

Economic Watch

Portugal | Growth is upheld, but there are signs of a slowdown

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Portugal's GDP underwent a surprise rise in the second quarter of the year with a growth of 0.6% QoQ (2.4% YoY), in line with the revision of the 2016 and 2017 figures published by the INE. This progress was mainly due to an increase in gross capital formation and an improvement in the external sector, and despite weak growth in domestic final consumption. This growth translated into an increase in employment, albeit a smaller increase than in the previous quarter.

Based on the indicators available so far, **BBVA Research estimates that growth in 3Q18 will be approximately 0.3% QoQ SWDA¹** (see Figure 1). This forecast would be the result of the continuation of the trend towards moderate growth in consumption observed in recent quarters, together with the foreseeable weakening of the external sector as a result of the slowdown in European growth.

Growth in Portuguese households' consumption stagnated in 2Q18

Growth in Portugal's GDP continued to be strongly underpinned by domestic demand, which contributed +0.5 pp to growth in 2Q18, 0.2 pp less than in the previous quarter, whereas net external demand added 0.1 pp to GDP (-0.3 pp in 1Q18, see Figure 2).

In contrast with what we saw in the first quarter of the year, gross capital formation, which grew by +2.3% QoQ in 2Q18, compared with +1.2% QoQ in 1Q18, was the component making the biggest contribution to GDP growth — 0.4 pp, 0.2 pp more than in 1Q18. Investment support for GDP growth was due to changes in inventories and investment in machinery and equipment, each contributing +0.2 pp. Overall gross fixed capital formation grew 1.3% QoQ, 0.6 pp more than was observed in 1Q18, with increases in investment in machinery and equipment and transport equipment (+4.3% QoQ and 2.0% QoQ respectively) and a fall in investment in construction -0.3% QoQ in 2Q18.

Meanwhile, **private consumption had a slight quarter-on-quarter increase of +0.1% in 2Q18 (2.3% YoY)** following the +0.6% QoQ observed in the previous quarter. Although the contribution of public consumption remains insignificant — in 2Q18 it grew by 0.3% QoQ (0.9% YoY, see Figure 3).

The external sector picks up in 2Q18 and contributes positively to growth

In 2Q18, exports grew 2.3% QoQ (1.7 pp more than in 1Q18) in real terms², while imports grew 2.0% QoQ (0.9 pp more than in 1Q18). Thus, contrary to what was observed in the first quarter, net external demand contributed positively to the growth of the Portuguese economy in the amount of +0.1 pp in 2Q18. Exports and imports of services revealed the largest increases during the period, +3.1% QoQ and +2.7% QoQ respectively. Exports of mineral products made the most significant contribution (+2.1 pp) to growth in nominal exports of goods, while the most important contributors to growth in imports in the second quarter were machinery and mechanical and electronic equipment.

1: Seasonally and working-day adjusted (SWDA) data.
2: Chain-linked volume data (reference year = 2011).

The unemployment rate fell to 2002 levels, boosted largely by job creation in the agricultural and manufacturing sectors

Portugal continued to create employment in the second quarter of the year, albeit at a slower pace: **+0.4% QoQ SWDA (+2.7% YoY)**. The biggest contribution (0.6 pp) to the quarter's growth came from the agriculture, forestry and fisheries sector, which was followed by the service sector (0.4 pp). Hiring by the manufacturing industry recovered from the 0.8 pp QoQ decline seen in the first quarter of the year, and contributed 0.4 pp in 2Q, mainly due to the 3.9% QoQ increase in employment in the construction sector (as against the decline of 3.9% QoQ in 1Q18). Thus, **the unemployment rate fell by 0.7 pp to 7.0% in 2Q18, the lowest level since 2002** (see Figure 4).

3Q18: Growth could be around 0.3% QoQ

Third quarter data available to date point to a **moderation in Portugal's GDP growth, which is expected to be around 0.3% QoQ for 3Q18**.

One of the factors behind this scenario is **weakening of the external sector**, which in turn reflects the slowdown in growth in Europe, the presence of protectionist risks and the increased price of oil. This could lead to shrinkage in exports of goods, despite the second quarter's surprising upside. **In July 2018 exports fell by 1.4% month-on-month SWDA** (in June they had increased by 2.6% MoM), while imports fell by 6.5% MoM SWDA after increasing by 12.2% MoM in June. Even so, in year-on-year terms both exports and imports of goods continued to grow, by 13.0% and 11.0% respectively (see Figure 5).

The tourism sector for its part is also showing signs of slowing. **Seasonally adjusted tourist arrivals stagnated in July** after falling by 0.9% MoM SWDA in June, with **average QoQ falls of 0.3% SWDA during the first half of the year**. As a result, overnight stays in hotels in 2Q18 fell by 5.7% QoQ SWDA (in 1Q18 they had increased by 0.4%), mainly due to the 6.9% QoQ decline in foreign guests, while the decline in resident guests was a mere 1.3% QoQ.

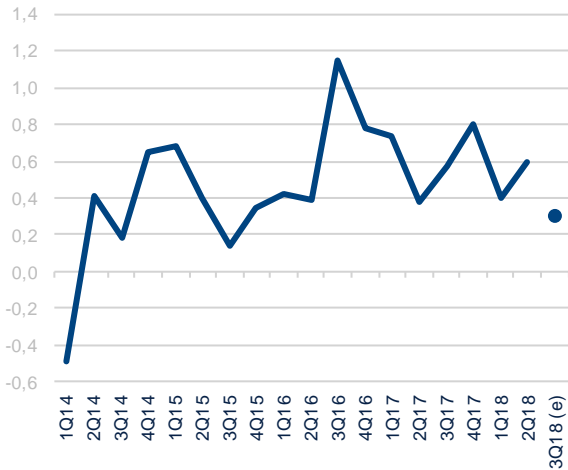
Apart from this, most indicators point to a possible slowdown in household spending. Firstly, the data referring to the employment growth rate reflect a slight fall in August -0.1% m/m corrected for seasonality (-0.2% m/m Jul-18), while the unemployment rate held steady at 6.8%. In addition, **retail sales fell once more in July — by 1.0% MoM SWDA**, after falling by 1.6% MoM in June and following the sharp (4.8% MoM) increase seen in May, although they are still ahead of those of the same period of last year (see Figure 6). **The positive trend observed in consumer confidence since May 2017 was reverted**. However, in contrast with this, **new consumer credit transactions with households grew in nominal terms by 23.2% YoY in June 2018** (22.2% YoY in real terms), having posted double-digit year-on-year growth rates since October 2017, except for March (7.6% YoY) (see Figure 7).

In the manufacturing sector, **the machinery and equipment production index fell by 11.00% MoM SWDA in July**. Its month-on-month trend has been negative since April 2018, but even so it has accumulated double-digit year-on-year growth rates since May 2017 (July 2018 5.5% YoY, see Figure 8). As for manufacturing industry's confidence, it increased by 1.5% MoM SWDA in August 2018, but is below the levels seen in 2S17 and 1Q18.

Lastly, **new lending to non-financial undertakings increased considerably in April compared with the same month last year**. Loans of up to €1 million increased by 18.4% YoY, ending 2Q18 with growth of 9.5% QoQ, while loans of more than €1 million increased by 46.6% YoY in April 2018 (in 2Q18 they had decreased by 5.6% QoQ).

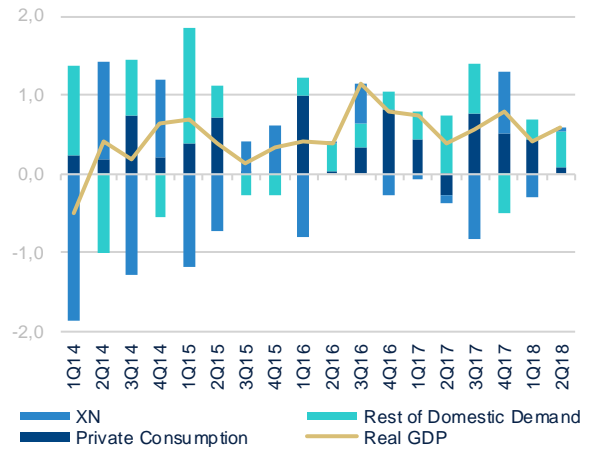
Main activity indicators

Figure 1 MICA-BBVA: GDP growth (% QoQ) and forecasts



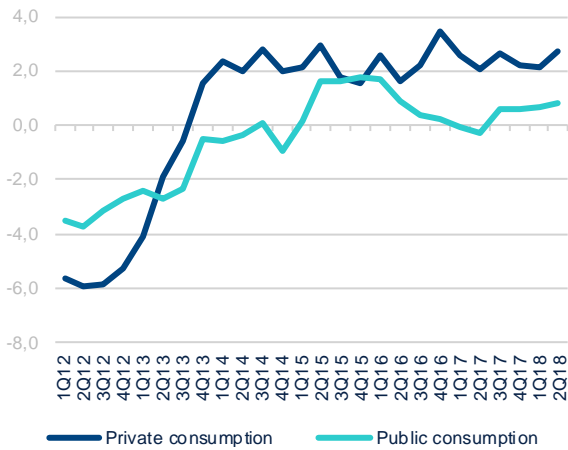
Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 2 GDP (% QoQ) and contribution by components (pp)



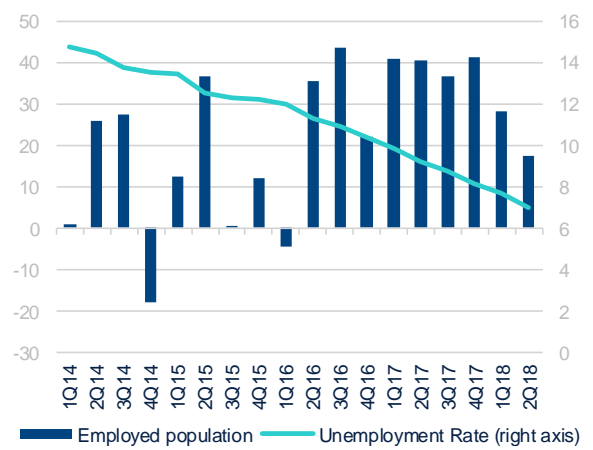
Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 3 Trends in public and private consumption (% YoY)



Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 4 Number of people in employment (quarterly change in thousands of persons) and unemployment rate (%)



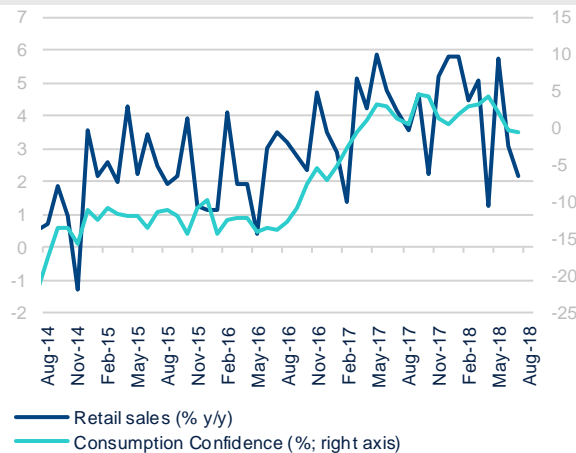
Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 5 Indicators associated with the external sector (% YoY)



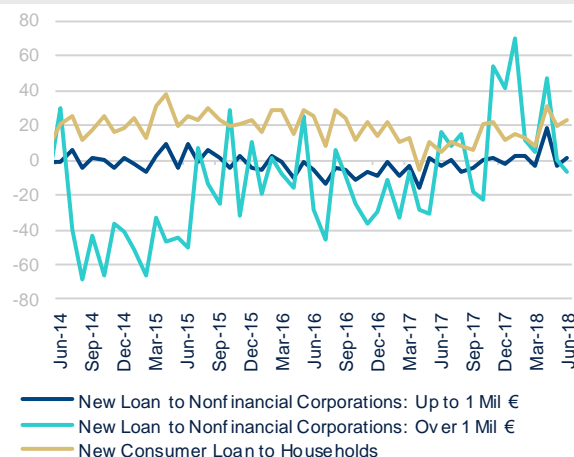
Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 6 Indicators associated with consumption



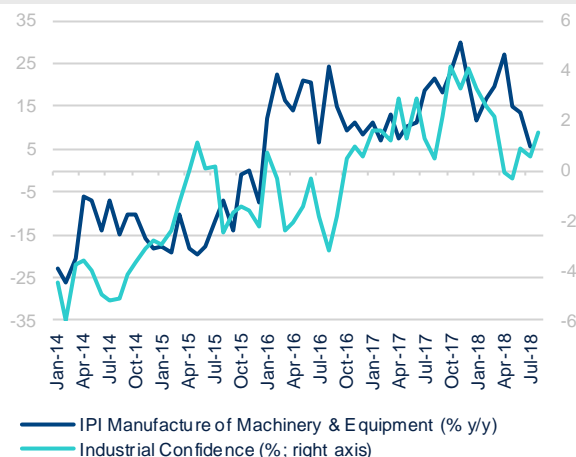
Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 7 New lending to businesses and households (% YoY)



Source: BBVA Research based on INE (Spanish Office of National Statistics) data

Figure 8 Indicators associated with industry



Source: BBVA Research based on INE (Spanish Office of National Statistics) data

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