BBVA Research

Portugal Economic Outlook

2Q20

Creating Opportunities

Key messages

- A global recession is inevitable as a result of the containment measures implemented to curb the spread of the coronavirus. This is a global shock with very clear negative effects and a high degree of uncertainty.

- In Portugal, GDP could fall by about 6.5% in 2020, and the unemployment rate could exceed 10%, although uncertainty is particularly high, especially in relation to the duration of the restrictions imposed and their impact on different sectors. There are many scenarios that are still possible under reasonable assumptions.

- Although GDP growth could reach 4.9% in 2021, the level of activity observed before the crisis is not expected to recover until 2022. The speed of recovery will be limited by the high level of job destruction and exposure to particularly affected sectors.

BBVA Research

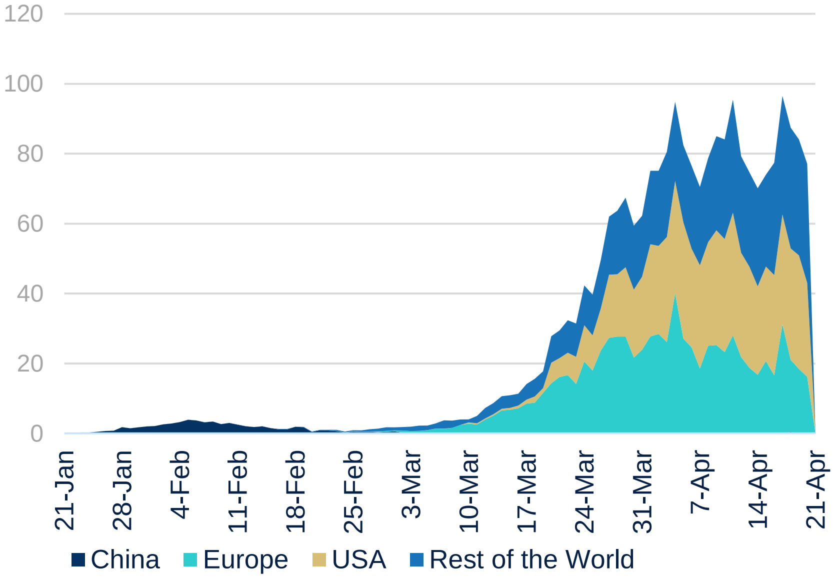
01

Global Economic Outlook 2Q20

Creando Oportunidades

In addition to the cost in human lives, the expansion of COVID-19 from east to west entails a recession for the world economy

DAILY CASES OF COVID-19 (*)
(THOUSANDS OF PEOPLE)



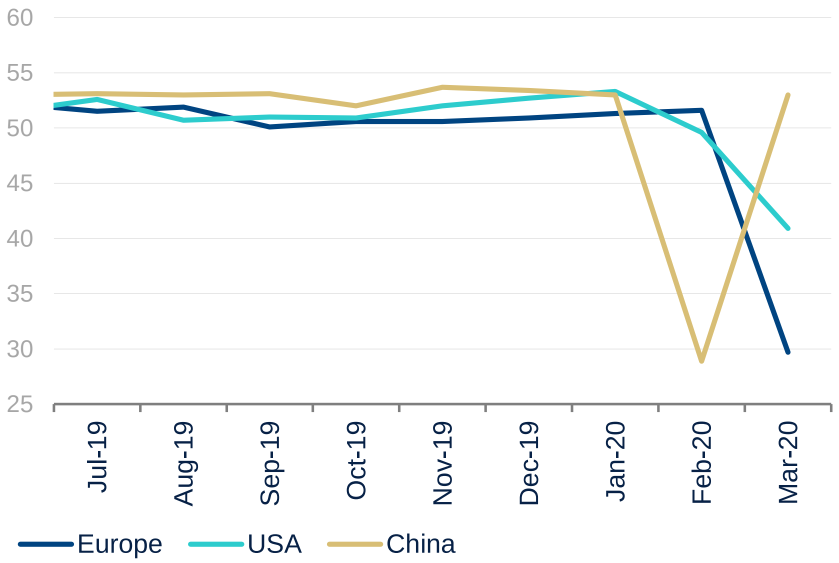
(*) Europe includes Italy, Spain, Germany, France and the United Kingdom.
Source: BBVA Research based on data from John Hopkins University.

- COVID-19 has directly affected more than 2 million people since its outbreak in China in mid-January.
- In Asia, the initial expansion is currently under control.
- In Europe, it has advanced with intensity and is currently in the remission phase.
- America is the focus right now, especially USA, where the outbreak seems to be reaching a peak.

The activity indicators already show the highly contractive effects of COVID-19 in the main geographical areas

PMI INDICATORS

(MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)

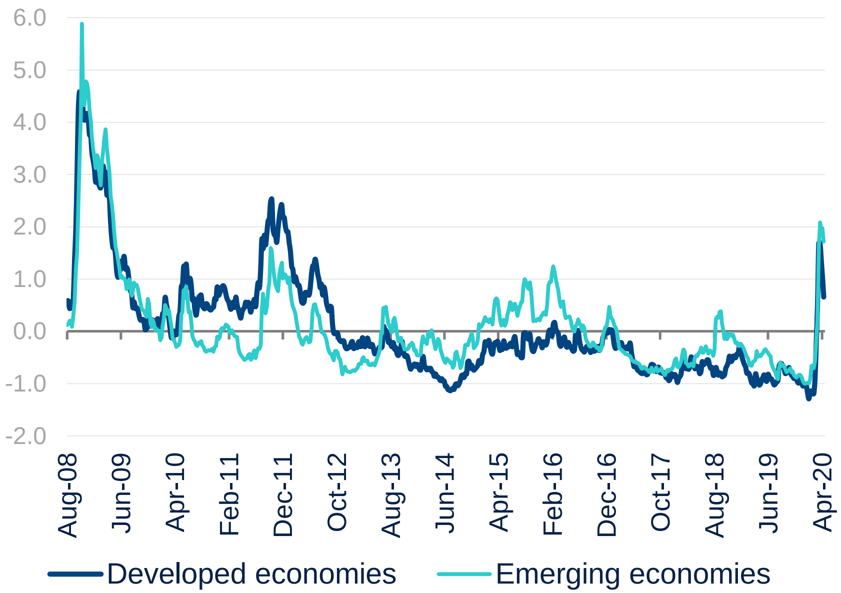


Source: BBVA Research based on Haver.

- The supply shock due to confinement is the main channel of impact in the very short term.
- Other channels:
  - Demand (confidence, social consumer goods).
  - Financial (cost of financing, financial wealth destruction).
  - Other supply shocks (global value chains).
- Confidence and employment indicators show a very severe impact in 2Q20.
- In China, there are already signs of a rapid recovery in activity.

Financial tensions have escalated rapidly, but there are signs of moderation after central bank actions

BBVA RESEARCH INDEX OF FINANCIAL TENSIONS
(AVERAGE FROM 2006 = 0)

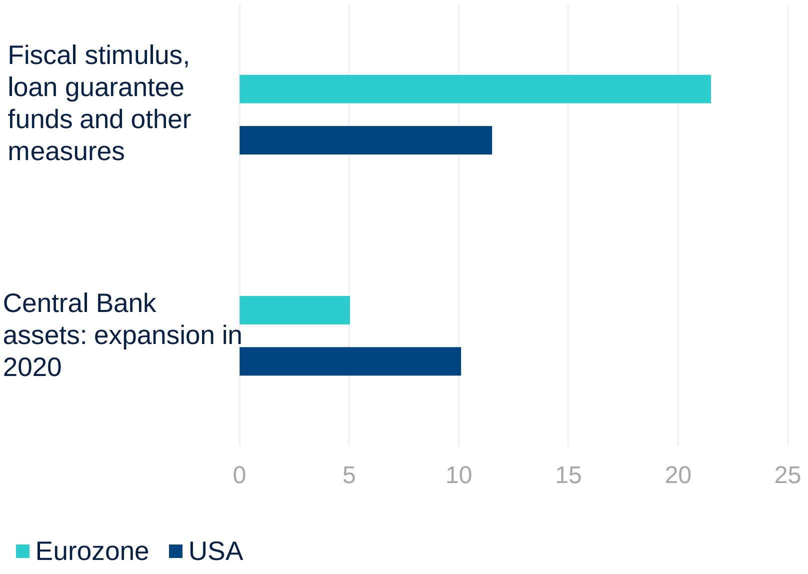


Source: BBVA Research

- Sharp and widespread financial tensions without reaching 2008 levels:
    - Stock market falls from very high levels.
    - Record levels of volatility.
    - US Dollar shortages.
    - Increase of corporate risk (especially high-speculative debt).
    - EMs: currency depreciations, rebound in risk premia, outflows.
    - Enlargement of peripheral risk premia.
- This time, unlike the 2008-09 financial crisis, the banking system has not been a source of specific concerns.
- The rapid and aggressive action of central banks has limited financial deterioration.

Massive stimulus measures are being put in place to limit the impact on activity and prevent disruptions in financial markets

STIMULUS MEASURES: EUROZONE AND USA (*)
(% OF GDP)



(*) Nominal GDP data for 2019 has been used for the calculations. The expansion of central bank assets includes information up to April 10th for the ECB and until April 13th for the Fed.
Source: BBVA Research based on data from the EU, the ECB and the Federal Reserve.

Aggresive and immediate stimulus

- USA:
  - Significant fiscal package.
  - Fed: rate cuts, reinforcement of QE, multiple credit and liquidity facilities.
- Eurozone:
  - Fiscal stimulus at a national and EU level (ESM, EIB, Commission's unemployment insurance scheme).
  - ECB: new QE program (PEPP, more flexible).
  - Very relevant loans guarantee funds.

High uncertainty: we anticipate a deep recession with a rapid but incomplete recovery

Main assumptions of our economic scenario

EXPANSION OF COVID-19

China, Italy and Spain as a benchmark for the evolution of new cases

No new cycles of widespread contagion

CONFINEMENT MEASURES

Around 6 to 8 weeks

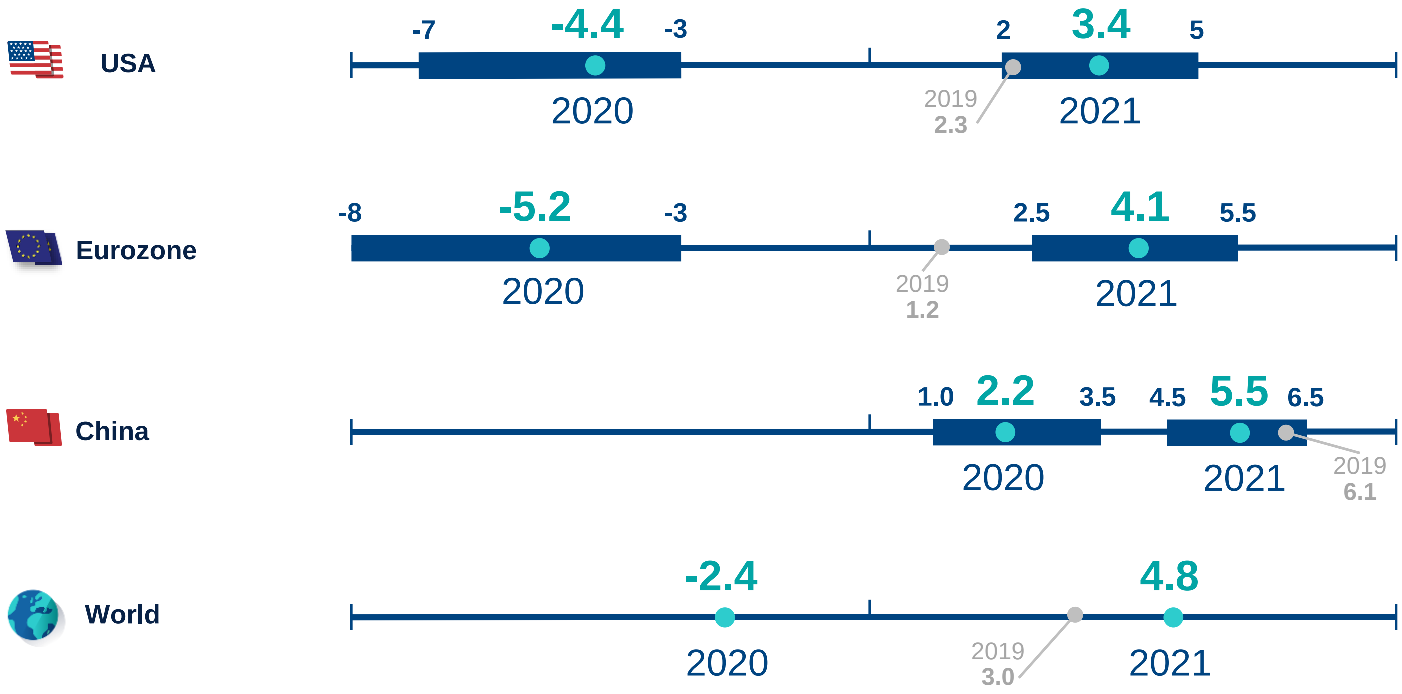
Gradual reversal

ECONOMIC STIMULUS MEASURES

They will be maintained or amplified

High effectiveness (real and financial)

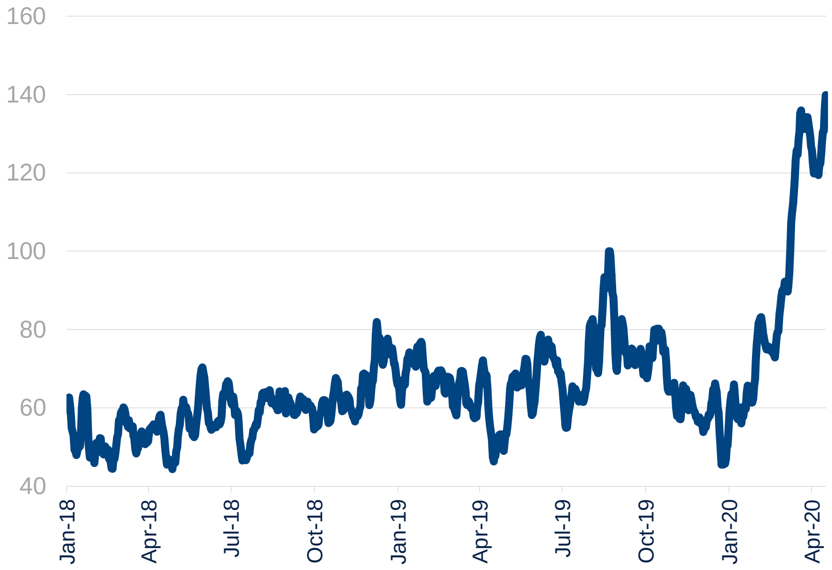
Growth forecasts: a global recession in 2020, followed by a partial recovery in 2021



GDP growth in %. Forecasts for 2020 and 2021
Source: BBVA Research

Uncertainty is exceptionally high and the balance of risks is skewed downwards

ECONOMIC UNCERTAINTY INDEX (*)
(AUGUST 21st 2019 = 100)



(*) Weighted average sentiment of media news where the associated "economy" and "uncertainty" topics appear and weights it by the coverage of these news.
Source: BBVA Research based on GDELT data

Epidemiological uncertainty:

- Pandemic control deadlines.
- Speed of the “opening” process.
- Possible new waves of infections.
- Availability of a vaccine or treatment.

Economic uncertainty:

- Stimulus effectiveness.
- Effect on public and private debt levels.

Financial uncertainty:

- Rebound of financial tensions.
- Systemic crisis risk.

The pandemic raises many questions about the long term.

Research

02

Portugal
Economic Outlook
2Q20

New GDP growth baseline scenario

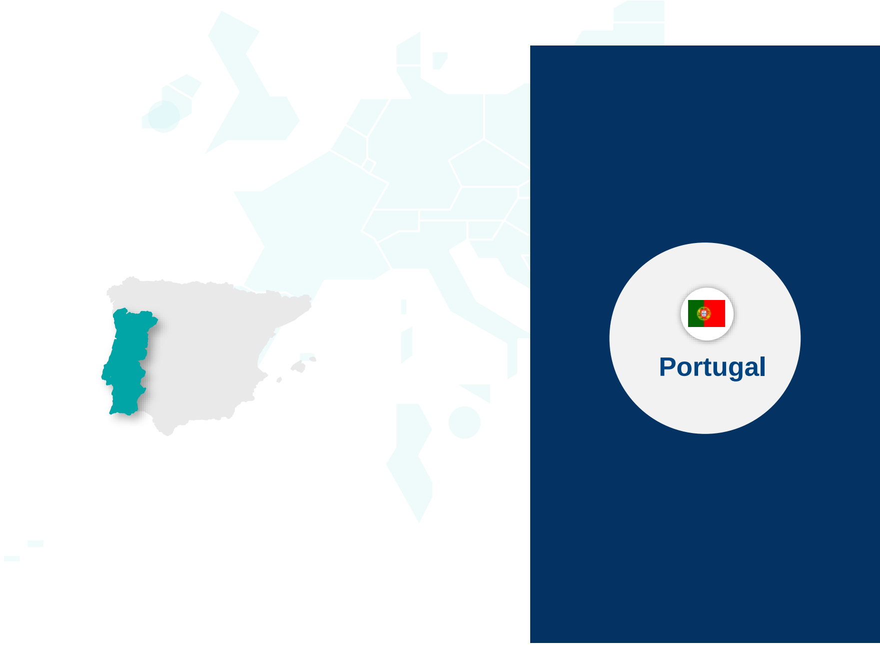
2019 +0.3 pp ▲ **2.2%**

2020 -8.2 pp ▼ **-6.5%**

-8.0% — -5.0%

2021 +3.2 pp ▲ **4.9%**

4.0% — 6.0%



▲ Forecast revised upward

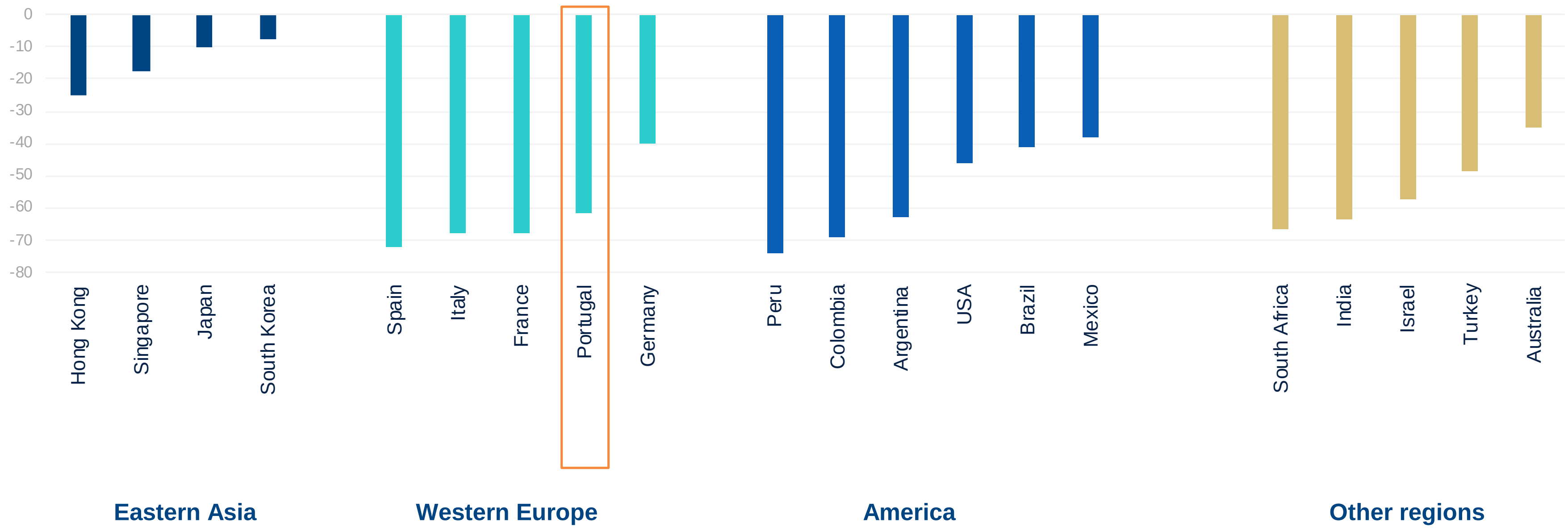
▼ Outlook downgraded

Source: BBVA Research

Confinement measures are helping to control the epidemic, but they are slowing down the economic activity

INDICATOR OF MOBILITY TRENDS TO PLACES OF WORK

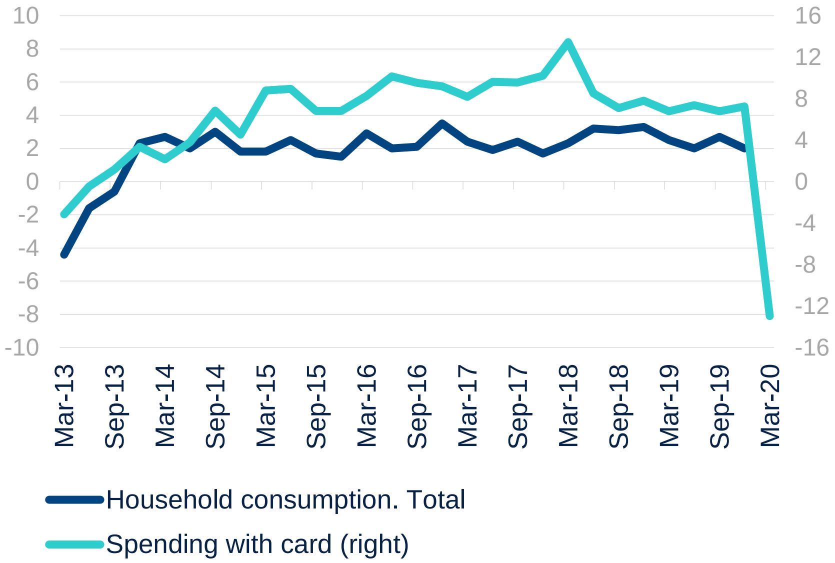
(VARIATION IN % BETWEEN THE PERIOD FROM MAR 30th TO APR 5th AND JAN 3rd TO FEB 6th)



Source: BBVA Research based on Google data (COVID-19 Community Mobility Reports).

The impact on the economy is being substantial

NOMINAL HOUSEHOLD CONSUMPTION AND CARD EXPENDITURE*
(SWDA DATA, % YoY)



*Expenditure with payment cards at Point of Sale (POS) terminals in Portugal.
Source: BBVA Research based on Bank of Portugal and INE data

- Portugal POS card expenditure data have a high correlation with national consumer spending in the Quarterly National Accounts figures.
- The fall in nominal credit card spending during the first quarter of 2020 would imply a decline in household consumption for the same period, in line with our scenario (-1.9% QoQ).
- Adjustments could have been greater in "social consumption" sectors such as leisure, tourism, transport, etc. Others, such as food, would have benefited from changes in people's consumption patterns.

The impact on the economy is being substantial

PORTUGAL: GDP GROWTH
(% QoQ, SWDA)

4Q19	1Q20
+0.7	-2.5(e)

- The containment measures adopted point to a significant adjustment in supply.
- Just over 50% of accommodation and catering companies have had to close temporarily, commerce and other services (16%).
- Other indicators also reveal substantial adjustments. Vehicle registrations fell by 57% YoY in March (production by 46% YoY), the use of public transport in Porto and Lisbon was reduced by around 80% from 25 March, while electricity consumption fell by 8% YoY between 18 and 31 March.
- An estimated fall in activity of 2.5% QoQ in 1Q20.

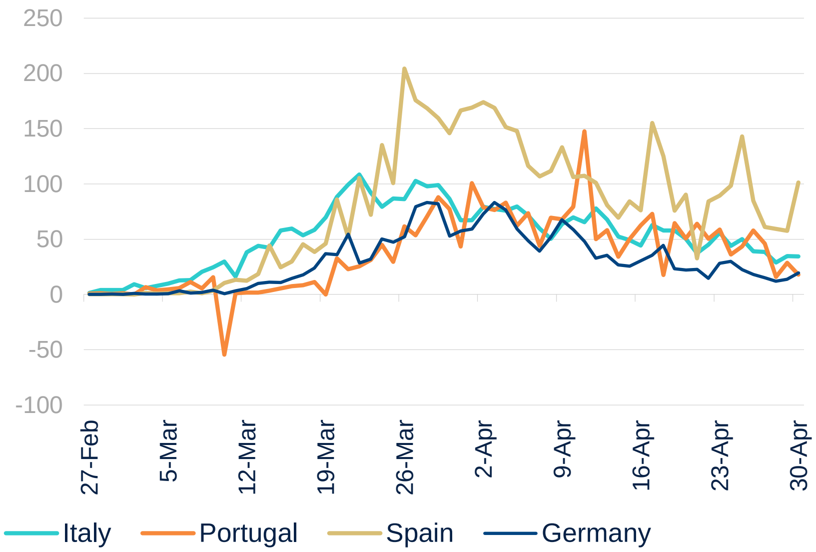
(e) Estimate.
Source: BBVA Research based on INE data.

Source: INE (Fast and Exceptional Enterprise Survey – COVID-19), ACAP, REN and MOOVIT

Where is the Portugal economy heading?

Assumption: The state of alarm is lifted in the first week of May

DAILY VARIATION OF CORONAVIRUS CASES
(PER MILLION POPULATION)



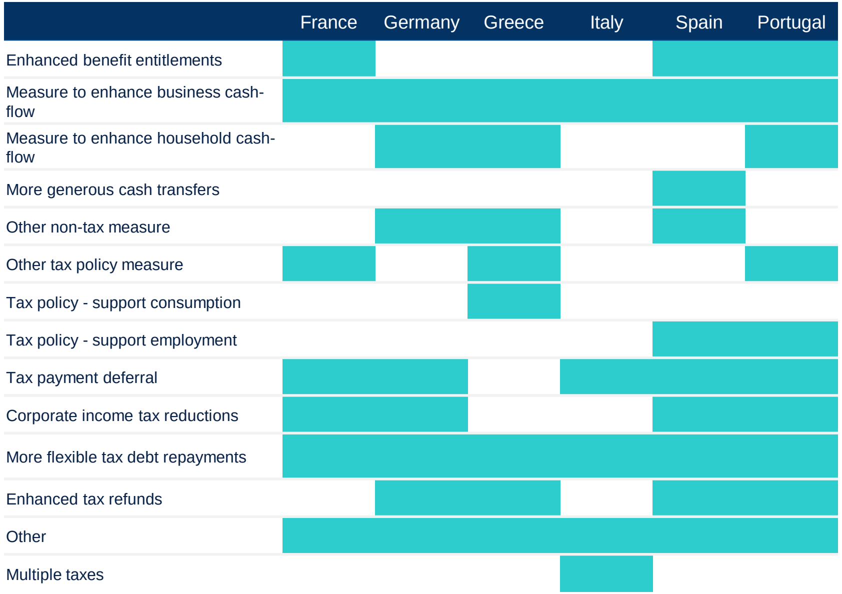
- Containment measures are having the desired effect of reducing the number of infections.
- The current levels of virus transmission have allowed Portugal to start a gradual lifting of the measures restricting activity which will be implemented from the beginning of May according to a fortnightly timetable.
- In any case, there is uncertainty about the effects that the resumption of activity may have on the evolution of the epidemic, so the development of the de-escalation plan is subject to the recommendations of the experts.

Source: BBVA Research based on Johns Hopkins University data (data updated at 00:00 GMT)

Where is the Portugal economy heading?

The measures adopted will soften the impact on the economy

TYPE OF MEASURE TAKEN BY COUNTRY

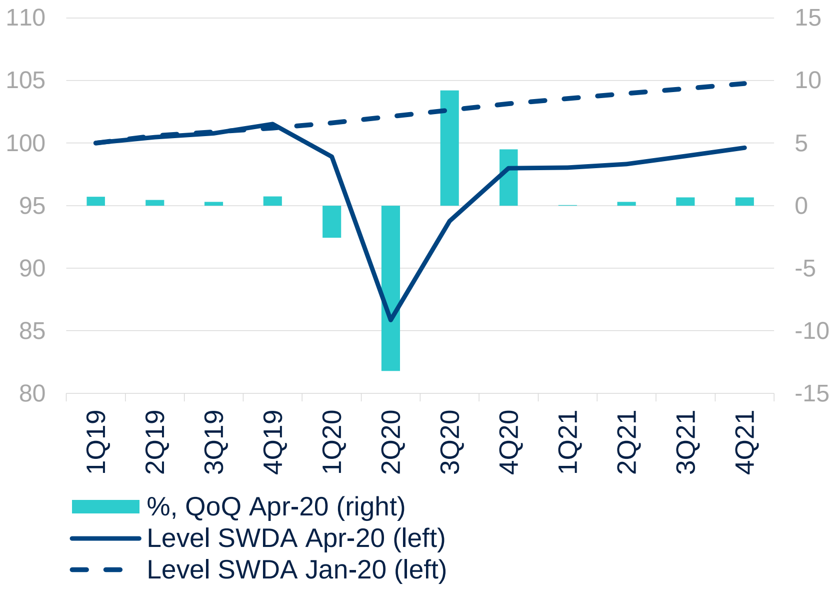


Source: BBVA Research based on OECD

- Portugal, like other European States, has implemented a series of measures to contain the pandemic with the aim of saving lives and focusing aid on those who need it most.
- The measures have been mainly aimed at supporting family incomes, containing job destruction and ensuring that solvent businesses with liquidity problems survive.
- The design of many of the measures would have prevented a further deterioration in activity or in income distribution.

Portugal: growth forecasts

GDP: LEVEL AND GROWTH
(LEVEL: SEASONALLY ADJUSTED INDEX (1Q19 =100); GROWTH: QoQ, %)



Source: BBVA Research based on INE data.

- The fall in activity during the second quarter will be significant, but we expect an intense recovery starting from the third quarter. In any case, it will not be sufficient to immediately return to the pre-crisis level of activity on the forecast horizon.
- The exit speed will be restricted by adjustments in sectors that will not exit in a V-shape and by the relative greater destruction of jobs.
- There is a risk that some of the short-term effects will become permanent.

Risk: the design of an exit strategy that guarantees the safety of the population and reduces the impact on the activity

THE EXIT STRATEGY SHOULD BE BROADLY BASED ON 3 PILLARS:

1 Continuous learning from initiatives adopted and the experiences of other countries

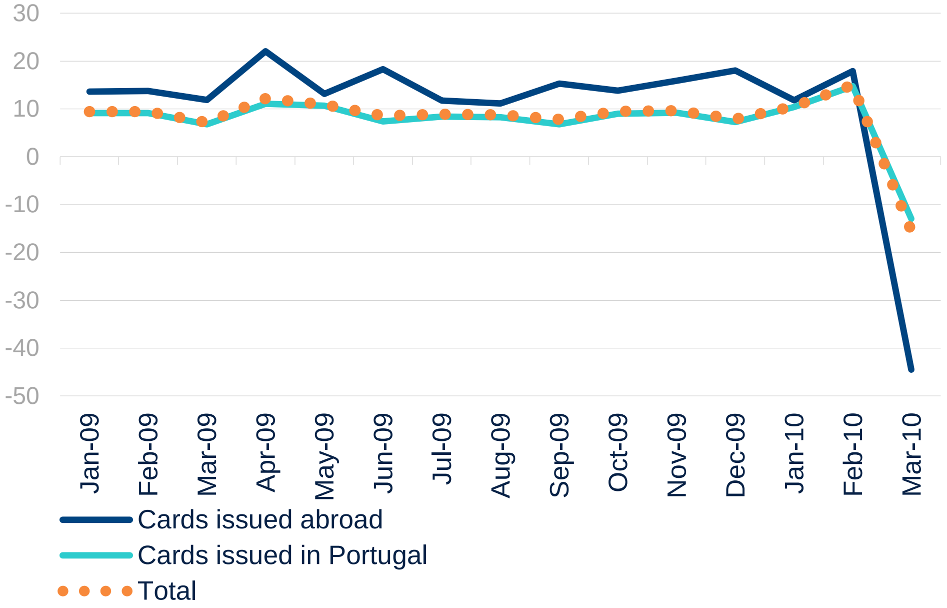
2 Monitoring the capacity of the health care system

- Evolution of infections
- Hospital infrastructure
- Development of treatments

3 Efficient implementation of monitoring protocols

Risk: a V-shaped recovery will be more difficult in certain sectors

CARD EXPENDITURE: MONTHLY EXPENDITURE, BY NATIONALITY OF THE CARD*
(2020 VS. 2019, %)



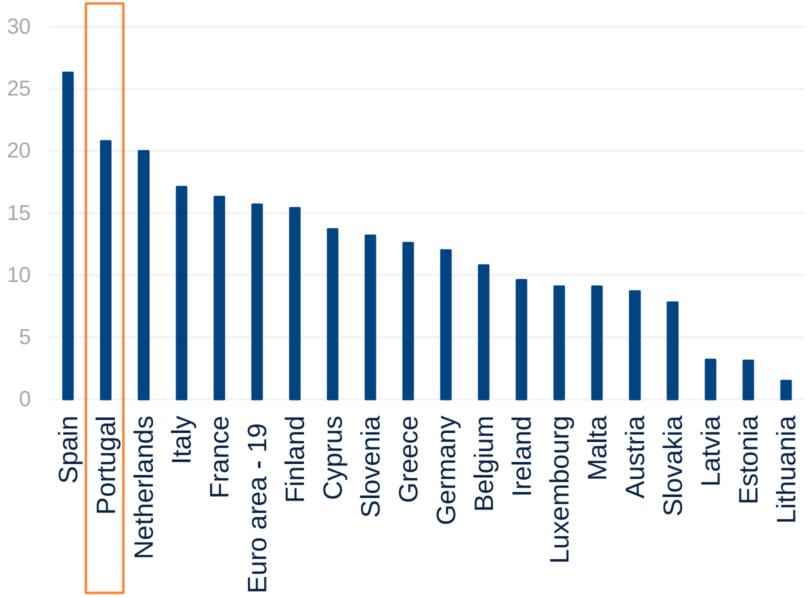
*Expenditure with payment cards at Point of Sale (POS) terminals in Portugal.
Source: BBVA Research based on Bank of Portugal data.

- Tourism contributes to 8% of GVA and 9% of employment* in Portugal.
- In 2019, external tourism revenues reached 8.7% of GDP**. Half were recorded between April and September.
- Between 2015 and 2019, employment in the branches of activity linked to tourism grew by 50% more than the aggregate of services. The carry-over effect on other sectors is important.
- Slower recovery is expected:
  - Limitations on movement and population concentrations.
  - Need to ensure that there is no contagion between the origin and destination markets.

*Satellite account of Tourism, 2018, INE
**Balance of payments, 2019

Risk: the duality of the labor market increases job destruction

TEMPORARY CONTRACTS
(% TOTAL)

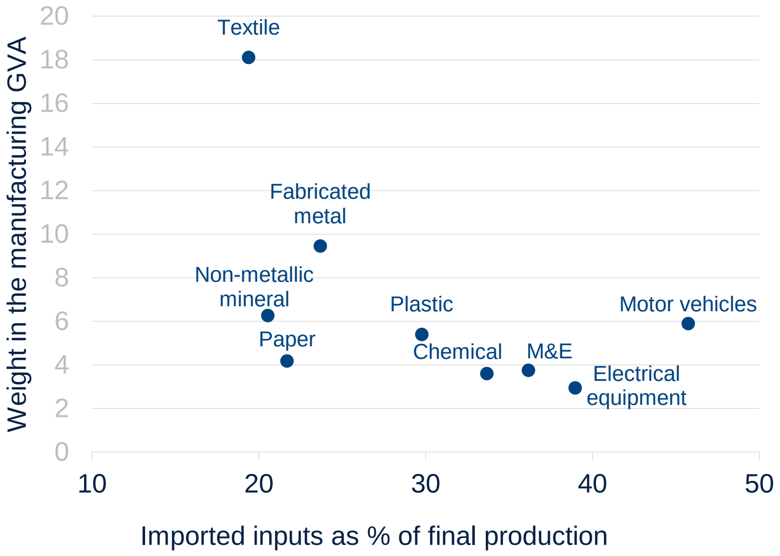


Source: BBVA Research based on Eurostat

- Portugal has the second highest proportion of temporary contracts in the euro area (5 pp above the average).
- The high share of workers with a temporary contract increases the likelihood of a higher adjustment in activity.
- These groups, together with those who are not in the formal market, are more unprotected.
- Progress must be made in mechanisms that protect these people while providing incentives for more efficient adjustments that ensure the survival of enterprises and jobs.

Risk: slower recovery of the production chain

PORTUGAL: RELATIVE WEIGHT OF IMPORTED INPUTS AND GVA OF SELECTED MANUFACTURING SUBSECTORS (%)

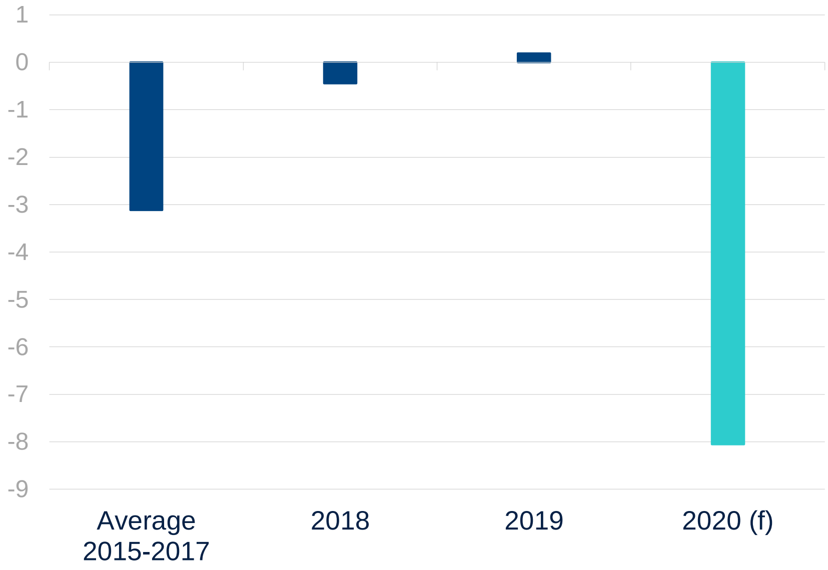


Source: BBVA Research based on the input-output tables of the OECD

- The manufacturing sector is the one with the greatest dependence on imported goods and where the greatest bottlenecks can be generated as a result of disruption to value chains.
- In particular, key industries such as automotive, chemicals, metallurgical and textiles may see their recovery restricted by the complex links in their value chains.
- The more synchronized the recovery is, the stronger it will be.

Risk: new pressures on public deficit

PORTUGAL: PUBLIC DEFICIT
(% of GDP)



(f): Forecast
(1): Includes the variation in interest expenditure
Source: BBVA Research based on national sources

- The various pandemic containment measures implemented will impact the 2020 deficit.
- The risks on the deficit scenario are concentrated in that (i) the temporary measures become permanent; (ii) the deterioration of activity is greater and requires a greater fiscal effort, or (iii) the guarantees begin to be executed in the face of an increase in business insolvency.
- It is essential to make progress on agreements that leave no room for doubt about the support that the euro area countries as a whole will give to each of their members in scenarios where the prioritization of the population's health could give way to a further deterioration in activity.

03

Forecasts

Forecasts

% YoY	2019	2020 (f)	2021 (f)
Private consumption	2.3	-5.2	3.7
Public consumption	0.8	1.2	0.3
Gross fixed capital formation	6.5	-26.8	12.2
Domestic demand*	**2.7**	**-8.1**	**4.2**
Exports	3.7	-21.5	8.5
Imports	5.2	-25.4	7.1
External demand*	**-0.6**	**1.6**	**0.6**
Real GDP at market prices	**2.2**	**-6.5**	**4.9**
Employment	0.9	-4.2	2.2
Unemployment rate (% of labor force)	6.6	10.1	8.3
CPI (annual average)	0.3	0.2	0.6
GDP deflator	1.7	0.6	1.0
Public deficit (% GDP)	0.2	-8.1	-5.2

* Contribution to GDP growth (f) Forecast.
Source: BBVA Research based on INE, Banco de Portugal y HAVER

BBVA Research

Portugal Economic Outlook

2Q20

Creating Opportunities