European Commission

Directorate-General for Economic and Financial Affairs

The Economic Adjustment Programme for Portugal

Eighth and Ninth Review

EUROPEAN ECONOMY

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EXECUTIVE SUMMARY

A joint EC/ECB/IMF mission met with the Portuguese authorities in Lisbon between 16 September and 3 October to assess compliance with the terms and conditions set out in Memorandum of Understanding as updated following the Seventh Review of the Portuguese Economic Adjustment Programme. *The objectives of the Programme are to restore sound public finances, improve competitiveness and put Portugal's economy back on the path of sustainable growth and job creation. This report provides an assessment of compliance and summarises the findings of the mission.*

Amid early signs of a recovery in economic activity, programme implementation remains broadly on track. *External adjustment is ongoing, with Portugal gaining export market shares for the third year in a row. Against this background, the Portuguese authorities remain determined to achieve the objectives of the programme despite increasingly challenging circumstances in the third year of implementation. Building on the significant achievements since the beginning of the programme, the authorities persevere in their efforts to complete the remaining required fiscal adjustment and important and wide-ranging structural reforms continue to be implemented. Nevertheless, the government's financing conditions have deteriorated since the summer, after the political crisis in July has raised market concerns about the government's commitment to the reform programme while its capacity to continue the economic adjustment has been put into question by a series of Constitutional Court rulings against key policy measures.*

Following the favourable growth surprise in the second quarter, economic activity is now projected to contract by 1.8 percent in 2013, before expanding by 0.8 percent in 2014. *This represents an upward revision of 0.5 and 0.2 percentage points, respectively. The situation in the labour market stabilised in line with economic activity, with total employment increasing by 0.8 percent in the second quarter and unemployment, after peaking at 17.6 percent in February/March, falling back to 16.5 percent in August. However, labour-market conditions remain a source of major concern, notably with regard to youth unemployment. The steady rebalancing of the economy towards the tradeables sector continues and the current account is forecast to reach a surplus of about 1 percent of GDP this year on the back of continued strong growth of exports and a sustained compression of imports.*

The programme's 2013 fiscal deficit target of 5.5 percent of GDP (not accounting for the cost of bank recapitalisations) is within reach. *Budget execution has been generally supported by solid revenue performance and improved expenditure control. Nevertheless, underperformance in some parts of the budget is posing challenges. The government is addressing these challenges with a combination of permanent and one-off measures, including by drawing on the provisional budget allocation, reducing the funds available to line ministries, and setting up a one-off debt recovery scheme for outstanding taxes and social security contributions. Public sector reforms continue with a view to, amongst others, strengthening financial management, reforming the revenue administration including reinforcing the fight against tax evasion, streamlining public administration, restructuring state-owned enterprises, improving the efficiency of the health sector and reducing costs of public-private partnerships.*

Fiscal adjustment will continue in 2014 with the objective to achieve the 4 percent of GDP deficit target, as agreed in the context of the Seventh Review. *In view of an expected negative net carry-over from the 2013 budget execution, the adjustment needs in 2014 have increased. Nevertheless, reflecting a thorough assessment of the balance between the necessary fiscal consolidation, economic growth, and financing prospects, it was agreed to reaffirm the fiscal deficit target of 4 percent of GDP, underscoring the authorities' commitment to successfully achieving the objectives under the programme. To enhance the equity and efficiency of public spending, the key consolidation measures to be proposed in the budget for 2014 appropriately aim at rationalising and modernising public administration, improving the sustainability of the pension system, and achieving cost savings across ministries. A rigorous implementation of the 2014 draft budget will be a decisive step in the transition to a post-programme environment. In the event that some of the measures were to be found unconstitutional, the government would need to reformulate the draft budget in order to meet the agreed deficit target. However, in view of the rapidly shrinking room of manoeuvre in identifying appropriate consolidation measures this would*

imply increasing risks to growth and employment and reduce the prospects for a sustained return to financial markets. Possible changes to the 2014 budget would have to be re-assessed in the context of the next programme review.

Portuguese banks have significantly improved their capital ratios and, with a more balanced funding structure and available liquidity, are in a good position to weather short periods of uncertainty and cope with a potential further deterioration in asset quality. *Banks continued to experience negative net profits in the first half of 2013, burdened by the recognition of impairments and provisions, the negative evolution of net interest income and high funding costs. On the positive side, deposits have been stable throughout all segments and deposit rates in the system have gradually decreased. Borrowing from the Eurosystem represents about 9 percent of Portuguese banks' liabilities and comes mainly through long-term operations. Reflecting weak loan demand the financial sector continued its deleveraging at an elevated pace and reached a loan-to-deposit ratio of 122 percent at the end of the second quarter. Low consumer confidence and the necessary deleveraging process in the corporate sector keep new lending volumes at low level. Measures to ensure adequate funding for viable small and medium-sized companies are being implemented, including initiatives to encourage the diversification of financing sources.*

The programme's agenda of structural reforms is well advanced and effective implementation will be key to sustaining competitiveness gains. *Important progress has been made in the areas of labour markets. The reform of severance pay for fair dismissals marked a significant step, and the government is committed to working on amendments to the labour code provisions that were recently declared unconstitutional. The reform of the judiciary is near completion and some of the measures such as the new Code of Civil Procedure and the adoption of the Judicial Organization Act represent milestones in improving the efficiency of the court system and speeding up claims enforcement. The authorities are also committed to stepping up efforts to reduce rents in the sheltered sectors, particularly network industries and regulated professions. A comprehensive reform of corporate income tax is being implemented which, while respecting fiscal consolidation targets, will help improve Portugal's investment and growth perspectives. Progress is being made, although with some delays, in the reduction of barriers to doing business via easing of administrative burdens and licensing procedures. The authorities are also committed to exploring the scope for new initiatives, which will be especially important in view of the need to foster competitiveness and job creation.*

The combined Eighth and Ninth Review confirms that programme implementation continues. *Public debt remains sustainable; it is now expected to peak at 127.8 percent in 2013 and to decline thereafter. Portugal successfully sold 10-year bonds in May, the first long term bond sale since the programme's start. Having spiked toward 8 percent following the political crisis in July, the current yield on 10-year bonds is around 6 percent, amid thin trading volumes. A necessary condition for the country's return to market financing will be the government's reaffirmed ownership and resolute implementation of the programme. However, the risks from further negative rulings by the Constitutional Court cannot be discarded and could make the government's plans to fully access the debt market from mid-2014 on significantly more challenging.*

The successful completion of the combined Eight and Ninth Review will release EUR 3.7 billion from the EU and EUR 1.9 billion from the IMF, bringing overall financing to around EUR 72 billion (more than 90 percent of the total envelope). *These disbursements could take place in the last quarter of 2013 subject to the approval by ECOFIN and Eurogroup for the EU loans and the IMF Executive Board for the IMF loan. The government's programme is supported by loans from the European Union amounting to EUR 52 billion and a EUR 26 billion Extended Fund Facility with the IMF.*

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INTRODUCTION

1. The report assesses compliance with the terms and conditions set out in the Memorandum of Understanding as updated following the Seventh Review of the Portuguese Economic Adjustment Programme. The assessment is based on the findings of a joint European Commission (EC)/European Central Bank (ECB)/International Monetary Fund (IMF) staff mission to Lisbon from 16 September to 3 October ([1]). In accordance with the Council Implementing Decision amending Implementing Decision 2011/344/EU on granting EU financial assistance to Portugal ([2]), the mission assessed compliance with the conditionality associated with the ninth disbursement and progress towards the key objectives of the programme of sound public finances, restoring competitiveness and putting Portugal's economy back on the path of sustainable growth and job creation. It also revised the specific policy conditionality while keeping unchanged its main objectives.

2. The Economic Adjustment Programme was agreed by the Ecofin Council on 17 May 2011 and by the IMF Executive Board on 20 May 2011. The programme, which covers the period 2011-2014, entails an external financing by the European Union, the euro-area Member States and the IMF of some EUR 78 billion ([3]), for possible fiscal financing needs and support to the banking system. One third will be financed by the European Union under the European Financial Stabilisation Mechanism (EFSM), another third by the European Financial Stability Facility (EFSF), and the remaining third by the IMF under an Extended Fund Facility.

3. A successful completion of the combined Eighth and Ninth Review will pave the way for the release of the next loan instalment of around EUR 5.6 billion. This instalment will bring EU and IMF financing to around EUR 72 billion, representing more than 90 percent of total available financial assistance.

([1]) The cut-off date for the macro-economic and fiscal projections of this report is 15 October 2013.
([2]) OJ L 269 of 14.10.2011
([3]) The IMF share of the Programme was set in Special Drawing Rights (SDR). Due to a weakening of the Euro against the SDR compared with May 2011, the projected pay-out by the IMF in Euro has become higher.

1. ECONOMIC DEVELOPMENTS AND OUTLOOK

MACROECONOMIC OUTLOOK

4. Economic growth in the second quarter surprised on the upside, increasing by 1.1 percent quarter-on-quarter (q-o-q), following a 0.4 percent contraction in the first quarter. Growth in the second quarter was primarily driven by domestic demand, of which 0.3 percentage point (pp) was contributed by private consumption and 0.5 pp by changes in inventories. Gross fixed capital formation (GFCF) was flat in the second quarter. However, this figure was boosted by an aircraft purchase, excluding which the contribution of GFCF would have been negative at around -¼ pp. The growth contribution of net exports fell from 1.9 pps in the first quarter to 0.4 pp in the second as continued strong export growth was offset by fast growing imports partly explained by the afore-mentioned aircraft purchase but also by crude oil stocking in light of the relatively low oil prices. Hard and soft short-term indicators have continued their upward trend since the beginning of the year, pointing to a progressive bottoming out of the recession.

5. The outlook for economic activity has been moderately revised upward compared with the forecast of the 7th programme review. While recent short-term indicators are consistent with the projected turnaround of economic activity towards the end of this year, the acceleration of GDP in the second quarter was to a large extent driven by one-off factors. The macroeconomic outlook has therefore been revised upward only moderately compared with the previous projection, largely reflecting the mechanical impact of the better-than-expected second quarter growth on the annual average growth rates in 2013 and 2014. Real GDP is now forecast to contract by 1.8 percent in 2013 and to expand by 0.8 percent in 2014, corresponding to an upward revision by 0.5 pp and 0.2 pp respectively (see Table 1 for comparison with other projections). Growth is expected to be predominantly driven by net exports while the negative contribution of domestic demand is forecast to shrink from 3.7 pp in 2013 to 0.2 pp in 2014.

6. The labour market situation eased in the second quarter of 2013. Total employment increased by 0.8 percent in the second quarter, following a cumulative decline in employment of 4.3 percent in the previous two quarters. However, tourism and agriculture were the main contributing sectors to the employment expansion, raising questions regarding its durability. After peaking at 17.6 percent in February and March, the unemployment rate fell back to 16.5 percent by the end of the summer. Unemployment would have been higher had the fall in employment not been partly offset by a concomitant decline in labour market participation. Employment is forecast to contract by some 4 percent in 2013 and by another ½ percent in 2014, unchanged from the outlook of the 7th programme review. By contrast, the unemployment rate has been revised down by some 1 pp in 2013 and ¾ pp in 2014 and is now forecast to average at 17.4 percent in 2013 and 17.7 percent in 2014. Youth unemployment, while also somewhat retreating from its April peak of 40.4 percent, remains of particular concern.

Table 1.1: **Selected real GDP projections**

	2013	2014
COM 8th-9th Review (November 2013)	-1.8	0.8
Banco de Portugal (October 2013)	-1.6	n.a.
EIU (October 2013)	-1.5	0.5
Consensus (October 2013)	-1.9	0.1
PT authorities State Budget 2014 (September 2013)	-1.8	0.8
Banco de Portugal (July 2013)	-1.8	0.3
OECD (May 2013)	-2.7	0.2

Source: Commission services, Bank of Portugal, Ministry of Finance, The Economist, Consensus Economics and OECD

7. Rebalancing towards the export sector continues at a faster than expected pace. Exports have been booming since the beginning of the year with a broad-based contribution of various sectors and significant gains in market shares for both goods and services exports. Exports have been growing particularly strongly towards non-EU countries but have also risen above market growth towards the EU countries. In the second quarter, the contribution of exports to growth was almost counterbalanced by the high import growth. The surprisingly large increase in imports in the second quarter is likely to have been driven by various one-off factors (aircraft purchase, crude oil) and should subside somewhat in the forthcoming quarters. The current account is now forecast to reach a surplus of about 1 percent of GDP this year, revised up from 0.1 percent in the 7th programme review, and to continue improving over the forecast horizon.

Table 1.2: **Macroeconomic projections of the 8th and 9th programme reviews**

	8th-9th Review (Sept 2013)				7th Review (March 2013)			
	2012	2013	2014	2015	2012	2013	2014	2015
	year-on-year volume change							
Gross domestic product	-3.2	-1.8	0.8	1.5	-3.2	-2.3	0.6	1.5
Private consumption	-5.4	-2.5	0.1	0.7	-5.6	-3.5	0.1	1.0
Public consumption	-4.8	-4.0	-2.8	-2.2	-4.4	-2.6	-2.0	-1.9
Fixed investment	-14.3	-8.5	1.2	3.7	-14.5	-7.7	2.5	4.9
Exports of goods and services	3.2	5.8	5.0	5.3	3.3	0.8	4.4	4.9
Imports of goods and services	-6.6	0.8	2.5	3.7	-6.9	-3.9	3.1	4.3
	contributions to real GDP growth							
Domestic demand excl. inventories	-6.9	-3.7	-0.3	0.7	-7.1	-4.1	0.0	1.1
Change in inventories	0.3	0.0	0.0	0.0	0.1	-0.1	0.0	0.1
Net trade	3.8	2.0	1.0	0.8	4.0	1.8	0.6	0.4
Employment (y-o-y change)	-4.2	-3.9	-0.5	0.4	-4.2	-3.9	-0.5	0.4
Unemployment rate (level)	15.9	17.4	17.7	17.3	15.7	18.2	18.5	18.1
HICP (y-o-y change)	2.8	0.6	1.0	1.2	2.8	0.7	1.0	1.5
Current external balance (% of GDP)	-1.9	0.9	0.9	1.0	-1.9	0.1	0.1	0.0
General government net lending (% of GDP)	-6.4	-5.9	-4.0	-2.5	-4.8	-5.5	-4.0	-2.5
General government consolidated gross debt (% of GDP)	124.1	127.8	126.7	125.7	123.6	122.9	124.2	123.1

Source: Commission services

8. Inflation in consumer prices is decreasing. HICP inflation dropped to 0.7 percent in the first half of this year, significantly below the euro-area rate of 1.6 percent. Annual average inflation is forecast to remain at 0.6 percent in 2013 and to reach 1 percent in 2014. The re-instatement of two monthly bonus payments for public-sector workers (equivalent to a 16.7 percent increase in public sector wages) has a discernible effect on total-economy labour costs and will also impact on the GDP deflator in 2013.

9. Uncertainties with regard to the macroeconomic outlook are high. On the one hand, the on-going broad-based improvement of high frequency indicators suggests that the economy may have posted positive growth in the third quarter of this year, again beating expectations. In addition, important progress has been achieved in reforming the corporate income tax regime and the judicial sector while cutting red tape, which may pave the way for more dynamic investment. These factors would imply a slight upside risk to the headline growth forecast for 2013 and 2014. On the other hand, the sustainability of the projected recovery in 2014-15 is contingent on positive developments in trade and financial markets, which remain fragile. The ability of Portugal to progressively regain access to the sovereign bond market at more favourable interest rates remains a key forecast assumption, also underpinning confidence in the broader economy. A failure or significant delay in re-accessing markets would have a strong negative impact on the prospects for economic growth. In addition, household and corporate deleveraging pressures could weigh more heavily on private consumption and investment than is assumed in the baseline forecast, while the export performance strongly hinges on the assumed recovery in the euro area economy.

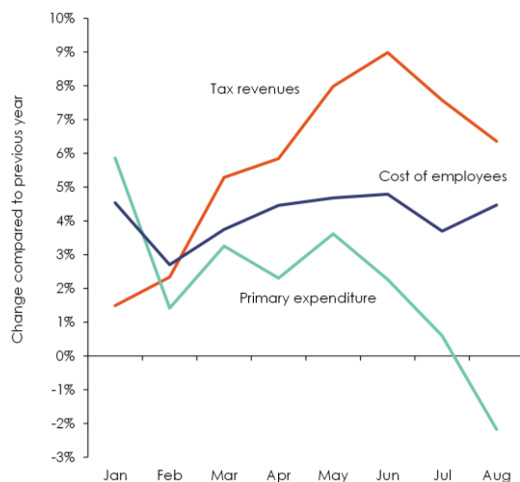
FISCAL DEVELOPMENTS

10. In cash terms, budgetary execution in the first eight months of the year was in line with the supplementary budget targets. Budget execution up to August recorded an improvement in the government cash deficit (net of extraordinary factors) by about 0.6 percent of GDP, compared with the same period of last year, supported by a solid performance of state tax revenues and a generally tight execution of expenditure. At the same time, shortfalls in non-tax revenues and overspending in some specific expenditure categories are weighing on the outlook for budgetary execution.

11. State tax collection in the first eight months of the year was robust. The good performance is driven by direct taxes, which up to August grew by 19 percent whereas indirect taxes fell by 2.3 percent, compared with the same period of last year. Both personal income and corporate income tax collection were ahead of target as a result of enhanced revenue collection efforts (e.g.

efficiency of the large taxpayer office), as well as policy measures introduced earlier this year, such as the changes in the advanced payments mechanism or the introduction of limits to loss offsets for corporate taxation. A better-than-expected macroeconomic performance may also have contributed to the improved collection of these taxes. VAT revenues up to August fell by 2.1 percent, in line with the projections of the supplementary budget. It is worth noting, however, that VAT collection has improved in some of the sectors where incentives were introduced for final customers to ask for invoices (notably, in the restaurant and hotel sector). A decline was also recorded for other indirect taxes except for the circulation tax and the tax on alcoholic beverages, while stamp duties were clearly below target.

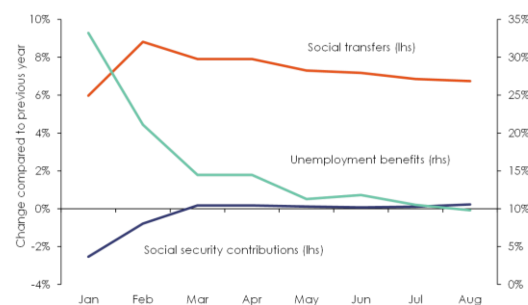
Graph 1.1: **Budget execution: Tax Revenues, Cost of Employees and Primary Expenditure. January - August 2013 (cash-data)**



(1) includes non-consolidated data for the State and Autonomous Funds and Services. Primary expenditure includes data for the State subsector only.
Source: Portuguese Ministry of Finance and Commission services

12. Expenditure execution in the first eight months of the year was broadly in line with the supplementary budget projections, but overruns are likely in the rest of the year. Risks of overruns stem, in particular, from the outstanding 14th salary bonus payment (as the share of public sector workers who opted for deferred payment in November is not known) and some delays in the execution of other expenses. In addition, some outlays, such as the contribution to the EU budget, have turned out higher than projected while receipts from some non-tax revenues (sales and other current and capital revenue) have been below expectations. The fiscal gap implied by the expected over-run in expenditure and shortfall in non-tax receipts will be compensated by a number of ad hoc measures (see below).

Graph 1.2: **Budgetary outturn for Social Security. January - August 2013 (cash-data)**



(1) includes non-consolidated data for Social Security.
Source: Ministry of Finance and Commission services

13. Social Security recorded a positive cash balance in the first eight months of the year. This is explained by the extraordinary transfer from the State agreed in the supplementary budget and increased transfers from the European Social Fund. Social security contributions are broadly in line with the estimates of the supplementary budget. However, one of the measures introduced in 2013, namely social contributions from unemployment and sickness benefits above minimum levels, is yielding less than expected due to technical implementation problems following its redesign after the ruling of the Constitutional Court in April. Nevertheless, the overall collection of social contributions is in line with projections due to the over-performance of the "extraordinary solidarity contribution" (CES) on pensions, the better macroeconomic environment and increased collection efficiency. On the expenditure side, unemployment benefits and subsidies to employment support are now expected to be lower than initially planned on the back of a more favourable labour market situation. Social transfers are expected to be substantially higher than in the previous year due to the reinstatement of the two bonus pension payments, but this effect had already been budgeted. The public sector pension regime (Caixa Geral de Aposentações – CGA) is

Table 1.3: **Stock of arrears January - July 2013 (EUR million)**

	2013 (1)						(2)	(3)=(2)-(1)	
Subsector of the General Government	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**∆ Jul-Jan**	**% total**
Central Government excluding NHS	54	57	54	61	56	53	55	1	2%
NHS classified in General Government	23	28	26	48	14	20	32	9	1%
Reclassified entities	19	18	18	19	19	18	18	0	1%
Local Government	1,234	1,158	1,130	1,084	991	949	902	-331	31%
Regional Government	946	945	952	1,073	1,061	1,066	911	-35	32%
Total	2,274	2,206	2,180	2,284	2,141	2,107	1,918	-357	66%
Total Consolidated	2,199	2,133	2,107	2,217	2,077	2,047	1,864	-335	65%
Other entities outside General Government									
Enterprises excluding NHS	40	45	49	50	51	56	74	34	3%
NHS incorporated hospitals	727	784	773	817	858	917	951	224	33%
p.m.: health sector inside + outside GG	750	812	799	864	872	937	982	232	34%
TOTAL	2,966	2,962	2,929	3,084	2,986	3,020	2,888	-77	
p.m.: percent of GDP	1.8	1.8	1.8	1.9	1.8	1.9	1.8		

(1) Consolidated data concerns data net of intra-government sector arrears. Total amounts adjusted for arrears' settlement.
Source: Ministry of Finance and Commission services

expected to require additional state transfers to compensate for the underperformance of one of the measures introduced in the 2013 budget (the inclusion of cash supplements in the contributions' base).

14. Budget execution in other sectors of general government was broadly in line with expectations. The balance of state-owned enterprises continued improving up to August owing to cost-reduction efforts and voluntary redundancy schemes and despite strains from the reinstatement of the 13th and 14th bonus salaries. In the health sector, significant cost reductions since 2010 have been partially reversed in 2013 as a result of the reinstatement of the 13th and 14th bonus salaries and the increase in contributions to the public sector pension system. In addition, there has been a renewed build-up of arrears in SOE hospitals that needs to be examined (see below). Local governments' budget execution is in line with projections. In this context, it needs to be taken into account that 2013 is the first year in which the collection of the local property tax ('IMI') is based on three instalments instead of two, which makes the accurate intra-annual profile difficult to assess. At the regional level, budgetary execution of the Autonomous Region of Açores is in line with projections and that of the Autonomous Region of Madeira better than expected, supported among other factors by a good performance of corporate income tax and strict expenditure control.

15. In national account terms, the government deficit in the first half of 2013 amounted to 7.1 percent of GDP. Excluding the extraordinary capital injection to BANIF, the deficit in the first semester amounted to 6.2 percent of GDP, which represents an improvement by 0.6 pp of GDP compared with the deficit in the same period of last year - if one-offs are excluded. The attainment of the 5.5 percent of GDP deficit target for the whole year is contingent on overcoming a number of challenges, as some deviations from the national accounts estimates underlying the supplementary budget were identified during the mission (see Section 2).

Arrears

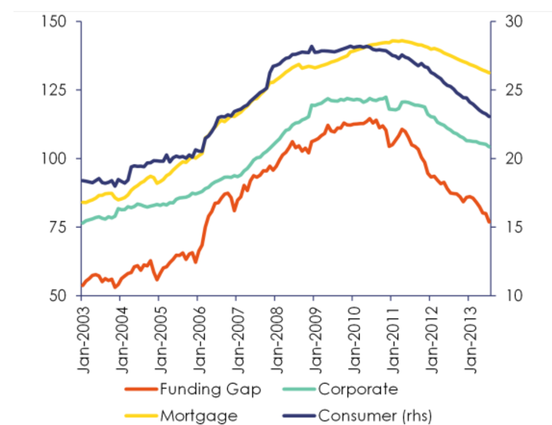
16. Whereas the overall amount of arrears is lower than at the beginning of the year, progress in preventing the accumulation of new arrears is mixed. The implementation of the 'Support Programme for the Local Economy' (PAEL) is behind a large drop in local government arrears. The overall envelope of the programme amounts to about EUR 800 million, which is below the EUR 1 billion initially envisaged. The Court of Auditors already cleared most of the programmes submitted by the municipalities and about EUR 400 million have already been

transferred, while another EUR 200 million still awaits approval by the Court of Auditors. It is likely that a part of the remaining EUR 200 million will not be disbursed until the end of this year. All in all, local government arrears should at least be halved by the end of the year compared with the EUR 1.2 billion outstanding in January. The Autonomous Region of Madeira is gradually implementing its strategy to pay arrears after the European Commission's Directorate General for Competition cleared the operation involving a EUR 1.1 billion state-guaranteed loan. In the health sector, after successfully concluding the negotiations with the pharmaceutical industry in September, the second debt settlement programme, worth EUR 432 million, will soon be launched. Even if a substantial decrease in the stock of arrears is to be expected by the end of the year, new arrears are still being accumulated in some sectors – particularly SOEs hospitals – in spite of the commitment control law. SOEs hospitals accumulate about EUR 34 million of new arrears per month which compares with about EUR 75 million last year. Although the reduction is significant, more efforts are needed to reach the overall target of halting any further accumulation. In December 2013, a follow-up IMF-led technical assistance mission will analyse the functioning of the commitment control law, particularly in problem areas such as SOE hospitals.

FINANCIAL MARKETS AND FINANCIAL SECTOR DEVELOPMENTS

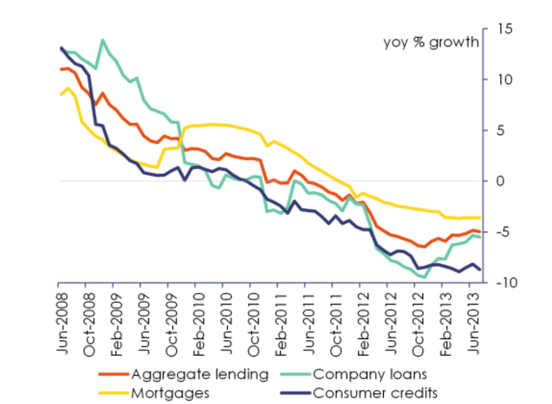
17. The provision of bank lending to the non-financial private sector continues to decline, although at a slower pace. New corporate lending over the last 12 months has been 20 percent below the past decade's annual average, while new loans under a EUR 1 million ceiling are about 25 percent below the corresponding average. Fresh monthly mortgages amount to roughly a sixth compared with the decade's average which is partly explained by the high interest rates on mortgages compared with pre-Lehman years, but mainly by low consumer confidence. As housing loans typically have a longer maturity than loans to non-financial corporations, the mortgage stock fell by 3.6 percent between July 2012 and July 2013 whereas loans to companies contracted by 5.5 percent. New consumer credit was a bit more than half the previous decade's average causing the stock of outstanding loans to fall by 8.7 percent over the same period (Graphs 1.3 and 1.4).

Graph 1.3: **Loan stock evolution per segment**



Source: Bank of Portugal

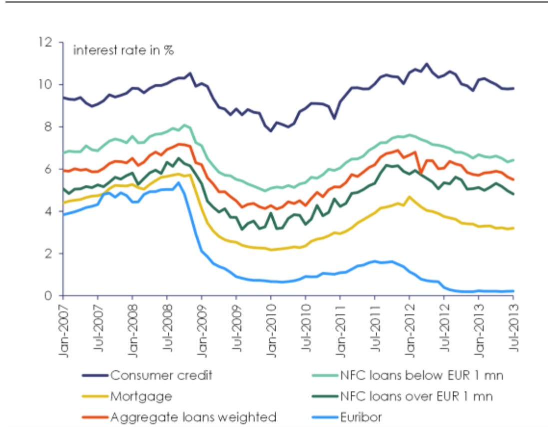
Graph 1.4: **Yearly growth per loan segment**



Source: Bank of Portugal

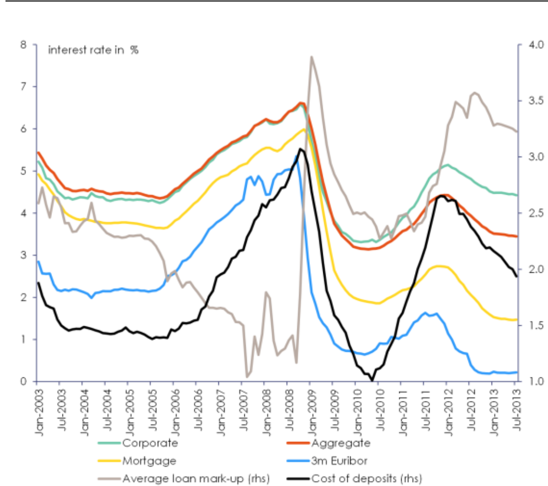
18. Reduced remuneration of deposits has fed through to lower loan rates. Due to better capitalisation and increased system liquidity Portuguese banks have reduced deposit remuneration rates, thus contributing to reduce their overall cost of funding. The improved funding situation has led to higher competition in lending, in particular for lower-risk SMEs, resulting in slightly declining lending rates for this corporate segment compared with the situation one year ago (Graph 1.5). This can be traced in the average loan mark-up on Euribor, expressed as a difference between the latter and the interest banks earn on aggregate loans (Graph 1.6).

Graph 1.5: **Interest rate for new loans, evolution per segment**



Source: Bank of Portugal

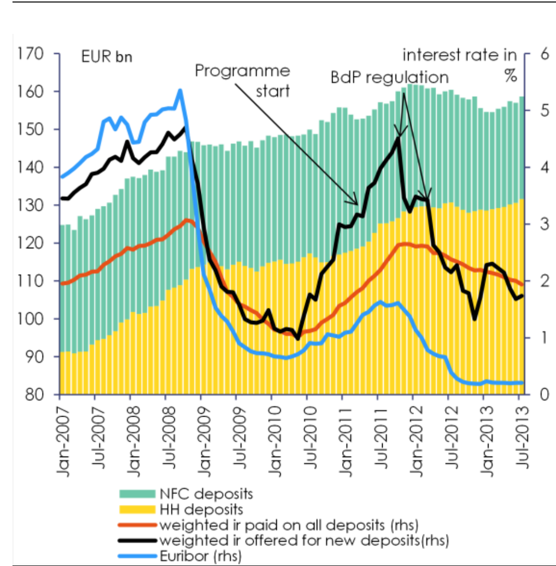
Graph 1.6: **Nominal interest rate earned by loan stock segment and average loan mark-up**



Source: Bank of Portugal

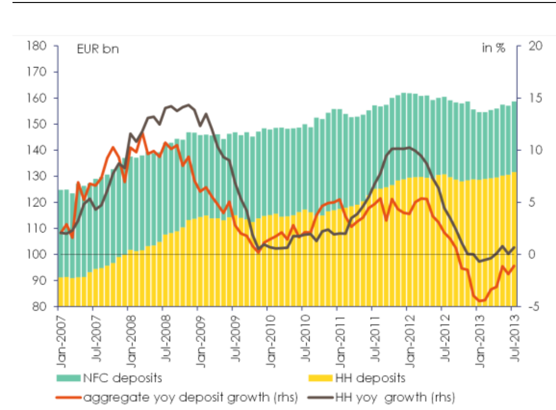
19. Household deposits are growing again, while corporate deposits are no longer declining. Deposit interest rates continued to come down in 2013. In Portugal, the share of longer term deposits in the deposit base is higher than in other euro area countries. Consequently, it takes relatively longer for the flow of new deposits to influence the stock's average interest rate (Graph 1.7). The weighted cost of deposits fell below 2 percent in July. Overall, deposits have been growing again since the start of the year when the decline in company deposits stopped. Due to the reinstatement of the 13th and 14th salary in the public sector, household deposits reached a new all-time high in July, with the underlying upward trend presumably driven by precautionary savings (Graph 1.8).

Graph 1.7: **Lower deposit remuneration slowly brings down the cost of funding**



Source: Bank of Portugal

Graph 1.8: **Deposit growth by segment**



Source: Bank of Portugal

20. Profitability prospects remain weak for most Portuguese banks. Subdued economic activity and high unemployment in recent years has put pressure on the balance sheets of banks. The banking sector has accumulated losses for an extended period, recording only one quarter of positive net profits over the past two years. Over EUR 1 billion of losses in the first half of 2013, of which EUR 765 million alone in the second quarter, clearly highlight the strains under which the banking sector remains, with a meaningful portion of the losses explained by the recognition

Table 1.4: **Soundness indicators**

%	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2
Return on Equity (1)	7.2	7.6	7.1	6.7	6.2	4.3	2.4	-3.8	6.3	1.0	-0.3	-4.2	-3.8	-7.2
Gross Income on Assets	2.5	2.6	2.6	2.7	2.4	2.5	2.5	2.5	2.6	2.7	2.6	2.5	2.1	2.1
Cost to Income Ratio	57.7	57.1	57.2	57.6	59.1	58.3	59.0	61.4	56.1	52.9	56.5	58.9	67.5	68.9
Non-Performing Loans	5.5	5.6	5.9	5.3	5.7	6.3	6.9	7.4	8.1	9.2	9.9	9.8	10.4	10.6
Coverage Ratio	62.9	62.1	60.2	60.8	59.5	57.9	55.5	57.8	53.5	51.2	50.9	54.4	54.1	54.1
Capital Adequacy Ratio (2)	11.3	10.9	11.0	11.1	11.4	11.0	10.1	10.7	10.7	12.3	12.3	12.6	13.0	13.1
Core Tier 1 Ratio (3)	7.8	7.8	8.0	8.1	8.4	8.7	8.5	9.6	9.6	11.2	11.3	11.5	11.9	11.9
Loan-to-deposit ratio	163.4	166.6	158.4	157.8	156.7	149.7	146.2	140.2	136.9	136.3	133.3	127.9	124.0	122.6

(1) Cumulated ROE. Income before minority interests / Average shareholders' equity before MI.
(2) Excluding the banks in resolution.
(3) The Core Tier 1 ratio according to Programme definition and excluding the banks in resolution.
Source: Bank of Portugal

of losses associated with non-performing loans. In addition to the gradual deterioration in the quality of assets, banks have experienced a squeeze on net interest income (down by 29 percent y-o-y) as a result of a combination of persistently low interest rates and falling new lending volumes (see Table 1.4). The costs of CoCos have added to the already high funding costs since the middle of 2012. Going forward, asset quality may deteriorate further, although at a slower pace, while net income is projected to recover from 2014 onwards. The net interest margin of banks should remain low also due to the banks' limited scope for re-pricing their assets. However, the major improvements in capital and funding structures coupled with the available liquidity put the banking sector in a better position than a year ago.

21. Banks have become less restrictive in financing the economy ([4])**.** In a context of improved solvency and more available liquidity, credit spreads on new loans have been gradually declining, although a relatively high risk perception remains one of the main drivers of supply constraints as reported by banking sector sources. In parallel, credit standards and terms applied to new lending have not shown any major changes. However, there is a general tendency towards adopting slightly less restrictive criteria in terms of lending margins and non-interest charges. These affirmations are also reflected in the perception that non-financial corporations convey when applying for new or roll-over credits; only 10 percent of firms active in the services sector or manufacturing industry mention bank credit access as a major hurdle for their business development plans. However, that number rises to 55 percent for construction and real estate related firms, reflecting the rebalancing of the economy. Lending to households remains depressed amid low consumer confidence and a general reluctance to spend on housing and on durable goods. Nonetheless, credit standards and conditions in the household segment remain broadly unchanged and the view of banking sources is that the decline in new household lending is mostly justified by demand side factors, including the low albeit improving consumer confidence levels and the continued subdued situation in the real estate market.

([4]) See also the conclusions from the Bank Lending Survey, July 2013, Bank of Portugal.

2. PROGRAMME IMPLEMENTATION

FISCAL POLICY

Fiscal consolidation in 2013

22. The general government cash-adjusted deficit for programme purposes reached EUR 4,795 million up to August. This is well below the third quarter target of EUR 7,300 million established in the performance criteria of the Memorandum of Economic and Financial Policies (MEFP), and leaves room for accommodating the cumulative deficit of the month of September. The achievement of this cash position was possible due to relatively robust tax revenue growth and expenditure control in the first eight months of the year, as described above. However, the remainder of the year will put substantial strain on some items, especially on the expenditure side (e.g. interest payments, reinstatement of 14th bonus salary and pension). Budgetary challenges have also been identified as a result of lower-than-expected non-tax revenues.

23. The mission has revised the 2013 fiscal projections in national accounts terms and identified some deviations with respect to the supplementary budget. These include a capital injection into BANIF (0.4 percent of GDP), which is however not considered for programme purposes. The remaining deviations stem from shortfalls related to the reprogramming of EU funds and the postponement of the sale of a port concession and other factors such as the underperformance of some non-tax revenues, the transfer to Greece of dividends from Greek bonds in Banco de Portugal's investment portfolio, lower than expected contributions to the public employees' pension scheme and expenditure overruns on the wage bill and on intermediate consumption. The net effect of these slippages is estimated to increase the 2013 deficit by 0.5 percent of GDP (excluding the capital injection into BANIF). The budgetary impact would have been higher had the provisional budget allocation of 0.3 percent of GDP not been used to partly offset the revenue shortfalls/expenditure overruns.

24. Corrective measures amounting 0.5 percent of GDP should ensure that the 5.5 percent of GDP deficit target (net of bank recapitalisation costs) is met. These include, notably, the reduction of available funds for investment and tighter control on intermediate consumption of line ministries amounting to an overall 0.1 percent of GDP. In addition, the government has announced a debt recovery scheme for taxes and social security contributions to be implemented before year end and expected to yield about 0.4 percent of GDP in 2013. Overall, the budget deficit target of 5.5 percent of GDP for 2013 remains in reach subject to the successful implementation of the corrective measures as well as continued tight expenditure control during the rest of the year, as announced by the government.

25. The fiscal effort as measured by the improvement in the structural balance is estimated at 0.5 percent of GDP this year. This falls slightly short of the 0.6 percent of GDP envisaged at the 7th review. The expected underperformance is explained by budgetary overruns as detailed above and the delayed implementation, and/or the overestimation in the yields, of some consolidation measures, especially the measures introduced with the supplementary budget in response to the Constitutional Court (CC) ruling of April 2013. The government had reacted promptly to the CC ruling in April by proposing replacement measures, but some of these measures, such as the reprogramming of the EU funds or the changes to the unemployment and sickness benefits, proved to be technically difficult to implement within the necessary timeframe. The negative opinion of the CC at the end of August on the requalification scheme also required the modification of the relevant proposal to accommodate the concerns of the Court. The political crisis in July and the subsequent government reshuffle also delayed the implementation of some measures. In addition, in purely mechanical terms the improvement in the macroeconomic conditions has enhanced the cyclical component of the deficit reduction at the cost of the structural component.

Fiscal consolidation in 2014

26. The government has reaffirmed its commitment to the 4 percent of GDP deficit target for 2014. The fiscal projections are underpinned by consolidation measures with an estimated net amount of 2.3 percent of GDP, including permanent measures and some one-offs. In net terms, more than 70 percent of the measures

Table 2.1: **Arithmetic of the government deficit: from the deficit in one year to the next**

(+) means balance-improving impact; (-) means balance-reducing impact	% of GDP
2011 balance (observed)	**-4.3**
p.m. 2011 balance (without one-offs)	**-7.3**
Primary balance drift in 2012	-4.0
Change in interest expenditure	-0.3
Dissipation of one-offs and non-recurrent effects from previous year	-3.0
Consolidation measures	5.8
One-off measures	-0.6
2012 balance (observed)*	**-6.4**
p.m. 2012 balance (without one-offs)	**-5.8**
Primary balance drift in 2013	-3.0
Change in interest expenditure	0.0
Dissipation of one-offs and non-recurrent effects from previous year	0.6
Consolidation measures	4.5
Reistatement of the 13th and 14th salary and pension	-1.5
One-off measures	-0.1
2013 balance (target)*	**-5.9**
p.m. 2013 balance (without one-offs)	**-5.8**
Primary balance drift in 2014	-0.5
Change in interest expenditure	0.0
Dissipation of one-offs and non-recurrent effects from previous year	0.1
Consolidation measures	2.2
One-off measures	0.1
2014 balance (target)	**-4.0**
p.m. 2014 balance (without one-offs)	**-4.1**

(1) Balance in year t equals balance in year t-1 plus nominal primary balance drift in year t, plus the impact of the change in interest expenditure in year t, plus the impact of the dissipation of the one-offs and non-recurrent measures from year t, plus the impact of new consolidation measures in year t.
(2) The Primary Balance Drift includes the change in the balance level that would take place without discretionary measures removing the effect of one-off measures. It includes the impact of economic activity on the balance, including the composition of growth, and the structural increase in expenditure in real terms, e.g. the increase in pension expenditure.
* For the purposes of the Programme, the budget deficit in 2012 would exclude the impact of CGD recapitalisation (about 0.5% GDP), and in 2013 BANIF recapitalisation (about 0.4% GDP).
Source: Ministry of Finance and Commission services

are expenditure reducing (80 percent in gross terms). In spite of a projected improvement in the macroeconomic outlook, these measures are needed to cater for a negative primary balance drift of 0.5 percent of GDP reflecting, amongst others, the carry-over from the budgetary slippage in 2013 and the rebuilding of the provisional budget allocation (see Table 2.1). Offsetting this effect will therefore require a higher consolidation effort in 2014 than envisaged at the 7th review. In fact, the cumulative value of the consolidation package necessary to achieve the agreed fiscal targets has not changed (i.e. about EUR 4.7 billion over 2013-2014). However, a part of the effort has been shifted to 2014 since the initially planned frontloading to 2013 of about 0.8 percent of GDP of the consolidation package has been achieved only partially. All in all, the structural balance is expected to improve by 1.1 percent of GDP in 2014 (see Table 2.2).

27. The fiscal consolidation is predominantly based on the savings measures identified in the framework of the public expenditure review (PER). The PER package is an important element of the broader reform of the State with the objective of increasing equity and efficiency in the provision of public services and social transfers. The PER aimed at identifying savings and the potential for streamlining processes in the public administration with the direct involvement of line ministries. The savings identified include permanent expenditure-reducing measures amounting to EUR 3.1 billion (1.8 percent of GDP) in 2014. The PER measures act along three main axes: (1) reduction of the public sector wage bill; (2) pension reform and (3) sectoral expenditure cuts across line ministries and programmes. The reduction in the wage bill in 2014 aims at diminishing the size of the public-sector work force while shifting its composition towards higher-skilled employees, aligning the

Table 2.2: **Fiscal targets and structural adjustment 2011-2015**

	2011	2012	2013	2014	2015
Budget balance	-4.3	-6.4	-5.9	-4.0	-2.5
Programme budget balance	-4.3	-6.0	-5.5	-4.0	-2.5
Budget balance, net of one-offs	-7.3	-5.8	-5.8	-4.1	-2.5
Structural balance	-6.5	-4.1	-3.7	-2.6	-1.8
Primary balance	-0.3	-2.1	-1.6	0.3	1.7
Structural primary balance	-2.5	0.2	0.7	1.7	2.5
Fiscal adjustment	3.5	2.6	0.5	1.1	0.8
Fiscal effort (EDP definition)	2.3	2.3	0.5	1.1	0.9

Source: Ministry of Finance and Commission services

public sector work rules with those of the private sector and making the remuneration policy more transparent and merit-based. Specific reforms include the implementation of a requalification scheme that would allow to adjust the skills of the workforce to the public sector needs, aligning public sector working hours with those in the private sector (i.e. increase from 35 to 40 hours work week), introduction of a bank of hours, reduction in holiday entitlements, the implementation of a mutual agreement redundancy scheme (which is estimated to generate one-time upfront costs of slightly more than 0.1 percent of GDP) and the introduction of a single wage scale as well as the streamlining of wage supplements. A comprehensive pension reform will generate another important part of the savings and will be based on equity principles and income progressivity, thereby protecting the lowest pensions. Specifically, the reforms aim at reducing the current differences between the civil servants' system (CGA) and the general system and at increasing the statutory retirement age by changes to the sustainability factor. The 'extraordinary solidarity contribution' introduced in 2013, worth 0.3 percent of GDP, will be maintained. However, this measure will be adapted to take into account the cumulative impact of other pension reforms. Survivors' pensions of both CGA and the general pension regime will be streamlined, in particular in cases where these accumulate with other pensions. Finally, savings in intermediate consumption and expenditure programmes across line ministries will be substantially stepped up.

28. In addition, the government will implement some smaller-scale permanent revenue consolidation measures worth about 0.4 percent of GDP. These measures aim at further improving the efficiency and equity in the current tax and benefit system and reducing excessive rents in some sectors. They include an increase in the corporate tax rate on expenses related to company cars, higher excises for tobacco and alcohol, a surcharge on the car tax for diesel passenger vehicles, reducing tax exemptions in property taxation for pension and real state funds as well as caps to the social security contributions of members of statutory bodies. In addition, a special levy on energy will be imposed to boost state revenue and with the additional effect of curbing excessive rents from the energy sector. Part of the revenue generated by this levy will be used to reduce the tariff debt. The levy on financial institutions (banking system) and a fee on the media spectrum will be increased. Finally, the government plans to sell online gambling licences and to tax this activity, regularising a growing market that is currently not properly regulated.

29. A number of one-off measures also aim to contribute to the achievement of the deficit target, more than offsetting the one-off costs related to the mutual agreement termination of public sector employment contracts. These measures consist of the transfer of the CTT (postal service) health fund to the government sector, the sale of concessions of marina and silos operations, the sale of land in the Port of Lisbon as well as special dividends from the sale of excess oil reserves by a public company.

30. The legislative processes underpinning the PER reforms are underway but some measures have suffered setbacks. The mutual agreement redundancy scheme is already in place

for the less qualified public sector employees. Other schemes targeted to specific public sector functions are currently under preparation. The implementation of the 40-hour work week has already started while simultaneously being assessed by the Constitutional Court. The requalification scheme has been revised to address the concerns raised by the Constitutional Court at the end of August. Overall, several of the legislative and regulatory amendments necessary to implement the PER reforms are already in force or await Parliamentary approval. Other legislative changes were submitted to Parliament in October or are implemented through budget provisions and should enter into force as of 1 January 2014. In order to mitigate the political and legal risks, it will be important to seek broad political support. In addition, the President of the Republic has the right to submit reform proposals which are potentially contestable from a constitutional point of view to a prior legal review by the Constitutional Court which has to be completed within four weeks. Should some of the measures be found unconstitutional, either following such a review or after a legally binding Court ruling, the government would have to reformulate the Budget in order to meet the agreed deficit target. However, in view of the rapidly shrinking room of manoeuvre in identifying appropriate consolidation measures this would imply increasing risks to growth and employment and would reduce the prospects for a sustained return to financial markets.

31. As part of the reforms to boost competitiveness and growth, the Portuguese government will undertake a comprehensive reform of the corporate income tax (CIT) as from 2014. The reform, ambitious in scope, has been carefully designed by a reform Committee and submitted to public consultation over the summer. It encompasses a substantial simplification of the tax structure, reduces compliance and administrative costs and revamps the tax code to make Portugal more attractive to foreign investment, whilst applying strict anti-abuse provisions. Notably, it also aims at gradually lowering the marginal tax rate to stimulate higher investment and growth. It reduces the strong debt-bias of the Portuguese corporate tax system and extends the loss carry-forward-period.

Fiscal consolidation over the medium term

32. Sustained fiscal consolidation beyond the programme period should bring the deficit below 3 percent of GDP in 2015. Under the current macroeconomic scenario permanent fiscal consolidation measures amounting to about 1.2 percent of GDP will be necessary to reach the 2.5 percent deficit target in 2015. This translates into a fiscal effort, as measured by the change in the structural balance, of 0.9 percent of GDP and an improvement in the structural primary surplus from 1.7 percent of GDP to 2.5 percentof GDP (see Table 2.2). Going further, the government is committed to fulfil the requirements of the fiscal compact of a structural deficit of 0.5 percent of GDP by 2017.

Debt developments

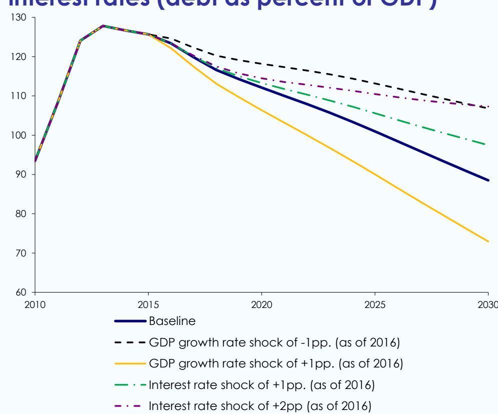
33. The debt-to-GDP ratio is expected to peak at 127.8 percent in 2013 and to decline thereafter. The upward revision with respect to the 7th review is explained by the correction of the 2012 debt data, which is now slightly higher, and the non-realisation of some short-term debt reducing operations. In particular, the Social Security Financial Stabilisation Fund is now expected to increase its holding of Portuguese government bonds more gradually and privatisation receipts will be mostly retained in Parpublica as the company will possibly be reclassified into the general government in September 2014 when the new ESA 2010 enters into force. Moreover, the Treasury cash balances at the end of the year are estimated to be higher by about EUR 2 billion than previously assumed. These effects are somewhat mitigated by a better nominal GDP projection. Assuming further that the Medium Term Objective (MTO) of a structural deficit of 0.5 percent of GDP will be reached from 2017 on, the debt-to-GDP ratio would be on a steeper downward path falling below 100 percent in the second half of the next decade.

Box 2.1: **Government Debt and Fiscal Sustainability in Portugal**

Under the programme scenario, government debt is projected to peak at 127.8 percent of GDP in 2013 before starting a gradual decline. The baseline long-term calculations shown below incorporate the programme scenario up to 2017. The programme scenario includes fiscal consolidation measures up to 2015 and showing no-policy-change for the outer years. More details on these figures are shown in Table 7 in the annex. The turning point in 2014 is the result of achieving a small primary surplus, combined with a positive, albeit still modest, GDP growth rate. After 2017, it is assumed that: (i) the structural primary fiscal balance remains unchanged at a surplus of 2.6 percent of GDP; (ii) nominal interest rates are around 4.5 percent; (iii) nominal GDP growth fluctuates between 3.5 and 4 percent; (iv) ageing costs are taken into account following the Commission's 2012 Ageing Report projections; and (v) the expected fiscal impact of PPPs costs and bank recapitalisation costs of EUR 12 billion over the programme period are factored into the analysis.
Full compliance with the programme's consolidation path ensures a gradual decline of the debt ratio over the longer term. Nevertheless, for a significant number of years the debt ratio would remain higher than before the current crisis. The graphs in this box present a sensitivity analysis with respect to macro-economic risks, the effect of alternative fiscal consolidation paths, and the potential impact of contingent liabilities such as reclassifications and other changes in the government perimeter.

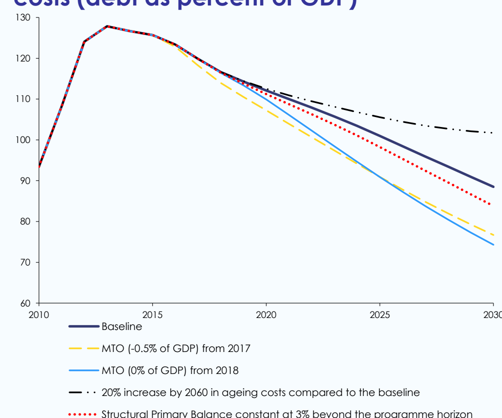
Graph I illustrates the sensitivity of the debt trajectory to macro-economic assumptions by considering a shock to real GDP growth and hikes in interest rates as from 2016. A lower GDP growth rate by one percentage point or a higher interest rate on maturing and new debt by two percentage points would put at risk the declining trend over the medium term, although the effect of these shocks are now mitigated compared with the analysis of the previous review reflecting more favourable growth prospects during the programme timeframe. An interest shock of 1 percentage point would slow down the pace of debt reduction but keep the declining trend. Conversely, a positive shock to growth in the medium-term on account of the structural reforms undertaken would result in visibly lower debt-to-GDP ratios and a faster pace of debt reduction *

Graph I: Macroeconomic risks-growth and interest rates (debt as percent of GDP)



Source: Commission services

Graph II: Fiscal consolidation and ageing costs (debt as percent of GDP)



Source: Commission services

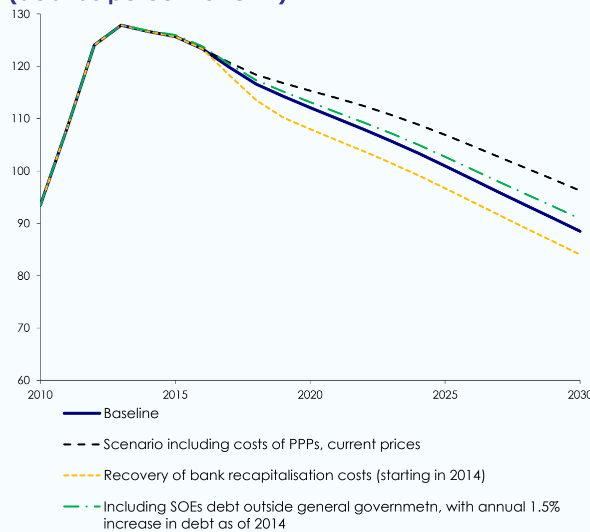
Additional fiscal consolidation beyond 2015 and the programme horizon would clearly accelerate the debt reduction path (Graph II). In particular, reaching the Medium Term Objective (MTO) of a structural deficit of 0.5 percent in 2017 as per Fiscal Compact requirements would require a cumulative fiscal effort of about

(Continued on the next page)

Box (continued)

1.2 percent in 2016 and 2017 and reaching a primary surplus of nearly 4.0 percent. Maintaining the MTO over the longer term horizon will require primary surpluses of up to 3.9 percent up to 2020, declining gradually to close to 3.0 percent over the following decade. Under these assumptions, the debt to GDP ratio would accelerate its decline already in 2016, falling below 100 percent in the second half of the next decade and maintaining the sustainable downward path thereafter. A slower pace of consolidation but aiming at a more ambitious MTO of 0 percent would also bring down the debt-to-GDP ratio in the long run. On the other hand, if ageing costs are allowed to rise significantly (simulated as a 20 percent increase) **, the fall in the ratio would be severely curtailed, stabilising at a high level in the absence of compensating fiscal consolidation.

Graph III: Changes in general government perimeter (debt as percent of GDP)



Source: Commission services

Graph III illustrates the impact of changes in the government perimeter. The inclusion of all gross costs of PPPs and the debt of all state-owned enterprises (SOE) classified outside general government would lead to an increase in government debt, especially if further increases in SOE debt are not reined in. The ongoing renegotiation of PPPs contracts will limit the cost of a reclassification scenario. The envisaged privatisation programme combined with the necessary reforms to reduce SOEs operational costs and a strategy to reduce their debt burden will also contain the risks stemming from SOEs. By the same token, a quick repayment of the bank recapitalisation funds to the government would accelerate the adjustment towards lower debt-to-GDP ratios

Overall, the debt sustainability analysis reveals that the debt reduction path of the baseline is shows across a number of plausible scenarios. However, a solid reduction path is only attainable if fiscal responsibility is maintained also after the end of the programme period.

* Not taking into account the positive indirect effects of the higher GDP growth on the fiscal balance.
** According to the EU ageing report Portugal is part of the low risk countries where the increase in age related expenditure is amongst the lowest in Europe.

FISCAL STRUCTURAL REFORMS

Fiscal policy framework

34. Portugal remains committed to further strengthening Public Financial Management. The Ministry of Finance has set up a Reform Unit with the broad remit of revising the Budget Framework Law (BFL), which is currently fragmented, imprecise in some areas and too detailed in others. An IMF-led technical assistance mission took place in July 2013 recommending a deep restructuring of the law to be organised along the major phases of the budget preparation and execution cycle, reducing the detailed requirements of budget documentation and improving the provisions of cash management and auditing. The new law should also reform the organisational structure by empowering programme coordinators and modernising the financial departments in line ministries. Finally, the classification structure of the budget should be simplified. Given the scope of the reform, the deadline for submission to Parliament of a draft law was postponed to the first quarter of 2014 following a report by the Reform Unit assessing the strengths and weaknesses of the BFL and providing suggestions for amendments including a new structure. Adequate implementation of the law will be key to success; therefore, an action plan operationalizing the implementation of the law will be prepared by the eleventh review. A follow-up technical assistance mission is expected before the end of the year. In parallel to the preparatory works to reform the BFL, the authorities are executing the action plan for public financial management defined in the 2013 Budget and reinforcing the implementation of the commitment control.

Revenue administration

35. The recent tax administration reforms have improved efficiency in the fight against tax evasion but further efforts are required. The government has successfully put in place the VAT e-invoicing reform that introduced mandatory invoicing and electronic transfers of invoice data for all businesses and transactions. The information gathered in the centralised database allows improving the effectiveness of the tax administration in fighting tax evasion by, for example, tracking potential mismatches between the VAT amounts invoiced and the amounts deducted/paid by taxpayers and better targeting audits when irregularities are detected. It is now important to enhance the operational capacity for analysing the data in a timely and effective manner. The scheme that introduced tax incentives for consumers to ask invoices in certain sectors is also proving successful, as demonstrated by the growth of the VAT base and collection in those sectors in the last months (which compares with a negative evolution in the aggregate collection of all other sectors). Whilst these have been promising steps forward, fighting fraud and evasion must remain a top priority.

36. Most revenue administration initiatives are progressing as planned. The pilot compliance projects for high-net-wealth individuals and self-employed professionals continue to be reinforced, and the plans for the phasing in of a risk management unit are advancing. The improved information from the unified monthly tax returns and the unified form on independent workers' annual revenue will be key inputs for a risk analysis of the compliance situation. The authorities remain committed to the target of closing 25 percent of local tax offices by year- end. There are delays in the targeted increasing in the number of tax inspectors to 30 percent of the tax administration staff, which should be achieved by the end of 2013.

37. The scheme for the settlement of tax debt and overdue social contributions approved in early October could have a short-term positive impact on tax collection but has potential downsides. On the positive side, by normalising the tax situation of debtors the scheme may alleviate financial hardship and facilitate access to community funds requiring a regularised tax situation. However, with a view to avoiding the negative effects of a frequent repetition of such schemes the government has committed to forego any such tax debt recovery schemes in the future (the last such scheme occurred in 2002).

Regional and local governments

38. Regional and local policy frameworks have been strengthened. The new regional and local finance laws have been approved and will enter into force at the beginning of 2014. They adapt the local and regional budgetary frameworks

to the principles and rules of the revised Budgetary Framework Law, strengthen fiscal accountability, limit the scope for lower tax rates in the Autonomous Regions, strengthen the auditing and enforcement powers of the central tax administration, and include requirements for data provision to support the revenue projections. The revision of the laws was done in close consultation with stakeholders. The reduction of the number of parishes from 4050 to 2882 became effective after the local elections as the newly elected officials took office. While most of the jobs in the parishes are on a voluntary basis, the authorities estimate that direct savings of EUR 8.8 million per annum will be attained from the elimination of bodies and functions, but more important yet hard-to-quantify gains are expected from economies of scale and a better quality of merged services.

39. Budget execution and public sector reforms in the two autonomous regions are on track. In Madeira, budget execution is in line with expectations, both due to increasing revenue – reflecting higher tax rates and a better than expected performance of the regional economy - and contained expenditure. Arrears accumulation has been reversed in the summer following some repayment of the stock of arrears. Negotiations on the two motorway PPPs with the aim of achieving important savings have started and the regional authorities are, despite some initial difficulties, confident of reaching agreement later this year. There is also some progress on the restructuring and privatisation of Madeira's SOEs. In the Azores, due to good expenditure control and strong revenues – following a good season of tourism and agriculture as well as higher tax rates – the budget (in terms of public accounts) showed a small surplus of EUR 1.2 million in August and arrears have come down to EUR 3.7 million. A small budget deficit of EUR 27 million is expected at end-2013, and for 2014 the objective is to reach a balanced budget, in spite of lower State transfers. SOEs in the Azores have undergone a process of consolidation and are overall in balance.

Public administration reform

40. Public administration reform continues to make good progress. In addition to the respective measures in the context of the public expenditure review, the process of staff reduction is ahead of the programme objective (staff reduction across all layers of government by 2 percent per year in 2012-14) as a 6 percent reduction relative to end-2011 was already achieved by June 2013. This resulted essentially from early retirement, the termination of fixed-term contracts (mainly teachers) and restrictions on new recruitment. The application of shared services for financial resources in the central administration ('GeRFiP') and for human resources in the Ministry of Finance ('GeRHuP') is improving management efficiency, but will take more time than expected for the about 10,000 employees of the tax administration across the country. The Labour Law for Public Workers, of which a draft was submitted to the Parliament by end-October, consolidates the fragmented legal bases for public administration employees and facilitates a more consistent application. A programme measure to review the regulation of associations and observatories was modified to take into account, on the one hand, the legal heterogeneity of observatories with only few being public and, on the other hand, the high number of 40,000 private associations. The authorities will review public financial support to private associations on the basis of information becoming available through a new legal obligation to regularly report on benefits granted by the public administration to the private sector (Law 64/2013).

SOEs, PPPs and privatisations

41. The new framework law for state-owned enterprises (SOEs) has been published and will enter into force on 3 December. It encompasses a set of changes including the Ministry of Finance's enhanced shareholder role (and similarly municipalities' role vis-à-vis local SOEs) and the creation of a new taskforce inside the ministry to cope with the enhanced responsibilities for the whole SOEs spectrum, particularly the consolidated financial planning and monitoring and the first level legality checks. At the same time, SOEs indebtedness is now subject to clear limits for long-term debt and risk derivative instruments, with the public debt agency (IGCP) assuming a key monitoring role. The SOEs cash position will in the future be centrally managed by IGCP.

42. SOEs achieved overall operational balance in 2012 but this is not assured for 2013 and beyond. SOEs, in particular in the transport

sector, have been undergoing a comprehensive restructuring programme including the optimisation of services, an update of tariffs (prices and system) and a significant reduction in personnel since the beginning of the programme. However, further restructuring will be necessary to ensure that operational balance at sector level is also assured in 2013 and beyond, given that the reinstatement of the 13th and 14th bonus salaries in the public sector is posing significant new challenges to expenditure reduction. At the same time, the government is working on strategies to deal with the heavy indebtedness of several SOEs. Águas de Portugal (AdP), the holding company of several inter-municipal water companies, is undergoing a significant restructuring, including mergers to foster the sustainability of the sector in the mainland, while the regulatory framework is being adapted to the future corporate framework in the sector.

43. Privatisation plans continue even though the programme target in terms of proceeds has already been achieved. The Council of Ministers decided on 10 October to privatise up to 70 percent of the postal company (CTT) through an initial public offering until the end of the year, hand in hand with – and subject to – the revision of the postal sector's regulatory framework and the definition of the concession. The sale of EGF, the waste management company within AdP, is delayed by one quarter with binding offers now expected for early 2014. The privatisation of CP Carga (freight subsidiary of CP) and of TAP (national air carrier) will proceed as soon as market conditions allow. Meanwhile, efforts to improve their operational balance and profitability will continue. Public transport services in Lisbon and Oporto (Carris and Metro de Lisboa; STCP and Metro do Porto) are being restructured with a view to opening their concessions to private operators.

44. The administrative capacity to deal with PPPs is improving. Revised contracts on the basis of the preliminary agreements regarding nine road concessions that were successfully renegotiated between the grantor and the concessionaires remain to be approved by the lending consortia and the Court of Auditors. The revised contracts are expected to achieve important savings in 2013 and beyond. The preliminary agreements bring sustainability and certainty back to the sector, with a fairer burden sharing between public and private partners, thereby correcting errors from previous renegotiations. More than half of the savings to the budget result from a decrease in shareholders' internal rates of return. Lower costs from operation, maintenance and major repairs – also stemming from a downward revision of regulatory requirements in line with EU standards (completed by end of October) – play a crucial part in the expected savings. Lending banks are to contribute with more flexible guarantees and alternative risk mitigation tools (e.g. the State gives real tolls collection as collateral to compensate for lower debt service coverage ratios) that enable lower cash flow requirements to each project without jeopardising its financial soundness. The Ministry of Finance's PPPs central unit (UTAP) is playing a pivotal role in delivering valuable financial and legal expertise to these renegotiations. UTAP is also providing consultancy services to road PPPs renegotiations in the Autonomous Region of Madeira and is helping the Ministry of Internal Affairs in auditing the technical performance of the joint emergency and security network system (SIRESP). The tender for the new Hospital Lisboa Oriental PPP, launched in 2008 but suspended before awarding, was reassessed and a final decision is expected shortly. Nevertheless, the importance of the project to the on-going hospital reform was confirmed and should there be no award of the current tender UTAP, together with the Ministry of Health, will assess if the project should be developed as a public investment project through a traditional public procurement procedure or alternatively as a PPP.

Healthcare sector

45. Policy implementation is continuing broadly in line with programme deadlines. The ongoing reforms have already produced important savings: in 2013, with expenditure in the National Health Sector (NHS) expected to be about 14 percent lower than in 2010 (corresponding to EUR 1.3 billion in savings). In a context of reduced budget transfers to the sector (-11 percent since 2010), all cost categories show a consistent reduction and the consolidated deficit of the sector (Central Government and SOEs together) shows a significant reduction from EUR 818 million in 2010 to a forecasted EUR 65 million in 2013. In addition, by the end of 2013, an important stock of

overdue debt will have been paid through the debt settlement programme (about EUR 1.9 billion). While arrears have not been fully eliminated (a stock of about EUR 500 million remains to be paid), their accumulation rate and payment time have been reduced.

46. The healthcare sector faces major challenges related to increasing labour costs and lower State transfers. Given the high share of wages in overall expenditure, the reinstatement of the 13th and 14th bonus payment has led to significant cost pressures in 2013. In addition, in 2014 the sector may face additional budget cuts if alternative horizontal expenditure-reducing measures do not materialise. This limits the sector's ability to tackle the existing stock of arrears and may even lead to their renewed increase. As a result, the authorities will have to intensify ongoing reforms, notably the centralised purchasing of goods and services and the on-going hospital reform. A further agreement with the pharmaceutical industry may also be crucial to contain spending in this area.

47. Revenues from moderating fees (co-payments) and fees charged to cross-border/foreign patients have continued increasing in 2013. While the increase in revenue was somewhat lower than expected, these fees presumably also dampened expenditure since the number of unnecessary emergency consultations has apparently decreased at the same time. The authorities continue improving the billing and collection process and have set a goal of 90 percent collection for SOEs.

48. Regarding pharmaceuticals, the authorities continue fine-tuning the set of measures adopted since 2011. These measures have led to important savings on spending on outpatient pharmaceuticals. Public spending fell by 11.6 percent in 2012 and by an additional 7 percent in the first half of 2013. Private spending associated with cost-sharing saw a reduction by 11.9 percent in 2012 and an additional 11.2 percent reduction in the first half of 2013. Savings on inpatient pharmaceuticals in hospitals have been slower to materialise. In 2012, spending was at around EUR 930 million including credit notes received as a result of the agreement with the pharmaceutical industry. In 2013, spending remained broadly unchanged (0.5 percent reduction in the first half of the year). The overall (outpatient plus inpatient) spending targets for 2012 (1.25 percent of GDP) were achieved. Spending objectives for 2013 (1 percent of GDP) are on track through a combination of measures including the application of an international price reference system in the hospital sector (already in place), administrative price reductions (already in place) and the potential implementation of the claw-back agreement with the industry for 2013.

49. The share of e-prescription is now more than 99 percent in NHS facilities and 83 percent in private practices. Additional steps are planned to further reduce the cases for manual prescription. Regarding compulsory INN (active substance) prescription, concerns raised by the observed increase in the use of exemptions to INN prescriptions are being addressed by the authorities. The improved e-prescription system allows for both prescription and dispensing information on the basis of which the authorities can investigate outlier behaviour of both pharmacies and doctors. In about 40-50 percent of all cases the 5 cheapest medications are dispensed, which represents a slight reduction from earlier in the year, probably related to the increase in exemptions. Therefore, the authorities are considering an additional set of measures that are to enhance a greater dispensing and use of outpatient generic medicines in order to achieve the 2013 target of 45 percent of all outpatient prescription reimbursed by the NHS (currently at 39 percent). Additional measures promoting the use of less costly medicines are in place, namely centralised purchasing and the implementation of the national formulary. The authorities are currently monitoring divergences between prescription and dispensing and the use of exemptions to INN prescription.

50. With regard to primary care, the authorities continue to take steps to create new family care units (USFs), ensure that all the population is served by family doctors and implement patient medical records. These measures aim at reducing the current share of patients not covered by family doctors. In addition, the system of electronic medical records can improve safety of care and avoid the duplication or unnecessary use of services such as diagnostics. This remains a crucial albeit difficult and challenging reform.

51. Regarding the hospital sector, important savings were realised in 2012 and authorities continue to focus on further cost reductions and efficiency increases. Operational costs went down by 6 percent in 2012 compared with 2011 (about EUR 316 million). In 2013, overall operating costs may remain more or less at the level of 2012, mostly because of the increase in the remuneration of employees (reinstatement of 13th and 14th salary bonus payment). All other categories of costs show a reduction in the first half of 2013 compared with the same period of 2012. In this context, authorities reconfirmed their commitment to implement the ongoing hospital reform. The main concern now is to finalise the 3-year strategic plans for hospitals which are to deliver important cost reductions from now to 2016. These plans are based on the general targets for hospital reorganisation by region and the respective overall savings of EUR 400 million in the best case scenario. These additional savings will be the result of further merging, restructuring, closing or redistribution of departments and the consequent reduction of beds and reallocation of staff.

52. The use of centralised purchasing is advancing, but there is still room for further extension, notably in areas outside medicines and for which centralised procurement is not compulsory for SOE hospitals. The on-going centralised tenders now cover a substantial list of goods but also services and IT and the authorities have presented a plan for further centralised purchasing. The authorities also continue to develop a uniform coding for medical devices and, as a consequence of which more centralised tenders will become possible. This is important as medical devices constitute an important share of hospital costs and have not seen as substantial a reduction as other cost items. Centralised purchasing is expected to contribute significantly to the further reduction in hospital costs in 2014.

FINANCIAL SECTOR

53. Banks' solvency levels are adequate for the current needs. Banks' own funds increased substantially in the past year boosted primarily by capital injections of EUR 5.6 billion from the Bank Solvency Support Facility (BSSF). However, the central bank remains vigilant and continues to closely monitor the banks' capital positions through regular stress tests and both onsite and offsite thematic assessments. At banking sector level, the Core Tier 1 ratio stands at a comfortable 11.9 percent, a level which is adequate to cover immediate bad debt costs and weather the foreseen deterioration of the loan portfolio and short periods of volatility surrounding the sovereign. This capital buffer remains considerable across the board when using the new CRD IV rules for evaluating banks' own funds. In a hypothetical scenario of a full implementation of the CRD IV/CRR guidelines, most of the top eight banks would be able to meet the 7 percent Common Equity Tier 1 (CET1) ratio. Banco de Portugal is currently developing a transition approach to introduce the new capital rules applicable from January 2014.

54. The crisis management toolkit has been improved allowing effective intervention in troubled banks. Portugal, similar to many European countries, lacked domestic resolution tools. This restricted the authorities' intervention powers in failing banks, ultimately exposing taxpayers to major losses. The key objective of the newly created resolution framework is to make resolution feasible without systemic disruptions and without burdening the State. Hence, the Resolution Fund, entirely financed by the banking system through yearly contributions and proceeds from the bank levy, is an integral part of the new framework and has been operational since the end of the first quarter of 2013. It held about EUR 55 million by end-September 2013. Banco de Portugal has put in place a dedicated bank resolution team that can quickly borrow staff resources from other divisions of the bank if the need arises. The recapitalisation legislation is currently in the process of being adjusted to the new European state aid rules and already enables the government to request mandatory recapitalisation operation on a proposal by Banco de Portugal.

55. Taking advantage of new regulatory tools, the corporate and household debt restructuring is proceeding, thus contributing to a smoother deleveraging of the private sector. Further to the implementation of the banking sector legislation aimed at monitoring and mitigating excessive credit risk and promoting an orderly debt restructuring of banks' household clients, the Banco de Portugal presented

aggregated system data on the out-of-court debt settlement of defaulted bank loans. While preliminary figures suggest that the legislation actually encourages the voluntary settlement of debts overdue, a key goal of the framework is to promote the restructuring of debts via agreement between the parties (under the general regime). The Banco de Portugal remains vigilant in regard to the correct application of the framework. The authorities have completed a survey of insolvency stakeholders, including users, to inquire about the appropriateness of the existing corporate debt restructuring tools and possible gaps or bottlenecks. The survey findings allow the authorities to consider possible incremental improvements to the new corporate insolvency and recovery system implemented in 2012. To support the efforts aiming at the successful restructuring of viable companies facing temporary financial difficulties, three state/bank-funded investment vehicles worth EUR 220 million were set up («Revitalizar» funds).

56. Steps were taken to expand the use of commercial paper as an alternative financing source for companies, notably SMEs. A detailed draft legislative proposal to modify the regulatory environment applicable to the commercial paper market has been prepared. Concrete taxation measures forming part of the enhancements to the commercial paper regime are still to be presented, as well as an assessment of the respective budgetary implications. The final proposal is expected to be approved by the Council of Ministers by end-November.

57. Proposals to improve the governance of the National Guarantee System (NGS) and the allocation of government-sponsored credit lines to SMEs were presented. The NGS has contributed to the financing of SMEs in Portugal since its inception in the mid-nineties and, through its guaranteed credit system, has approximately EUR 2.9 billion of outstanding exposures in guarantees to SMEs. However the system shows some deficiencies at the level of pricing mechanisms and room for improvement of the risk management capabilities which hinder a fully efficient allocation of the dedicated financial resources to SMEs. Furthermore, while the financial supervision of the system's mutual guarantee societies and the management company of the counter guarantee fund follow a model in line with international best practice, weaknesses were found in the supervision and public disclosure of the counter guarantee fund, which are an obstacle to the effective management and monitoring of the State's exposure to the NGS operations. The system's scrutiny mechanisms in place from a public accounting perspective remain unclear. Therefore, building on the recent external audit to the NGS and on a set of policy recommendations, the authorities submitted a plan containing measures to improve the performance of the government-sponsored credit lines and the governance of the NGS. These measures will be implemented by January 2014. Regular reporting on the implementation of the above measures will be carried out. With these changes in place, it is expected that the credit lines will bring further advantages for SMEs, budgetary risks for the state will be reduced and, more generally, the credibility of the system will improve. The authorities prepared the first quarterly report on the allocation of these credit lines.

58. The authorities are exploring possible additional initiatives to improve financing opportunities for SMEs. The authorities are actively contributing to the current EU-level discussions on the setup of new innovative risk sharing financial instruments to support the provision of finance to SMEs in Europe, including Portugal. Such instruments rely on public and private resources. On the public side, the instruments being explored resort to the combination of national allocations under the ESIF, EU programmes dedicated to SMEs (COSME and Horizon 2020) and resources from the EIB and the EIF. The public participation aims at boosting private sector resources and incentivising capital market investments in SMEs. Furthermore, building on the recent agreement on a State guarantee for existing and future exposures of the EIB to the Portuguese economy, the EIB is expected to step up its efforts to facilitate the financing of the corporate sector in Portugal, in particular the economically viable SMEs operating in the tradable sectors.

59. The stock-taking exercise aiming at streamlining and centralising the management of EU structural funds continues. By Resolution of the Council of Ministers, the authorities approved in June a new institutional model for the governance of the European Structural Funds

aiming at a better political coordination of the funds as a whole, and at the concentration of the programming, coordination, certification and payment functions in a single institution. Accordingly, in August, the IFDR, IGFSE and QREN Observatory were abolished and merged into a new body, the Development and Cohesion Agency (Agência para o Desenvolvimento e Coesão, I. P.). At the same time, the authorities continue developing an initiative that aims at improving the effectiveness of structural funds for the 2014-2020 programming period, to be allocated to the private sector. This entails setting up a 'specialised financial institution' that will progressively absorb existing structures. The potential fiscal risks linked to the implementation of such an initiative will be monitored closely, while respecting the relevant EU competition legislation.

STRUCTURAL REFORMS

Reform of labour, goods and services markets

Labour market

60. The labour market performance in the second quarter showed some positive signs. According to the National Statistics Office, unemployment decreased by 66,200 persons and employment increased 72,400 persons in the second quarter. According to the authorities, only a quarter of the change in unemployment can be explained by seasonal effects (strong employment effects in the agriculture and tourism sectors). Active labour market programmes, such as 'Impulso Jovem', could have contributed to the strong fall in youth unemployment. Furthermore, around a quarter of all new employment contracts were permanent ones. In terms of qualifications, absolute increases were strongest up to secondary education, with tertiary education flat. However, the youth unemployment rate remains very high at 36.8 percent and, in order to foster the integration of young people in the labour market, the Government is further committed to implement a Youth Guarantee.

61. The third stage of the severance payments reform was implemented on 1 October 2013. Severance payments for open-ended contracts were reduced from 20 to 12 days per year of work. For fixed-term and temporary contracts, severance payments were reduced from 20 to 18 days during the first three years of contract. Accumulated rights up to the date of the entry into force of the new rules are preserved. Simultaneously, the government has enacted two compensation funds that will cover part of the severance payments. Employers will contribute with 1 percent of the wage of new hires to the compensation funds 0.925% is allocated to an individual account and will be used by the employer upon termination of the employment contract (or will revert to the employer in case of contract termination without right to severance payment); 0.075% of the contribution is allocated to a mutual fund which will be used by the social security when employers fail to meet their obligations under the severance payments rules. Until 2015, firms can apply for reimbursement from the State of their contributions to the funds.

62. The Constitutional Court ruled that part of the revisions of the definition of the dismissal rules introduced by the Labour Code revision of August 2012 were not in line with the Portuguese Constitution. In case of redundancies, the Labour Code revision had eliminated a tenure rule that an employer needed to follow (in case of a redundancy in a section with multiple identical posts) and established that the employer decides on which worker(s) to dismiss, based on objective and non-discriminatory criteria. The revision had also abolished the need for the employer to prove that there were no other suitable positions in the firm for the employee at risk of being dismissed. In addition, the Labour Code had introduced changes to the definition of dismissal based on unsuitability, making them possible without prior changes to the work place and abolishing the need for the employer to prove that there were no other suitable positions in the firm for the employee at risk of being dismissed on grounds of unsuitability. With the exception of the enlarged scope of the definition of dismissals based on unsuitability, the other changes to the definition of dismissals, which are important to tackle the high labour market segmentation, have been ruled unconstitutional by the Court. The authorities are now looking into alternative reform options that can achieve a similar impact as the provisions ruled unconstitutional while respecting the Court ruling. Several other changes to the labour code were deemed constitutional, notably performance-related dismissals, the bank of hours,

the reduction in overtime compensation, the suspension of four public holidays, and the elimination of up to 3 days of leave, even though some of these changes – as foreseen in the revision to the labour code – cannot prevail over arrangements in collective agreements.

63. **Measures taken to further facilitate the conclusion of agreements at firm level have not yet produced effects.** Following the tripartite agreement of March 2011 and the MoU, the Labour Code revision of August 2012 introduced the possibility that sectoral collective agreements regulate the conditions under which the agreement could be changed at firm level on matters related to functional and geographic mobility, working time and remuneration. In addition, the firm-level threshold for unions to be able to delegate the conclusion of firm-level collective agreements to works councils has been reduced from 500 to 150 workers. A report prepared by the authorities has concluded that no use has been made yet of these new provisions. In fact, collective bargaining at sectoral level decreased drastically since 2010, while firm-level collective bargaining remained stable. The sharp decline in the overall number of new collective agreements is problematic in view of the important role of collective bargaining in absorbing the high unemployment levels.

64. **The authorities continued to implement measures to improve the role of Active Labour Market Policies.** The authorities have presented a description of the functioning of the job counselling / job search assistance and the activation / sanctions systems. It was considered that there is further scope to improve the role of these systems in facilitating the transition from unemployment to employment, in particular by improving the profiling and strengthening activation. There was good progress in implementing the action plan to revamp the Public Employment Services, with the majority of the measures already concluded. There are some positive results in terms of job placements and job offers. The authorities are also preparing a plan to increase the cooperation with the private sector in placing the unemployed. Training is being adapted to the changing profile of the unemployed and there is an attempt to reinforce short training modules to reduce risks of lock-in effects, while maximising the number of unemployed that receive training. Dual-apprenticeship systems and education and vocational training will continue to be important priorities. More efforts will be made to monitor the extent to which training contributes to increasing employability.

Education

65. **Reforms in the education sector are advancing well even though some measures are somewhat delayed.** The monitoring tool aimed at enhancing the information available regarding the national education network has been further enriched. This tool is expected to be an essential source of information for better targeted and more efficient policy decisions and is now fully operational. The authorities have also approved a very significant number of additional school autonomy agreements. Once signed, the total number of agreements will be more than 200, going much beyond the initial objective of 80 agreements for the school year 2013/2014. As a result, around 25 percent of public schools will enjoy enhanced autonomy. The government is still working on possible improvements in the financing of schools in order to take better account of evaluation and performance criteria. The number of hours of vocational education in work context was enlarged in the vocational courses, in order to develop the technical component of the education framework, allowing the trainees the chance to apply the acquired knowledge and develop new skills to make easier either their immersion in the labour market or the possibility of going on with their studies. The setting up of the professional schools of reference is behind schedule. They will not be operational before the next school year as the government is still drafting the relevant legislation and negotiating protocols with the business sector. Reporting on the latest developments in the apprenticeship system and the latest cycle of external evaluation of schools is of sufficient quality. The government will outline in future programme reviews options for improvements of the system of external evaluation.

Box 2.2: **Export Performance: The Role of Sectoral and Geographical Factors**

Portuguese and global exports grew at annual average rate of around 11 percent in nominal terms in the period 2000-2007, leaving the share of Portuguese exports practically unchanged at 0.40 percent during this period. From 2007 to 2010, however, Portugal experienced a decrease in nominal exports of 5.4 percent, while global exports increased by 12.8 percent, resulting in a decrease of the share of Portuguese exports in world exports to 0.34% in 2010. From 2010 to 2012, Portugal experienced a significant 19.8% increase in its exports, which – while still below its pre-crisis performance – outpaced the 8.0% increase in world exports and led to an increase in the share of Portuguese exports to 0.37% in 2012 (see Table 1, first 3 columns).

Table 1 : Portuguese Export performance indicators

Time		Share of Portuguese exports in world exports [1]	Growth of Portuguese exports [2]	Growth of World exports [3]	Difference in relative growth rates (in pp)* [4]	Contribution of Initial Specialization by Country (IGS) (in pp) [5]	Market Share Gain by Country (MSGG) (in pp) [6]	Contribution of Initial Specialization by Sector (ISS) (in pp) [7]	Market Share Gain by Sector (MSGS) (in pp) [8]
2000		0.40%							
	2000-2007		111.76%	110.34%	1.43	4.60	-3.17	-13.41	14.84
2007		0.40%							
	2007-2010		-5.38%	12.82%	-18.20	-1.25	-16.95	-2.75	-15.45
2010		0.34%							
	2010-2012		19.77%	8.03%	11.74	-7.25	18.99	0.01	11.73
2012		0.37%							

Source: Commission services based on the UN COMTRADE data (HS 1992 Commodity Classification), Nominal USD

*Growth rate of Portuguese total exports minus growth rate of global imports (proxied by exports).

Note: The components of the decomposition should be interpreted as weighted market share gains (MSGG and MSGS) or weighted dynamism of the specific market (IGS and ISS). Table 1 decomposes the difference between Portuguese export growth and world export growth, with positive (negative) values indicating increasing (decreasing) global market share. Export dynamism is gauged on the basis of initial sectoral specialisation (ISS) and initial geographical specialisation (IGS). A sector is dynamic if its global imports (in this case proxied by its global exports) grow at a faster pace than the world total imports (proxied by global exports). Similarly, a destination country is dynamic if its total imports (proxied by its global exports), grow faster than the world total imports (again proxied by global exports).

A decomposition of exports performance in Portugal into contributions from product and geographical components over the periods 2000-2007, 2007-2010 and 2010-2012 indicates that Portugal has regained market share between 2010 and 2012 both within its product markets and among its destinations. However, between 2010 and 2012, the Portuguese export growth was limited by its specialisation in slow growing geographical destinations (column 5) while its initial sectoral specialisation has played a neutral role (column 7). The generally negative contributions from these two components suggest an unfavourable product and geographical composition of exports as the country has specialised in products with less dynamic global demand and in less dynamic destination markets. These two factors to some extent can be considered "exogenous" to the exporting country in the short run, in the sense that given a country's initial specialisation, the dynamism of the products it exports and of its destination markets is beyond the country's control.

Graphs I to IV shed more light on the components of market share gains. The first two graphs shows the contribution of initial specialisation by destination country relative to the contribution due to market share gain experienced in each destination country, for the periods 2007-2010 and 2010-2012. Portugal has experienced market share gains in all of its main destinations in 2010-2012. For example, despite observing that total imports of Spain decreased by 3.1% in the period 2010-2012, Portuguese exports to Spain increased by 0.4%, resulting in a market share gain. This suggests that Portugal is experiencing competitiveness gains vis-à-vis its competitors. This situation represents a reversal relative to 2007-2010 when Portugal was losing market share in seven out of the ten most important Portuguese export destinations (see Table 2 for details per main country of destination). However, from 2010 to 2012, Portuguese exports have had mainly other

(Continued on the next page)

Box (continued)

European countries as a final destination and these were mainly countries experiencing lack of dynamism in their import market, which contributed negatively to the aggregate Portuguese market share.

The Portuguese exports to Angola have increased by 11.1% while Angola's total imports increased by 5.1%, representing a market share gain for Portugal. However, given Portugal's exports weight in total Angolan imports (19.6%), the recent growth in market share for this destination is unlikely to proceed at the same pace in a sustainable manner.

Table 2: Growth of Portuguese and World exports by country (average annual growth rate)

	2000-2007		2007-2010		2010-2012	
	PT	World	PT	World	PT	World
Spain (22.49%)	2.20	1.80	-0.70	-1.60	0.40	-3.10
Germany (12.29%)	0.80	1.40	-0.30	1.00	3.40	0.50
France (11.83%)	1.40	1.20	-0.80	1.10	4.80	-1.20
Angola (6.60%)	4.00	3.80	1.10	2.90	11.10	5.10
UK (5.28%)	0.20	1.20	-1.20	-0.30	3.80	1.90
World	1.50	1.50	-0.60	1.30	4.60	1.90

Table 3: Growth of Portuguese and World exports by country (average annual growth rate)

	2000-2007		2007-2010		2010-2012	
	PT	World	PT	World	PT	World
5. Mineral Products (10.19%)	2.94	2.10	2.78	2.67	9.40	1.12
11. Textiles And Textile Articles (9.12%)	0.40	1.09	-1.25	0.29	1.95	0.92
15. Base Metals (8.20%)	2.49	2.19	-1.35	-0.36	5.68	1.49
16. Machinery; Electrical Equipment (15.11%)	1.42	1.27	-3.16	0.63	4.97	1.58
17. Vehicles, Aircraft, Vessels (11.66%)	1.21	1.43	-0.79	-0.23	3.11	3.00
World	1.54	1.53	-0.61	1.35	4.61	1.95

Source: Commission services based on the UN COMTRADE data (HS 1992 Commodity Classification), Nominal USD.

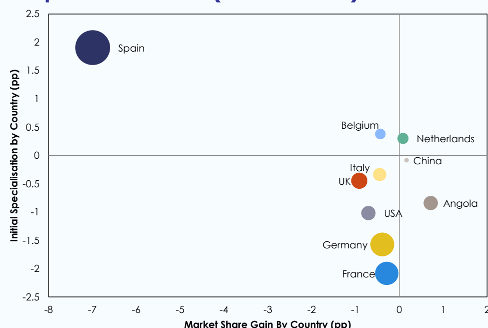
Note: The percentage between the brackets represent the weight in Portuguese exports in 2012.

Graphs III and IV show the contribution of Portugal's initial specialisation to its export growth relative to the market share gains by sector. The high number of relatively large bubbles suggests that Portuguese exports are relatively well diversified. In particular, the Herfindahl concentration index (HCI) indicates that Portuguese exports are more diversified than world total imports (For Portugal HCI is 0.093, 0.081 and 0.082, while for the world it is 0.124, 0.119 and 0.116 for 2007, 2010 and 2012 respectively).

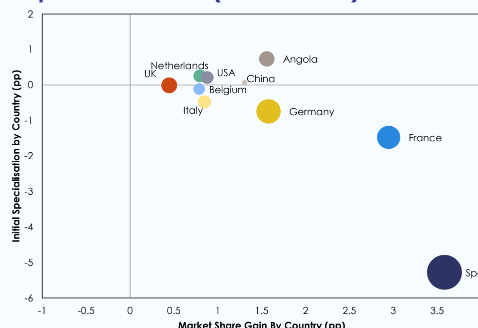
During the period 2010-2012 Portugal has gained market share in most sectors, except for "Vehicles, Aircraft and Vessels" and "Articles of Stone, Cement, Ceramic and Glass ". This is a reversal compared with the period 2007-2010 where Portugal was losing market share in most of its most important sectors. This finding supports the previous conclusion that Portugal is gaining competitiveness. At the same time, these graphs show that the performance related to its initial specialisation by sector has been heterogeneous since 2007, as important sectors display both positive and negative initial specialization contributions (large bubbles above and below the x-axis).

Graphs I-IV: Components of the Portuguese market share gains

Graph I: Countries (2007 – 2010)



Graph II: Countries (2010 – 2012)



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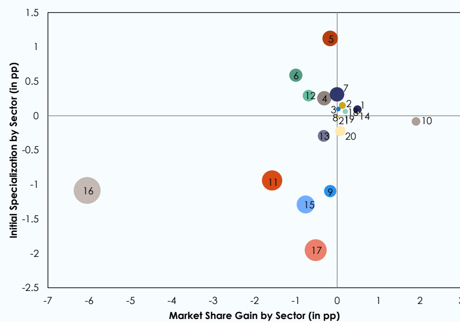
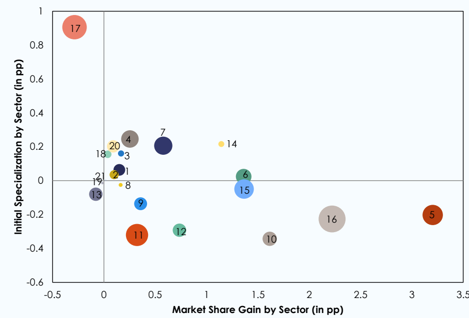
Box (continued)

Graph III: Sectors (2007 – 2010)



Graph IV: Sectors (2010 – 2012)



Source: Commission services based on the UN COMTRADE data (HS 1992 Commodity Classification), Nominal USD

* The size of the bubble indicates the weight of this destination/sector on total Portuguese export at the beginning of the period.

Note (Countries): This contains the 10 biggest destinations for Portuguese exports.

Note (Sectors): 1. Live Animals: Animal Products; 2. Vegetable Products; 3. Animal or Vegetable Fats and Oils; 4. Prepared Food stuffs, Beverages, Tobacco; 5. Mineral Products ; 6. Chemical Products; 7. Plastics and Rubber; 8 . Raw Hides And Skins, Leather; 9. Wood And Cork; 10. Pulp Of Wood And Paper; 11.Textiles And Textile Articles; 12. Footwear, Headgear, Umbrellas; 13. Articles Of Stone and Cement; Ceramic and Glass; 14. Precious Stones and Metals; 15. Base Metals; 16. Machinery; Electrical Equipment; 17. Vehicles, Aircraft, Vessels; 18. Instruments And Watches; 19. Arms And Ammunition; 20. Miscellaneous Manufactured Articles; 21. Works Of Art And Antiques.

Energy

66. The measures ensuring energy regulator's independence and its capacity to guarantee an efficient and competitive functioning of the energy sector are being gradually phased in. Important amendments to the ERSE bylaws were published in June 2013. ERSE's bylaws, which were published after the framework law on functioning of National Regulatory Authorities (NRA) was approved by the Council of Ministers, do not need to be amended, as they already comply with the framework law. During the legislative process in the Portuguese Parliament a few changes were introduced in the NRA framework, but none with material impact in ERSE’s bylaws.

67. Rent-reducing measures implemented so far to eliminate the tariff debt by 2020 and ensure the sustainability of the system appear to be insufficient. The June update of the energy tariff debt dynamics up to 2020 shows a clear worsening relative to the forecasts presented in 2012 and more recent figures indicate that the elimination of the tariff debt by 2020 would require real electricity price increases of close to 2 percent per year, ½ percentage point above initial projections and raising further concerns about the impact of the tariff on competitiveness. The report also shows that the increase in the real electricity price would not be sufficient to eliminate the tariff debt and additional measures would need to be taken despite the fact that the government has already implemented most of the measures agreed by the Council of Ministers in May 2012. The most significant additional measure envisaged by the government is the introduction of a contribution on energy generators preventing windfall profits resulting from the increase in electricity prices in the MIBEL market caused by the levy on the Spanish generators. This measure, though welcome to counter a perverse effect on wholesale prices, is not a cost reducing and sustainability-enhancing measure. Meanwhile, negotiations on the Sines and Pego power plants, which were expected to achieve some savings, reached an impasse. The remuneration scheme for co-generation was revised and establishes that existing co-generation facilities that do not use a

renewable source of energy will transition into market remuneration after 10 years, receiving in the meantime the new tariff set by executive order. A new energy levy on energy operators is under preparation. EUR 100 million of the levy's revenue will stay in the state budget while the remainder will be channelled to reduce the electricity tariff deficit. At this stage the details are not known and two aspects need to be closely monitored: i) ensuring that this levy will not translate into further end-user price increases; ii) gauging the implications of the this levy in terms of the impact and feasibility of other cost-reducing measures foreseen to address the sustainability of the electrical system. Annual audits of co-generation plants to ensure that plants which do not fulfil the requirement for co-generation do not receive support are on-going. Finally, the report on the CMEC scheme and the process for extension of the concession of the public hydro resource has been delivered. Further analysis on the implication of the report and the need for potential measures to address the points identified as sources of distortion will be discussed at the next review.

68. The authorities have presented the plan to create a single logistics operator for switching suppliers (OLMC). According to this plan the single platform will be created no sooner than October 2014. This long delay is explained by the necessity to create the electricity platform from scratch. An independent logistics operator is important to ensure a non-discriminatory treatment of all electricity and gas suppliers and a smooth supplier switching process. Until the electricity suppliers switching platform is fully unbundled from the incumbent, the responsibility to ensure a level playing field for the new entrants will fall to a large extent on the energy regulator and the competition authority.

Telecommunication and Postal Services

69. Significant steps towards compliance with the Court of Justice ruling of 7 October 2010 have been undertaken recently. The tenders for the designation of the universal service provider(s) through an efficient, objective, transparent and non-discriminatory mechanism were launched. The activities under tender 1 (universal service connection to a public communications network at a fixed location and telephone services to the public) were awarded to independent operators. The activities under tender 2 – public pay phones – were awarded to the incumbent. The third tender 'providing a comprehensive directory and a full-service inquiry' was not completed due to the lack of offers. At the time of drafting the report, the final assignments for tenders 1 and 2 are still pending and the historical contract with the incumbent operator has not yet been cancelled. The contract for activities under tender 3 will be directly awarded for a maximum period of 1½ years. Meanwhile, the authorities will redesign the terms of the tender so as to make it more attractive for the bidders.

70. The amended framework for the provision of universal service for postal services is about to be adopted. These amendments will bring the postal law and the concession contract with the incumbent operator - CTT - in line with the European Directives. This is an important milestone in the opening-up of the postal sector to competition. The new framework also ensures that after the year 2020 the postal universal service will be subject to competitive pressure as in 2020 the current designation period for the incumbent operator will expire.

Transport

71. The implementation of some of the transport measures is delayed. With regard to ports, policy decisions are urgently required to ensure that efficiency gains and cost-savings are passed on to port customers and that the port operation concession holders respect minimum performance criteria as provided for in the 5+1 Plan presented last year. As to railways, the unbundling of CP Carga freight terminals are dependent on a final valuation of these assets and will then be transferred to REFER, the rail infrastructure operator, by the end of the year. REFER is expected to present a coherent strategy towards reaching operational balance for discussion at the next review, as significant additional effort is needed in this respect. The launch of public transport concessions in Lisbon and Oporto has been postponed and is not expected before the first quarter of 2014. The adoption of the long-term vision for transport, setting out and prioritising medium-term transport infrastructure investments, is waiting for input from the recently created Working Group on this matter; this group is expected to present a final report on key

transport projects for the coming multi-annual financial framework 2014-2020 shortly. Lastly, the government is drafting the by-laws for the new transport regulator due by early December. The timely adoption of the by-laws is essential to ensure an effective regulatory oversight in the transport sector.

Services and professions

72. Work on the improved sector-specific legislation has progressed but the adoption of the regulatory framework for the construction sector is delayed. The construction laws were originally foreseen to be sent to Parliament by the end of 2012 and are now expected to be sent to Parliament in coming months. The fees charged for authorisations and certificates as well as the value of the yearly regulatory taxes in the construction sector will be revised in order to ensure their proportionality in time for the adoption of the construction laws. Concerning the other sector-specific legislative amendments, progress in aligning legislation with the principles of the Services Directive has continued steadily. 59 out of 68 legal regimes have been submitted by the government for publication or for subsequent adoption by the Parliament, as required by the legislative framework. Legislative amendments for the remaining sectors should be adopted by the end of the year.

73. The report compiling the final results of the second phase of investigation of regulated professions without professional associations has been finalised and submitted as required. Following the recommendations of the Commission for the Regulation of Access to Professions, this second phase report identified requirements on access to professional activities that are no longer justified or proportionate and will be eliminated accordingly.

74. Following the adoption of the horizontal framework law on public professional associations the professional bodies' bylaws and internal rules are being amended accordingly. The law is a first step towards ensuring a more open access for the exercise of some highly regulated professions and an improvement in the legal framework applicable to public professional associations. To complete the reform on highly regulated professions, the amended professional bodies' statutes and internal rules will be approved by the government and subsequently submitted to Parliament with the aim of bringing them in conformity with the principles laid down in the law and removing requirements that are not justified or proportionate. However, the submission of these revised bylaws to the Parliament is delayed and is now expected by the end of the year.

75. Progress has been made on the work to improve the functioning of the Point of Single Contact ("Balcão do Empreendedor"). A clear roadmap and work programme is in place and updated monthly. The operational deliverables needed for this reform will be completed by the next review. The "Zero Authorisation" project that abolishes authorisations/licensing and substitutes them with a declaration to the PSC is fully operational and the platform is available to all levels of administration, including all municipalities. Some further simplification may be needed to ensure better usability by businesses.

Reform of framework conditions

Housing market

76. The process of updating rental contracts signed before 1990 and their gradual transition to the general system has started. The full implementation of the system was dependent on information relating to tenants' personal income in 2012, which was made available in June. In addition, all complementary legislation following the publication of the Housing Rental Market has been adopted. The "Balcão do Arrendamento" is fully operational; it has already dealt with more than 2 000 requests of eviction. The Monitoring Committee which has been set up to monitor the impact of the reform has already delivered its first quarterly report. The data and information regarding the impact of the reform are still limited given the short time elapsed since its full implementation. A fully-fledged first evaluation of the impact of the reform is expected by early 2014. The revaluation of the housing stock has been completed, giving rise to an increase of 115 percent in the cadastral value of the housing stock.

Competition and sectoral regulators

77. Progress to ensure the functioning of the Competition authorities and National Regulator Authorities has been steady. The framework law setting the main principles of the functioning of the main National Regulatory Authorities (NRAs), including those relating to their independence and autonomy, was published in August 2013. The proper and timely implementation of the new by-laws of the respective regulators is essential to confirm that the new legal framework is a significant step forward. The corresponding amendments to the bylaws of the NRA will be approved by the government by early December.

Judicial system

78. Considerable progress has been made in the ambitious programme of judicial reform. Several major structural changes to the judicial system have already entered into force or are about to do so. Among them are the comprehensive new Code of Civil Procedure that came into force in September and aims at speeding up civil and commercial litigation, a new Judicial Organisation Act to streamline the court system, and improved regulation of enforcement agents.

79. Significant headway has also been made in reducing the backlog of court cases. A special task force was created to examine pending cases and has successfully closed 45 percent of the cases existing up to May 2011. In addition, the resolution rate has greatly improved. In the first quarter of 2013, the number of cleared enforcement cases has increased to 158 percent compared with fourth quarter of 2012.

80. The efficiency of the enforcement system will continue to be further enhanced by the measures adopted in the new Emergency Law 4/2013. This law introduced a set of urgent measures to combat the remaining backlog of cases, and were included in the new Civil Procedure Code. Another proposed law (Procedimento Extrajudicial Pré-Executivo) will create a pre-trial triage which will, in particular, be able to identify cases to be settled out of court.

81. New laws will strengthen the authority and financing structure of the oversight body for enforcement agents and insolvency administrators. Together with the new fee structure that incentivises speedy enforcement, these bills will significantly strengthen the discipline and efficiency of the enforcement profession, and hasten the clean-up of long-pending cases.

82. The new Code of Civil Procedure that came into force in September is the most comprehensive re-think in almost a century, and has been widely praised by legal professionals. Among the Code's provisions are a limit of 10 on the number of witnesses that each party can call in civil cases, and tight new restrictions that make it harder for parties to delay hearing dates. The proper implementation of the new Code of Civil Procedure is supported by an extensive team of IT specialists, who, on the request of judges, court clerks and other members of legal profession introduce the necessary changes in the instantaneous fashion. Also, a task force of experts provide rapid answers on the new procedures prescribed by the Code.

83. The Judicial Organisation Act was adopted by Parliament in June and will enter into force in 2014. The law sets out a major streamlining of the judiciary, reducing the number of courts and improving efficiency through the creation of court clusters to allow for greater economies of scale and professional specialization. It also sets workload standards and performance targets for courts and judges, and makes it possible to allocate resources, including judges, where bottlenecks occur. The law constitutes a significant change in the organisation and management of the judiciary with a greater focus on performance accountability and service delivery, bringing Portugal in line with best practice elsewhere in Europe.

84. The Competition Court, set up in 2012 has been properly resourced and is fully operational, responding well to an increased workload.

Box 2.3: **Reforms in the Judicial Sector**

The scope of the judicial reforms was stipulated in the "Justice" part of the Memorandum of Understanding. The reforms were possible thanks to good cooperation between the Portuguese authorities, the legal system's players and the EC, ECB and IMF. The MoU foresaw several cornerstone reforms, particularly the new regulatory framework for the enforcement agents, the new Code of Civil Procedure and the Judicial Organisation Act which triggered changes in by-laws, kick-started new IT systems and applications and necessitated various temporary task forces.

New Code of Civil Procedure

The Code of Civil Procedure (Law 41/2013) came into force in September 2013. The Code facilitates the swift conduct of the proceedings by the judges and the parties. The new Code limits the number of witnesses for each party to a maximum of ten and makes it harder for parties to delay the hearing dates. It foresees the closure of civil and commercial cases that are inactive for 6 months due to the inactivity of the parties. The Code also foresees the closure of enforcement cases wherein debtor's assets have been searched for 3 months without success and neither the creditor nor the debtor have been able to indicate specific assets to be seized. The Ministry of Justice allocated significant human resources to the implementation of the Code. Programmers, technicians, technical coordinators and project managers dedicated 17,820 hours to this project. The IT system (CITIUS) was installed on over 13,000 clients' computers and 335 servers in 1½ months. A specialised helpdesk of 85 technicians provides direct support to the courts. A task force of experts provides rapid answers and training on the new procedures prescribed by the Code. Since the publication of the Code on 26 June, 3 decree-laws and 7 ordinances have been enacted to further implement specific aspects of the new Code.

The Judicial Organisation Act

The Act adopted by Parliament in June (Law 62/2013 replacing Law 3/99) will enter into force in 2014. It provides for a streamlining of the judiciary, reducing the number of courts of first instance from 234 to 23. By enlarging each first instance court's territorial jurisdiction and aligning them with the administrative districts, it aims at improving efficiency through the creation of court clusters to allow for greater economies of scale and professional specialisation. It foresees setting annual and triennial strategic objectives agreed upon between the Ministry of Justice and the Councils for the Judiciary. Other reforms include the introduction of process management, improvement and clarification of the function of court managers, and a possibility of electronic processing of the same process for the secretarial acts at various points of the court.

The Enforcement Agents' Framework

The MoU put a particular stress on the efficiency of the enforcement process which complements the declaratory process in debt recovery. Specially constituted task forces audited all civil and commercial enforcement cases all pending 1,208,842 cases in May 2011 and closed 541,775 (45%). The courts and enforcement agents also stepped up clearance of all enforcement cases, including those filed after May 2011. These efforts were aided by the enactment of Decree-Law 4/2013.

The functioning of the Commission for the Efficiency of Enforcement Procedure (CPEE) has been improved through more effective IT tools. The CPEE has, on the basis of ordinance 2/2012, access to several IT systems, i.e. of the courts (CITIUS) and of the enforcement agents (SISAAE). This resulted in a tighter supervision. In the first quarter of 2013, 266 enforcement agents were inspected vs. 16 in the same quarter of 2012. 22 disciplinary proceedings were concluded by imposing penalties. CPEE will be replaced by the Comissão de Acompanhamento dos Auxiliares de Justiça (CAAJ) which will supervise and regulate

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Box (continued)

enforcement agents and insolvency administrators. CAAJ will be an independent entity focussing on the efficiency of the enforcement and insolvency judicial systems and on the quality standards of the legal professions at stake.

Ordinance 308/2011 introduced a more transparent regime for the bank accounts of enforcement agents, enabling an easier identification of all transactions performed through bank accounts related to an enforcement case. The new fee structure of the Ordinance 225/2013 aligned the costs of the enforcement action to the tasks of the enforcement agent.

Alternative Dispute Resolution (ADR)

Several ADR regimes were revised, i.e. the civil and commercial arbitration regime (Law 63/2011) and the justice for the peace court regime (Law 54/2013) while others were created, i.e. the mediation regime (Law 29/2013) and the tax arbitration regime (Decree-law 10/2011 and Ordinance 112-A/2011). The promotion of ADR is in line with out-of-court mechanisms envisaged in other areas, i.e. in the field of companies' and debts' restructuring (PER and SIREVE).

High value cases (cases above EUR 1 Million)

One of the reforms undertaken on the basis of the MoU focussed on the issue of the high number of outstanding high value tax cases. All the efforts put by the courts, special task forces and the Tax Administration started to bring positive results in 2013. While the number of filed cases show a decreasing trend, the ration of cases won by the tax office increases.

A significant role in the increase of the efficiency of tax courts in terms of cases over EUR 1 Million was played by the special task forces of judges assigned to tribunals in Lisbon and Oporto by Law 59/2011. The number of pending cases in the courts of 1st instance decreased although the number of appeals is increased. A permanent solution dealing in a structured way with this category of tax cases is currently under discussion.

Business environment

85. Liquidity constraints on non-financial corporations continue to be an issue of concern. The Decree Law 62/2013 of 10 May adopted by the government is not fully in line with the New Late Payments Directive 2011/7/EU. The main provision which is considered not to be in line with the Directive is Article 12 of the Decree Law, which provides that the deadline of a maximum of 60 calendar days to proceed to the payment of commercial transactions involving public entities providing healthcare will not be fully applicable until 31 December 2015. Microcorporations and small firms are however outside the scope of this exception. The Directive states that, as from 16 March 2013, Member States must ensure that in commercial transactions in the health sector the period of payment does not exceed 60 days following the receipt of the invoice by the debtor. The argument provided by the Portuguese authorities for such an exception is that full compliance both with the Directive and with the ongoing strategy for the settlement of arrears, which was agreed in the context of the programme, would entail a very significant cash disbursement with a very negative fiscal impact. The Commission has requested additional information to the Portuguese authorities and could launch an infringement procedure in the coming months for non-compliance.

86. The recently introduced VAT cash accounting regime will improve the financial and cash flow situation of businesses. Companies opting for this regime will pay/deduce the VAT when the payments from their customers/to their providers take place, rather than when the invoices are actually issued, as is currently the case. The measure applies to companies from all sectors of the economy with a turnover of up to EUR 500,000 and it entered into force on 1 October.

Licensing

87. Most legal reforms envisaged to ease licensing requirements to businesses are behind schedule. This delay concerns almost all sectors in which reforms are awaited such as territorial planning, geology, commercial or tourism activities. The recent changes in some of the Secretaries of State dealing with these various reforms seem to be a main reason for this delay. Moreover, in some cases the government has decided to change the approach and therefore legal texts do not build on the work that had been carried out by the previous teams. The high number of legal provisions to be adopted poses some concerns regarding the administrative capacity to adopt all of them over the next months. The New Legal Regime on Urbanism and Building (RJUE), which is expected to be adopted by November 2013, is a critical piece of complementary legislation on which progress in other areas depends. Progress has been achieved in some areas, such as (1) the draft Base Law for Soils, Territorial Planning and Urbanism proposal has been submitted to Parliament; (2) the adoption of a Decree Law which fast-tracks the decisions regarding licensing requirements of investment projects over EUR 25 million; (3) the adoption of a new Environmental Impact Evaluation regime, whose compliance with the European legal is being assessed by the Commission; and (4) two ordinances on industrial licensing.

Box 2.4: **Summary of compliance with policy conditionality for the 8th and 9th Review**

The joint EC/ECB/IMF staff mission concluded that the implementation of the Programme is broadly on track.

Fiscal policy	For the third quarter of 2013, the quantitative performance criteria on the general government cash-adjusted deficit and debt are within reach. In national accounts terms, some deviations on the budgetary execution with respect to the supplementary budget have been identified, but the government has taken corrective measures to secure the 5.5 percent of GDP deficit target. However, the improvement of the structural balance will be lower than initially expected due to the incomplete implementation of some measures and replacement by one-offs. Part of the 2013 slippage will carry over to the next year, partially shifting the fiscal effort necessary to continue the consolidation path. The fiscal adjustment towards the 4 percent of GDP deficit target in 2014 will predominantly proceed on the basis of the public expenditure review and other smaller-scale measures as defined in the draft Budget.
Fiscal-structural	Public finance management: The reform of the Budget Framework Law is ongoing, although with some delays with respect to the original schedule. Given the envisaged scope of the reform, the deadline for submission to Parliament was postponed to the first quarter of 2014, following a report identifying the main areas of reform. In order to ensure a rapid and complete implementation after approval, an action plan identifying the operational changes necessary will also be prepared. The authorities are executing the action plan for public financial management defined in the 2013 budget. Revenue administration: The recent VAT e-invoicing reform is improving efficiency in the fight against tax evasion and supporting tax collection. The information gathered following recent reforms on data transmission will underpin further analysis of the current tax compliance situation and prompt targeted audits. Ongoing projects to strengthen compliance are making good progress, whilst there are some delays in the recruitment of tax inspectors. Regional and local administration reform: The new regional and local finance laws were approved and will enter into force at the beginning of 2014. The reduction of the number of parishes from 4050 to 2882 became effective after the local elections as the newly elected officials took office. Budget execution in Madeira and Azores is in line with expectations. Public administration reform: The process of staff reduction is ahead of the programme objective (reducing staff across all layers of government by 2 percent per year from 2012 to 2014) as a 6 percent reduction relative to end-2011 was already achieved by June 2013. The application of shared services for financial resources in the central administration ('GeRFiP') and for human resources in the Ministry of Finance ('GeRHuP') is improving management efficiency. State-owned enterprises (SOEs): The new legal regime for SOEs was published (Decree-Law 133/2013, 3 October) and shall enter into force by 3 December. The shareholder's role is given to the Ministry of Finance and a new dedicated taskforce will be appointed to carry out the tasks that are now centrally monitored by the Ministry. Debt management, risk derivative instruments and cash position of SOEs shall be centrally managed by the treasury agency. Health: Policy implementation continues broadly in line with programme deadlines. Reforms have delivered substantial efficiency gains and related savings and a large stock of overdue debt will be paid by the end of this year (though not fully eliminated). Increased labour costs have nevertheless absorbed some of these savings and, as a result, the authorities will have to intensify existing reforms. The authorities reconfirmed their commitment to implement a hospital reform which is ongoing and to continue to fine-tune the set of measures concerning pharmaceuticals, notably in hospital settings where savings have been slower to materialise.

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Box (continued)

Financial sector	Monitoring banks' potential capital shortfalls: Further to the reflection the OIP findings in the implementation of the SIP recommendations on asset quality and stress testing methodologies, the update of the treatment of collective impairments was finalised. Results of the review of the impairments in the credit portfolios of the eight largest national banking groups (only components more strongly affected by business cycle) confirmed the adequacy of the level of impairments booked in the balance sheet and the resilience of the banking system with respect to solvency. Supervisory organisation: BdP is carrying out the preparatory work leading to the conclusion of a thematic review of banks' operational capacity in the area of loan restructuring and asset recovery. A new supervisory function was set up within the BdP and the assessment of the distressed loans management framework is ongoing. Ex-BPN legacy management: Parvalorem concluded the competitive bidding process to outsource the management of the credits currently held by Parvalorem, having awarded the contract to two contractors. Early intervention, resolution and deposit guarantee framework: BdP concluded the analysis of the recovery plans of the eight largest banking groups. Guidelines to the system are being finalised. The Resolution Fund has been up and running since the first quarter of 2013 and received due contributions from the banks. A dedicated resolution unit was set up within BdP. Financing alternatives for the corporate sector: The preliminary detailed assessment on the grouped issuance of corporate debt has been submitted but issuance was postponed to mid-2014. The first draft of the amendments to the rules governing the commercial paper market was submitted and discussed. Government-sponsored credit lines: An external audit of the National Guarantee System was conducted and a roadmap presented with a set of milestones to be accomplished. The first quarterly monitoring report on the allocation of government-sponsored credit lines was submitted. Corporate insolvency: The authorities released in July the first quarterly monitoring report on the implementation of the new restructuring tools. The results of surveys of insolvency stakeholders, including users, were presented.
Reform of labour, goods and services markets	Labour market and education: The third stage of the severance payments reform was implemented on 1 October 2013. It reduces severance payments up to 12 days per year of work. The measures taken to further facilitate the conclusion of agreements by council works at firm level (organised decentralisation) have not yet produced effects. In addition, the Constitutional Court ruled against part of the revisions of the dismissal rules introduced by the revised Labour Code in August 2012. In the area of education, the monitoring tool has been further enriched and the number of trust agreements signed is beyond expectations; the setting up of the professional schools of reference is behind schedule. Energy: Implementation of the electricity costs reduction and tariff debt elimination by 2020 is on-going. The new update report of the energy tariff debt dynamics shows that the elimination of the tariff debt by 2020 would require real electricity price increases of close to 2 percent per year and even then the tariff debt will not be eliminated without additional measures. The negotiations on the Sines and Pego power plants have reached an impasse. Following the submission of the report on the CMEC scheme and the process for extension of the concession of the public hydro resource, further analysis of, and discussions on the consequences of the report and the potential need for additional measures will continue in the next review. The remuneration scheme for co-generation facilities that do not use a renewable source of energy was revised. A new energy levy on energy operators is under preparation and should be implemented along with the 2014 State budget. Its impact on the tariff debt and end user prices will have to be monitored. Transport: There is little progress to be highlighted as most reforms are delayed. Policy reforms in ports are urgent to increase their efficiency and ability to be competitive in international markets. Further progress is required to ensure operational balance of the rail infrastructure manager by 2015. A clear long-term strategy for the transport sector is still missing. The transfer of the CP Carga terminals to REFER is expected by the end of the year. Services and professions: Progress on the adoption of the legislative amendments to align legislation with the principles of the Services Directive has continued steadily. However the Construction laws have further delays. The submission of the revised bylaws to the Parliament following the adoption of the horizontal framework law on public professional associations is delayed. Some progress is observed in making the Point of Single Contact fully operational.

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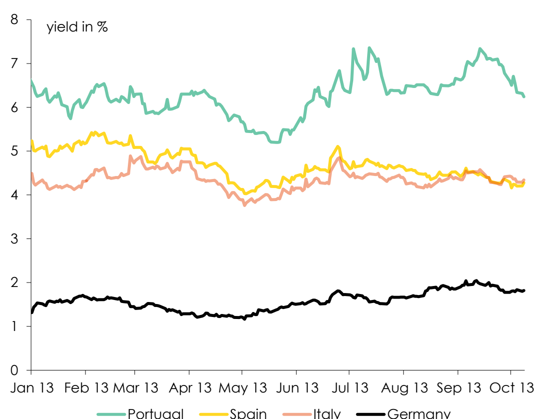
Box (continued)

Reform of framework conditions	Housing market: The process of updating rental contracts signed before 1990 and their gradual transition to the general system has started. The Monitoring Committee which has been set up to monitor the impact of the reform has already delivered its first quarterly report. Competition and sectorial regulators: The framework law setting the main principles of the functioning of the main National Regulatory Authorities (NRAs) was published in August 2013. The corresponding amendments to the bylaws of the NRA will be approved by the government in early December. Judicial system: Considerable progress has been achieved in implementing the ambitious programme, with the reforms being nearly completed. Significant headway has also been made in reducing the backlog of court cases. Business environment: The recently introduced VAT cash accounting regime is expected to improve the financial and cash flow situation of businesses. The Commission considers that Decree Law 62/2013 of 10 May adopted by the government is not fully in line with the New Late Payments Directive 2011/7/EU. Licensing: The Base Law for Soils, Territorial Planning and Urbanism proposal has been submitted to Parliament and some other pieces of legislation have been adopted to make a more business-friendly regulatory system. However, most legal reforms envisaged to ease licensing requirements to businesses are behind schedule.
Data	Requirements under the Programme have been observed. Work is ongoing to improve further data submission.

3. PROGRAMME FINANCING

88. Since late spring, when sovereign bonds traded at pre-programme levels, market sentiment towards Portugal has deteriorated significantly notwithstanding some recent improvement. Global factors became less favourable for vulnerable sovereigns over the summer as the expectation of upcoming Fed "tapering" led to upward pressure on sovereign yields more generally. Real money investors started exiting riskier investments by shifting into safer sovereigns, which now offered a more attractive yield-to-risk ratio. The political crisis in Portugal, which erupted in early July, also raised investor concern about the government's stability and its commitment to the reform programme. Another Constitutional Court ruling against an important fiscal measure in August raised further doubts about the government's capacity to push through the necessary reforms. As a consequence, investors demanded higher premiums to reflect increased sovereign risk and Portuguese bond yields decoupled from other European sovereigns.

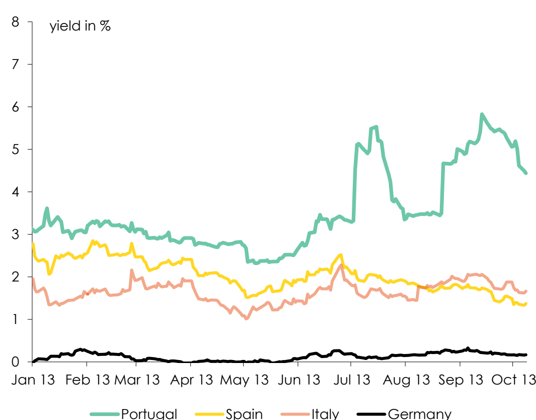
Graph 3.1: **10-Year government bond yield**



Source: Bloomberg

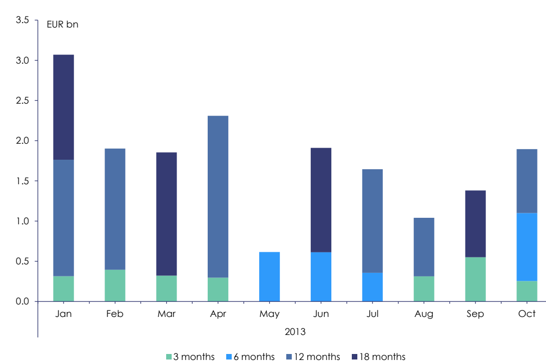
89. The Portuguese Treasury has mainly tapped the domestic market for sovereign financing. Since May, the Treasury has increased the net issuance of Treasury bills by EUR 2.4 billion, mainly concentrating on longer maturities in this segment. Sales of retail debt products also made a small contribution to sovereign financing, and the Treasury expects this trend to continue. To that end, the Treasury introduced a new medium-term product in early October for the retail market, which is expected to deliver cost savings in relation to the current pricing of 5-year bonds. Privatisation receipts amounting to EUR 1 billion were recorded in September. Furthermore, in July the Social Security Financial Stabilization Fund was granted permission to invest up to EUR 4 billion of its foreign reserves into domestic sovereign debt.

Graph 3.2: **2-Year government bond yield**



Source: Bloomberg

Graph 3.3: **Short-term auctions issuance**

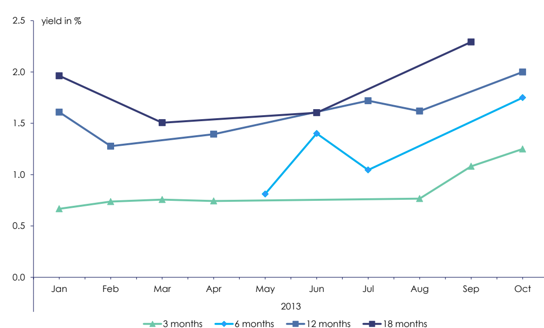


Source: IGCP

90. Portugal's market access depends heavily on the governments' commitment and ability to implement the programme. The very low liquidity in the market seen in September, particularly in the short end of the yield curve, showed that investors were waiting to see whether the government was willing and capable to pursue the programme or whether, on the contrary, declining social support and adjustment fatigue would force it to step down its ambition and slow the implementation of reforms. The government's

restated commitment to the fiscal deficit targets and planned reforms have already triggered positive reactions in the market and brought more risk-tolerant investors back to Portuguese bonds. However, rigorous implementation of the agreed measures and policies in the coming months will be crucial in restoring the prospects for regaining full market access. In addition, the risks from further negative rulings by the Constitutional Court cannot be discarded which could make the government's plans to fully access the debt market from mid-2014 on significantly more challenging.

Graph 3.4: **Short-term auctions weighted average yield**



Source: IGCP

91. Assuming full disbursement of programme financing, Portugal is fully funded for the remainder of the programme period, but restoration of market access is vital for the post-Programme period. The Treasury has accumulated a fairly large cash buffer, which stood at nearly EUR 15 billion by end-September (including deposits in the BSSF). Together with the remaining official loan disbursements and assuming broad roll-over of Treasury bills, the funding will – under current assumptions - be sufficient to cover the sovereign needs until at least the middle of next year. The use of the above-mentioned domestic market sources could extend the coverage period further. At the same time, considerable risks related to the public finances exist, stemming from budgetary slippages and potential losses of state owned enterprises. As Portuguese banks' and corporates' access to finance at sustainable yields is closely linked to that of the sovereign, the latter's efforts to regains market access are important for the entire economy. Furthermore, looking to the post-programme period restoring market access is essential in light of debt redemptions falling due in the second half of 2014.

92. The successful completion of the combined 8th and 9th reviews will pave the way for the disbursement of around EUR 5.6 billion, of which some EUR 3.7 billion will come from the EU and around EUR 1.9 billion from the IMF. With the disbursement of this tranche, more than 90% of the total financing envelope under the programme will have been disbursed.

ANNEX 1

Assessment of Compliance: Monitoring Table

Actions for the eighth and ninth review (to be completed by end Q1-2013 and Q2-2013)		*Status*
Fiscal Structural	**[3.6]** Publish a fiscal strategy document for the general government (April).	**Observed.**
	[3.8] Define the characteristics of the medium-term budgetary framework.	**Modified.** The operational characteristics of the medium-term budget framework and of the Budget Framework Law in general will be defined in an action plan. A draft will be prepared by the eleventh review and finalised by Q1-2014.
	[3.10] Adapt the local and regional budgetary frameworks.	**Observed.** The new regional and local finance laws were approved and will enter into force at the beginning of 2014.
	[3.11] Coordinate with MoF to exchange information along the lines defined in the draft financing laws.	**Observed.** Coordination mechanisms in the new regional and local finance laws will be applied to the extent possible for the preparation of the regional and local budgets for 2014.
	[**3.17**] Adopt the follow-up legislation to strengthen the governance of SOEs in accordance with international best practices.	**Observed.** Decree-law 133/2013, 3 October shall enter into force by 3 December.
	[3.18] Comprehensive review of wages scales in SOEs.	**Delayed.** A new deadline was set for Q4-2013
	[3.22 ii] Increase the personnel working in auditing of the tax administration by 30% of the total staff.	**Delayed.** The recruitment process is ongoing but with delays. It is expected to end by Q4-2013.
	[3.23] Prepare an evaluation report on the measures for the different economic sectors.	**Partially observed.** A report evaluating the tax incentive for final consumers to ask for invoices in hard-to-tax sectors was prepared. For the other reforms related to the e-invoicing VAT system an evaluation report will be prepared by Q4-2013.
	[3.25] Review the regulation on the creation and the functioning of associations and observatories.	**Modified.** The authorities will review public financial support to private associations by Q1-2014.
	[3.27 ii] Complete the implementation of the strategy of shared services in the area of human resources (GeRHup) in the Ministry	**Partially observed.** The roll-out of GeRHup to the Tax Authority will only be feasible by May 2014.

	of Finance.	
	[3.32] Review the Special Mobility Law.	**Observed.** The Special Mobility Law was revised into a Requalification Scheme. Following a Constitutional Court opinion, a new revision was submitted to the Parliament.
Financial sector	**[2.9]** Finalise the update of the treatment of collective impairments expected to be finalised at the latest by end-June 2013.	**Observed.** The review of the impairments in the credit portfolios of the eight largest national banking groups have confirmed the adequacy of the level of impairments booked in the balance sheet and the resilience of the banking system in what concerns its solvency.
	[2.12] Outsource the management of the credits currently held by Parvalorem to a professional third party […] through a competitive bidding process by [mid-2013], at the latest.	**Observed.** Loans in Parvalorem were split into four specific asset segments. Two successful bidders were awarded the contracts (on 14 August) to manage two segments each.
	[2.13] Analyse the recovery plans of the top 8 banks. Settle the initial contributions by banks by mid-June 2013.	**Observed.** Recovery plans analysis has been completed and gaps were identified. System guidelines are being finalized. The Resolution Fund is up and running since Q1 2013 and received from banks both the initial contribution (June) and yearly contribution (September). BdP dedicated a unit of six employees (full time equivalents) for resolution and plans to add further staff. The unit will formulate the resolution plans based on the reports provided by the banks.
	[2.16] Prepare report on the implementation of the new restructuring tools (end-June). Conduct a survey of insolvency stakeholders to inquire about the appropriateness of the existing restructuring tools and possible gaps or bottlenecks.	**Observed.** The authorities delivered in July the first quarterly monitoring report on the implementation of the new restructuring tools. A survey of insolvency stakeholders, including users, was conducted and its results presented in a report.
	[2.18 ii] Finalise the assessment of the grouped issuance of corporate debt to obtain capital market financing (end-April).	**Partially observed.** The preliminary detailed assessment on the grouped issuance of corporate debt has been submitted. The issuance was postponed to mid-2014.
	[2.18 iii] Prepare a first draft of the necessary amendments of the rules governing the commercial paper market (end-June) and review any	**Partially observed.** The first draft of the amendments to the rules governing the commercial paper market was submitted and discussed. The draft text already underwent a set of restricted consultations. The review of tax

	potential tax implications.	implications is pending.
	[2.19] Present a report on quarterly monitoring and reporting mechanism on the allocation of the government sponsored credit lines. Conduct an external audit of the National Guarantee System with a report of the main findings and policy recommendation to be submitted by (end-April).	**Observed.** The authorities delivered in July the first quarterly monitoring report on the allocation of government-sponsored credit lines. The external audit of the National Guarantee System has been duly conducted and policy recommendation presented in a roadmap with a set of milestones to be accomplished.
Health care system	**[3.37]** Implement contingency measures including administrative price reductions.	**Ongoing.** The authorities have reached an agreement with the pharmaceutical industry for spending in 2013. Therefore this measure does not need to be implemented.
	[3.41] Introduce in the e-prescription system a first set of guidelines.	**Observed and ongoing.** The authorities have introduced the information on guidelines into the system. Authorities are monitoring/auditing the compliance to guidelines. Such auditing will assess the need for fine-tuning the system.
	[3.42] Produce a report assessing the legislation aimed at removing all effective entry barriers for generic medicines.	**Observed.** The report was submitted and showed that following the introduction of new legislation only one new case has been taken to Court, many court cases were dropped or taken to arbitration and many new medicines entered the market. The authorities are working on fine-tuning the system notably to understand how to further reduce costs of arbitration.
	[3.50] Make the web-portal with publicly available information fully operational.	**Observed.** The web portal is now available at http://benchmarking.acss.min-saude.pt/
	[3.52] Define the service portfolio for NHS hospitals and the detailed strategic 3-year plans for hospitals.	**Partially observed and ongoing.** The authorities presented plans from some regions and the remaining work is ongoing
	[3.53] Prepare annual reports on plans to reallocate qualified and support staff within the NHS.	**Observed and ongoing.** A report was submitted but will need to be updated in view of the hospital reform and consequent adjustments of services and staff.
	[3.55] Finalise the implementation of the new internal control procedures manual.	**Delayed.** The process is ongoing but with delays. It is expected to be completed by end 2013.
Labour market and	**[4.2]** Enter into force the revision of the Labour Code defining the new	**Observed.** It entered into force the 1 October 2013.

education	severance pay regime.	
	[4.5] Present a report on wage adjustments linked to productivity at firm level and how these measure are applied in collective agreements. If needed, prepare an action plan to ensure works council can negotiate wages at firm level.	**Observed.** The report has been presented. It shows that no use has yet been made of the provisions to facilitate the conclusion of collective agreements at firm level. More specifically 1) sectoral collective agreements have not been made use of the provision of specifying the condition under which the agreement can be changed at firm level and 2) there are no cases where work council have been delegated to conclude a collective agreement. The authorities need therefore to continue to monitor the use of those provisions and, together with social partners, consider other possibilities to enhance the conclusion of collective agreements at firm level.
	[4.6] Present a report on expenditure and financing of ALMPs, the role of job counselling and propose actions to improve the effectiveness of employment and training measures.	**Observed.** The report has been presented**.**
	[4.7 i] Make operational an analysis, monitoring, assessment and reporting system.	**Observed.** The tool has been substantially enriched and is already operational as an instrument for policy decisions.
	[4.7 ii, ii] Define and implement funding framework for public schools and schools under autonomy agreements.	**Partially observed.** There is a funding framework for public schools but it is not clear whether performance criteria are important enough.
	[**4.7 ii, iii**] Report on the results and the follow up of the first year of the new evaluation cycle.	**Observed.** A good report on the features and results of the new inspection model has been presented.
	[4.7 iii] Establish "professional schools of reference".	**Ongoing.** The Government has provided updated information; the professional schools of reference will not be set up until the next school year.
	[4.7 iv] Prepare an assessment on the latest developments in the apprenticeship system.	**Observed.** The assessment has been presented.
Goods and services markets	**[5.1]** Ensure the National Regulatory Authority's all powers foreseen in the package.	**Observed.**

	[5.2] Implement the plan to create a new gas and electricity logistics operator independent company.	**Partially observed.** The New Platform will become fully operational only in October 2014.
	[5.3] Conclude the measures aiming at reducing excessive rents and to address the sustainability of the national electricity system.	**Observed.** The revised medium-term tariff debt projections provided in the update report showed additional upward pressure. Several additional measures were then proposed and might be implemented. Recent developments point to the need of further measures. Negotiations concerning the Sines and Pego power plants have come to a standstill.
	[5.4] Following the report on the CMEC scheme and the process for the extension of the concession of the public hydro resource by the former CAE hydro power plants, analyse and discuss the consequences of the report and the need for potential measures.	**Ongoing.**
	[5.5] Conclude the measure to limit the policy costs of renewables under the special regime.	**Observed.** Legislation setting the terms for the compensation for wind producers was approved and implemented.
	[5.6] Conclude the measures to revise the remuneration scheme for co-generation and report on the progress of the annual audits for co-generation plants.	**Partially observed.** Further legislative action to improve efficiency of the support system is foreseen. Annual audits of co-generation plants are on-going.
	[5.8] Proceed with the designation of universal service providers.	**Partially observed.** The tenders were held, though the historical contract has not been cancelled yet and the new contracts have not become operational.
	[5.10] Amend the decree-law laying down the framework of the contract and renegotiating the amendment of the said contract with CTT.	**Partially observed.** The legal documents containing the amendments have not been published yet and the renegotiation of the contract with the CCT has not been completed.
	[5.12] Assess the existing rail, road and port networks and present a set of investment priorities for the 2020 and 2030 horizons.	**Delayed.** A Working Group was created and the Government is now expected to present it by the end of the year.
	[5.13 iii] Ensure that the new railway Public Service Obligation (PSO) contracts concluded on rail passenger transport respect EU	**Delayed.** The Government has presented a timeline by which PSOs are expected to be signed by the end of the year.

	legislation including Regulation (EC) N° 1370/2007 and provide a detailed breakdown of state contributions for each line under PSO.	
	[5.13 vi] Ensure that the main rail terminals currently owned by CP Carga are transferred to another entity.	**Delayed.** Plans to ensure the transfer to REFER are already ongoing.
	[5.15] Deliver and enforce policies that ensure strong integrated policy-making, strategic planning and surveillance functions common to all ports.	**Delayed.** The Government is now expected to present proposals at the next review.
	[5.16] Submit and approve by the Parliament the amendments to the sector specific legislation.	**Partially observed.** Internal work within the government on the preparation of the remaining reforms has been progressing and most of them were shared and are being discussed with EC/ECB/IMF. At this stage 59 out of 68 legal regimes have been completed under the Services Directive. The final drafts of the laws on construction and reserve of activity have further delays.
	[5.17] Launch a 2nd phase of investigation of the review of regulated professions to eliminate unjustified requirements.	**Observed.** The Government has completed this 2nd phase and delivered a report with the conclusions.
	[5.18] Submit to Parliament the professional bodies' amended statutes.	**Delayed.** Negotiations with the professional associations have been lengthy. The submission to parliament of revised bylaws for the professional associations of these professions is expected to have further delays.
	[5.19 i] Adapt the content and information available at the PSC for the missing 33 amended regimes to ensure conformity with the Services Directive and make available online forms for the completion of procedures.	**Partially observed.** Lack of sufficient administrative capacity was mentioned as a reason for delays However progress has been made. 41 regimes were published online on the PSC and 5 online procedures are under construction.
	[5.19 ii] Adapt the content and information available at the PSC for the 15 regimes to ensure conformity with the Professional Qualifications Directive.	**Partially observed.** All the regimes were analysed and 4 online procedures are under construction.

	[5.19 iii] Make available in PSC on-line procedures for the registration, installation, modification, occupation of public space regimes.	**Observed.**
	[5.19 iii] Make the PSC operational.	**Observed.**
	[5.19 iii] Prepare the extension of the PSC to major municipalities.	**Observed.**
	[5.19 iii] Make fully operational the "Zero Authorisation" project.	**Broadly observed.**
	[5.19 iii] Make the "Zero Authorisation" platform available to all levels of administration, including municipalities.	**Observed.**
Housing market	**[6.1]** Finalise the appraisal of the taxable value of the housing stock.	**Observed.**
	[6.3] Review of the impact of all housing market reforms.	**Partially observed.** A special Monitoring Committee has been set up and a first report has been prepared and published on housing market but a more comprehensive review of the reform has not been made yet because of the delays in the full implementation of the new legal framework. This review is now awaited by the first quarter of 2014.
Judicial system	[**7.1**] Eliminate the court backlog.	**Observed:** All enforcement cases pending on 17 May 2011 have been analysed. Efforts were made to diminish the number of backlogged cases with the result of closing 45% of the cases pending on 17 May of 2011.
	[7.2] Prepare quarterly reports on implementation status of measures to achieve reduction of the backlogged enforcement cases.	**Observed.** Seventh Report was sent in August 2013.
	[7.3] Submit to Parliament a draft bill to strengthen the authority and financing structure of the CACAJ.	**Observed.** The bill was submitted on 28 June 2013.
	[7.3] Approve by the government fee structure that incentivises speedy enforcement.	**Observed.** The fee structure was approved on 28 June 2013.
	[7.4] Publish quarterly reports on recovery rates, duration and costs of corporate insolvency cases starting	**Observed.** Report on the first quarter of 2013 sent in August 2013 and made available at the website of the Directorate-General of Justice

	from **[Q3-2011]**, within four months after the end of the end of relevant quarter.	Policy on the 31st of July.
Competition, public procurement and business environment	**[7.7]** Submit to Parliament the framework law for regulators.	**Observed.** The framework law was published on 28 August 2013. The various by-laws are now under preparation.
	[7.8] Submit a report analysing the impact of the amendments to the revised Public Procurement Code as well as of the enhanced role of the Court of Auditors.	**Partially observed.** The report on the impact of the Public procurement Code was presented but not on the enhanced role of the Court of Auditors.
	[7.10] Implement the New Late Payments Directive.	**Partially observed.** The Decree Law aimed at transposing the Directive was published on 10 May 2013; however, the Commission has already expressed its doubts regarding full compliance and has already got in contact with the national authorities to require clarification and further information.
	[7.11] Include all municipalities and all levels of public administration within the scope of the Simplex Programme.	**Ongoing.** The Government has presented information regarding the state of play.
Licensing	**[7.12]** Carry-out a fully inventory and an analysis of the costs of all regulations in the economy (at central, regional and local levels).	**Ongoing.** The government has presented some first ideas at the review.
	[7.13] Study the feasibility of a rule that prohibits at all levels of government the creation of a new regulation generating costs for businesses without elimination of an existing regulation.	**Partially observed.** The Government is working on draft legislation that may include such a rule.
	[7.14] Create a working group to analyse applications for the licensing of planned investment projects.	**Observed.** A Decree Law has been already adopted by the Government and submitted for publication in the Official Gazette.
	[7.15 i, iii, iv, v, vi] Review the legal regimes at all levels of Government in the area of territorial planning.	**Partially observed.** The Government submitted to Parliament the proposal of the New Base Law of Soil and Territorial and Urbanism Planning early October. The complementary legislation such as RJUE and RJIGT has not been adopted

		yet.
	[7.17] Change the legal regime for Environmental Impact Evaluation.	**Observed.** The new legal regime was adopted by the Council of Ministers.
	[7.18 i] Implement zero licensing procedures for Type 2 and 3 industries.	**Partially observed.** The Government has adopted the ordinance setting the information required for the prior authorisation of industries of Type 1, 2 and 3.
	[7.18 ii] Define and establish the Zones of Responsible Enterprises.	**Observed.** The Government has adopted an Ordinance setting the legal framework, powers and requirements of the Zones of Responsible Enterprises.
	[7.18 iii] Create and define standardized industrial licenses.	**Ongoing.**
	[7.18 iv] Ensure that the new Industrial Licensing is aligned with the review of the New Base Law of Soil and Territorial and Urbanism Planning.	**Ongoing.**
	[7.18 v] Ensure that the new Industrial Licensing is aligned with the review of the Legal Regime for Urbanism and Building.	**Ongoing.**
	[7.19] Review the commercial licensing regime.	**Delayed.** The Government is expected to adopt the legal changes by the end of the year.
	[7.20] Review the geological licensing regimes.	**Delayed.** The legal proposals are now expected by the next review.
	[7.21] Review the licensing in tourism.	**Delayed.** The legal proposals are now expected by the next review.

ANNEX 2
Commission Services Macroeconomic Projections 2012-2017

Table 1: Use and supply of goods and services (volume)

Annual % change	2012	2013	2014	2015	2016	2017
1. Private consumption expenditure	-5.4	-2.5	0.1	0.7	0.9	1.0
2. Government consumption expenditure	-4.8	-4.0	-2.8	-2.2	-0.9	-0.9
3. Gross fixed capital formation	-14.3	-8.5	1.2	3.7	4.1	4.3
4. Final domestic demand	**-6.8**	**-3.7**	**-0.3**	**0.6**	**1.1**	**1.2**
5. Change in inventories	--	--	--	--	--	--
6. Domestic demand	**-6.7**	**-3.7**	**-0.3**	**0.7**	**1.1**	**1.2**
7. Exports of goods and services	3.2	5.8	5.0	5.3	5.5	5.5
7a. - of which goods	4.1	5.6	4.9	5.5	5.5	5.5
7b. - of which services	0.7	6.6	5.3	4.9	5.5	5.5
8. Final demand	**-4.2**	**-1.1**	**1.3**	**2.1**	**2.5**	**2.6**
9. Imports of goods and services	-6.6	0.8	2.5	3.7	4.4	4.6
9a. - of which goods	-6.4	1.2	2.7	3.8	4.5	4.7
9b. - of which services	-7.8	-1.5	1.5	3.5	4.3	4.0
10. Gross domestic product at market prices	**-3.2**	**-1.8**	**0.8**	**1.5**	**1.7**	**1.8**
Contribution to change in GDP						
11. Final domestic demand	-7.1	-3.7	-0.3	0.6	1.0	1.1
12. Change in inventories + net acq. of valuables	0.1	0.0	0.0	0.0	0.0	0.0
13. External balance of goods and services	3.8	2.0	1.0	0.8	0.6	0.6

Table 2: Use and supply of goods and services (value)

Annual % change	2012	2013	2014	2015	2016	2017
1. Private consumption expenditure	-4.0	-2.0	1.1	2.0	2.4	2.5
2. Government consumption expenditure	-11.6	2.9	-3.9	-4.4	-0.1	-0.1
3. Gross fixed capital formation	-13.9	-10.6	2.4	6.6	6.9	7.2
4. Final domestic demand	**-7.2**	**-2.5**	**0.3**	**1.5**	**2.7**	**2.8**
5. Change in inventories	--	--	--	--	--	--
6. Domestic demand	**-7.0**	**-2.4**	**0.3**	**1.5**	**2.7**	**2.8**
7. Exports of goods and services	4.6	5.2	5.9	6.4	6.6	6.6
8. Final demand	**-4.0**	**-0.3**	**2.0**	**3.0**	**3.9**	**4.1**
9. Imports of goods and services	-5.3	-1.4	2.6	4.4	5.2	5.4
10. Gross national income at market prices	-2.3	-1.1	0.3	1.8	3.1	3.2
11. Gross value added at basic prices	-3.4	0.7	1.6	2.3	3.3	3.4
12. Gross domestic product at market prices	**-3.5**	**0.1**	**1.7**	**2.5**	**3.4**	**3.5**

Table 3: Implicit price deflators

% change in implicit price deflator	2012	2013	2014	2015	2016	2017
1. Private consumption expenditure	1.5	0.6	1.0	1.2	1.5	1.5
2. Government consumption expenditure	-7.2	7.2	-1.1	-2.2	0.8	0.8
3. Gross fixed capital formation	0.4	-2.3	1.2	2.7	2.7	2.8
4. Domestic demand	**-0.4**	**1.3**	**0.6**	**0.8**	**1.6**	**1.6**
5. Exports of goods and services	1.4	-0.6	0.8	1.0	1.0	1.0
6. Final demand	**0.1**	**0.8**	**0.7**	**0.9**	**1.4**	**1.4**
7. Imports of goods and services	1.4	-2.2	0.1	0.6	0.8	0.8
8. Gross domestic product at market prices	**-0.3**	**1.9**	**0.9**	**1.0**	**1.7**	**1.7**
HICP	**2.8**	**0.6**	**1.0**	**1.2**	**1.5**	**1.5**

Table 4: Labour market and cost

Annual % change	2012	2013	2014	2015	2016	2017
1. Labour productivity (real GDP per employee)	1.0	2.2	1.3	1.0	1.1	1.2
2. Compensation of employees per head	-2.0	2.5	-0.8	-0.2	0.4	0.5
3. Unit labour costs	**-3.0**	**0.3**	**-2.1**	**-1.2**	**-0.7**	**-0.7**
4. Total population	-0.4	-0.7	-0.1	-0.1	0.0	0.0
5. Population of working age (15-64 years)	-1.0	-0.3	-0.1	0.0	0.0	0.0
6. Total employment (fulltime equivalent)	-4.2	-3.9	-0.5	0.4	0.6	0.6
7. Calculated unemployment rate - Eurostat definition (%)	**15.9**	**17.4**	**17.7**	**17.3**	**16.8**	**16.2**

Table 5: External balance

levels, EUR bn	2012	2013	2014	2015	2016	2017
1. Exports of goods (fob)	47.7	50.0	52.9	56.4	60.1	64.1
2. Imports of goods (fob)	55.4	54.8	56.3	58.8	61.9	65.3
3. Trade balance (goods, fob/fob) (1-2)	**-7.7**	**-4.7**	**-3.4**	**-2.4**	**-1.8**	**-1.2**
3a. p.m. (3) as % of GDP	***-4.7***	***-2.9***	***-2.0***	***-1.4***	***-1.0***	***-0.6***
4. Exports of services	16.2	17.2	18.3	19.3	20.6	22.0
5. Imports of services	9.5	9.2	9.3	9.7	10.2	10.7
6. Services balance (4-5)	**6.7**	**8.0**	**8.9**	**9.6**	**10.4**	**11.3**
6a. p.m. 6 as % of GDP	***4.0***	***4.8***	***5.3***	***5.6***	***5.8***	***6.1***
7. External balance of goods & services (3+6)	**-1.0**	**3.3**	**5.6**	**7.2**	**8.6**	**10.1**
7a. p.m. 7 as % of GDP	***-0.6***	***2.0***	***3.3***	***4.2***	***4.8***	***5.5***
8. Balance of primary incomes and current transfers	-2.2	-1.7	-4.0	-5.5	-6.3	-7.1
8a. - of which, balance of primary income	*-4.0*	*-6.0*	*-8.3*	*-9.7*	*-10.5*	*-11.3*
8b. - of which, net current Transfers	*1.8*	*4.3*	*4.3*	*4.2*	*4.2*	*4.2*
8c. p.m. 8 as % of GDP	*-1.3*	*-1.0*	*-2.4*	*-3.2*	*-3.5*	*-3.8*
9. Current external balance (7+8)	**-3.2**	**1.5**	**1.5**	**1.7**	**2.3**	**3.0**
9a. p.m. 9 as % of GDP	***-1.9***	***0.9***	***0.9***	***1.0***	***1.3***	***1.6***
10. Net capital transactions	3.5	4.4	4.6	4.3	4.6	4.7
11. Net lending (+)/ net borrowing (-) (9+10)	**0.3**	**5.9**	**6.1**	**6.1**	**6.9**	**7.7**
11a. p.m. 11 as % of GDP	***0.2***	***3.6***	***3.6***	***3.5***	***3.9***	***4.2***

Table 6: Fiscal accounts

	2012	2013	2014	2015	2016	2017
% of GDP						
Indirect taxes	13.7	13.3	13.4	13.5	13.5	13.4
Direct taxes	9.3	11.2	11.1	11.1	11.0	11.0
Social contributions	11.6	12.0	11.6	11.3	11.1	10.9
Actual	9.1	9.4	9.2	9.1	9.0	8.9
Imputed	2.5	2.6	2.4	2.2	2.1	2.0
Sales and other current revenue	4.9	5.6	5.5	5.7	5.6	5.7
Sales	2.8	2.9	2.7	2.7	2.7	2.7
Other current revenue	2.1	2.7	2.8	2.9	2.9	2.9
Total current revenue	**39.4**	**42.0**	**41.7**	**41.6**	**41.3**	**41.0**
Capital transfers received	1.5	1.2	1.1	1.1	1.1	1.1
Total revenue	**40.9**	**43.2**	**42.8**	**42.7**	**42.5**	**42.1**
Compensation of employees	10.0	10.6	9.4	8.8	8.5	8.2
Intermediate consumption	4.5	4.7	4.6	4.4	4.3	4.2
Social transfers in kind via market producers	4.5	4.5	4.3	4.1	4.0	3.9
Social transfers other than in kind	18.0	18.7	18.5	18.1	17.9	17.6
Interest paid	4.3	4.3	4.4	4.4	4.4	4.4
Subsidies	0.6	0.7	0.8	0.7	0.7	0.7
Other current expenditure	2.6	2.7	2.8	2.6	2.5	2.5
Total current expenditure	**44.5**	**46.4**	**44.7**	**43.1**	**42.4**	**41.6**
Gross fixed capital formation	1.7	1.9	1.8	1.7	1.7	1.7
Other capital expenditure	1.3	0.9	0.3	0.4	0.4	0.4
Total expenditure	**47.4**	**49.1**	**46.8**	**45.3**	**44.5**	**43.7**
General Government balance (ESA95)	**-6.4**	**-5.9**	**-4.0**	**-2.5**	**-2.0**	**-1.6**
General Government balance (Programme)	**-6.0**	**-5.5**	**-4.0**	**-2.5**	**-2.0**	**-1.6**
% change						
Indirect taxes	-4.1	-2.5	2.7	3.5	3.4	2.5
Direct taxes	-9.5	20.9	1.0	2.3	3.2	3.2
Social contributions	-9.1	3.6	-1.1	-0.6	1.3	1.6
Sales and other current revenue	4.2	13.9	0.3	5.3	2.7	4.1
Total current revenue	**-6.0**	**6.8**	**0.8**	**2.3**	**2.7**	**2.7**
Capital transfers received	-68.0	-22.4	-4.6	5.8	4.8	5.3
Total revenue	**-12.3**	**5.7**	**0.7**	**2.4**	**2.6**	**3.0**
Compensation of employees	-15.0	6.3	-6.6	-4.0	-0.7	0.0
Intermediate consumption	-6.4	6.1	-1.2	1.0	2.2	1.0
Social transfers in kind via market producers	-5.9	-0.9	-1.8	-3.5	0.5	0.5
Social transfers other than in kind	-0.5	4.5	0.2	0.6	1.9	1.9
Interest paid	4.1	0.5	1.8	3.2	4.6	3.8
Subsidies	-17.4	20.0	4.8	1.8	2.5	1.0
Other current expenditure	-4.8	4.9	7.3	-2.6	2.5	3.2
Total current expenditure	**-5.4**	**3.8**	**-1.5**	**-1.4**	**1.6**	**1.9**
Gross fixed capital formation	-38.6	12.5	-2.8	-3.6	3.5	3.5
Other capital expenditure	-11.0	-27.5	-65.1	45.3	2.5	3.1
Total expenditure	**-7.3**	**3.2**	**-2.9**	**-1.2**	**1.6**	**2.0**
Nominal GDP, EUR bn	165.1	165.3	168.2	172.3	178.2	184.5

Table 7: Government debt developments

	2012	2013	2014	2015	2016	2017
ESA95 deficit (% of GDP)	**-6.4**	**-5.9**	**-4.0**	**-2.5**	**-2.0**	**-1.6**
ESA95 gross debt (% of GDP)	124.1	127.8	126.7	125.7	123.5	120.0
	levels, EUR bn					
ESA95 deficit	**-10.7**	**-9.8**	**-6.8**	**-4.4**	**-3.6**	**-3.0**
Gross debt	204.8	211.4	213.0	216.6	219.9	221.5
Change in gross debt	19.6	6.5	1.6	3.7	3.3	1.6
Nominal GDP	165.1	165.3	168.2	172.3	178.2	184.5
Real GDP	170.4	173.4	172.1	169.5	166.7	163.6
Real GDP growth (% change)	**-3.2**	**-1.8**	**0.8**	**1.5**	**1.7**	**1.8**
Change in gross debt (% of GDP)	11.9	3.9	1.0	2.1	1.9	0.9
Stock-flow adjustments (% of GDP)	5.4	-2.0	-3.1	-0.4	-0.2	-0.8
	% of GDP					
Gross debt ratio	**124.1**	**127.8**	**126.7**	**125.7**	**123.5**	**120.0**
Change in gross debt ratio	15.8	3.8	-1.2	-1.0	-2.3	-3.4
	Contribution to change in gross debt					
Primary balance	2.1	1.6	-0.3	-1.8	-2.4	-2.8
"Snow-ball" effect	8.2	4.1	2.2	1.3	0.3	0.2
of which						
Interest expenditure	*4.3*	*4.3*	*4.4*	*4.4*	*4.4*	*4.4*
Real growth effect	*3.5*	*2.2*	*-1.0*	*-1.9*	*-2.1*	*-2.2*
Inflation effect	*0.4*	*-2.5*	*-1.2*	*-1.3*	*-2.1*	*-2.0*
Stock-flow adjustments	**5.4**	**-2.0**	**-3.1**	**-0.4**	**-0.2**	**-0.8**
Implicit interest rate	*3.9*	*3.5*	*3.5*	*3.5*	*3.6*	*3.7*

ANNEX 3
Indicative Financing Needs and Sources

Table 8: Financing needs and sources (EUR billion)

	2011 Jun-Dec	2012 Year	2013 Year	2014 Year	2011-2014 Total
Public sector deficit	**11.3**	**13.3**	**13.9**	**11.5**	**50.0**
Treasury balance [1]	7.1	8.9	8.9	6.7	31.7
Other public sector cash needs [2]	4.2	4.4	5.0	4.7	18.3
Amortization [3]	**9.5**	**27.8**	**11.0**	**13.9**	**62.2**
Medium- and long-term debt (incl debt exchange)	4.9	16.6	6.2	13.9	41.6
Other debt (retail, repos, incl SOE), net	4.6	11.2	4.8	0.0	20.6
Banking support [4]	**1.0**	**7.5**	**1.6**	**0.5**	**10.6**
Financing needs	**21.8**	**48.6**	**26.5**	**25.9**	**122.8**
Market financing	**-6.4**	**8.9**	**7.9**	**12.4**	**22.8**
Medium- and long-term debt	0.0	3.6	5.5	12.5	21.5
T-Bills, net	-6.4	5.3	2.4	0.0	1.3
Own resources [5]	**-5.7**	**12.3**	**8.6**	**5.4**	**20.6**
EU-IMF loan	**34.0**	**27.4**	**10.0**	**8.0**	**79.4**
EFSM/EFSF	21.0	19.2	6.6	5.2	52.0
IMF [6]	13.0	8.2	3.4	2.8	27.4
Financing sources	**21.8**	**48.6**	**26.5**	**25.9**	**122.8**

SOURCE: Portuguese authorities and Commission services' estimates.

1/ Calendar-year cash basis.

2/ Includes financing to state-owned enterprises, contributions to the ESM and the economic adjustment programme for Madeira, and repayment of arrears.

3/ Central government, excl. T-Bills.

4/ From 2012 includes actual banking sector needs; for 2011 - payments to BSSF.

5/ Includes privatisation receipts, use of deposits, pension fund assets and centralisation of cash management of general government entities.

6/ Numbers do not add up to EUR 26 bn due to changes in EUR-SDR rate compared to beginning of programme; SDR rate of 30/05/2013 applied for 2013-2014 disbursements, no revisions for 2011-2012 data.

Table 9: Planned quarterly disbursements (EUR billion)

Review	Period covered by disbursement	Approximate disbursement period	Loan disbursements[1]	of which IMF[2] (1/3)	of which EU (2/3)
Approval	Jun-Sept 2011	Jun-11	18.9	6.5	12.4
1	Q4-2011	Sep-11	11.6	4.0	7.6
2	Q1-2012	Dec-11	8.0	2.8	5.2
3	Q2-2012	Apr-12	14.8	5.1	9.7
4	Q3-2012	Jul-12	4.0	1.4	2.6
5	Q4-2012	Oct-12	4.3	1.5	2.8
6	Q1-2013	Jan-13	1.6	0.8	0.8
7	Q2-2013	Apr-13	2.8	0.7	2.1
8 & 9	Q3/Q4-2013	Nov-13	5.6	1.9	3.7
10	Q1-2014	Jan-14	2.7	0.9	1.8
11	Q2-2014	Apr-14	2.5	0.9	1.6
12	Q3-2014	Jun-14	2.6	0.9	1.7
	TOTAL		79.4	27.4	52.0

1/ Data is subject to revision due to EUR - SDR fluctuations.
2/ IMF disbursements are defined in SDR. Actual disbursement in EUR is subject to changes in the EUR-SDR exchange rate

ANNEX 4
Provision of Data (Reporting Requirements)

During the programme, the following indicators and reports shall be shared with the European Commission, the ECB and the IMF by the authorities on the agreed periodic basis. Data for past periods should also be included in subsequent transmissions in case of revision. Other indicators may also be requested to and reported by the Portuguese Authorities.

To be provided by the Ministry of Finance (or INE)	
Data on cash balances of the State Budget. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published by the Ministry of Finance (MoF). Data on tax revenue should be decomposed in gross tax revenue received and tax reimbursements paid by the State (detailed per main individual taxes)	Monthly, 3 weeks after the end of the month
Data on the cash balances of the other parts of General Government (Autonomous Funds and Services, Social Security and Other entities, including Incorporated State-owned enterprises (ISOEs) or extra-budgetary funds (EBF) not part of the State Budget, but which are, under the European System of Accounts (ESA95) and ESA95 Manual on Government Deficit and Debt rules, classified by the National Statistical Institute (INE) as part of the Central Government; [Regional and Local Governments (*Administrações Regionais and Locais*); Regional and local government-owned enterprises or companies, foundations, cooperatives, and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government, as defined in paragraph 4 of the TMoU) – progressively enlarged	Monthly, as soon as the data are available and no later than 7 weeks after the end of the month
Accrual data on budget execution of the National Health System (NHS)	Monthly, 3 weeks after the end of each month
Consolidated cash data on the General Government budget execution initially comprising the Central Government and Social Security and enlarging progressively the scope as in indicated in the TMoU, MoU and MEFP	Monthly, 7 weeks after the end of each month
Publish information on: number of general government staff on a quarterly basis (no later than 45 days after the end of the quarter); stock and flows over the relevant period per Ministry or employment entity (i.e. new hiring, retirement flows, special mobility condition flows, and exit to other government service, private sector or unemployment); average wage, allowances and bonuses. The regional and local administration will transmit the necessary information. Information on employment in SOEs (central, local and regional) and other public entities and/or bodies will also be compiled	Quarterly, no later than 45 days after the end of the quarter
Consolidated account on an accrual basis of the non-financial SOEs that are classified within the Central Government	Quarterly, 90 days after the end of the quarter (as of March 2012)
Data on the past and projected financing needs of SOEs, including for the major SOEs details on the financing needs for the operational	Monthly, 4 weeks after the end

balance, capital expenditure, interest payments and debt principal repayments	of the month
Data on arrears of: - the General Government, detailed by subsector - the incorporated (SOEs) government-owned hospitals that are not part of the General Government - other non-financial SOEs that are not part of the General Government	Monthly, 7 weeks after the end of each month (as of September 2011)
Information on Public-Private Partnerships (PPP) related revenue and expenditure, for those PPP reclassified within the General Government (in line with paragraph 5.2 of the TMoU)	Monthly, 30 days after the end of the each month
New guarantees granted by the State to SOEs, PPPs, banks and the non-financial private sector	Monthly, 30 days after the end of each month
Detailed information on called guarantees of the State	Monthly, 30 days after the end of each month
Data on proceeds from asset sales by the Central, Regional and Local Government	Monthly for Central Government Quarterly for Regional and Local Government 30 days after the end of reference period
Quarterly data on General Government accounts as per the relevant EU regulations on statistics, showing also the main items of the transition from cash balances to the General Government balances in national accounts	Quarterly, 90 days after the end of each quarter
To be provided by ESAME	
Report on progress with fulfilment of economic policy conditionality on a quarterly basis. In addition, a short summary report should be sent on a monthly basis	Quarterly (report), two weeks after the end of each quarter. Monthly (short summary report) two weeks after the end of each month for which a report is not due.
To be provided by the Debt Management Office	
Accrual data on interest spending of the State	Quarterly, 7 weeks after the end of the quarter

To be provided by the Ministry of Labour	
Data on labour market as follows: - layoffs by type - collective agreements by type and number of collective agreements that are extended by the Ministry of Labour to non-signatory firms - number of collective agreements that regulate the use of the Bank of Hours working time arrangement - proportion of unemployed receiving unemployment benefits - distribution of the unemployed in terms of amount of benefits received (mean of benefits received, median, number of unemployed receiving an unemployment benefit amount equal to the IAS and number of unemployed receiving the maximum amount of unemployment benefits allowed) - unemployment duration	Every six months, 6 weeks after the end of each semester
To be provided by Ministry of Justice	
Publishing quarterly reports on recovery rates, duration and costs of corporate insolvency cases	Quarterly, starting in the first quarter of 2011, within four months after the end of each quarter.

ANNEX 5
PROGRAMME DOCUMENTS

ANNEX 5
LETTER OF INTENT

Lisbon, 21 November 2013

Mr Jeroen Dijsselbloem
President
Eurogroup

Mr Rimantas Šadžius
Minister of Finance
Lithuania

Mr Olli Rehn
Vice President
European Commission

Mr Mario Draghi
President
European Central Bank

Dear Sirs,

The attached Memorandum of Understanding (MoU) describes the progress made in recent months towards the objectives laid out in our Programme. It also updates previous MoUs and highlights the policy steps to be taken in the months ahead.

We have made further progress toward the program objectives. Some delays generated by the political situation and government reshuffling over the summer, as well as new adverse rulings by the Constitutional Court on spending measures and labour reforms have been dealt with. The end-June deficit and performance criteria were met. All six structural benchmarks initially planned for the June-October period were met.

The macroeconomic outlook has recently improved. Growth and employment in the second quarter turned out to be better than expected, with sequential real GDP growth turning positive and unemployment falling, signaling that output may have bottomed out. Nonetheless, headwinds from private sector deleveraging and fiscal consolidation will remain significant. Though most structural reforms envisaged in the program are now in place, and are beginning to have an impact, we remain strongly committed to further reforms aimed at bolstering price and cost competitiveness and setting the basis for a strong and durable recovery. In this regard, significant steps are underway to further improve the dynamism and efficiency of the labor and product market, reduce costs for exporters, and further improve our business environment.

We are committed to achieving our fiscal objectives. This year's deficit target (5½ percent of GDP) is within reach, as we have tightened budget execution and taken exceptional measures to offset budget overruns earlier in the year and non-tax revenue shortfalls, some of them due to exceptional factors. As a prior action for completion of this review, we have submitted to Parliament a 2014 budget that aims at a general government deficit of 4 percent of GDP, as well as some of the necessary supporting legislation. The draft budget is, to a large extent, underpinned by the public sector reforms identified in the context of the public expenditure review, ensuring a consolidation strongly tilted towards permanent measures to reduce expenditure. Fiscal consolidation will continue in 2015, with a targeted deficit of 2½ percent of GDP.

We are committed to preserving financial sector stability and supporting a balanced and orderly balance sheet deleveraging in the economy. While the capital and liquidity conditions of the banking system remain adequate, Banco de Portugal (BdP) continues to vigilantly supervise the banking system in view of the challenging operating environment. Moreover, to facilitate the ongoing balance sheet adjustment, we are renewing our efforts to promote adequate funding conditions for the most productive and innovative segments of the economy, while ensuring prompt restructuring of viable firms in financial difficulties.

On the basis of the strength of the policies defined in this letter, and in light of our performance under the Programme, we request the completion of the combined eighth and ninth review under the Economic Adjustment Programme and the release of the ninth instalment under the Programme in the amount of EUR 3 700 million.

We remain confident that the policies described in the current and previous MoUs are adequate to achieve the objectives under the Programme. We stand ready to take additional measures should they be needed to meet the objectives of the Economic Adjustment Programme and will consult with the European Commission, the European Central Bank and the International Monetary Fund in advance of any necessary revisions to the policies contained in this letter and attached Memorandum.

This letter is copied to Ms Christine Lagarde.

Sincerely yours,

/s/	/s/	/s/
Paulo Portas	Maria Luís Albuquerque	Carlos da Silva Costa
Deputy Prime Minister	Minister of State and Finance	Governor of the Banco de Portugal

Attachments: Memorandum of Understanding (MoU); Memorandum of Economic and Financial Policies (MEFP); Technical Memorandum of Understanding (TMU)

ANNEX 5

MEMORANDUM OF UNDERSTANDING ON SPECIFIC ECONOMIC POLICY CONDITIONALITY

Eighth Update – 21 October 2013

With regard to Council Regulation (EU) n° 407/2010 of 11 May 2010 establishing a European Financial Stabilisation Mechanism (EFSM), and in particular Article 3(5) thereof, the eighth update of the Memorandum of Understanding on specific economic policy conditionality (MoU) details the general economic policy conditions as embedded in Council Implementing Decision 2011/344/EU of 17 May 2011 on granting Union financial assistance to Portugal. ([5])

The first disbursement of financial assistance from the EFSM took place following the entry into force of the MoU and of the Loan Agreement.

The Council Implementing Decision specifies that the release of further instalments is conditional on a positive conclusion of the reviews of conditionality that will take place throughout the three-year duration of the programme. These reviews will assess progress made with respect to the policy criteria in the Council Implementing Decision and specified in the Memorandum of Economic and Financial Policies (MEFP) and in this updated MoU, as well as Council Recommendations in the context of the Excessive Deficit Procedure.

The combined eighth and ninth quarterly review assessed compliance with the conditions to be met by end-September and the need and scope for additional policy steps. This eighth update of the MoU reflects the findings of the combined eighth and ninth review. The following reviews taking place in any given quarter will assess compliance with the conditions to be met by the end of the previous quarter or, where applicable, up to date of the mission.

If targets are missed or expected to be missed, additional action will be taken. The authorities commit to consulting with the European Commission (EC), the European Central Bank (ECB) and the International Monetary Fund (IMF) on the adoption of policies falling within the scope of this updated Memorandum, allowing sufficient time for review. Staff of the EC, the ECB and the IMF will, in cooperation with the Portuguese authorities, monitor and assess progress in the implementation of the programme and track the economic and financial situation. Staff will also monitor whether the implementation and effects of measures taken by the Portuguese authorities fall short of the commitments of previous versions of the MoU; such commitments might be re-inserted. To this effect the authorities commit to providing all required information as soon as available. In areas where there are risks of significant delays in the implementation of policies under this programme the authorities in cooperation with the EC, the ECB and the IMF consider making use of technical assistance.

Prior to the release of the instalments, the authorities shall provide a compliance report on the fulfilment of the conditionality.

([5]) On 8 April 2011, Eurogroup and ECOFIN Ministers issued a statement clarifying that financial support of the EU (European Financial Stabilisation Mechanism, EFSM) and the euro-area (European Financial Stability Facility, EFSF) would be provided on the basis of a policy programme supported by strict conditionality and negotiated with the Portuguese authorities, duly involving the main political parties, by the Commission in liaison with the ECB, and the IMF. Further to the EU support from the EFSM, loans from the EFSF will contribute to the financial assistance. The Loan Facility Agreement on the EFSF financing contribution specifies that the disbursements thereunder are subject to the compliance with the conditions of this Memorandum.

1. Fiscal policy

Objectives

Reduce the government deficit to 5.5 per cent of GDP in 2013, 4 per cent of GDP in 2014 and 2.5 per cent of GDP in 2015 by means of high-quality permanent measures, while minimising the impact of consolidation on vulnerable groups. In the medium term, the fiscal consolidation process will be maintained until a balanced budgetary position is reached, notably by containing expenditure. Growth-friendly tax policy will be pursued through, among other actions, a comprehensive reform of corporate taxation to promote investment and competitiveness.

Fiscal policy in 2013

1.1. The government will achieve a general government deficit target of no more than 5.5 per cent of GDP on an ESA95 basis ([6]) [Q4-2013].

1.2. Throughout the year, progress in achieving the year-end fiscal target will be assessed against the (cumulative) quarterly ceilings for the consolidated general government cash balance in the Memorandum of Economic and Financial Policies (MEFP), as defined in the Technical Memorandum of Understanding (TMU), without prejudice to full-year ESA-95 deficit targets [Q3 and Q4-2013].

1.3. Throughout the second half of the year, the government will rigorously implement the 2013 Budget Law as amended by the Supplementary Budget.

1.4. Budget execution has been supported by solid performance of state tax revenues and tight execution of some expenditure items. Nonetheless, by end-September some deviations have been identified with respect to the Supplementary Budget. These include a capital injection into BANIF (0.4 percent of GDP), which shall not be considered for the programme purposes. The remaining deviations have stemmed from shortfalls related to the reprogramming of EU funds and the delay in the sale of a port concession (one-offs) and other factors such as the underperformance of non-tax revenues, lower than expected contributions to the public pension scheme and overruns in the wage bill. After the use of the provisional budget allocations (0.3 percent of GDP), the net effect of the deviations is estimated to increase the 2013 deficit by 0.5 percent of GDP. To deliver the 5.5 percent of GDP deficit target, the government has taken corrective measures, notably the reduction of available funds for investment and tighter control on the intermediate consumption of line ministries. In addition, the government is implementing a one-off tax-and-social-security-contributions' debt recovery scheme, while committing not to have recourse to such schemes in the future and to further combating tax evasion and fraud.

Fiscal policy in 2014

1.5. The government will achieve a general government deficit of no more than 4 per cent of GDP in 2014 [Q4-2014].

1.6. Within the year, progress will be assessed against the (cumulative) quarterly ceilings for the consolidated general government cash balance in the Memorandum of Economic and Financial Policies (MEFP), as defined in the Technical Memorandum of Understanding (TMU), without prejudice to full-year ESA-95 deficit targets [Q1 and Q2-2014].

1.7. The Budget Law for 2014 will be consistent with a general government deficit ceiling of 4 percent of GDP. The measures defined below, worth 2.3 percent of GDP, will be implemented with the

([6]) In 2013 operations related to the banking sector support and restructuring strategy under the programme will not be considered for the assessment of compliance with the programme target for the general government deficit.

2014 Budget Law [Q4-2013] ([7]). Measures are primarily of permanent nature and expenditure reduction will account for about 80 percent of the consolidation.

Public Expenditure Review

1.8. The 2014 Budget will build on the public expenditure review carried out over the last year with the objective of enhancing the efficiency and equity of public spending. In particular, it aims at addressing inefficiencies within public sector functions and entities, reallocating resources towards growth-friendly spending areas and ensuring social equity of the expenditure programmes and the sustainability of public finances.

1.9. The package of permanent consolidation measures from the public expenditure review will amount to EUR 3.1 billion or 1.8 percent of GDP (net of income tax and social contribution reduced collections). One-off costs from the mutual agreement termination scheme will limit the savings to 1.7 percent of GDP in 2014. The package draws on the following three pillars:

i. Limiting outlays on the public wage bill by (i) reducing the size of the public sector workforce —addressing excessive employment in particular sub-sectors— while tilting its composition towards high-skilled and better-trained civil servants; (ii) ensuring convergence of the public sector work rules and regulations towards private sector standards, including regarding working hours, working time arrangements and holiday entitlements; and (iii) simplifying the remuneration policy by implementing a single wage scale and streamlining the wage supplements' scale. The reduction in the workforce will be achieved through a combination of policies, including lower replacement of retirees, mutual agreement termination schemes and enhanced use of the requalification programme. The savings for the wage bill from these measures should achieve around EUR 1.2 billion in gross terms (EUR 720 million taking into account the losses of government revenues from income taxes and social contributions). Also, as part of these horizontal measures, the increase in beneficiaries' contributions to the special health insurance schemes (ADSE, SAD and ADM) will raise revenues by at least EUR 130 million.

ii. A comprehensive pension reform based on equity principles and income progressivity, with a view to protecting those who earn the lowest pensions. Specifically, the reform will take into consideration the need to reduce the current differences between the civil servants’ regime and the general social security regime, aiming at enhancing the fairness of the overall pension system and the need to reassess its sustainability on the back of demographic developments. Accordingly, the reform will be based on three main elements: (i) effective increase by one-year in the retirement age to 66 years (implemented by adjusting the demographic sustainability factor); (ii) alignment of the rules for calculation of benefits of the public sector pension scheme, CGA, to the general pension regime, while protecting pension benefits below a minimum threshold which rises with the age of the beneficiary and avoiding double penalization of beneficiaries with a monthly pension below EUR 5030 and subject to the "extraordinary solidarity contribution" ([8]), and (iii) streamlining survivors' pensions of both CGA and the general pension regime, in particular in cases where these accumulate with other pensions. These pension reforms will achieve additional savings of around EUR 700 million in gross terms (around EUR 600 million net savings).

iii. Other savings will be generated through a combination of sector-specific reforms, which have been identified by line ministries in the bottom-up budgeting process. This will mainly include targeted personnel reductions (notably, through non-renewal of fixed-term contracts), further savings in intermediate consumption and investment and reduction of transfers. In the education sector, the rationalisation of the school network and a convergence of the teacher/student ratio towards levels of other EU countries will support these goals. Hospital reform and cost optimisation will contribute to

([7]) Prior action in the MEFP.
([8]) Structural benchmark in the MEFP.

savings in the health sector. The gross savings from the sector-specific reforms should attain around EUR 1850 million (EUR 1650 million in net terms).

1.10. The legislative processes necessary to underpin the public expenditure review reforms are advancing or shall advance according to the following timelines. The ordinance on mutual agreement terminations for less qualified workers is already in force and similar sectorial programs, notably for teachers, will be launched by [end-November 2013]. The law aligning the working hours of the public sector to the 40 hours in force in the private sector has been adopted but is currently under consideration by the Constitutional Court. The new draft law on the requalification programme (redesigned mobility pool) awaits Parliamentary approval, as well as the draft legislative changes for the convergence of the public pension regime to the general system. The draft Public Administration General Labour Law will be submitted to Parliament by [end-October 2013] ([9]). The single wage scale reform and the reduction of wage supplements will be made effective by [1 January 2014] and implemented through a budget provision ([10]). A report on a more comprehensive reform of single wage supplements is expected by [Q4-2013]. The draft amendments necessary for the increase in retirement age will be submitted to Parliament by [October 2013] ([11]).

Other fiscal measures

1.11. To compensate for the negative carryover from the 2013 budget execution and to achieve the 4 percent of GDP deficit target, the government will also implement the following permanent revenue consolidation measures, worth about 0.4 percent of GDP:

- Tax and social contribution measures (EUR 500 million): increase in the rate on autonomous taxation of company cars within the framework of the corporate income tax; base broadening and increased rates of excises on tobacco and increased rates on alcoholic drinks; surcharge on car tax on diesel passenger vehicles; elimination of fiscal exemptions in property taxation for pension funds and real estate funds; increased levy on financial institutions (banking system); tax and licensing fees for online gambling; increase of social security contributions by members of statutory bodies, by eliminating the cap on the calculation base.

- Other revenues: a special levy on the energy sector (yielding government revenue of EUR 100 million and channelling any excess in collection from that amount to reduce the electricity tariff debt); and a fee on media spectrum utilisation (EUR 10 million).

1.12. In addition, a number of one-off deficit-reducing measures (worth about 0.2 percent of GDP) will contribute to achieving the headline deficit target, more than offsetting the one-off costs related to the mutual agreement terminations of public sector employment contracts. These include the transfer of the CTT health fund to the government sector (EUR 180 million), the sale of a port and a silos company concession (EUR 170 million) and special dividends from the sale of excessive oil reserves (EUR 60 million).

1.13. A progressive "extraordinary solidarity contribution" on pensions, introduced in 2013, will continue to be applied. In 2014, the measure will be adapted to take into account the cumulative impact of other measures on pensions.

1.14. The State Budget will also put forward a comprehensive reform of the corporate income tax aimed at promoting simplification as well as boosting internationalisation and competitiveness of Portuguese companies. The main features of the reform include the redefinition of the tax base, the

([9]) Structural benchmark in the MEFP.
([10]) Prior action in the MEFP.
([11]) Prior action in the MEFP.

lowering of the statutory rate and the revamping of tax benefits. It also envisages a special taxation regime for small businesses, the simplification of ancillary tax obligations, the strengthening of the territoriality principle, extension of the tax losses deduction period and further reduction of the debt bias. It will be implemented within the existing budgetary envelope to respect the fiscal consolidation targets.

1.15. The standstill rule for tax expenditures at central, regional or local level will be maintained.

1.16. Efforts to fight tax evasion, fraud and informality for various types of taxes will be further strengthened, inter alia by increasing means available for audits and monitoring the new VAT e-invoicing system.

2. Financial sector stability, regulation and supervision and financing of the economy

Preserve financial sector stability; maintain liquidity and support a balanced and orderly deleveraging in the banking sector; ensure adequate financing and working capital for the productive sectors; strengthen banking regulation and supervision; develop and implement solutions that provide financing alternatives to traditional bank credit for the corporate sector; optimise the process for recovering the assets transferred from BPN to the three state-owned SPVs; streamline state-owned Caixa Geral de Depósitos; complete the bank resolution framework; complete the corporate and household insolvency frameworks and smoothen their implementation.

Maintaining liquidity in the banking sector

2.1. Encourage banks to strengthen their collateral buffers on a sustainable basis. The Banco de Portugal (BdP), in close cooperation with the ECB, will continue to monitor closely the liquidity situation of the banking system and stands ready to take the appropriate measures to maintain sufficient system liquidity [ongoing]. In parallel, the BdP will continue to explore new initiatives supporting the system's liquidity including through mechanisms allowing banks to securitise their high quality mortgages and SME credit.

Deleveraging in the banking sector

2.2. Banks' funding and capital plans and broader credit developments will continue to be monitored closely. The banking system should in the medium run eliminate its funding imbalances and reinforce its long-term viability. The BdP monitors the banks' implementation of the funding and capital plans aimed at achieving a stable market-based funding position. It is important to ensure that the pace and composition of the deleveraging, as also envisaged under the restructuring plans of state aided banks, does not jeopardise the provision of appropriate credit to finance productive investment and working capital in the private sectors of the economy, not least SMEs in the sectors of tradable goods and services.

Capital buffers

2.3. Ensure that current capital requirements by the BdP are respected including through the monitoring of the restructuring plans of banks having received public capital support [ongoing]. Monitor the banks' transition to the new capital rules as laid down in the Capital Requirements Directive IV package (CRD IV) ensuring that the banking system is ready to meet a Common Equity Tier 1 (CET1) capital ratio of 7% from 1 January 2014 as defined by the BdP. The implementation of the above framework will also need to be in accordance with the requirements currently envisaged in the EBA Recommendation on the preservation of capital for the banks that are subject to them. BdP ensures that the framework will also comply with any future regulatory initiatives at European level.

2.4. The BdP closely monitors the banks' compliance with the capital requirements and EBA recommendations with a view to promptly taking appropriate action if needed [ongoing].

2.5. Remain committed to providing further support to the banking system, if needed. In the event new capital needs were to arise encourage banks to seek private solutions while resources from the Bank Solvency Support Facility (BSSF) are available in line with the recently amended EU-state aid rules to further support viable banks, subject to strict conditionality. Avoid subsidising private shareholders and prevent further migration of private liabilities to the public sector balance sheet [ongoing].

Caixa Geral de Depósitos (CGD)

2.6. Continue to streamline the state-owned CGD group [ongoing].

Banking regulation and supervision

2.7. The BdP will continue to strengthen its supervisory organisation, optimise its supervisory processes and develop and implement new supervisory methodologies and tools [ongoing].

2.8. In addition, the BdP steps up the monitoring of banks, including via ad hoc audits [ongoing]. In this context, the BdP is conducting a special assessment programme of banks' operational capacity to effectively deal with loan restructuring and asset recovery. This exercise includes a survey of the Portuguese regulatory framework targeting the gaps and bottlenecks that hamper the adjustment of the private sector's balance sheet [November 2013]. As a follow-up to the BdP's instruction on identifying and reporting of restructured loans, BdP will require banks to disclose this information in their annual reports, starting in December 2013.

2.9. The BdP continues to monitor on a quarterly basis the banks' potential capital needs with a forward looking approach under stress conditions. Banks reflect the On-site Inspections (OIP) findings in the implementation of the SIP recommendations on asset quality and stress testing methodologies [ongoing]. Moreover, the BdP introduces a new top-down stress test to support its review of the bottom-up results. These enhancements will be included in the next round of quarterly stress tests, to be finalized in [November 2013].

2.10. The BdP remains committed to close coordination with home and host country supervisors, both within and outside the EU [ongoing].

Banco Português de Negócios

2.11. Gradually settle CGD's state guaranteed claim on the SPVs in cash, according to the schedule agreed with the EC, ECB and IMF staff. Any net recoveries on the assets held by the three state-owned SPVs will also be used to promptly repay CGD [ongoing].

2.12. Outsource the management of the credits currently held by Parvalorem to the firms selected through the bidding process with a mandate to gradually recover the assets over time. Ensure timely disposal of the subsidiaries and the assets in the other two state-owned SPVs.

Bank resolution framework

2.13. The early intervention, resolution and deposit guarantee framework has been strengthened. The BdP reviewed and issued recommendations on the recovery plans of the largest banks in the system and expects the remaining banks' submission by [end-November]. In parallel BdP prepares resolution plans based on the reports provided by banks.

2.14. Finalise the legislative process introducing the necessary amendments to the recapitalization law to reflect the recent Communication from the European Commission on the application of the state-aid rules to support measures in favour of banks in the context of the financial crisis. The legislator will closely follow the process of adoption of the EU Directive on bank resolution and recovery and will revise the national resolution framework as soon as the Directive is adopted [ongoing].

Central Credit Registry

2.15. The BdP enhances the data coverage of the Central Credit Registry (CCR) to include additional financial products and to add supplementary classifications to the loans already reported to the CCR. Continue efforts to permit access by the financial institutions to historical information on their potential new clients, subject to the authorisation of the Portuguese Data Protection Authority (CNPD). In parallel, the BdP assesses options for the disclosure of selected information by firms, on a voluntary basis, contained in other databases such as the Central Balance Sheet Database (CBSD) with a view to reducing information asymmetry between smaller companies and credit providers. These enhancements, as well as a first progress report on the two last referred issues, are expected to be completed by [Q4-2013].

Corporate and household debt restructuring framework

2.16. Implement the recently established framework for financial institutions to engage in out-of-court debt restructuring for households, smoothen the application of the framework for restructuring of corporate debt and implement an action plan to raise public awareness of the restructuring tools [ongoing]. Prepare quarterly reports on the implementation of the new restructuring tools [ongoing]. Align the reporting content of SIREVE with that already in place for PER [ongoing].On the basis of the recently conducted a survey of insolvency stakeholders explore alternatives to increase the successful recovery of companies adhering to the PER and the SIREVE [ongoing].

Monitoring of corporate and household indebtedness

2.17. Continue the monitoring of the high indebtedness of the corporate and household sectors through quarterly reports [ongoing].

Encouraging the diversification of financing alternatives to the corporate sector

2.18. The Ministry of Finance, the BdP, and other stakeholders, have put forward a set of measures to encourage the diversification of financing alternatives to the corporate sector.

i. focus the scope and prioritise the measures to be implemented [ongoing].

ii. Implement the pilot grouped issuance of corporate debt to obtain capital market

financing and/or explore similar initiatives to facilitate financing to SMEs including through the innovative risk sharing instruments currently under discussion at EU level [ongoing]

iii. prepare a draft of the necessary amendments of the rules governing the commercial paper market by [end-November] and review any potential tax implications in order to facilitate its expansion among a wider investor and issuer base and to increase the use of this alternative funding option by the corporate sector.

iv. Building on the agreement on a State guarantee for existing and future exposures of the EIB to the Portuguese economy, the authorities will strive to facilitate the financing of the corporate sector, in particular the economically viable SMEs operating in the tradable sectors [ongoing].

2.19. Assess scope for improving the performance and governance of existing government-sponsored credit lines by ensuring in the selection process the targeting of productive and viable companies with temporary financing difficulties, in line with EU state aid rules. In that context, revise the recently submitted roadmap containing the main steps aiming at improving the governance of the National Guarantee System (NGS) and making these schemes more efficient while minimizing risks for the State, including by (i) reviewing of the schemes' objectives and investment selection processes (ii) implementing measures to further enhance loan and guarantee pricing in favour of end users, including through the development of competitive bidding mechanisms for the allocation of guaranteed credit to the banks, with preliminary scenarios for competitive bidding schemes to be presented and discussed by [early November 2013]; (iii) upgrading of the NGS risk management capabilities; (iv) reviewing its governance structure; (v) improving the supervision, monitoring, management and public disclosure of the State exposure to the NGS operations. Further to the revision of the roadmap, implement the measures contained therein by [January 2014]. Regularly report on progress.

Prepare quarterly reports on the allocation of the government sponsored credit lines aimed at facilitating access to finance to SMEs, including by monitoring the balance sheet performance of the firms benefiting from these credit lines.

3. Fiscal-structural measures

Objectives

Improve the efficiency of the public administration by eliminating redundancies, simplifying procedures and reorganising services; regulate the creation and functioning of all public entities including SOEs, PPPs, foundations, associations; re-focus their activities to core public policy objectives and enhance their cost efficiency and fiscal sustainability; streamline the budgetary process, including by adopting new financing laws at regional and local level; strengthen risk management, accountability, reporting and monitoring of all parts of the general government. Government action will build on the recommendations provided by the EU/IMF technical assistance missions.

Public Financial Management framework

Reporting and Monitoring

3.1. Publish a comprehensive report on fiscal risks [each year as part of the budget]. The report will outline general fiscal risks and specific contingent liabilities to which the general government may be exposed, including those arising from Public-Private Partnerships (PPPs), SOEs and explicit guarantees to the banks. Technical assistance will be provided if necessary.

3.2. Publish a tax expenditure report [each year as part of the budget]. The report will define a clear methodology to estimate and to evaluate tax expenditures, in line with international best practices. The report will cover central, regional and local administrations.

3.3. Reduce the number of budget entities in view of reducing budget fragmentation and improving efficiency in the general government. In particular, this reform will be deepened by reviewing the classification of own revenues to enlarge central government revenues by the [tenth review].

Arrears

3.4. The stock of domestic arrears will be significantly reduced by the end of the programme period. A significant part of the existing arrears was reduced as laid down in the strategy for the settlement of

arrears. The Inspeção Geral de Finanças (IGF) will carry out inspections throughout the process to verify compliance of the commitment control system through a risk-based approach [ongoing].

3.5. IGF will reinforce the verification of local governments' arrears claims and commitment control systems. Disbursements under the Programa de Apoio à Economia Local (PAEL) will only take place where IGF has certified the full functioning of the commitment control system. Transparency of the use of the credit line will be ensured through the monthly publication of the amounts lent, disbursed, and used to settle arrears and other liabilities by municipality in the framework of the PAEL [ongoing].

Budgetary framework

3.6. Publish a fiscal strategy document for the general government [annually in April]. The document will be in compliance with the requirements of the Stability and Growth Pact and will specify 4-year medium-term economic and fiscal forecasts and 4-year costs of new policy decisions. Budgets will include a reconciliation of revisions to the 4 year fiscal forecasts attributable to policy decisions and parameter revisions e.g. policy decisions, changes in the macroeconomic environment.

3.7. Conduct a review of the Budget Framework law (BFL) to enhance budgetary procedures and principles of budgetary management, reinforce accountability, transparency and simplification, as well as fully transposing relevant EU legislation. The technical group for the review of the BFL will publish a report assessing the strengths and weaknesses of the law providing suggestions for amendments including a new structure for the law [Q4-2013]. The draft law will be submitted to Parliament by [Q1-2014].

3.8. In parallel to the review of the Budget Framework Law, the authorities will identify the operational changes necessary to ensure full implementation of the law with clear deadlines and responsibilities and defining in detail the characteristics of the medium-term budgetary framework, decision-making and prioritisation process, carry-over rules, commitment controls, and appropriate contingency reserves and related access rules. A draft action plan will by prepared for the [eleventh review] and finalised by [Q1-2014].

3.9. The government will ensure that the measures to implement the new budgetary framework at central government level will also be applied at regional and local level. Adequate structures of monitoring, fiscal reporting, and commitment control will be put into place [ongoing].

3.10. The Government's financial arrangement with the Autonomous Region of Madeira (RAM), which is in full compliance with the Memorandum of Understanding, will be implemented. The Portuguese Government will monitor progress of implementation by RAM and present the results on a quarterly basis in advance of the reviews of the Memorandum of Understanding [ongoing].

Public Private Partnerships

3.11. PPP road contracts shall continue to be renegotiated in line with the strategic plan presented by the government and with the regulatory framework revision concerning notably service levels, in order to obtain substantial fiscal gains, particularly in 2013, while ensuring a sustainable reduction in government liabilities [ongoing].

3.12. The government will continue to work towards implementing the PPP framework law, ensure the proper functioning of the new technical unit in the Ministry of Finance (UTAP) and develop the tools for managing and monitoring all PPPs. No PPP will be launched until the institutional framework measures are fully effective. UTAP will provide technical support to the regional government of Madeira in the renegotiation of road PPPs. Regions will be encouraged to design a similar framework for assessing fiscal risks derived from PPP, and other relevant public investments, as well as for monitoring their execution [ongoing].

3.13. The annual PPP report will provide a comprehensive assessment of the fiscal risks stemming from PPPs and concessions. The report will provide information and analysis at sectorial level and an analysis of credit flows channeled to PPPs through banks (loans and securities other than shares) by sector and an impact assessment on credit allocation and crowding out effects. This particular element will be done in liaison with the Banco de Portugal to the extent of data available to this entity. The report will serve as input to the fiscal risks assessment for the budget [Q3-2013].

State-owned enterprises

3.14. SOEs with commercial activity will reach operational balance from [end of 2012 onwards]. This will be achieved by substantially reducing operational costs and raising revenues. To this end the government is implementing the comprehensive SOEs strategy by reviewing the revenue structure and service provision of SOEs, with numerical targets on cost reductions, including measures to realign wages, reduce employment, and additional measures as appropriate. The government is further assessing options for managing the heavy debt load of SOEs, including Parpública [ongoing].

3.15. Following the comprehensive review of wage scales in the general government, an equivalent study of SOEs will follow in [Q4-2013].

3.16. Equivalent measures on operational results, debt, restructuring and governance will be taken at the local and regional levels, while respecting their administrative autonomy as foreseen in the law. The annual and quarterly SOEs reports will assess progress towards achieving these objectives for central and local SOEs. Each Autonomous Region will provide similar annual reports. These will serve as inputs to the fiscal risks analysis in the budget [ongoing].

3.17. Continue to implement the strategy to restructure Águas de Portugal (AdP) water and waste water services with a view to introducing private capital and management in concessions [ongoing].

Privatisation

3.18. The government continues to implement the privatisation programme under the new framework law for privatisation. The programme target of privatisation proceeds of about EUR 5 billion was already achieved. The sale of GALP and the small remaining stake in REN will be completed when the market conditions improve. The privatisation or concession of the freight subsidiary of CP (CP Carga) will be carried out as soon as further steps have been taken to increase its market value while restoring its operational balance. The tender for the privatisation of the national air carrier (TAP) will be carried out as soon as market conditions improve. The privatisation of Correios de Portugal (CTT) is ongoing with binding offers expected by [Q4-2013]. The final amendments of the postal legislation and concession, which are pre-conditions for the transaction, have been approved by the Council of Ministers. The sale or concession of a television channel and radio station belonging to RTP will be subject to the company's ongoing restructuring process and the improvement of market conditions. The sale of the waste management company (EGF) will be launched once changes underway in regulation of this sector are implemented, envisaging binding offers by [Q1-2014]. The government will further consider expanding the privatisation programme to include additional assets for sale or concession in 2013.

Revenue administration

3.19. The recent reforms of the Autoridade Tributária e Aduaneira (AT) will be deepened in 2013 and 2014 by targeting a business function-type structure. In particular, the following elements will be implemented:

i. reduce the number of municipal offices by at least 25 per cent in 2013 [Q4-2013] and 25 per cent in 2014 [Q2-2014];

ii. increase in the resources devoted to auditing in the tax administration to at least 30 per cent of the total staff, mostly through reallocations of staff within the tax administration and other parts of the public administration. The threshold should be attained by [Q4-2013];

iii. publish quarterly reports on duration and costs of tax cases starting from [Q4-2013] within four months after the end of the relevant quarter.

3.20. The reform of the VAT e-invoicing system that aims at curbing fraud and evasion has been put fully in place in 2013. An evaluation report of the measures for the different economic sectors will be prepared by [Q4-2013].

3.21. The authorities will continue to focus on measures to combat fraud and evasion and strengthen taxpayers' compliance. To this end the authorities will continue:

i. analysing the current tax compliance situation, including a risk analysis of different categories of taxpayers, notably focusing on income taxation. The analysis will leverage among others on information from the recently implemented unified monthly tax return and the unified form on Independent Workers' annual revenue [ongoing]. An assessment report will be prepared by [Q4-2013].

ii. building capacity in revenue administration by phasing in a more modern approach to managing compliance over a three-years period. In the short term this will focus on the reinforcement of key reforms such as the recently established compliance projects for high-wealth individuals and self-employed professionals and the establishment of a risk analysis unit [ongoing].

Public administration

Central, regional and local administration

3.22. On the basis of Law 64/2013 regulating the obligation of transparency on benefits granted by the public administration to the private sector and defining monitoring and reporting mechanisms, the authorities will review public financial support to private associations [Q1-2014].

3.23. The Inter-ministerial Group on Territorial Affairs will present a report with the following objectives:

i. Identify potential overlaps of services and jurisdictions and other sources of inefficiencies between the central and local levels of government, as well as new opportunities for decentralisation and outsourcing of services by the central government by the [eleventh review]

ii. Reorganise the network of decentralised services of ministries, aiming at increasing efficiency in the public sector and the quality of services for citizens and businesses. These shall be reorganised mainly through mergers of "lojas do cidadão" and other approaches, encompassing more efficient geographical areas and intensifying the use of digital government by the [eleventh review].

Shared services

3.24. Develop the use of shared services in the central administration by fully implementing the ongoing projects and by regularly assessing the scope for further integration:

i. complete the implementation of the strategy of shared services in the area of financial resources (GeRFIP) in central and regional administrations [Q4-2013];

ii. complete the implementation of the strategy of shared services in the area of human resources (GeRHuP) in the Ministry of Finance's entities by concluding the roll-out to the Tax Authority by [May 2014];

iii. continue the implementation of the "Overall Strategic plan to rationalise and reduce costs on ICT in Public Administration" [ongoing].

Human resources

3.25. Limit staff admissions in public administration to achieve annual decreases in 2012-2014 of at least 2 per cent per year (in full-time equivalents) in the staff of central administration and 2 per cent in local and regional administrations (in full-time equivalents); including a significant reduction of fixed-term contracts and the application of mutual agreement schemes on contract termination. The government will ensure the implementation of this measure at local administration level and will promote the initiatives needed so that each region will present its plan to achieve the same target [ongoing].

3.26. Following the comprehensive review of wage scales in the public administration and the survey on cash supplements, a revision of the remuneration policies aiming at their rationalisation and consistency among all public entities will be implemented. To this effect, the rules adjusting the single wage scale in the public administration and the monthly compensation paid will be included in the 2014 Budget Law [mid-October 2013] to be effective by [1 January 2014]. A report on a more comprehensive reform of wage supplements is expected by [Q4-2013].

3.27. Converge the system of social protection for staff in the Regime de Proteção Social Convergente (RPSC) to the pension rules of Regime Geral de Segurança Social [Q4-2013].

3.28. The Special Mobility scheme will be reviewed aiming at being more oriented to support Public Administration Reform, addressing training and requalification for a better allocation of Human Resources. The proposal of the Requalification Law will be revised: (i) to ease/simplify the procedures for the management of the employees that can be targeted with this tool; (ii) to address the compensation that will be paid during the requalification period and thereafter; and (iii) to be applied to all sectors of Public Administration, including teachers and health professionals [Q3-2013].

3.29. Present to Parliament a new public administration law to simplify and compile the existing rules of public sector employment along the structure of the private labour code by [end-October 2013] to be effective by [1 January 2014].

Health care system

Objectives

Improve efficiency and effectiveness in the health care system, inducing a more rational use of services and control of expenditures; generate additional savings in the area of pharmaceuticals to reduce the overall public spending on pharmaceutical to 1.25 per cent of GDP by end 2012 and to about 1 per cent of GDP in 2013; generate additional savings in hospital operating costs and devise a strategy to eliminate arrears.

The government will take the following measures to reform the health system:

Financing

3.30. The improvements in the billing and collection of revenues from NHS moderating fees (taxas moderadoras), insurance companies and fees for the treatment of cross-border/foreign patients, will result in additional revenues of €50 million [Q4-2013].

3.31. In the light of the urgency and size of the savings needed in the health sector to address large arrears and budget limitations, plans to achieve a self-sustainable model for health-benefits schemes for civil servants will be accelerated. The current plan foresees that the overall budgetary cost of existing schemes - ADSE, ADM (Armed Forces) and SAD (Police Services) - will be reduced by 50 per cent of the employers' contribution in 2013 through transfer of resources to the NHS in exchange for the provision of services. The employer's contribution rate will be reduced to 1.25% in 2014 and will be accompanied by an adjustment in the scope of health benefits [Q3-2013]. The system would become self-financed by 2016.

Pricing and reimbursement of pharmaceuticals

3.32. The government will monitor monthly pharmaceutical expenditures and ensure that the overall public pharmaceutical expenditure does not exceed the target of 1.25 per cent of GDP in 2012 and 1 per cent of GDP in 2013 [ongoing].

3.33. If public expenditure diverges from the objective that has been set for 2013, the government will implement contingency measures including administrative price reductions (in addition to the regular annual price revision), such as enacting legislation which automatically reduces 50% in prices of off-patent medicines which have had a market authorisation for 15 years and are currently not subject to generics competition in the Portuguese market [ongoing].

Prescription, monitoring of prescription and guidelines

3.34. Continue to improve the monitoring and assessment system of doctors' prescription behaviour regarding medicines and diagnostic in terms of volume and value and vis-à-vis prescription guidelines and peers. Feedback continues to be provided to each physician on a regular basis (e.g. quarterly), in particular on prescription of costliest and most used medicines [ongoing].

3.35. Continue to devise and enforce a system of sanctions and penalties, as a complement to the assessment framework [ongoing]. Assess the possibility of establishing agreements with private sector physicians for the application of prescription rules as applied in the NHS.

3.36. Strictly monitor the implementation of the legislation making it compulsory for physicians at all levels of the system, both public and private, to prescribe by International Non-proprietary Name (INN) to increase the use of generic medicines and the less costly available products. E-prescription systems should ensure INN prescription as default. A follow up report will be published by [December 2013].

3.37. Continue to publish clinical and prescription guidelines with reference to medical care, medicines and the realisation of complementary diagnostic exams on the basis of international prescription guidelines. Continue auditing their implementation and integrate them in the electronic prescription system [ongoing].

3.38. The above measures should aim at gradually and substantially increasing the share (in volume) of generic medicines reaching 45% of all NHS reimbursed medicines in the outpatient setting by end of 2013. This share will increase to 60% by the end of 2014.

Centralised purchasing and procurement and competition

3.39. INFARMED will continue implementing the uniform coding system and a common registry for medical devices, including 3 new families of medical devices per quarter [ongoing].

3.40. Continue to implement the centralised purchasing of medical supplies and services through the Central Purchasing Authority (SPMS), using the uniform coding system for medical supplies and pharmaceuticals. Continue to implement the compulsory use of a formulary in all hospitals to monitor the stock and flows of hospital medicines and medical supplies and monitor compliance with central purchasing. INFARMED will develop the national formulary (hospitals and outpatient) including 4 new therapeutic areas per quarter, starting in the second quarter 2013 to be finished by the [twelfth review].

3.41. Continue to monitor NHS spending with private providers delivering diagnostic tests and therapeutic services (with particular reference to dialysis, rehabilitation, respiratory care). Take further measures to increase competition among private providers and between private and public providers in these areas of service provision with a view to ensuring competition and fair prices in private markets. These measures should aim at reducing the overall spending of the NHS with private providers. Take measures to ensure competition in the pharmacies sector [Q4-2013].

Primary care services

3.42. As part of the reorganisation of health services provision and notably the concentration and specialisation of hospital services and the further development of a cost-effective primary care service, the Government reinforces measures aimed at further reducing unnecessary visits to specialists and emergencies and improving care coordination [ongoing]. This will be done through:

i. review the incentives system linked to performance assessment and continue to increase the number of USF units (Unidades de Saúde Familiares). Extend performance assessment to the other primary care units (UCSPs). Make sure that the new system leads to a reduction in costs and more effective provision;

ii. setting-up a mechanism to guarantee the presence of family doctors in needed areas to induce a more even distribution of family doctors across the country;

iii. moving human resources from hospital settings to primary care settings and reconsidering the role of nurses and other specialties in the provision of services;

iv. updating patients' registration lists and the national register in order to increase by at least 20 per cent the maximum number of patients per primary care/family doctor for health centres and by 10 per cent for the USF.

Hospital services

3.43. Continue to clear arrears in the health sector, within the overall strategy for settling arrears. Ensure standardised and tight control procedures for all health sector entities to ensure expenditure commitments stay within the budget allocated to each entity and therefore prevent the re-emergence of arrears [ongoing].

3.44. On the basis of the comprehensive set of indicators continue to produce regular quarterly reports comparing hospital performance (benchmarking) and the monthly hospital reporting sheet (tableaux de bord), using the results to establish targets for less performing hospitals [ongoing]. Make the web-portal with publicly available information fully operational [Q3-2013].

3.45. Hospital SOEs will change the existing accounting framework and adopt accounting standards and appropriate IT systems in line with the requirements for private companies and other SOEs. This will help improve the management of the enterprises and the quality of the financial oversight by the general government. The implementation of a common financial platform to all SOEs will be developed until the end of 2013. Reporting in the new accounting standard will be available at the end of 2013 through existing accounting systems. SOEs will test and progressively implement a central accounting platform: 10 in [Q1-2014]; 20 by the [twelfth review]; and the remaining SOEs will adopt a new central platform for the ACSS to gather real time information on hospital accounting.

3.46. Continue with the reorganisation and rationalisation of the hospital network through specialisation, concentration and downsizing of hospital services, joint management (building on the Decree-Law 30/2011) and joint operation of hospitals. The aim is to adjust hospital provision within the same health region, notably in the presence of newly established PPP hospitals, adjust the activity of some hospitals from curative care towards areas such as rehabilitation, long-term and palliative care and revise emergency and transplantation structures. These improvements aim at eliminating unnecessary duplication, achieving economies of scale and deliver additional cuts in operating costs by at least 5 per cent in 2013 while improving the quality of care provided. Overall, from 2011 to 2013, hospital operational costs must be reduced by at least 15 per cent compared to 2010 level. The reorganisation and rationalisation of the hospital network includes the following steps: the definition of the service portfolio for NHS hospitals and the definition of the detailed strategic 3-year plans for hospitals [Q3-2013]. The "Contratos Programa" for SOE hospitals for 2014 should be negotiated and signed until the end of [Q1-2014].

3.47. Annually update the inventory of all health staff and prepare regular annual reports presenting plans for the allocation of human resources in the period up to 2014. The report specifies plans to reallocate qualified and support staff within the NHS [Q4-2013].

3.48. Through the application of new payment scales for overtime and new rules to increase mobility within and across Regional Health Authorities (Administrações Regionais de Saúde - ARSs), overtime compensation is reduced by a further 20% in 2013 [Q4-2013].

Regional health authorities

3.49. The Regional Health Authorities (Administrações Regionais de Saúde - ARSs) are implementing the new internal control procedures manual, with the objective of having it finalised by [December 2013].

Cross services

3.50. Continue to develop the system of patient electronic medical records and ensure access to all relevant health care facilities [ongoing].

4. Labour market and education

Labour market

Objectives

Revise the unemployment insurance system to reduce the risk of long-term unemployment while strengthening social safety nets; reform employment protection legislation to tackle labour market segmentation, foster job creation, and ease the transition of workers across occupations, firms, and sectors; ease working time arrangements to contain employment fluctuations over the cycle, better

accommodate differences in work patterns across sectors and firms, and enhance firms' competitiveness; promote labour cost developments consistent with job creation and enhanced competitiveness; ensure good practices and appropriate resources to Active Labour Market Policies to improve the employability of the young and disadvantaged categories and ease labour market mismatches.

Address early school leaving and improve the quality of secondary education and vocational education and training, with a view to raising the quality of human capital and facilitate labour market matching.

Reforms in labour and social security legislation will be implemented after consultation with social partners, taking into account possible constitutional implications, and in respect of EU Directives and Core Labour Standards.

Employment protection legislation

4.1. The government will carry out reforms in the employment protection system aimed at tackling labour market segmentation, fostering job creation, and easing adjustment in the labour market [ongoing].

4.2. Following the changes to the dismissal rules as stated in laws n. 53/2011, n. 23/2012 and n. 69/2013, the government will prepare before the tenth review a report on the effects of these changes on relevant labour market indicators, taking also into account those areas of Employment Protection Legislation that have not been recently reformed.

4.3. Following the Constitutional Court ruling of 26 September 2013 the government will find alternative reform options with similar effect while respecting the ruling. After consultations with social partners, the alternatives will be discussed with EC/ECB/IMF staff at the time of the tenth review.

Wage setting and competitiveness

4.4. The government will promote wage developments consistent with the objectives of fostering job creation and improving firms' competitiveness with a view to correcting macroeconomic imbalances. To that purpose, the government will:

i. commit that, over the programme period, any increase in the minimum wage will take place only if justified by economic and labour market developments and agreed in the framework of the programme review [ongoing];

ii. ensure wage moderation when deciding on the extension of collective agreements that fulfil the criteria set out in Council of Ministers Resolution 90/2012, by taking into account the implications of the extension on competitiveness of non-affiliated firms [ongoing];

iii. prepare an independent review on the desirability of shortening the survival (sobrevigência) of contracts that are expired but not renewed (art 501 of the Labour Code) by [Q4-2013]. The government will present a summary of the system of survival of collective agreements, including data on the number of contracts for which termination was requested by one of the parties, number of agreements that are under "sobrevigência", and information on arbitration cases started in consequence of the expiration of collective agreements [October 2013].

Active labour market policies

4.5. The Government will ensure good practices and an efficient amount of resources to activation policies to strengthen job search effort by the unemployed and to other Active Labour Market Policies (ALMPs) to improve the employability of the young and disadvantaged categories and ease labour market mismatches. Following the preparation of a report assessing the effectiveness of ALMPs and the

publication of the Council of Ministers Resolution n.20/2012, which sets a plan to improve ALMPs, including the role of Public Employment Services (PES), the Government will present specific measures to strengthen the role of the job counselling and job search assistance as well as the activation and sanctions systems in facilitating the transition from unemployment to employment. [Q4-2013]

Education and training

4.6. The government will continue action to tackle low education attainment and early school leaving and to improve the quality of secondary education and vocational education and training, with a view to increasing efficiency in the education sector, raise the quality of human capital and facilitate labour market matching. To this purpose, the government will:

i. set up an analysis, monitoring, assessment and reporting system in order to accurately evaluate the results and impacts of education and training policies, notably plans already implemented (notably concerning cost saving measures, vocational education and training and policies to improve school results and contain early school leaving). [ongoing];

ii. in line with the action plan to improve the quality of secondary education the Government will: (i) continue to promote trust agreements with public schools and report about progress [ongoing]; (ii) define and implement a simple funding framework comprising performance and evaluation criteria for public schools, including those under autonomy agreements [Q4-2013]; (iii) following the assessment of the new inspection model, report on possible further improvements of the model [Q4-2013];

iii. in line with action plan on vocational and educational training (VET) the Government will report on: (i) involvement of businesses in the provisions of traineeships [ongoing]; (ii) action taken to reorganise modalities for the provision of VET, improve the quality and attractiveness of VET, and to enhance students' orientation and career guidance [ongoing]; (iii) the establishment of "professional schools of reference" [Q4-2013].

5. Goods and services markets

Objectives

Reduce entry barriers in network industries and sheltered sectors of the economy such as services and regulated professions so as to increase competition and reduce excessive rents. These measures should help improving the competitiveness of the Portuguese economy by lowering input prices, raising productivity and improving the quality of the products and services provided. This should contribute decisively to the social balance of the programme by reducing unwarranted sector protection and rents so that all segments of the society participate in the burden sharing of the needed adjustment.

Energy markets

Objectives

Complete the liberalisation of the electricity and gas markets; ensure the sustainability of the national electricity system and avoid further unfavourable developments in the tariff debt; ensure that the reduction of the energy dependence and the promotion of renewable energies is made in a way that limits the additional costs associated with the production of electricity under the ordinary and special (co-generation and renewables) regimes; ensure consistency of the overall energy policy, reviewing existing instruments. Continue promoting competition in energy markets and to further integrate the Iberian market for electricity and gas (MIBEL and MIBGAS).

Liberalisation of electricity and gas markets

5.1. Following the adoption of the legal framework regarding the scope of competence of the logistics operator for switching suppliers, implement the plan to create a new gas and electricity logistics operator independent company as presented in the seventh review [Q1-2014].

Ensure sustainability of the national electricity system

5.2. In the context of the measures to reduce excess rents and to address the sustainability of the national electricity system, and following the October information resulting from the regulator's preliminary assessment of access tariffs, provide an update on the tariff debt which analyses the impact of the measures already adopted on the projections of the tariff debt path up to 2020 and takes into account factors such as the reduction in demand and the CMEC annual evolution. Present any additional cost reduction measures that might be necessary to (i) eliminate excess rents and (ii) eliminate the tariff debt by 2020, ensuring a balanced burden sharing across the various stakeholders in the sector [mid-November 2013].

5.3. Following the report on the CMEC scheme and the process for the extension of the concession of the public hydro resource by the former CAE hydro power plants, analyse the consequences of the report and the need for potential measures [tenth review]; take the necessary measures to comply with EU regulations and decisions [ongoing].

5.4. Accelerate convergence to market-based pricing for co-generation operators in parallel with electricity market developments under the EU internal electricity and gas market legislation. The remuneration scheme for co-generation will be further revised to improve efficiency of the support system in ensuring continued guaranteed access of operators to electricity networks and markets with the calculation of explicit subsidies based on relevant price factors in the context of a competitive electricity market. The revision should ensure that the design of the support scheme allows a dynamic correlation between electricity market prices and the efficiency premium when the values of avoided externalities are not adequately reflected in electricity and other factor prices. This revision will be undertaken in line with the framework of the transposition of the energy efficiency directive [Q4-2013]. Ensure through annual audits that plants not fulfilling the requirements for co-generation do not receive the support, and report on the progress [ongoing].

5.5. For new contracts in renewables, revise downward the feed-in tariffs and ensure that the tariffs do not over-compensate producers for their additional costs as compared to market prices and they continue to provide an incentive to reduce costs further, through digressive tariffs. For more mature technologies develop alternative mechanisms (such as feed-in premiums). Report on action taken will be provided by [Q3-2013]. Decisions on future investments in renewables, in particular in less mature technologies, will be based on a rigorous analysis in terms of its costs and consequences for energy prices. International benchmarks will be used for the analysis and an independent evaluation will be carried out. Report on action taken will be provided by [Q3-2013].

Telecommunications and postal services

Objectives

Increase competition in the market by lowering entry barriers; guarantee access to network/infrastructure; strengthen power of the National Regulator Authority.

Telecommunications

5.6. Finalise the conclusion of the universal service contracts awarded through the tenders, in compliance with the Court of Justice ruling of 7 October 2010. [Q3-2013].

5.7. Following the corrective measures already taken, monitor the competitive situation in the telecommunications sector, in particular wholesale and retail broadband access, and mobile origination charges [ongoing].

Postal services

5.8. Following the transposition of the Third Postal directive, further liberalise the postal sector by amending the decree-law laying down the framework of the concession contract and renegotiating the amendment of said contract with CTT, in order to reflect the new law (Law 17/2012) transposing the Third Postal Directive; ensuring in particular that the current designation period for the universal service provision is shortened to 2020 and that investment needs and return on investment are taken into account when setting new designation periods [Q3-2013].

Transport

Adopt a strategic plan to: rationalise networks and improve mobility and logistic conditions in Portugal; improve energy efficiency and reduce environmental impact; reduce transport costs and ensure financial sustainability of the companies; strengthen competition in the railways sector and attract more traffic; integrate ports into the overall logistic and transport system, and make them more competitive.

Strategic Plan for Transport

5.9. Implement the Strategic Plan for Transport for 2011-2015, namely:

i. continue the reforms in the transport SOEs to achieve their EBITDA balance, by focusing efforts on the reduction of operational costs [ongoing];

ii. reduce the forecast debt burden of Estradas de Portugal through the reduction of PPP contracts' scope still in the construction phase, revision of shadow-toll schemes and the adjustment of the CSR (Road Service Contribution) to, at least, the inflation level. Analyse additional measures to further reduce the forecast debt burden of Estradas de Portugal [ongoing];

iii. focus the investment priorities in projects that present a positive cost-benefit ratio and contribute to the competitiveness of Portuguese exports, namely in the port and freight rail sectors [ongoing];

iv. reform the transport and infrastructures' regulatory framework in order to improve the effectiveness, efficiency and independence of the entities regulating the transport sector [end-November 2013].

5.10. Present a long term vision of the transport system and a list of actions to improve its efficiency and sustainability. It will specifically include an assessment of the existing rail, road and port networks and present a set of investment priorities for the 2020 and 2030 horizons, taking also into account TEN-T networks, with an estimate of the financial needs and the foreseen sources of financing [Q4-2013].

Railways sector

5.11. Continue with the transposition of the EU Railway Packages and in particular:

i. ensure that the rail regulator enjoys the independence required under the EU rail Directives, in particular regarding the rules of appointment and dismissal of the director of the rail regulator. Strengthen the capacities of the railway regulator to fulfil its regulatory mandate effectively, including appropriate human resources and synergies with other transport regulators in the context of the revision of national regulatory agencies by [end-November 2013];

ii. continue to implement the plans to bring the infrastructure manager to full operational balance by 2015. On the revenue side, track access charges for freight services should not be increased in order to prevent a deterioration of the competitiveness of rail freight services. Reintroduce incentives to REFER to reduce costs and access charges. Provide annual progress reports on the implementation of balancing revenues and expenditures [ongoing];

iii. ensure that the new Public Service Obligation (PSO) contracts concluded on rail passenger transport respect EU legislation including Regulation (EC) No 1370/2007, and in particular provide a detailed breakdown of state contributions for each line under PSO. Develop administrative capacity for a stepwise introduction of competitive tendering of PSOs starting with some suburban services. Ensure that the awarding authority has the required level of independence and competence and guarantees fair conditions of tendering [Q4-2013];

iv. present an assessment of the impact of the extended performance schemes on infrastructure charges in different traffic categories [Q1-2014];

v. continue to prepare the privatisation of the freight branch of the state-owned rail operator, by further implementing measures towards full operational balance by 2015 and assessing the investment plan on rail to fully enhance economic value of the company [twelfth review];

vi. on the basis of the assessment presented ensure that the main rail terminals currently owned by CP Carga are transferred to another entity that will guarantee non-discriminatory access to all rail freight operators [tenth review].

Ports

5.12. Take further steps to improve the governance model, the economic regulation and the operation of the maritime ports with the objective to enhance the competitiveness and the efficiency of ports in line with the Strategic Plan of Transport 2011-2015; the 5+1 Plano de redução de custos portuários, in particular:

i. Present a review of the port work law, in particular its impact on port usage cost and the overall savings generated by [Q4-2013].

ii. Deliver and enforce policies that ensure strong integrated policy-making, strategic planning and surveillance functions common to all ports in the country. Ensure that the regulator relevant for ports enjoys sufficient financial resources and administrative capacity to effectively carry out its function [end-November 2013];

iii. Deliver policy decisions and take actions, including those that foster the renegotiation of the existing port operation concessions, to ensure that (i) efficiency gains and cost-savings are passed to port customers; and (ii) concession-holders of terminals and land facilities in ports respect minimum performance criteria [tenth review].

iv. Deliver an exhaustive action plan in the form of a detailed timetable setting out deadlines for each action necessary for the implementation of the above mentioned measures [tenth review]

Other services sector

Objectives

Eliminate entry barriers in order to increase competition in the services sector; soften existing authorisation requirements that hinder adjustment capacity and labour mobility; reduce administrative burden that imposes unnecessary costs on firms and hamper their ability to react to market conditions.

Sector-specific legislation of Services

5.13. Further to the adoption of a significant number of amendments to the sector specific legislation, complete the adoption of Construction Laws and the others outstanding sectorial amendments necessary to fully implement the Services Directive and submit them to Parliament where necessary by [mid-October 2013] in view of approval by [Q4-2013]. The proportionality of fees linked to construction activities will be ensured by the date of adoption of the Construction Law [Q4-2013].

Regulated professions

5.14. Following the approval by Parliament of Law 2/2013 which establishes the horizontal legal framework meant to improve the functioning of the regulated professions (such as accountants, lawyers, notaries) for which regulation involves a professional body (Ordens or Câmaras), the government will submit to Parliament the professional bodies' amended statutes. These changes will (i) ensure that requirements affecting the access to and exercise of activity which are not justified or proportional, such as those restrictions to the use of commercial communication (advertising), reserves of activity and legal form and shareholding requirements under the Services Directive, will be eliminated and (ii) further improve the conditions for mobility of professionals (in and out of Portugal) in line with EU Directives in the area of free movement of professionals [Q4-2013].

Administrative burden

5.15. Continue the simplification reform effort by:

i. adapting the content and information available at the Point of Single Contact (PSC) for the missing 8 out of 50 amended and published regimes to ensure conformity with the Services Directive and for those that have not required amendments so far by the [tenth review] and make available online forms and procedures for these regimes by the [tenth review]. Constantly adapting the content and information available at the PSC to the remaining sector-specific regimes that are about to be adopted to ensure conformity with the Services Directive (see 5.13 above) at the latest 1 month after the adoption of each sector-specific regime, clearly differentiating information on requirements applicable to established providers and to cross-border ones, and by implementing online procedures for all sectors covered by the Services Directive no later than 2 months after adoption of the sector-specific regime;

ii. adapting the content and information available at the PSC for the outstanding regimes approved to ensure conformity with the Professional Qualifications Directive by and make available online forms and procedures by the [tenth review]. Constantly adapting the content and information available at the PSC to the new legislation to be adopted to ensure conformity with the Professional Qualifications Directive at the latest 1 month after the adoption of amendments, clearly differentiating information on requirements applicable to established providers and to cross-border ones, and by implementing on-line forms and procedures for each profession no later than 2 months after adoption of amendments;

iii. extending PSC to services not covered by the Services Directive [Q4-2013];

iv. extending the "Zero Authorisation" project to other services sectors of the economy [Q4-2013].

5.16. Provide a monthly update of the detailed work programme of AMA to fulfil 5.15.

6. Housing market

Objectives

Improve access to housing; foster labour mobility; improve the quality of housing and make better use of the housing stock; reduce the incentives for households to build up debt.

Property taxation

6.1. The government will gradually rebalance property taxation towards the recurrent real estate tax (IMI) and away from the transfer tax (IMT), while considering the socially vulnerable [ongoing].

Comprehensive review of the housing market

6.2. Following the adoption of the amendments to the New Urban Lease Act Law 6/2006 and the Decree Law which simplifies the administrative procedures for renovation, the government is undertaking and will publish a comprehensive review of the functioning of the housing market. The review will determine whether the new legal provisions adopted are sufficient to make the housing market more dynamic and, if necessary, will propose new policy measures [Q4-2013].

7. Framework conditions

Judicial system

Objectives

With the entry into force of the new Code of Civil Procedure and the adoption of the Judicial Organization Act in Parliament, all measures under the Memorandum of Understanding have already been implemented or are about to enter into force, and various of these are already bringing positive results. Improvement of the functioning of the judicial system, which is essential for the proper and fair functioning of the economy, through: (i) ensuring effective and timely enforcement of contracts and competition rules; (ii) increasing efficiency by restructuring the court system, and adopting new court management models; (iii) reducing slowness of the system by eliminating backlog of courts cases (including tax court cases) and by facilitating out-of court settlement mechanisms is well underway. The oversight body for enforcement agents and insolvency administrator (CAAJ) will be established shortly after the CAAJ law has entered into force. Equally, stepping up efforts to raise public awareness of the successful reforms in the judicial sectors would add value and recognition to these efforts and results.

In addition to the above, the government will:

7.1. Publish quarterly reports on recovery rates, duration and costs of corporate insolvency cases starting from Q3-2011 and on the clearance rate of enforcement court cases starting from Q3-2013, within [four months after the end of the relevant quarter].

Competition, public procurement and business environment

Objectives

Ensure a level playing field and minimise rent-seeking behaviour by strengthening competition and sectoral regulators; avoid special rights of the state in private companies (golden shares); reduce administrative burdens on companies; ensure fair public procurement processes; improve effectiveness of existing instruments dealing with export promotion and access to finance and support the reallocation of resources towards the tradable sector.

Competition and sectoral regulators

7.2. The Government shall take the necessary measures to ensure that the Portuguese State or any public bodies do not conclude, in a shareholder capacity, shareholder agreements the intention or effect of which hinder the free movement of capital or which influence the management or control of companies [ongoing].

7.3. Going beyond elimination of special rights of the State, the authorities also commit to ensuring that obstacles to free movement of capital will not be created by their action. The authorities acknowledge that the discretion granted under the amended article 13(2) of the Framework Law of Privatisations (Law 11/90 amended by Decree 3/XII of the Parliament of 5 August 2011), if used, shall be restricted solely to the concrete privatisation operation and thus used in such a proportionate manner that privatisation's implementing laws will not set or allow holding or acquisition caps beyond the privatisation transaction [ongoing].

7.4. Following the recently published framework law on regulators – which aims at (i) establishing a regulatory environment that protects the public interest and promotes market efficiency, (ii) guaranteeing the independence and financial, administrative and management autonomy of the National Regulatory Authorities in the exercise of their responsibilities, in full compliance with EU law, including the necessary conditions to guarantee adequate human and financial resources and being able to attract and retain sufficiently qualified staff and (iii) strengthening the overreaching role of the Competition Authority in enforcing competition rules, therefore supporting and complementing the effect of the recently adopted competition law – the government will approve the corresponding amendments to the bylaws of the National Regulatory Authorities [Q4-2013].

Public procurement

The government will modify the national public procurement legal framework and improve public contracts award practices to ensure a more transparent and competitive business environment and improve efficiency of public spending. In particular, it will:

7.5. building on the report already submitted, include more up-to-date information of the impact of the amendments to the revised Public Procurement Code and carry out an assessment of the enhanced role of the Court of Auditors in ensuring compliance with public procurement rules by [Q3-2013].

Business environment

7.6. Following the set-up of the procedures for requesting VAT exemptions for exporting firms and to simplify procedures associated with indirect exports, the government will assess the impact of this measure by [Q4-2013].

7.7. Follow up any EU decision taken regarding compliance with the Directive 2011/7/EU on Late Payments Directive transposition.

7.8. To improve the financial situation of business, establish an optional VAT cash accounting regime [Q3-2013] and assess the impact of this measure by [Q1-2014].

Licensing environment

Objectives

The government is launching a new comprehensive programme to tackle excessive licensing procedures, regulations and other administrative burdens in the economy. These explicit and implicit barriers represent a major obstacle for economic growth in Portugal. Companies face substantial costs and uncertainty which affect investment decisions, thus limiting job creation. Furthermore, these barriers affect small and medium-sized enterprises in a disproportionate way because they have fewer resources to surpass these obstacles, deteriorating the competitive environment. Foreign investment is also affected disproportionally because national companies have information advantages. The various new initiatives laid out below cover all families of licenses and will have a substantial impact in the business environment. The reviews of the legal regimes of environment and territory planning and of industrial and commercial licencing aim at ensuring their mutual compatibility.

Regulatory simplification

7.9. Continue reducing administrative burdens by including municipalities and all levels of public administration within the scope of the Simplex Programme [ongoing].

7.10. To deal with the legacy of excessive licence procedures and other administrative burdens, the government will carry out an inventory and an analysis of the costs of regulations that are likely to have a higher impact on economic activity (at central, regional and local levels) [Q1-2014]. On the basis of the analysis the government will devise a roadmap for regulatory simplification.

7.11. To prevent future growth in excessive licenses and regulations, the government will adopt a rule that makes mandatory for all levels of government, when creating a new regulation generating costs for businesses, to propose the elimination of an existing regulation or regulations with an equivalent cost [Q3-2013].

Environment and territory planning

7.12. In consultation with the relevant stakeholders, review the legal regimes at all levels of Government in the area of territorial planning, in order to increase and facilitate the establishment of investors while at the same time limiting urban sprawl. In particular, the authorities will :

i. Following the submission to Parliament of the Base Law of Soil and Territorial and Urbanism Planning (Lei dos Solos), in view of its adoption by the Parliament by [Q4-2013] ensure that will be aligned with the new Industrial Licensing regime (measure 7.14) ;

ii. Adopt and make operational a Risk Sectorial Plan by the [tenth review];

iii. review the legal regimes of the Territorial Management Instruments (RJIGT) and of the related regulations by the [tenth review];

iv. adopt a legal provision for the regularisation of activities not in accordance with Territorial Management Instruments by the [tenth review];

v. harmonise the Regional Plans – new generation will be included within the new legal regime of RJIGT by the [tenth review];

vi. review the Legal Regime for Urbanism and Building (RJUE), that should be aligned with, the new Industrial Licensing regime (measure 7.14) by the [tenth review].

7.13. Increase a nationwide land registration system (registo cadastral) to allow a more equal (perequitativa) distribution of benefits and costs in the execution of urban planning. The government will:

i. implement a Legal Regime of Land Registration (registo cadastral) [Q4-2013];

ii. create a diploma on Land Registration and Land Registration Experts [Q4-2013];

iii. review the cartography for plans regime and the diploma on Cartography [Q4-2013];

iv. enforce the Council of Ministers Resolution 56/2012 by [Q4-2013], to collect all land registration procedures, currently scattered in various departments.

Industrial Licensing

7.14. Implement the new Industrial Licensing regime by means of fully implementing the approved System of Responsible Industry (SIR - Sistema da Indústria Responsável) as follows:

i. Approve regulations on zero licensing procedures on licensing procedures for Type 2 and Type 1 industries [Q3- 2013], in view of their full integration in the one-stop shop (Balcão do empreendedor). Implement fast-track procedures for Type 1 industries [ongoing];

ii. define and establish the Zones of Responsible Enterprises (ZER – Zonas Empresariais Responsáveis) by [Q3-2013], which will allow the installation of industries in areas previously licensed with all industrial, building and environmental provisions required by national and European law;

iii. create and define standardised industrial licenses [ongoing];

iv. ensure that the new Industrial Licensing is aligned with, and strengthened by, the review of the New Base Law of Soil and Territorial and Urbanism Planning while at the same time limiting urban sprawl (measure 7.12 i);

v. ensure that the new Industrial Licensing is aligned with, and strengthened by, the review of the Legal Regime for Urbanism and Building (RJUE - measure 7.12 vi).

Commercial licensing

7.15. Review the commercial licensing regime. Approve the new legal regime for commercial actives and establish the Programme for the Competitiveness of Commerce and Services activities (Programa para a Competitividade do Comércio e Serviços), which will simplify and condense in a single law more than 20 dispersed existing legal regimes [Q4-2013].

Geology

7.16. Review the geological licensing regimes, including:

i. the legal regime concerning the licensing of mining and geological production and investment in line with international best practices in this field by the [tenth review];

ii. simplify the legal and bureaucratic procedures pertaining to mining and geological investments, especially in terms of assessment, search, development, and production activities by the [tenth review].

Tourism

7.17. Review the Licensing in Tourism regime:

i. eliminate or transform into a voluntary regime the mechanism of prior communication in the Regime for Urbanism and Building [Q3-2013]. Simplify the legal regime for touristic establishments [Q3-2013];

ii. expand the range of ex post control mechanisms in urban operations, significantly reducing administrative procedures and costs for developers [Q3-2013];

iii. simplify and make more transparent the requirements on the classification of the several types of touristic establishments (number of stars) [Q3-2013];

iv. review of the sanction legislation on the touristic establishments regime as a way to fight informal touristic economy, giving more powers to ASAE (Authority for Economic and Food Safety) [Q3-2013].

ANNEX 5
MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

October 24, 2013

I. MACROECONOMIC OUTLOOK

1. Activity. The near-term economic outlook has improved since the seventh review. First, output and employment surprised on the upside in the second quarter, with real GDP expanding (by 1.1 percent quarter-over-quarter) for the first time since late 2010 and the unemployment rate declining to 16.4 percent from 17.7 percent. Second, recent high frequency indicators point to some stabilization in activity and confidence. In light of this, we now expect the economy to contract by 1.8 percent in 2013, compared to 2.3 percent at the time of the seventh review, with the revision reflecting mainly a less negative contribution from domestic demand and strong growth of exports of goods and services, which however is largely offset by an upward revision of imports. Accordingly, the projected 2013 unemployment rate has been revised down from 18.2 to 17.4 percent. Output is expected to remain broadly flat for the rest of the year, and to pick up gradually during the course of 2014—consistent with growth of some 0.8 percent for the year as a whole and unemployment peaking at 17.7 percent—underpinned by a gradual pick-up in investment, conditioned on the continued alleviation of uncertainty and a sustained improvement in confidence. Reflecting still weak domestic demand, we expect headline inflation to average around 0.6 percent this year. Notwithstanding the improved near-term outlook, uncertainties remain as the drag of private sector deleveraging and fiscal consolidation on growth could turn out to be stronger than expected.

2. External adjustment. The current account balance has continued to adjust at a faster pace than envisaged previously. It is now projected to turn into a surplus of about 1 percent of GDP this year (compared to an expected 0.3 percent of GDP at the time of the seventh review) and remain at that level next year, bringing the cumulative adjustment since 2009 to some 12 percent of GDP. The revision is largely driven by higher exports—including tourism receipts that increased by 8 percent in January through July. Strong demand from non-EU trading partners and an improvement in Portugal's export market shares in most markets continue to underpin robust export growth. In the short term, weaker demand from trading partners remains the main downside risk to these projections. Although most structural reforms envisaged in the program are now in place and are beginning to have an impact, maintaining robust export growth over the medium term will require continued improvement in external competitiveness.

II. FISCAL POLICY

3. 2013 Budget Execution. While the end-June quantitative performance criteria on the general government cash balance and debt were met, we need to overcome a number of budgetary challenges. Overall, we expect to meet our annual deficit target (5½ percent of GDP, excluding the BANIF recapitalization costs of 0.4 percent of GDP), but with an unfavorable net carry-over from the 2013 budget execution to 2014 of some 0.4 percent of GDP and the need to rebuild a budgetary reserve (0.3 percent of GDP). Specifically:

- Budgetary overruns and revenue shortfalls totaling about 0.8 percent of GDP reflect a combination of one-off factors (0.2 percent of GDP) stemming from a shortfall in the reprogrammed EU funds and delays in the planned port concession, as well as pressures (0.6 percent of GDP) from increased contributions to the EU budget, the transfer to Greece of the income from the Greek bond holdings in Banco de Portugal's investment portfolio (consistent with the Eurogroup agreement), shortfalls in contributions to the public pension scheme, and overruns in wages and intermediate consumption. In addition, despite efforts to apply the commitment control law, slippages in the health sector are causing a net accumulation of arrears in SOE hospitals (some €300 million year-to-date).

- Nevertheless, the use of the provisional budget allocation (0.3 percent of GDP), the reduction in funds available to the line ministries (0.1 percent of GDP), and recourse to a one-off tax and social security contribution debt recovery scheme (0.4 percent of GDP) should offset these deviations.

Under these assumptions, underlying structural primary adjustment would reach nearly 0.5 percent of GDP.

4. Fiscal path for 2014-15. We remain committed to achieving our 2014 deficit target of 4 percent of GDP in 2014—consistent with a structural primary adjustment of 1 percent of GDP. To achieve these objectives while arresting the accumulation of domestic arrears, measures of around 2.3 percent of GDP will be needed in 2014. Most of these measures have been drawn from the public expenditure review (PER—see below). We have submitted the Budget Law to Parliament on October 15 as a prior action for the completion of this review. Fiscal consolidation will continue in 2015, with a targeted structural primary adjustment of about 1 percent of GDP.

5. Public Expenditure Review (PER). We modified the package of expenditure reforms initially identified in the context of the PER to reflect consultations with social partners as well as the recent developments, including an adverse Constitutional Court ruling. The reforms are proceeding. The expected yield of the PER package is now €3.1 billion (net of reduced income taxes and social contribution collections) or €2.9 billion when including the upfront costs of mutual agreements terminations in 2014. There was a rebalancing of the package toward sector-specific measures. Savings will be generated mainly by limiting outlays on the public wage bill and pensions—which account for over two-thirds of primary spending and where Portugal spends more in comparison to peer countries—as well as sector-specific reforms, with a view to increase equity and efficiency in the provision of social transfers and public services. The underlying reforms are organized around three main pillars: (i) a wage bill reform, (ii) a pension reform, and (iii) sector-specific savings.

a. PER—wage bill reform. The overall objective of the wage bill reform (0.9 billion in net savings) will be to (i) reduce the size of the public sector workforce—addressing excessive employment in particular sub-sectors—while tilting its composition toward high-skilled and better-trained civil servants; (ii) ensure convergence of the public sector work rules and regulations toward private sector legal regimes (including regarding working hours, working time arrangements, and holiday entitlements); (iii) increase beneficiaries' contributions to ensure self-sustainability of public sector health subsystem; and (iv) simplify the remuneration policy by implementing a single wage scale and streamlining the wage supplement scale. The reduction in the workforce will be achieved through a combination of policies, including lower replacement of retirees, voluntary separations (scheme launched on September 1), and use of the redesigned mobility pool. The increase in working hours to 40-hours per week will also help, while generating efficiency gains more broadly. The current status of the various legislative changes needed to implement these reforms is as follows:

i. The Law aligning the working hours of the public sector to the 40 hours in force in the private sector was already approved. It is now under consideration by the Constitutional Court.

ii. Following the consultations with social partners, the new draft public administration labor law—aiming at aligning current public employment regime to the private sector rules, including for working hours and holiday time—will be submitted to Parliament by end-October (structural benchmark).

iii. The draft law on the redesigned mobility pool was also submitted and approved by Parliament, but subsequently deemed unconstitutional by the Constitutional Court and returned to Parliament for amendments. We have redesigned the scheme and the revised draft law now awaits parliamentary approval.

iv. The single wage scale reform and the reduction to the wage supplements will be made effective by January 1, 2014, implemented through a budget provision (prior action). A report on a more comprehensive reform of wage supplements is expected by end-December.

b. PER—pension reform. A pension reform is expected to generate 0.6 billion of net savings. It is based on equity principles with preservation of minimum socially-acceptable income levels, thus protecting those who earn the lowest pensions. Specifically, the reform takes into consideration the need to reduce the current differences between the civil servants' regime and the general social security regime, aiming at enhancing the fairness of the overall pension system. Moreover, while reforms implemented over the past two decades have contributed to long-term sustainability, the amount of pension benefit payments for which the government is currently liable makes the system excessively costly under the current circumstances reassessing the need to take into account demographic developments. Accordingly, the reform is based on three main elements: (i) an effective increase by one-year in the statutory retirement age to 66 years—implemented by adjusting the demographic sustainability factor (prior action); (ii) aligning the rules and benefits of the public sector pension funds, CGA, to the general pension regime by changing one of the replacement rate parameters from about 90 to about 80 percent for all applicable beneficiaries, while avoiding double penalization of CGA beneficiaries, with a pension below €5,030, with the CES contribution (structural benchmark), and (iii) means testing survivors' pensions of both CGA and the general pension regime, in cases where these accumulate with other pensions. Each of these reforms is implemented through modifications to the relevant laws. The necessary legislative proposals have been submitted to Parliament.

c. Sector-specific expenditure savings. Other savings under the PER (1.65 billion of net savings) are generated through a combination of sector-specific reforms, which mainly include intermediate consumption cuts and targeted nonrenewals of fixed-term contracts. Additional cutbacks in SOE and PPP expenditure are generated through further negotiation and operational restructuring. In the education sector for example, rationalization of the school network and a convergence of the key indicators, namely class size, towards peer levels are at the core of our reforms. In the health sector, savings come from further restructuring of the hospital network.

6. Additional measures. Due to the negative carryover from the 2013 budget execution and upward expenditure pressures, the PER measures need to be complemented by permanent measures amounting to €0.6 billion (0.4 percent of GDP) to achieve the budget deficit of 4.0 percent in 2014. These include new revenue measures (on company cars, online gambling, diesel passenger cars, alcohol and tobacco, banking, and media spectrum), a reduction of fiscal benefits for pension and real estate funds and a special levy on the energy sector (with revenues in excess of €100 million to be used to reduce the electricity tariff deficit). A number of one-off operations (including port concessions, sales of excess oil reserves, and a transfer from the CTT health fund) adding to €0.4 billion (0.2 percent of GDP) will also contribute to achieving our deficit target, more than offsetting the one-off upfront costs related to the mutual agreements for termination of public sector employment contracts (by about 0.1 percent of GDP).

7. Legal safeguards. To mitigate legal risks from future potential Constitutional Court rulings, we will continue to respect the following principles. First, expenditure reforms will be designed with the principle of public/private sector and intergenerational equity in mind as well as the need to address the sustainability of social security systems. Second, legislation underpinning the expenditure reforms will be duly justified on compliance with the fiscal sustainability rules in the recently-ratified European Fiscal Compact, which now ranks higher than ordinary legislation. Third, the government will rely as much as possible on general laws—rather than on one-year budget laws—consistent with the structural nature of the reforms. This also allows the possibility of prior constitutional review of the said laws, thus permitting early reaction on the part of the government in case these reforms raise constitutional issues.

8. Debt Path. Under the programmed fiscal path, gross debt is set to peak at close to 128 percent of GDP in 2013 (or at about 122 percent of GDP net of IGCP's projected deposits in 2014). The increase in

the debt peak vis-à-vis the seventh review is explained by the suspension of the transfer of the State's CGD shares to Parpública, by the postponement of the reallocation of the Social Security portfolio from foreign assets to government securities, now scheduled to be completed by end-2014, and by a higher projected Treasury cash balance at end-2013.

9. CIT Reform. We have launched a far-reaching reform of the Portuguese corporate income tax (CIT) regime aimed at boosting investment and growth. The reform committee presented in July 2013 its recommendations. They consist in simplifying the CIT regime through a broadening of the tax base, the gradual lowering of the rate, the reduction of multiple surcharges, and the rationalization of the incentive schemes. The report also focuses on steps enhancing legal stability, lowering compliance costs, and aiming at reducing litigation. In addition, measures are proposed to improve the international competitiveness of the tax and strengthen the territorial approach, including through the adoption of a universal participation exemption regime (while respecting international standards). The reform would also envisage reducing policy-induced debt bias. It will be implemented within the existing budgetary envelope. A draft law on the CIT reform has already been submitted to Parliament.

III. CONTAINING FISCAL RISKS

10. Public Financial Management. We have made further progress in advancing our Public Financial Management reform, but controlling domestic arrears remains challenging, particularly in the health sector. Important steps have been taken in transposing the EU economic and governance fiscal framework. The process will be completed by the first quarter 2014, along with further changes to streamline budgetary procedures. In parallel, we will identify the operational changes necessary to ensure full implementation of the BFL in a draft action plan to be prepared by the eleventh review. We will publish a tax expenditure report as well as a comprehensive Fiscal Risks Report together with the Budget Law. We remain committed to reverting the accumulation of new domestic arrears, the stock of which amounted to €2.9 billion at end-July 2013. While we will proceed with a second settlement program in the health sector—in the value of €432 million—following the same procedures envisaged in the March 2012 strategy document, we are concurrently working with the enforcement authorities in order to effectively sanction public officials who do not comply with the commitment law. Moreover, we are strengthening our efforts to rein in expenditures in this sector through appropriate budgeting and ensuring effective savings measures.

11. Revenue Administration. We have completed the property revaluation process—with approximately 5 million properties revalued—a key measure of the 2013 budget. To bolster revenue performance in support of our medium-term fiscal objectives, we remain determined to make further progress in curbing tax evasion. Recent steps in this direction included making fully operational the new Large Taxpayer Unit and conducting successfully a VAT invoicing reform. To limit the impact of the tax and social security contribution debt recovery scheme announced in early October, we have publicly committed not to have recourse to such new schemes in the future and will tighten sanctions for criminal offenders. Looking ahead, key steps to strengthen compliance will include (i) phasing in of a modern compliance risk model, including by establishing a Risk Management Unit; (ii) strengthening PIT compliance management—the pilot projects on the High Net Wealth Individuals and the Self-employed Professionals, and strengthened control of the monthly PIT withholding information, are key instruments in this respect; and (iii) further modernizing tax litigation, building on the results obtained so far.

12. Public Administration. Streamlining public administration continues to be a government priority. We have made significant progress in reducing the size of the public sector, reducing the number of public employees by 6 percent since end-2011, reaching our 2-percent annual average target ahead of time. The next step in our reform agenda is the adoption of a general public administration law and other PER reforms to modernize and rationalize public administration (see paragraph 5).

13. State-Owned Enterprises. Despite the negative financial impact from the reinstatement of the 13th and 14th month salaries due to the Constitutional Court rulings, cost-reduction efforts and voluntary redundancy programs have moved enterprises significantly closer to operational balance. Looking ahead, we will maintain formal cost-cutting objectives for those firms still showing operating deficits, while other firms will be required to continue improving operating balances with a view to reducing debt burdens and financial costs. We also continue to manage the high debt burdens of some firms, and treasury support has remained within the envelope of budgeted transfers. To further strengthen SOE governance, the Council of Ministers approved in August a Decree-Law which concentrates all shareholder functions in the Ministry of Finance along with the creation of a dedicated Technical Unit. The law also reinforces the monitoring of SOE debt by centralizing borrowing decisions at the Debt Management Agency (IGCP). The unwinding of most derivative contracts of SOEs during 2013 also contributed to reduce significantly financial costs and risks.

14. Privatization. The privatization program is broadly on track, and proceeds have exceeded the initial program target. The sale of the airport operator, ANA, has now been formally completed. While preparing the changes in the legal framework for postal services, we have launched the privatization process for the postal company CTT, and expect to receive binding offers by end-2013. The sale of the airline, TAP, however, is still on hold, after the initial privatization plan fell through at end-2012 due to inadequate financial assurances by the final bidder. We are actively seeking buyers for the group as a whole and the process will be re-launched in the near future. The privatization of the rail cargo firm, CP Carga, has also been postponed with a view to maximizing market value while restoring its operating balance. We have prepared a strategic plan for the water and waste sectors, with a view to improving their efficiency, including by introducing private capital and management in the system. Binding offers for the sale of the waste management business are currently anticipated for the first quarter of 2014. Opening water concessions to private capital and management is expected to take longer. The government will further consider expanding the privatization program to include additional assets for sale or concessions.

15. Public-Private Partnerships (PPPs). We have taken further steps to achieve a fiscally-responsible PPP model. First, we have launched a major renegotiation of road PPPs. The objective is to generate permanent savings by rationalizing OPEX, CAPEX, and the private partner's internal rate of return. In the case of sub-concessions, savings will be generated by also reducing the scope of the relevant contracts. MoUs have now been signed with most concessionaires, offering good prospects for reaching the revised savings goal of €300 million in 2013, consistent with the supplementary budget. Second, the Ministry of Finance PPP unit is gaining a pivotal role, working towards enhancing fiscal transparency, improving reporting on PPPs, and expanding its field of action to other sectors, namely health and security, and advising the autonomous region of Madeira. Finally, the ongoing revision of the regulatory framework for the road and rail sector is also part of the strategy to achieve sustainability in these sectors, by reducing operation, maintenance and major repair requirements in line with EU standards. This revision is to be completed by end-October.

16. Regional and Local Governments. The Regional and Local Finance Laws were approved by Parliament and published in September. They will improve the inter-governmental fiscal framework, notably by applying the same principles of the Budgetary Framework Law to subnational governments. Moreover, we have streamlined the organization of Parishes, significantly reducing their number. The establishment of a coordination council between the central and subnational governments is expected to enhance the exchange of information in order to support budgetary planning. The credit line to support local governments' arrears settlement is being implemented, following the necessary procedures to validate the claims. The regional government of Madeira's program with the State is broadly on track, but we will continue to closely monitor budgetary risks.

Safeguarding Financial Stability

17. Bank supervision. While compliance of the banking system with regulatory capital remains satisfactory, the challenging operating environment warrants continued vigilance. Against this backdrop, the BdP is pursuing various initiatives that seek to further strengthen banks' resilience, and maintain financial stability.

- Credit Impairment Review. Following two earlier on-site inspection programs in 2011 and 2012, the BdP has successfully completed a new credit impairment review, with the support of the participating banks' external auditors and an external consultant. The audit focused on (i) the verification of current impairment levels for a broad sample of credits, notably high-risk exposures; (ii) a follow-up of the findings identified in the original on-site inspections program related to collective impairment; and (iii) an assessment of the banks monitoring process related to the management and fair value calculation of the participation units held by the banks in restructuring funds. The limited impairment deviations identified by the review have already been addressed by the affected banks through impairment reinforcements, reflected in their end-June results. Moreover, follow-up recommendations have been issued to the banks, with all the high priority items expected to be implemented by end-December 2013.

- Review of Restructuring Processes. While the enhanced legal toolkit on corporate and household insolvency is now fully operational, further efforts remain necessary to promote early and effective use of the new restructuring tools. In this context, the BdP has initiated a special assessment program of banks' operational capacity in the area of loan restructuring and asset recovery, to ensure that the banking system can effectively support the balance sheet adjustment of the private sector, through timely engagement with troubled debtors before their viability is in jeopardy. The special program, which benefits from external expertise, will evaluate the effectiveness of management processes regarding problem loans, with a special focus on early detection. The exercise will also include a broader survey of the Portuguese regulatory framework, including any remaining gaps and bottlenecks in the implementation of the new debt restructuring tools. The BdP aims to complete the special program by early November 2013.

- Communication Strategy. Building on experiences from the various inspection programs and to promote greater transparency on its ongoing supervisory efforts, the BdP plans to publish by mid-November minimum standards for the calculation of credit impairments, including guidance on collateral valuation. Moreover, as a follow-up to the BdP's requirements on identifying and reporting of restructured loans (Instruction No. 18/2012), banks will be required to disclose this information in their annual reports, starting in December 2013.

18. Stress test exercise. Banks are making progress implementing the recommendations on their stress testing methodologies and impairment projections, issued as part of the original on-site inspections program. In this context and to further enhance the rigor of the quarterly stress test exercise, the BdP has further enhanced its credit risk model used to provide methodological guidance on default probabilities to the participating banks. Moreover, the BdP is introducing a new top-down stress test to support its review of the bottom-up results. These enhancements will be included in the next round of quarterly stress tests, to be finalized in November 2013.

19. Transition to CRD IV. Capital requirements under the program will be set in accordance with the CRD IV package. Accordingly, as of January 1, 2014, the BdP will replace the existing targets and require banks to maintain, at a minimum, a common equity Tier 1 capital level of 7 percent, as defined in CRD IV package considering all the transitional provisions related to the definition of capital. Additional measures will also be in place to preserve banks' current capital buffers, ensuring that they remain commensurate with the challenging operating environment. The new requirements and additional measures will be included in the law transposing the CRD IV package as well as in implementation instructions from the BdP before year end. The implementation of the above framework will also need to comply with the requirements currently envisaged in the EBA Recommendation on the preservation of

capital for the banks that are subject to them. We will also ensure compliance with any future regulatory initiatives at European level.

20. BSSF. We remain committed to providing further support to the banking sector, in the event new capital needs were to arise. While we will continue to encourage banks to seek private solutions, resources from the Bank Solvency Support Facility (BSSF) remain available to support viable banks if needed. The resources in the BSSF will solely be utilized to provide public support, if needed, to the banking system. State aid will remain subject to strict conditionality, in line with the recently amended EU state-aid rules, aimed at avoiding subsidizing private shareholders and preventing migration of private liabilities to the public sector balance sheet, while ensuring adequate lending to the real economy.

21. Recovery and Resolution Plans. The BdP has reviewed and issued recommendations on the recovery plans of the largest banks, and expects to receive the plans from all the other banks by end-November 2013. Institutions for which resolution plans are mandatory have submitted the data required in the supervisory notice of December 2012, and these are currently being reviewed by the BdP. We have submitted to Parliament the necessary amendments to the recapitalization law to reflect the recent Communication from the European Commission on the Application of the State-aid Rules to Support Measures in Favor of Banks in the Context of the Financial Crisis. Moreover, we remain committed to swiftly transposing the new EU Directive on bank recovery and resolution once it has been adopted.

22. Funding and Liquidity Conditions. Nonstandard measures by the ECB to restore the proper transmission of monetary policy have helped ease liquidity pressures and continue to play a pivotal role in absorbing remaining funding constraints, while strengthened collateral buffers provide an important shield against potential adverse shocks. In parallel, we continue to explore with our European partners further initiatives to support funding conditions, including potential mechanisms to securitize banks' high quality mortgage and SME credit. Moreover, the new platforms recently created by the BdP for interbank secured and unsecured lending have become fully operational, supporting the functioning of the domestic interbank market.

23. Initiatives to Promote Orderly Deleveraging. Despite improvements in liquidity conditions, the credit situation remains challenging, especially among SMEs. In this context, banks' funding and capital plans should continue to ensure that the deleveraging process takes place in an orderly manner to achieve a stable market-based funding position, while adequate and sustainable financing is provided to the economy. To support this objective, we are stepping up our efforts to promote more efficient financing allocation to the productive segments of the economy through further enhancements to our existing government-sponsored measures, in line with EU state-aid rules, as well as the promotion of alternative private funding options for SMEs. Specifically,

- Government-Guaranteed Credit Instruments. We will continue to strive to improve the performance of existing government-guaranteed credit lines, in line with international best practice. On the basis of the recent external audit of the National Guarantee System (NGS), we have defined a detailed implementation plan of key policy recommendations aiming at making these schemes more efficient and minimizing risks for the State. The recommendations include (i) a review of the schemes' objectives and investment selection processes; (ii) measures to further enhance loan and guarantee pricing mechanisms in favor of end users, including through the development of competitive bidding mechanisms for the allocation of guaranteed credit to the banks, with preliminary scenarios for competitive bidding schemes to be presented and discussed by mid-November 2013; (iii) an upgrade of the NGS risk management capabilities and review of its governance structure; (iv) improved monitoring, management, and public disclosure of the State exposure to the NGS operations. We will regularly report on progress with the implementation of these measures, which are expected to be fully finalized by end-January 2014. Moreover, to support viable firms in financial difficulties, we will explore possible modalities for the provision of guaranteed credit in line with EU state aid rules, conditional on the successful completion of a corporate debt restructuring process, with an initial proposal expected by early-November. We will

continue to monitor the balance sheet performance of the firms benefiting from government-guaranteed credit lines through our newly established quarterly monitoring framework.

• Development of SMEs Commercial Paper. We are exploring possible changes to the regulatory environment applicable to the commercial paper market to facilitate its expansion among a wider investor base and increase the use of this alternative funding option by the corporate sector, notably SMEs. The necessary draft amendments to the existing rules are currently under discussion and are expected to be approved by the Council of Ministers by end-November.

New initiatives to facilitate credit to firms by the Ministry of Finance, Ministry of Economy, and other relevant entities will be primarily focused on streamlining and improving the efficiency of existing schemes, without creating additional burden on or posing risks to public finance. In this context, the government is conducting a stock-taking exercise aiming at streamlining and centralizing the management of EU structural funds for the 2014-2020 programming period.

24. Central Credit Registry. Efforts to promote information sharing, especially for SMEs, are ongoing. The BdP has recently published a new instruction requesting banks to report in the Central Credit Registry (CCR) additional loan information, including (i) as of January 2014, identification of nonperforming and restructured loans; and (ii) as of July 2014, information on government guarantees, as well as the identification of overdue and written-off loans disputed in court. Moreover, the BdP is currently finalizing a proposal for a revision of the decree law regulating the CCR to allow further enhancements, such as the inclusion of additional financial instruments. Additional efforts to permit financial institutions to access historical information on their potential new clients, subject to authorization by the Portuguese Data Protection Authority (CNPD), are in progress. In parallel, the BdP is assessing available options for reducing information asymmetry for smaller companies, taking also into consideration other available data sources, such as the Central Balance Sheet Database (CBSD).

25. BPN SPVs. We are implementing the strategy for managing the distressed assets from Banco Português de Negócios (BPN). Two companies have been selected through a competitive bidding process to manage the credit portfolios currently held by Parvalorem, a state-owned Special Purpose Vehicle (SPV). In parallel, the disposal of the participations and assets held by the other two state-owned SPVs is progressing. CGD's state-guaranteed claim will be gradually settled in cash, according to the schedule agreed with the EC, ECB, and IMF staff. Any net recoveries realized on the assets will also be applied towards the settlement of CGD's claim.

IV. BOOSTING EMPLOYMENT, COMPETITIVENESS, AND GROWTH

26. Overall Reform Strategy. The ultimate objective of our structural reform agenda is to enhance competitiveness and the business environment, so as to boost medium-term growth and job creation prospects. Significant steps have already been taken on the labor and product market fronts, where reforms have been designed to alleviate nominal rigidities, facilitate adjustment, and foster a reallocation of resources toward the tradable sector. Important steps have also been taken to reduce red tape and raise the efficiency of the judicial system. Nonetheless, we are determined to further advance structural reforms. In light of this, we are working toward identifying unaddressed policy distortions and other potential priority reform areas.

27. Labor Market Institutions. Significant steps have been taken over the past couple of years to make the labor market more dynamic and efficient—including the reform of the Employment Protection Legislation, the reform of unemployment benefits and the reform of the wage-setting mechanism. A new reform of severance pay also entered into force more recently (October 1 Structural Benchmark). In light of the recent Constitutional Court ruling against legislative provisions that made it easier for firms to lay off employees in case of redundancy or unsuitability, the government's immediate priority will be to find alternative reform options that respect the ruling.. Following consultations with social partners, the

alternatives will be discussed with IMF/EC/ECB staff at the time of the tenth review. Looking ahead, by end-November, we intend to enhance the activation of the unemployed by improving the role of the counseling services and by stepping up job search requirements, so as to create incentives for job seekers to accept offers and facilitate the job matching process. In view of the still extremely high unemployment, we also intend to continue to assess policy options to promote an adjustment more favorable to employment. In this context, the government will discuss at the time of the tenth review and present by end-December 2013 a report assessing policy options in three main areas: (i) ensuring more effective decentralization of wage bargaining; (ii) ensuring more wage flexibility; and (iii) study proper alignment of incentives to challenge dismissals in court.

28. Energy. We continue our efforts to improve the sustainability of the national electricity system. Steps have been taken in the past year to reduce excessive rents, mainly through renegotiation. The overall initial cost reduction targets were largely met, although with shortfalls for some specific measures. Nonetheless, our revised medium-term tariff debt projections (June 15 Structural Benchmark) clearly show strong upward pressures on the system debt, reflecting partly downward pressures on demand for electricity are generating. A number of additional measures are being considered to help reduce debt. Since we are concerned about the potential impact of large electricity price increases on competitiveness, we are investigating other options to better balance the burden of adjustment between the various stakeholders of the electricity sector, notably by eliminating remaining excess rents.

29. Ports. We are taking steps aimed at reducing costs for exporters. Following reductions in fees on port use (TUP-Carga) and a revision of the Ports Work Law, we are now seeking effective transmission of lower labor costs to end-users of port services. In particular, we will engage with concessionaires with a view to modifying existing concession contracts so as to foster price reduction. Specifically, the next steps include designing by the time of the tenth program review a strategy and a detailed timetable for measures ensuring the cost reduction and enhanced performance of both port authorities and port operators. We will also revise incentives for port operators by adopting a new performance-based model for future concessions and encourage entry of new operators. A review of the overall cost savings for exporters generated through these reforms will be conducted by December 2013.

30. Regulation. A framework law for the functioning of regulators was recently enacted. The law: (i) establishes a regulatory environment that protects the public interest and promotes market efficiency, (ii) guarantees the independence and financial, administrative and management autonomy of the National Regulatory Authorities in the exercise of their responsibilities, including the necessary conditions to safeguard adequate human and financial resources being able to attract and retain sufficiently qualified staff, and (iii) strengthens the role of the Competition Authority in enforcing competition rules. The corresponding amendments to the bylaws of the National Regulatory Authorities will be approved by the Government by end-November. Once the NRA framework law and follow-up bylaws and internal regulations are in place, the regulators will continue to pursue the adoption of best international regulatory practices, including by organizing international peer review exercises.

31. Services. Reforms in the services sector aim at eliminating entry barriers and increase competition. Significant progress has already been made in amending sector-specific legislations to align them with the Services Directive. We expect adoption by Parliament of the remaining necessary amendments—including to the Construction Law—by end-2013, and the related ordinance, ensuring appropriateness of fees linked to construction activities. The new legal framework aiming at improving the functioning of the regulated professions for which regulation involves a professional body (such as accountants, lawyers, notaries) was published earlier this year. The professional bodies' statutes are being amended accordingly for submission by the government to Parliament by yearend, including by eliminating unjustified restrictions to activity and further improving the conditions for mobility of professionals in line with EU Directives in the area of free movement of professionals.

32. Licensing and Administrative Burden. Tackling excessive licensing procedures, regulations and other administrative burdens—which are impeding the establishment, operation, and expansion of firms—is a government priority. Although we have faced delays in some areas due to the recent changes in the government and administrative capacity constraints, we remain strongly committed to meeting our revised timeline. Immediate priorities include: (i) adoption of the New Legal Regime on Urbanism and Building (RJUE) by the time of the tenth program review; (ii) completion of an inventory of the regulatory costs in the economy, starting with the most burdensome, on a basis of which we will devise a roadmap for a regulatory simplification; and (iii) completion of the reforms to simplify licensing procedures in the areas of tourism, commerce and industry. We will step up our efforts to make fully operational the Point of Single Contact, an e-government portal which allows administrative procedures to be done online. The new VAT cash accounting regime will also support an improvement of the business climate.

33. Judiciary. Most of the key judicial reforms have been successfully implemented. In particular, the new Code of Civil Procedure that entered into force on September 1, 2013 will speed up civil and enforcement proceedings. Another key legislation, the Judicial Organization Act, was adopted by Parliament in June 2013, and we have started to take steps to enable a smooth implementation by setting up a task force and adopting a wide range of implementing legislation. With respect to targeted measures to reduce the backlogged enforcement cases, an additional 179,000 enforcement cases have been cleared, bringing down the total number by about 344,000 enforcement cases since November 2011. We will publish quarterly reports on the clearance rate of enforcement court cases from the third quarter 2013 onwards (within four months after the end of the relevant quarter). We will establish the oversight body for enforcement agents and insolvency administrators (CAAJ) shortly after the entry into force of the CAAJ law, which was submitted to Parliament for approval in June 2013. The CAAJ law will enhance the supervision of enforcement agents, and thus further complement reforms implemented under the new Code of Civil Procedure and the new fee structure for enforcement agents, which entered into force on September 1, 2013 to incentivize speedier enforcement proceeding.

Table 1. Portugal: Quantitative Performance Criteria

(Billions of euros, unless otherwise indicated)

	Mar-13		Jun-13		Sep-13	Dec-13	Mar-14
	Program	Actual	Program	Actual			
1. Floor on the consolidated General Government cash balance (cumulative)	-1.9	-1.4	-6.0	-3.8	-7.3	-8.9	-1.7
2. Ceiling on accumulation of domestic arrears by the General Government (continuous indicative target) 1/	0.0	Not met	0.0	Not met	0.0	0.0	0.0
3. Ceiling on the overall stock of General Government debt	182.2	178.5	187.3	184.1	188.9	191.3	193.0
4. Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by the general government (continuous performance criterion)	0.0	...	0.0	...	0.0	0.0	0.0

1/ Domestic arrears for the purpose of the program increased by close to €0.4 billion in the first half of 2013, largely due to the accumulation of arrears by SOE hospitals.

Table 2. Portugal: Structural Conditionality: Seventh Review under the EFF

	Measure	Timing	Status
Prior Actions			
1	Submit to parliament a draf 2014 budget consistent with the general government deficit target of 4 percent of GDP (MEFP ¶4-6)		Met
2	Submit to Parliament a draft Law or a budget provision to implement the single wage scale PER measure.		Met
3	Submit to Parliament a legislative proposal that increases the statutory retirement age to 66 years.		Met
Structural Benchmarks			
A. Fiscal policy			
1	Submit to Parliament a new draft public administration labor law that will aim at aligning current public employment regime to the private sector rules, including for working hours and holiday time, and termination of tenure.	July 15, 2013	Partially Met 1/
2	Submit to Parliament a draft law on the redesigned mobility pool.	End-June 2013	Met 2/
3	Submit to Parliament a legislative proposal that increases the statutory retirement age to 66 years.	July 15, 2013	Changed to prior action
4	Submit to Parliament a legislative proposal that aligns the rules and benefits of the public sector pension fund, CGA, to the general pension regime.	July 15, 2013	Met with delay
A. Strengthen financial stability			
5	Submit to Parliament amendments to the law governing banks' access to public capital.	End-January, 2013	Met
B. Enhance competitiveness and address bottlenecks to growth			
6	Enact the severance pay reform that reduces severance payments to 12 days per year for all new permanent labor contracts	October 1, 2013	Met
7	Update projections of the medium-term energy tariff debt path and identify policy options to eliminate the tariff debt by 2020 .	June 15, 2013	Met
C. Strengthen fiscal institutions and reduce fiscal risks			
8	Revise and submit to Parliament the draft regional and local public finance law.	End-Dec 2012	Met
9	Implement a full-fledged Large Taxpayer Office (LTO), to cover audit, taxpayer services, and legal functions concerning all large taxpayers, including the adoption of account managers.	End-Dec 2012	Met

Notes:

1/ The decree-law aligning working hours of the public sector to 40-hours per week as in the private sector was already submitted and approved by the Parliament. The new draft public administration labor law will be submitted to Parliament by end-October.

2/ The draft law on the redesigned mobility pool was submitted and approved by Parliament. However, it was rejected by the Constitutional Court and has returned to Parliament for amendments.

ANNEX 5
TECHNICAL MEMORANDUM OF UNDERSTANDING

October 24, 2013

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the indicators subject to quantitative targets (performance criteria and indicative targets), specified in the tables annexed to the Memorandum of Economic and Financial Policies. It also describes the methods to be used in assessing the Program performance and the information requirements to ensure adequate monitoring of the targets. We will consult with the EC, the ECB, and the IMF before modifying measures contained in this letter or adopting new measures that would deviate from the goals of the Program, and provide the EC, the ECB, and the IMF with the necessary information for Program monitoring.

2. For Program purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "Program exchange rates" as defined below, with the exception of the items affecting government fiscal balances, which will be measured at spot exchange rate (i.e., the rate for immediate delivery) prevailing on the date of the transaction. The Program exchange rates are those that prevailed on May 5, 2011. In particular, the exchange rates for the purposes of the Program are set €1 = 1.483 U.S. dollar, €1 = 116.8390 Japanese yen, €1.09512 = 1 SDR.

3. For reporting purposes, the MoF and BdP will employ the reporting standards and templates considered to be appropriate given the transmission of data covered by this TMU, unless otherwise stated or agreed with the EC, the ECB and the IMF.

General Government

4. Definition. For the purposes of the Program, the General Government, as defined in the Budget Framework Law, Law No. 91/2001 of August 20, amended by Law 22/2011 of May 20, includes:

4.1. The Central Government. This includes:

4.1.1. The entities covered under the State Budget, which covers the budgets of the Central Administration, including the agencies and services that are not administratively and financially autonomous, agencies and services that are administratively and financially autonomous (Serviços e Fundos Autónomos – SFA).

4.1.2. Other entities, including Incorporated State-owned enterprises (ISOE), or extra-budgetary funds (EBF) not part of the State Budget, but which are, under the European System of Accounts (ESA95) and ESA95 Manual on Government Deficit and Debt rules, classified by the National Statistical Institute (INE) as part of the Central Government.

4.2. Regional and Local Governments, that include:

4.2.1. Regional Governments of Madeira and Azores and Local Governments (Administrações Regionais and Locais);

4.2.2. Regional and local government-owned enterprises or companies, foundations, cooperatives and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government.

4.3. Social Security Funds comprising all funds that are established in the general social security system.

This definition of General Government also includes any new funds, or other special budgetary and extra budgetary programs or entities that may be created during the Program period to carry out operations of a fiscal nature and which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE in the correspondent subsector. The MoF will inform the EC, ECB, and IMF of the creation of any such new funds, programs, entities or operations at the time of its creation or statistical re-classification or, in the case of Regional and Local Governments, at the time the Government acknowledges its creation.

The General Government, as measured for purposes of Program monitoring in 2013, shall not include entities nor operations (including pension funds) that are re-classified into the General Government during 2013, but shall include those reclassified in 2011-12. ([12])

The General Government, as measured for purposes of Program monitoring in 2014, shall not include entities nor operations (including pension funds) that are re-classified into the General Government during 2014, but shall include those reclassified in 2012-13.

5. Supporting Material

5.1. Data on cash balances of the State Budget will be provided to the EC, the ECB and the IMF by the MoF within three weeks after the end of the month. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published by the MoF.

5.2. Data on the cash balances of the other parts of General Government as defined in paragraph 4 ([13]) will be provided to the EC, the ECB and the IMF by the MoF within seven weeks after the end of the month. Data will include detailed information on revenue and expenditure items. Data will also include detailed information on PPP-related revenues and expenditures for those PPP reclassified within the General Government sector according to ESA 95, and called guarantees.

5.3. Data on domestic and external debt redemptions (securities), new domestic and external debt issuance (securities), change in the domestic and foreign currency assets and liabilities of the Central Government at the BdP and other financial institutions will be provided to the EC, the ECB, and the IMF by the BdP within 40 days after the closing of each month.

5.4. BdP will provide to the EC, the ECB, and the IMF detailed monthly data on the financing of the General Government, as defined in ESA95, within seven weeks after the closing of each month.

5.5. Data on the revenues, operating expenses, capital expenditure, remuneration of personnel, EBITDA, and number of staff will be provided for state-owned enterprises (SOEs) on a quarterly basis, within 7 weeks after the end of each quarter. Aggregate data for the SOEs within the perimeter will be provided, with company-specific information for REFER, Estradas de Portugal, Metro de Lisboa, and Metro de Porto. Furthermore data for Comboios de Portugal and Parpública (outside the perimeter) will also be provided.

([12]) An operation refers to part of a legal entity that is involved in the production or delivery of goods and services—including government services provided on a nonmarket basis. As such, it does not include transactions relating to the assets or liabilities of an entity. For example, should an entity handle a number of PPPs, reclassifying only one PPP would be considered as reclassifying an operation. In contrast, taking over part of an entity's debt by the government would not qualify for the exclusion. On this issue, see also paragraph 13.

([13]) In 2011, data exclude regional and local government-owned enterprises or companies, foundations, cooperatives and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government, i.e., entities referred in paragraph 4.2.2.

QUANTITATIVE PERFORMANCE CRITERIA, INDICATIVE CEILINGS, AND CONTINUOUS PERFORMANCE CRITERIA: DEFINITIONS AND REPORTING STANDARDS

A. Floor on the Consolidated General Government Cash Balance (Performance Criterion)

6. Definition. The consolidated General Government cash balance (CGGCB) is defined as the sum of the cash balances of the entities covered by the State Budget, the ISOE, the Regional and Local Governments, and the Social Security Funds, and other entities and EBFs, as defined in paragraph 4. Privatization receipts will be excluded from cash receipts. In 2012 and beyond, revenues from the reclassification of pension funds into the general government will not be accounted for as cash revenues for the purpose of the calculation of the consolidated general government cash balance. In 2012-13, the cash proceeds from the sale of the ANA airport concession will be accounted for as cash expenditure-reducing transactions. The net acquisition of financial assets for policy purposes, including loans and equity participation will be recorded as cash expenditures, except for transactions related to the banking sector support and restructuring strategy under the Program. Called guarantees (excluding those related to the banking sector support and restructuring strategy), where entities of the General Government make cash payments on behalf of entities that are not part of the General Government, will be recorded as cash expenditures.

6.1. The Cash Balance of the State Budget. The cash balance of the State Budget will be measured from above the line, based on budget revenues (recurrent revenue plus nonrecurrent revenue, including EU revenues, minus tax refunds) minus budget expenditures of the State Budget as published monthly on the official website of the DGO of the MoF, and in line with the corresponding line items established in the State Budget. Budget expenditures will exclude amortization payments but include salaries and other payments to staff and pensions; grants to Social Security Funds, medical care and social protection; operational and other expenditure, interest payments; cash payments for military equipment procurement; and EU expenses.

6.2. The Cash Balance of the Regional and Local Governments, Social Security Funds, ISOE and Other Entities or EBFs. The cash balance of each of these parts of the General Government will be measured from above the line, based on revenues minus expenditures as it will be provided by the DGO of the MoF in the monthly General Government budget execution report (see Para 5), and in line with the corresponding line items established in their respective budgets. All entities including ISOE that prepare accrual-based financial statements will submit monthly cash flow statement in accordance with form and content specified by the MoF. The reporting by Local Government will be phased as set out in paragraph 8 below.

6.3. Adjustor. The 2013 and 2014 quarterly floors on the consolidated general government cash balance will be adjusted for the cumulative amount of arrears settled in the context of the arrears clearance strategy: (i) health sector arrears (up to €432 million), (i) local government arrears settled through the €1 billion credit facility created in May 2012, and (ii) RAM government arrears subject to concluding the agreement with the central government (up to €1.1 billion).

Other Provisions

7. For the purpose of the program, the expenditure of the central government that is monitored excludes payments related to bank support, when carried out under the program's banking sector and restructuring strategy. However, any financial operation by central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to the EC, ECB, and IMF.

8. Quarterly consolidated accounts for the General Government on a cash basis will be reported for internal, EC, ECB, and IMF monitoring 7 weeks after the reference period, starting with the first quarter

of 2012. The reports will be published externally starting with December 2011 data. SOEs will be consolidated with the general government accounts starting with the first quarter 2012. The larger municipalities (defined as those with a population of 100,000 voters or more) are required to provide monthly reports under current arrangements, and their cash balance will be included in the calculation of the monthly cash General Government balance. The cash balance of the smaller municipalities, i.e. those with a population of under 100,000 voters, will be excluded until any necessary legal changes requiring them to provide monthly reports have been put in place. In this transitory period, the MoF will provide a monthly estimate of the cash balance of these smaller municipalities excluded from the General Government reports to the EC, the ECB, and the IMF.

9. Supporting Material

9.1. Data on cash balances of the State Government, ISOEs, Regional and Local Government and Social Security Funds will be provided to the EC, the ECB and the IMF by the MoF within seven weeks after the end of each month. The information provided will include general government net acquisitions of financial assets for policy purposes, including loans and equity participations, as well as called guarantees where entities that are part of the General Government make cash payments on behalf of entities that are not part of the General Government.

9.2. The MoF will submit quarterly data on General Government accounts determined by the INE in accordance with ESA 95 rules, showing also the main items of the transition from cash balances to the General Government balances in national accounts. The reconciliation will be accompanied by necessary explanatory materials for any indication of potential deviation of the annual general government cash target from the annual general government accrual target determined in accordance with ESA 95 rules.

B. Non-Accumulation of New Domestic Arrears by the General Government (Continuous Indicative Target)

10. Definitions. Commitment, liabilities, payables/creditors, and arrears can arise in respect of all types of expenditure. These include employment costs, utilities, transfer payments, interest, goods and services and capital expenditure. Commitments are explicit or implicit agreements to make payment(s) to another party in exchange for that party supplying goods and services or fulfilling other conditions. Commitments can be for specific goods and services and arise when a formal action is taken by a government agency, e.g., issuance of a purchase order or signing a contract. Commitment can also be of a continuing nature that require a series of payments over an indeterminate period of time and may or may not involve a contract, e.g. salaries, utilities, and entitlement payments. Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources (usually cash) embodying economic benefits or service potential. In relation to commitment, the liability arises when a third party satisfies the terms of the contract or similar arrangement. Payables/creditors are a subset of liabilities. For the purposes of the program payables/creditors exclude provisions, accrued liabilities. Arrears are a subset of payables/creditors. For the purposes of the Program domestic arrears are defined as payables/creditors (including foreigner commercial creditors), that have remained unpaid for 90 days or more beyond any specified due date (regardless of any contractual grace period). In case no due date is specified, arrears are defined as payables/creditors that have remained unpaid for 90 days or more after the date of the invoice or contract. Data on arrears will be provided within seven weeks after the end of each month. The continuous indicative target of non-accumulation of new domestic arrears requires that the total arrears at the end of any month are not greater than the corresponding total at the end of the previous month—based on the same perimeter with respect to the entities covered. This also includes arrears that are being accumulated by the SOEs not included in the General Government.

11. Supporting Material. The stock of arrears will be measured through a survey. Reports on the stock of arrears of the General Government are being published monthly. The MoF will provide

consistent data on monthly expenditure arrears of the General Government, as defined above. Data will be provided within seven weeks after the end of each month and will include total arrears classified by the different constituent sectors of the General Government sub-sector as defined in paragraph 4, as well as the monthly amounts of arrears cleared under the arrears clearance strategy (see paragraph 6.3).

12. Adjustor. In 2013 and 2014, the monthly change in the stock of arrears will be adjusted for any stock adjustment related to the arrears clearance strategy as per paragraph 6.3. This will allow monitoring the underlying flow of new arrears.

C. Ceiling on the Overall Stock of General Government Debt (Performance Criterion)

13. Definition. The overall stock of General Government debt will refer to the definition established by Council Regulation (EC) No 479/2009 of 25 May 2009 on the application of the Protocol on the Excessive Deficit Procedure annexed to the Treaty establishing the European Community. For the purposes of the Program, the stock of General Government debt will exclude: (i) debt contracted for bank restructuring, when carried out under the Program's banking sector support and restructuring strategy; (ii) IGCP deposits; and (iii) (from end-September 2011) the 'prepaid margin' on all EFSF loans.

14. Adjusters. For 2013, the ceiling of the overall stock of General Government debt will be adjusted upward (downward) by the amount of any upward (downward) revision to the stock at end-December 2012 general government debt of EUR 204.5 billion. From 2014 onwards, the ceiling of the overall stock of General Government debt will be adjusted upward (downward) by the amount of any upward (downward) reclassification of entities or operations that affects the stock at end-December of the previous year.

15. Supporting Material. Quarterly data on the total stock of General Government debt as defined in paragraph 12 will be provided to the EC, ECB, and IMF by the BdP no later than 90 days after the end of each quarter, as reported to the ECB and the Eurostat. Monthly estimates will be provided to the EC, ECB and IMF by BdP no later than seven weeks after the end of each month.

D. Non-Accumulation of New External Debt Payments Arrears by the General Government (Continuous Performance Criterion)

16. Definition. For the purposes of the Program, the definition of debt is the same as in paragraph 12. An external debt payment arrear will be defined as a payment on debt to nonresidents, contracted or guaranteed by the general government, which has not been made within seven days after falling due (taking into account any applicable contractual grace period). The performance criterion will apply on a continuous basis throughout the Program period.

17. Supporting Material. Any external debt payment arrears of the General Government will be immediately reported by the MoF.

E. Bank Solvency Support Facility

18. The dedicated Bank Solvency Support Facility (BSSF) account will be maintained at the Bank of Portugal. As per previous review, resources for the BSSF will be agreed at each review and deposited in the dedicated account.

F. Overall Monitoring and Reporting Requirements

19. Performance under the Program will be monitored from data supplied to the EC, the ECB, and the IMF by the MoF and BdP. The authorities will transmit to the EC, ECB, and IMF any data revisions in a timely manner.

ANNEX 6

INDICATIVE TIMELINE

Indicative timeline of financial sector and structural measures in the Memorandum of Understanding on specific economic conditionality ([14])

Actions for the tenth review (to be completed by end Q3-2013 or by the tenth review)	
Fiscal structural	**[3.3]** Reduce the number of budget entities. **[3.13]** Utilise the annual PPP report as input to the fiscal risks assessment for the budget. **[3.28]** Revise the proposal of the Requalification Law.
Health care system	**[3.31]** Reduce the employer's contribution rate by 1.25% in 2014 and add an adjustment in the scope of health benefits. **[3.44]** Make the web-portal with publicly available information on hospital services fully operational. **[3.46]** Define the service portfolio for NHS hospitals and the detailed strategic 3-year plans for hospitals.
Goods and services markets	**[5.3]** Analyse the consequences of the report on the CMEC scheme and the hydro power plants related issues; assess the need for potential measures. **[5.5]** Provide a report on action with regard to new contracts in renewables and alternative mechanisms for mature technologies, also on future investments in renewables. **[5.6]** Finalise the conclusion of the universal service contracts awarded through the tenders. **[5.8]** Follow the transposition of the Third Postal Directive by further liberalising the postal sector and renegotiating the contract with CTT. **[5.11 vi]** Ensure that the main terminals owned by CP Carga are transferred to another entity that will guarantee non-discriminatory access to all rail freight operators. **[5.12 iii]** Deliver policy decisions and take actions, including those that foster the renegotiation of the existing port operation concessions. **[5.12 iv]** Present an exhaustive action plan assessing the forthcoming steps in the reform of ports. **[5.15 i]** Adapt the content and information available at the PSC in line with the Services Directive and make available online forms and procedures for these regimes. **[5.15 ii]** Adapt the content and information available at the PSC for the outstanding regimes approved to ensure conformity with the Professional

([14]) Square brackets identify paragraph numbers in the MoU as signed on 21 November 2013.

Actions for the tenth review (to be completed by end Q3-2013 or by the tenth review)	
	Qualifications Directive and make available online forms and procedures.
Judicial system	**[7.1]** Start the assessment on the clearance rate of enforcement court cases, the first report will be published four months after. **[7.5]** Complete the already submitted report with more up-to-date on the revised Public Procurement Code and further assessment of the role of the Court of Auditors in ensuring compliance with public procurement rules. **[7.8]** Establish an optional VAT cash accounting regime.
Licensing	**[7.11]** Adopt a rule that makes mandatory when creating a new regulation generating costs for businesses to eliminate existing regulation with equivalent cost. **[7.12 ii]** If feasible, put in place the rule that prohibits at all levels of government the creation of the new regulation generating costs for businesses without the elimination of an existing regulation. **[7.12 iii]** Review the legal regimes of the Territorial Management Instruments (RJGT) and of the related regulations. **[7.12 iv]** Adopt a legal provision for the regularisation of activities not in accordance with Territorial Management Instruments. **[7.12 v]** Harmonise the Regional Plans. **[7.12 vi]** Review the Legal Regime for Urbanism and Building (RJUE). **[7.14 i]** Approve regulations on zero licensing procedures on licensing procedures for Type 1 and 2 industries. **[7.14 ii]** Define and establish the Zones of Responsible Enterprises (ZER). **[7.16 i]** Review the legal regime concerning the licensing of mining and geological production and investment in line with international best practices. **[7.16 ii]** Simplify the legal and bureaucratic procedures pertaining to mining and geological investments. **[7.17 i]** Eliminate or transform into a voluntary regime the mechanism of prior communication in the Regime for Urbanism and Building and simplify the legal regime for touristic establishments. **[7.17 ii]** Expand the range of expos control mechanisms in urban operations. **[7.17 iii]** Simplify and increase transparency of the requirement on the classification of the several types of touristic establishments.

Actions for the tenth review (to be completed by end Q3-2013 or by the tenth review)	
	[7.17 iv] Review the sanction legislation, giving more powers to ASAE.

Actions for the eleventh review (to be completed by end Q4-2013or by the eleventh review)	
Financial sector	**[2.8]** BdP must implement a survey of the Portuguese regulatory framework, as part of the special assessment of banks' operational capacity. **[2.9]** Expand quarterly stress tests with new techniques such as a new top-down stress test. **[2.13]** Submission to the BdP of the recovery plans by the non-largest banks. **[2.15]** Enhance the data coverage of the Central Credit Registry (CCR), permit access by the financial institutions to information on new clients after authorisation of the Portuguese Data Protection Authority (CNPD) and to disclose information by firms, voluntarily, in the Central Balance Sheet Database (CBSD). The two last referred issues must be reflected in a preliminary report. **[2.18 iii]** Prepare a draft of the necessary amendments of the rules governing the commercial paper market. **[2.19 ii]** Revise the roadmap for improving the governance of the National Guarantee System (NGS) by implementing measures to enhance loan and guarantee pricing in favour of end of users.
Fiscal structural	**[3.7]** Conduct a review of the Budget Framework law (BFL), publishing a report assessing the law and providing suggestions to modify if necessary. **[3.8]** Prepare a draft action plan for the BFL. **[3.15]** Implement a study of SOEs with similar characteristics as the comprehensive review of wage scales in the general government. **[3.18]** Evaluation of the possible binding offers to privatise Correios de Portugal (CTT). **[3.19 i]** Reduce the number of municipal offices by at least 25 per cent in 2013. **[3.19 ii]** Increase the resources devoted to auditing in the tax administration to at least 30 per cent of the total staff. **[3.19 iii]** Publish quarterly reports on duration and costs of tax cases within four months after the end of the relevant quarter. **[3.20]** Prepare an evaluation report assessing the reform of the VAT e-invoicing system.

Actions for the eleventh review (to be completed by end Q4-2013or by the eleventh review)	
	[3.21 i] Make a report analysing the current tax compliance situation. **[3.23 i, ii]** The Inter-ministerial Group on Territorial Affairs will present a report identifying inefficiencies and proposing solutions to cope them. **[3.24 i]** Complete the implementation of the strategy of shared services in the area of financial resources (GeRFIP) in central and regional administrations. **[3.26]** Include in the 2014 Budget Law the rules adjusting the single wage scale in the public administration and the monthly compensation paid. Publish a report on a more comprehensive reform of wage supplements. **[3.27]** Converge the system of social protection for staff in the Regime de Proteção Social Convergente (RPSC) to the pension rules of Regime Geral de Segurança Social. **[3.29]** Present to the Parliament a new public administration law.
Health care system	**[3.30]** Additional revenues of EUR 50 million due to improvements in the billing and collection of revenues. **[3.36]** Publish a follow-up report on implementation of the prescription by International Non-proprietary Name (INN). **[3.41]** Monitor NHS spending with private providers, encourage competition among private and between private and public providers and take measures to ensure competition in the pharmacies sector. **[3.47]** Update the inventory of all health staff and prepare annual reports presenting plans for the allocation of human resources in the period up to 2014. **[3.48]** Reduce overtime compensation by further 20% in 2013, by applying new payment scales for overtime and increasing mobility. **[3.49]** The Regional Health Authorities (ARSs) must finalise the new internal control procedures.
Labour market	**[4.4 iii]** Prepare an independent review on the desirability of shortening the survival of contracts that are expired but not renewed and present a summary of the system of survival of collective agreements. **[4.5]** Provide specific measures to strengthen the role of the job counselling and job search assistance as well as the activation and sanctions systems in facilitating the transition from unemployment to employment. **[4.6 ii (ii)]** Define and implement a simple funding framework comprising performance and evaluation criteria for public schools at the secondary education level. **[4.6 ii (iii)]** Report on possible further improvements of the new inspection model

Actions for the eleventh review (to be completed by end Q4-2013or by the eleventh review)	
	for secondary schools. **[4.6 iii (iii)]** Establish "professional schools of reference".
Goods and services markets	**[5.2]** Present additional cost reduction measures to eliminate excess rents and the tariff debt by 2020. **[5.4]** Revise the remuneration scheme for co-generation to ensure efficiency and competitiveness in the electricity market. **[5.9 iv]** Reform the transport and infrastructure's regulatory framework. **[5.10]** Present a long term vision of the transport system and a list of actions to improve its efficiency and sustainability. **[5.11 i]** Ensure that the rail regulator follows independence requirements by the EU rail directives and its regulatory mandate is fulfilled. **[5.11 iii]** Ensure Public Service Obligation (PSO) contracts on rail passenger transport respect EU legislation assess the state contributions and develop a proper administrative capacity. **[5.12 i]** Present a review of the port work law. **[5.12 ii]** Ensure that the relevant regulator for ports has sufficient financial and administrative resources to carry out its function. **[5.13]** Complete the adoption of Construction Laws and other outstanding sectoral amendments and submit them to the Parliament. Proportionality of fees linked to construction activities will be ensured after adoption of the Construction Law. **[5.14]** Submit to Parliament the professional bodies' amended statutes. **[5.15 iii]** Extend PSC to services not covered by the Services Directive. **[5.15 iv]** Expand the "Zero Authorisation" project to other services sectors of the economy.
Housing market	**[6.2]** Publish a comprehensive review of the functioning of the housing market.
Judicial system	**[7.4]** Approve the amendment to the bylaws of the National Regulatory Authorities. **[7.6]** Assess the impact of the procedures for requesting VAT exemptions for exporting firms and the simplification of indirect exports. **[7.12 i]** Base Law of Soil and Territorial and Urbanism Planning (Lei dos Solos) must be aligned with the new Industrial Licensing regime.

Actions for the eleventh review (to be completed by end Q4-2013or by the eleventh review)	
	[7.13 i] Implement a Legal Regime of Land Registration (registo cadastral). **[7.13 ii]** Create a diploma on Land Registration and Land Registration Experts. **[7.13 iii]** Review the cartography for plans regime and the diploma on Cartography. **[7.13 iv]** Enforce the Council of Ministers Resolution 56/2012. **[7.15]** Review the commercial licensing regime.

Actions for the twelfth review (to be completed by end Q1-2014, end Q2-2014 or by the twelfth review)	
Financial sector	**[2.19]** Implement measures included in the National Guarantee System (NGS) roadmap.
Fiscal-structural	**[3.6]** Publish a fiscal strategy document for the general government (April 2014). **[3.7]** Submit to Parliament the draft of the Budget Framework law (BFL). **[3.8]** Finalise the draft action plan of the BFL. **[3.18]** Modify regulation in order to sale the waste management company (EGF), the sale will depend on the different binding offers. **[3.19 i]** Reduce the number of municipal offices by 25% in 2014. **[3.22]** Review public financial support to private associations. **[3.24 ii]** Conclude the roll-out to the Tax Authority (May 2014). **[3.26]** Rules adjusting the single wage scale in the public administration and the monthly compensation paid must be effective. **[3.29]** New public administration rule must be effective.
Health care system	**[3.40]** INFARMED must finish the national formulary. **[3.45]** Implement a central accounting platform for at least up to 20 of them. **[3.46]** Negotiate and sign "Contratos Programa" for SOE hospitals for 2014.
Goods and services markets	**[5.1]** Implement the plan to create a new gas and electricity logistics operator independent company. **[5.11 iv]** Present an assessment of the impact of the extended performance

Actions for the twelfth review (to be completed by end Q1-2014, end Q2-2014 or by the twelfth review)	
	schemes on infrastructure charges in different traffic categories. **[5.11 v]** Continue to prepare the privatisation of the freight branch of the state-owned rail operator.
Judicial system	**[7.8]** Assess the impact of the optional VAT cash accounting regime.
Licensing	**[7.10]** Carry out an inventory and an analysis of the costs of regulations.