CATÓLICA-LISBON

Forecasting Lab | NECEP

Executive Summary

In the 4th quarter of 2016, the Portuguese economy likely grew 0.6% over the previous quarter and 1.8% year-on-year. This estimate is partly due to the positive surprise of the latest GDP data released by INE for the 3rd quarter of 2016, which indicated a 0.8% growth over the previous quarter (1.6% year-on-year). If this estimate proves correct, GDP growth in 2016 is 1.3%, 0.4 percentage points (p.p.) above the forecast in the previous Quarterly Newsletter.

The occurrence of positive **temporary shocks** on GDP, in particular those resulting from **fiscal policy** that has become progressively more intense throughout the last calendar year with the reduction of the VAT tax rate applicable to restaurants in July and the full reinstatement of the cuts to civil servants wages in October, might explain this result. Thus, the abovementioned estimate for quarterly GDP growth has additional uncertainty related to this fiscal stimulus and it might not reflect a stronger underlying dynamic of the economy. Given the «neutral» nature of the Government Budget for 2017, that fiscal effect could favor the economic growth in the first semester, with expected year-on-year changes in GDP close to the 2% threshold.

Therefore, NECEP revised the GDP growth forecast for **2017** in +0.6 p.p. with a new central projection of **1.7%** but involving a large confidence interval. Once temporary effects deplete, the Portuguese economy might return to a moderate growth path with projected GDP growth of around **1.4% in 2018 and 2019**.

The **main risks** to the Portuguese economy are still financial, either from capital needs by the banking sector or fiscal consolidation requirements. The Government's target for the general balance in 2016 (-2.4% of GDP) is realistic but the official publicly available information are not clear about the way it was be attained. The **high debt ratio** (130% of GDP) remains a latent risk that may affect the financing of investment, given the **upward pressure to interest rates**. The **weakness in investment** is a matter of concern that explains, in part, the perspectives for moderate growth in the forecasting horizon (2019), noting that the gross fixed capital formation should contract in 2016.

The **external outlook** is now slightly more benign, with a stronger recovery in the euro zone and surprisingly optimistic outlook for the US economy, despite the unusual risks surrounding the new Trump administration. The process around *Brexit* remains uncertain, and it is not yet clear what its impact will be for the European and World economies.

Forecasts from Católica Lisbon Forecasting Lab – NECEP

Region	Indicator	2016Q3 a)	2016Q4	2016	2017	2018	2019
Portugal	GDP (% change on previous quarter)	0.8	0.6	-	-	-	-
	GDP (year on year % change)	1.6	1.8	1.3	1.7	1.4	1.4
	Private consumption (q-o-q % change)	0.4	0.6	-	-	-	-
	Private consumption (y-o-y % change)	1.9	2.5	2.1	1.5	1.4	1.4
	Unemployment rate (%)	10.5	10.5	11.1	10.4	10.2	10.0
	Consumer prices (annual % change)	0.6 b)	0.6 b)	0.6	1.2	1.5	1.6
Euro area	GDP (% change on previous quarter)	0.3	0.6	-	-	-	-
	GDP (year on year % change)	1.7	1.8	1.7	1.5	1.7	1.7

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