in the Stability Programme 2017-2021. However, as in 2016, the Portuguese Government might resort to a set of executive measures to meet its own nominal targets.

The improvement in economic conditions in 2017 lead to an upward revision of 0.2 pp on the **GDP growth in 2018,** to **2.1%.** The uncertainty surrounding this projection is high, but it reflects an already favourable estimate of GDP trend growth next year. This improved outlook may spread to the **2019** GDP growth projection, with a new central point of **1.9%**, an upward revision of 0.3 pp. The Portuguese economy may be in a sweet spot with above average and growing trend GDP growth.

Unusually high uncertainty surrounds these projections coming from internal and external conditions. On the domestic front, doubts remain about the **soundness of fiscal consolidation** and the pace of public debt reduction in the context of persistent risks in the financial sector, but also about government resistance to political pressure to abandon fiscal discipline. On the external front, the risks observed over recent quarters on the reorientation of **US and UK economic policy** and their consequences for the world economy and the euro area remain. The clearer sign of **monetary policy normalization**, both in the US and in the euro zone, also poses an additional risk to heavily indebted economies such as the Portuguese.

Forecasts from Católica Lisbon Forecasting Lab – NECEP

Region	Indicator	2017Q1 a)	2017Q2	2017	2018	2019
Portugal	GDP (% change on previous quarter)	1.0	0.7	-	-	-
	GDP (year on year % change)	2.8	3.3	2.7	2.1	1.9
	Private consumption (q-o-q % change)	0.8	0.4	-	-	-
	Private consumption (y-o-y % change)	2.2	2.7	2.6	2.3	2.0
	Unemployment rate (%)	10.1	9.0	9.4	8.9	8.7
	Consumer prices (annual % change)	0.8 b)	1.1 b)	1.6	1.6	1.6
Euro area	GDP (% change on previous quarter)	0.6	0.7	-	-	-
	GDP (year on year % change)	1.9	2.3	2.2	1.8	1.6

a) Official values (Statistics Portugal – INE/Eurostat); b) Values at the end of the quarter.