



Portugal—Concluding Statement of the Third Post-Program Monitoring Discussions

Lisbon, February 4, 2016

A Concluding Statement describes the preliminary findings of IMF staff at the end of an official staff visit (or ‘mission’), in most cases to a member country. Missions are undertaken as part of regular (usually annual) consultations under [Article IV](#) of the IMF's Articles of Agreement, in the context of a request to use IMF resources (borrow from the IMF), as part of discussions of staff monitored programs, or as part of other staff monitoring of economic developments.

The authorities have consented to the publication of this statement. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF's Executive Board. This mission will not result in a Board discussion.

An International Monetary Fund (IMF) mission visited Lisbon during January 27—February 3, 2016, for the third Post-Program Monitoring discussions—part of the IMF's regular surveillance of countries with IMF credit outstanding above 200 percent of quota. The IMF mission was coordinated with the European Commission and the European Central Bank. At the end of the visit, the mission issued the following statement:

The Portuguese economic recovery has been underway for three years, and the unemployment rate is now close to pre-crisis levels. The country has regained the confidence of foreign investors and has been able to borrow in international markets on very favorable terms and at long maturities. Looking ahead, however, growth prospects remain constrained by high levels of indebtedness and structural bottlenecks. High public debt leaves little scope for relaxation of the fiscal stance. Further reforms are also needed to raise the economy's growth potential, mitigate downside risks, and alleviate the burden of private sector debt. In addition, bank balance sheets need to be strengthened to avoid further negative surprises.

In the third year of economic recovery, Portugal's growth rate has leveled off at around 1.5 percent, in line with the euro area average. Portugal's successful stabilization of the economy under the Economic Assistance Program paved the way for the ongoing recovery, a marked rebalancing of its sources of growth, and a sharp drop in unemployment. Given that the economy is still facing high debt levels and structural constraints, IMF staff expects growth to ease gradually as the impact of supportive external conditions fades. Risks to the outlook are tilted to the downside, underscored by the rise in sovereign risk premia, elevated uncertainty regarding global growth, and recent financial sector developments.

Portugal needs to build on the progress made in recent years in stabilizing the level of public debt through its successful fiscal adjustment. Looking forward, a continuation of these efforts would help maintain Portugal's hard-won credibility and market confidence. In this context, the authorities' commitment to medium term fiscal consolidation is welcome.

The 2016 Draft Budgetary Plan (DBP) implies a loosening of the fiscal stance. The structural primary balance is estimated to have deteriorated by 0.5 percent of GDP in 2015, and is projected to loosen by a further 0.8 percent in 2016. The authorities are targeting an overall fiscal deficit of 2.6 percent of GDP, higher than the 1.8 percent deficit projected in the 2015 Stability Program. IMF staff's assessment points to a higher overall deficit of 3.2 percent of GDP, reflecting the staff's macroeconomic and revenue projections. In addition to sufficiently ambitious budgetary targets, the authorities should consider maintaining appropriate buffers to guard against fiscal risks. These include the additional fiscal costs of proposals such as the 35-hour work week for public sector employees, and of the reconsideration of recent privatization and concession agreements, or of any contingent liabilities arising from the financial sector.

The banking system's balance sheets need to be strengthened to avoid further negative surprises and protect taxpayers. Recent developments underscore the need to continue to build on past efforts to improve bank profitability, asset quality, and governance. Banks should seek to restore profitability with a greater sense of urgency, by intensifying efforts to reduce operating costs, divesting from non-core and unprofitable activities, and improving asset quality. In this context, banks should also accelerate the reduction of non-performing exposures with the help of more ambitious capital plans. Efforts to strengthen bank's internal governance should continue, allowing problems to be identified and addressed early on.

A more ambitious approach to corporate debt workouts is needed. A substantial share of banking system assets remains tied up in low productivity activities, holding back the economy's growth potential. At the same time, limited incentives to deleverage for both banks and their clients have weighed on the pace of corporate debt reduction. Further progress in debt reduction would help free up credit for new and higher productivity firms.

The authorities' intention to remove structural impediments to growth is welcome. In a monetary union, reforms to labor and product markets are essential to increase flexibility and competitiveness, while safeguarding against downside risks. Substantial progress has been made in this regard in recent years. A weakening of reform momentum going forward could diminish medium-term prospects for growth, employment, and income. As labor market reforms are critical to spur job creation, changes to policies that have made hiring and collective bargaining more flexible could adversely affect prospects for the unemployed. Efforts to strengthen the social safety net are welcome, although the recent increase in the minimum wage could make it more difficult for the low-skilled to find employment.

The mission would like to express its gratitude to the Portuguese authorities, and our counterparts at the European Commission and the European Central Bank for a close and constructive dialogue.

