8 June 2018

Public Finance

Portuguese Republic Rating Report

Credit strengths

- Euro-area membership
- Improving budgetary performance
- Ongoing structural reforms
- Favourable debt profile

Credit weaknesses

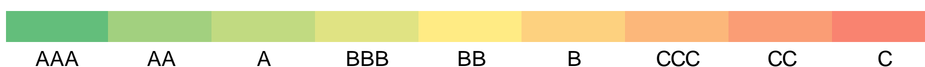
- High public and external debt
- High private-sector debt
- Elevated implicit liabilities
- Low potential growth

Rating rationale and Outlook:

The BBB rating is supported by Portugal's euro-area membership, economic recovery, ongoing reduction of economic, fiscal and external imbalances, resilient debt structure and commitment to further structural reforms. Very high public, private and external debt levels, including elevated implicit liabilities, and comparatively low potential growth rates pose challenges. The Stable Outlook reflects Scope's view that the upside potential from a continued reduction in economic, fiscal and external imbalances is balanced by the downside risk stemming from the elevated imbalances themselves, the unwinding of which, while ongoing, will require continued commitment by the Portuguese authorities.

Figure 1: Sovereign scorecard results

Scope's sovereign risk categories	Portugal	Peer comparison	
		Average	Spain
Domestic economic risk			
Public finance risk			
External economic risk			
Financial risk			
Political and institutional risk			
Qualitative adjustment (notches)	-		2
Final rating	BBB		A-



NB. The comparison is based on Scope's Core Variable Scorecard (CVS), which is determined by relative rankings of key sovereign credit fundamentals. The CVS peer group average is shown together with one selected country chosen from the entire CVS peer group. The CVS rating can be adjusted by up to three notches depending on the size of relative credit strengths or weaknesses.

Positive rating-change drivers

- Steady reduction in public debt
- Higher growth potential
- Reduction external imbalances

Negative rating-change drivers

- Reversal of fiscal consolidation
- Markedly lower GDP growth
- Increases in external imbalances

Ratings and Outlook

Foreign currency

Long-term issuer rating	BBB/Stable
Senior unsecured debt	BBB/Stable
Short-term issuer rating	S-2/Stable

Local currency

Long-term issuer rating	BBB/Stable
Senior unsecured debt	BBB/Stable
Short-term issuer rating	S-2/Stable

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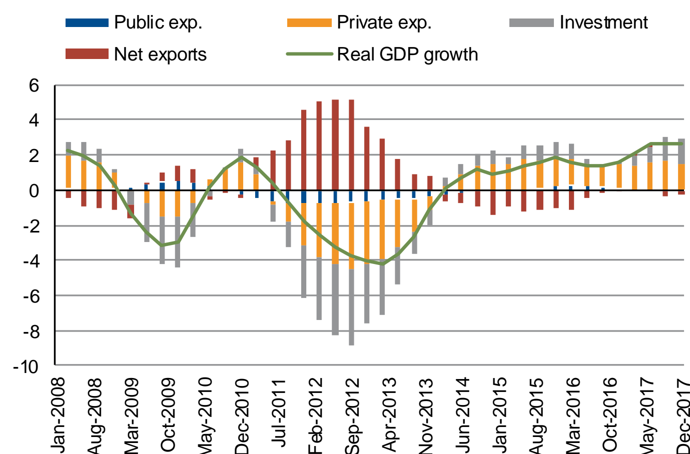
Domestic economic risk

Growth potential of the economy

Robust growth prospects in line with euro-area level

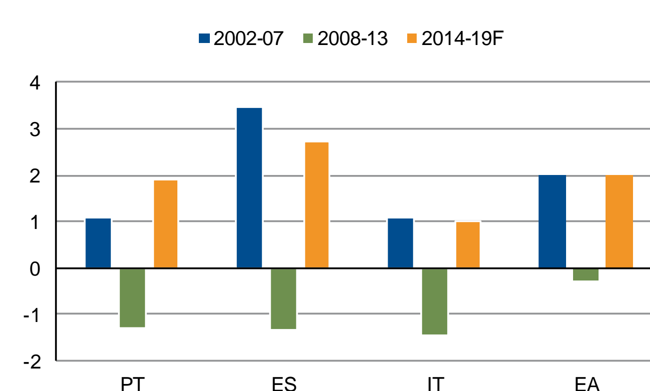
Following two consecutive shocks, namely the Great Financial Crisis and the euro-area crisis, during which Portugal lost market access and requested financial assistance in May 2011 amounting to EUR 78bn, the Portuguese economy has undergone a significant structural adjustment. Since Portugal's exit from the three-year economic adjustment programme in June 2014, its economy has grown on average by around 1.8%, in line with the euro-area average. This has been driven by a rebalancing of the economy towards the tradable sector, in particular tourism, strong private consumption due to the turnaround in the labour market, and a sustained rebound in investment. Portugal has also benefited from the ECB's accommodative monetary policy as well as favourable external conditions, particularly in the euro area. Finally, the stabilisation of the banking system is now also facilitating the efficient reallocation of resources, thus contributing to the investment recovery of the Portuguese economy.

Figure 2: Real GDP growth, %



Source: Haver, INE, Scope Ratings

Figure 3: Average real GDP growth, %



Source: Haver, EC, Scope Ratings

Moderate growth rates over the medium term

Going forward Scope expects growth rates to slow from the 2.7% level recorded in 2017 to around 2% over the medium term – still above the long-term growth potential of the economy, which Scope estimates at around 1.5%. As the output gap closes in 2018-19, Scope expects fiscal policy support to remain mildly positive, and private consumption and investment to soften gradually. Continued household deleveraging, in light of low savings rates, is likely to somewhat dampen consumption despite labour market improvements and the minimal growth in real wages. By contrast, investment growth is expected to remain robust over the medium term due to the need to rebuild capital stock, the normalisation of EU fund allocation, and the maintenance of favourable financing conditions[1]. Finally, on the back of competitiveness gains, the contribution of net exports is set to remain mildly positive, given a structural adjustment in the Portuguese export sector with a broader diversification by sectors and markets.

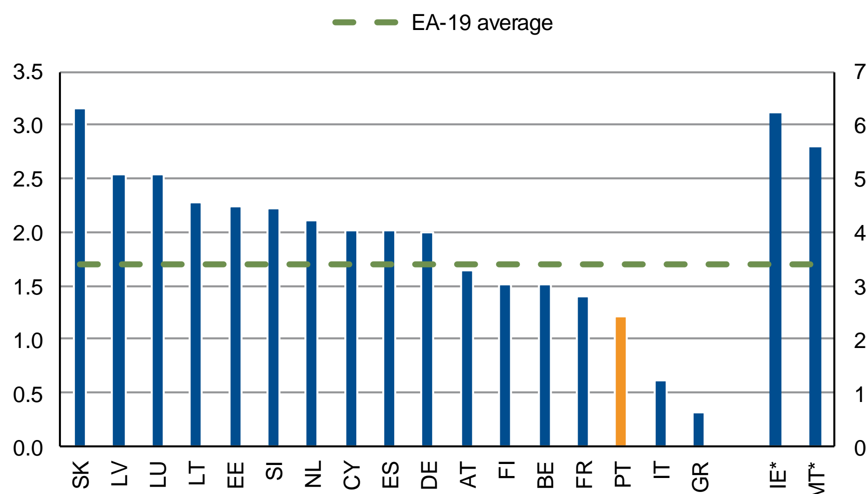
Subdued productivity growth and demographic challenges a constraint to Portugal's growth potential

While the short-to-medium-term growth outlook is robust, Portugal's long-term economic growth prospects face considerable challenges. The IMF and European Commission estimate potential growth at around 1.0% to 1.5%[2], constrained by structural bottlenecks, including weak productivity growth, in part due to low investment levels, skill shortages and unfavourable labour force demographics. These constraints are reflected in Portugal

[1] Banco de Portugal; Projections for the Portuguese Economy 2018-2020, March 2018
[2] IMF Article IV and EC Country Report March 2018. https://ec.europa.eu/info/sites/info/files/2018-european-semester-country-report-portugal-en.pdf

having the third lowest potential GDP growth rate among euro-area members, just above that of Italy and Greece.

Figure 4: GDP potential growth, three-year average, %



Source: Haver, AMECO, Scope Ratings

Economic policy framework

Comprehensive reforms during crisis period…

Economic growth has also benefited from an effective economic policy framework overall, in particular from a combination of comprehensive reforms by Portuguese authorities and changes in the euro area's institutional architecture, alongside the ECB's ongoing accommodative monetary policy. The Portuguese authorities' long-term focus on structural changes in skills, investment, export orientation, and in the labour market was further bolstered by their demonstrated ability to legislate and implement comprehensive economic, fiscal and financial sector reforms, particularly under the economic adjustment programme. These reform efforts are underpinning the country's economic recovery[3].

…at the national…

In this context, Scope highlights the structural reforms to boost potential growth, create jobs and improve competitiveness; the fiscal consolidation strategy, supported by structural fiscal measures and better fiscal control over public-private partnerships and state-owned enterprises (SOEs); and the financial sector strategy based on recapitalisation and deleveraging[4]. During its adjustment programme, Portugal was in fact one of the 'reform champions', as evidenced by the OECD's responsiveness to the reform indicator. Scope notes that structural reforms have continued to be implemented since the exit of the programme, particularly in the financial but also the public and corporate sectors[5].

…and European level

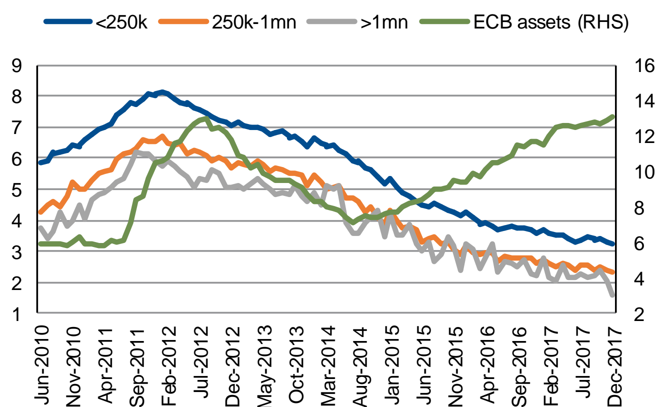
At the same time, Portugal, along with all euro-area member states, has benefited from the overhaul of the euro-area architecture, which has improved the ability to adjust to crises. While further progress is needed to deepen the Economic and Monetary Union – notably the completion of the Banking and Capital Markets unions – the establishment of the European Stability Mechanism as the conditional lender of last resort for sovereigns, along with the ECB's unconventional and accommodative monetary policy programmes, has been appropriate for Portugal.

[3] https://voxeu.org/article/turnaround-portuguese-economy
[4] European Commission.
[5] An overview can be found on slide 58: https://www.igcp.pt/fotos/editor2/2018/Apresentacao_Investidores/IGCP_Investors_20180525.pdf

The ECB's accommodative monetary stance is determined by the low level of interest rates and the expectation that they will remain low over a prolonged period, the net purchases of securities under the asset purchase programme until at least September 2018, the large volume of the securities portfolio acquired during the asset purchase programme's past three years, and the commitment to reinvest securities as they mature for as long as required[6].

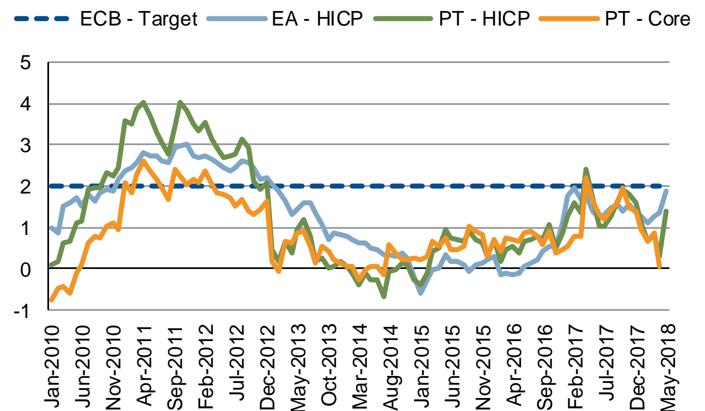
In Scope's opinion, the national structural reforms, combined with euro-area governance reforms and the ECB's actions, have led to a significant decline in financing rates for all economic sectors, including for non-financial corporations (NFCs), whose borrowing rates have dropped 400-500bp depending on loan size and maturity. At the same time, Scope notes that the sustained accommodative monetary policy stance is also adequate for Portugal given the still-subdued price levels. While annual headline inflation rose to 1.6% last year, driven by higher energy prices, the price level is low with inflation of around 1.4% in May 2018, markedly below the ECB's target of just under 2%.

Figure 5: NFC borrowing rates (%) and ECB assets (% of GDP)



Source: Haver, ECB, Scope Ratings

Figure 6: Harmonised index of consumer prices, %



Source: Haver, ECB, Eurostat, Scope Ratings. NB. Core inflation excludes energy and food.

Macroeconomic stability and sustainability

Low-skilled, low-income jobs…

Scope identifies two macroeconomic vulnerabilities for Portugal: a comparatively large share of low-income, low-skilled jobs and the subdued investment levels. Scope notes positively that, based on INE data, Portugal has recovered around 450,000 of the 800,000 jobs lost during the crisis and reduced unemployment to 7.4% as of April 2018, the lowest level in 10 years and below the euro-area average of 8.4% (2018E). However, according to the EC, persons i) available to work but not seeking jobs, ii) seeking work but not immediately available, and iii) underemployed working part-time still constitute around 10% of the active population, pointing to further slack in the labour market.

In addition, aggregate wage growth remains subdued as most job openings were in sectors with low-skilled profiles and below-average salaries. In fact, 22.7% of workers were covered by the minimum wage at the end of the first semester of 2017 while the percentage of low-skilled workers (defined as individuals with a lower secondary education or below) remained high at 48% in 2016, down from 61% in 2011 but still markedly above the EU average of 18%[7]. In Scope's opinion, while the gradual reduction

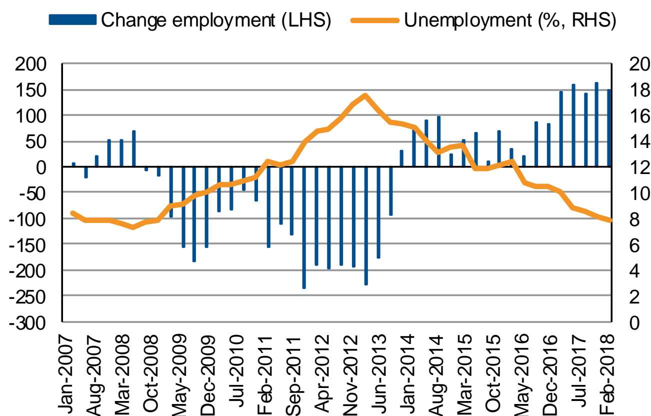
[6] https://www.ecb.europa.eu/press/pr/date/2017/html/ecb.pr171026.en.html
[7] EC, Post-programme surveillance report, Autumn 2017

in the share of jobs with lower education levels is positive[8], along with a steady increase in the level of education[9], the comparatively still large share of low-skilled and low-income jobs may weigh negatively on productivity and the tax base in the long run, as well as increase the risk of sustained income inequality among vulnerable groups.

…and a low investment level constitute a potential long-term productivity challenge

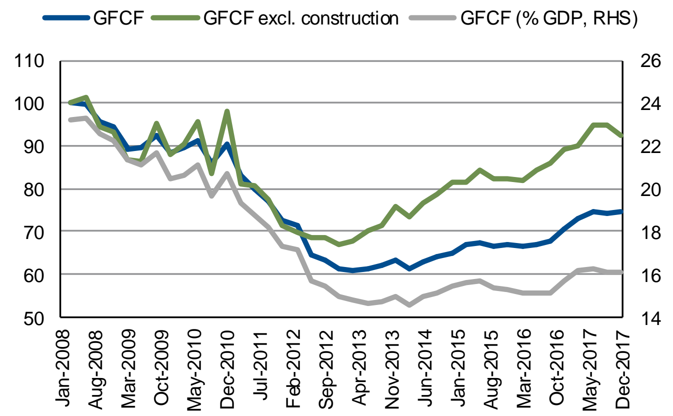
At the same time, Scope notes that despite a recent recovery in investments, the overall investment level of the economy, at 16.7% of GDP for 2018E, remains significantly below the euro-area average of 20.4% of GDP. This reflects the sharp decline in gross fixed capital, by around 6pp of GDP since 2008 – a substantial decline since the peak of 28% of GDP recorded in 2000. Conversely, Scope notes that investment, except for in construction, has recovered since Q2 2013 and is now almost back to the pre-crisis level. Finally, given the importance of EU funds for co-financing public investment projects, public investment is likely to gather pace in the coming years, somewhat closing the investment-stock gap compared to peer levels.

Figure 7: Employment and unemployment, four-quarter moving sum ('000s), % labour force



Source: Haver, INE, Scope Ratings

Figure 8: Investment, gross fixed capital formation; 2008=100; % of GDP (RHS)



Source: Haver, INE, Scope Ratings

Public finance risk

Fiscal policy framework

Comprehensive fiscal framework at EU and euro-area levels

As an EU member, Portugal is part of the EU's fiscal policy framework, which is centred on the 1997 Stability and Growth Pact (SGP). This pact has been modified via reforms in 2005, the 2011 Six Pack (five regulations and one directive), the 2013 Two Pack (two regulations), and the Treaty on Stability, Coordination, and Governance of 2012 (Fiscal Compact)[10]. In addition to these rules national legislation also sets a multi-annual limit for expenditure financed by general revenue, specifically the Multi-annual Budgetary Planning Framework (MBPF).

Fiscal consolidation led to EDP exit but CGD recapitalisation widened deficit in 2017

Against this backdrop, Scope notes that Portugal reduced its fiscal balance to 1.9% in 2016 from 11.2% in 2010, which led to the country's exit from the EU's excessive deficit procedure in June 2017. However, in 2017 the government deficit stood at 3.0% of GDP,

[8] Based on INE data: The share of employment with a basic (or no) education level declined gradually from 57.8% in Q1 2011 to 42.9% in Q1 2018.

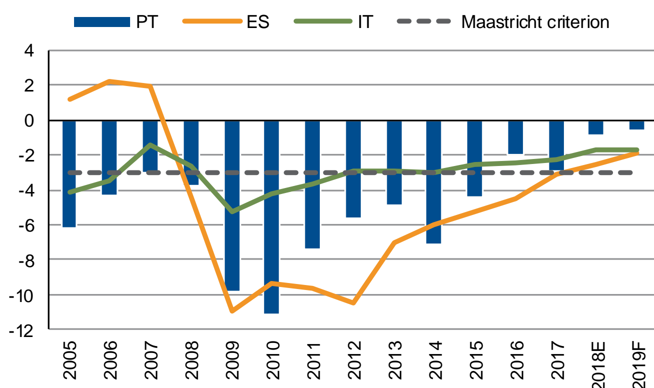
[9] Portugal is part of a very small group of countries that have made steady, broad-based progress in the various rounds of the OECD PISA assessments. https://voxeu.org/article/turnaround-portuguese-economy

[10] The 1997 SGP included three EU-wide rules: ceilings of 3% of GDP for the overall fiscal deficit and 60% of GDP for public debt (corrective arm), as well as a requirement for medium-term budget positions to be 'close to balance or in surplus' (preventive arm). The 2005 reform of the SGP aimed at enhancing the economic rationale underlying the rules and improving their flexibility by introducing country-specific medium-term objectives (MTOs) set in structural terms. The Six Pack reform in 2011 was designed to improve enforcement by adding an expenditure benchmark to the preventive arm and making the debt criterion in the corrective arm operational. The Fiscal Compact and Two Pack reforms of 2012 and 2013 reinforced monitoring and surveillance in the euro area and called for anchoring EU rules at the national level. In 2015, revised guidance on the implementation of the SGP increased its flexibility to encourage investment and structural reforms and to account for the economic cycle. IMF 2015, 'Reforming Fiscal Governance in the European Union'

interrupting the path of reducing the nominal deficit of the last two years. More than two-thirds of this result was influenced by the recapitalisation of Caixa Geral de Depósitos, which led to a 1pp increase in the deficit compared to the 2016 level.

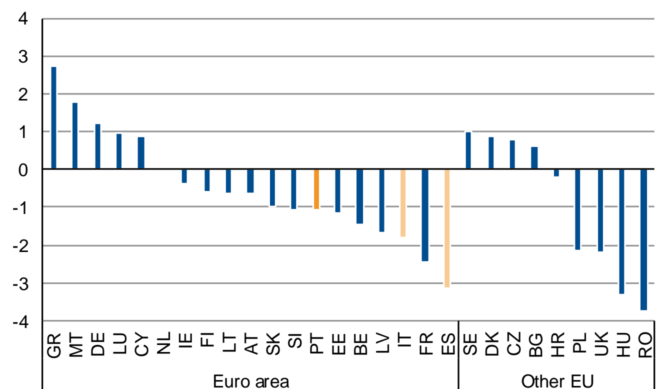
Despite this higher deficit, the Portuguese Public Finance Council highlights that, excluding the net negative impact of temporary and non-recurrent measures, the deficit stood at 0.8% of GDP. In 2017, the correction of the fiscal imbalance accelerated in adjusted terms, as the improvement of 1.6pp of GDP was more than double that of the previous year.

Figure 9: Overall fiscal balances, % of GDP



Source: Haver, AMECO, Scope Ratings

Figure 10: Structural balance, % of GDP, 2017-19F



Source: Haver, AMECO, Scope Ratings

Some structural adjustment

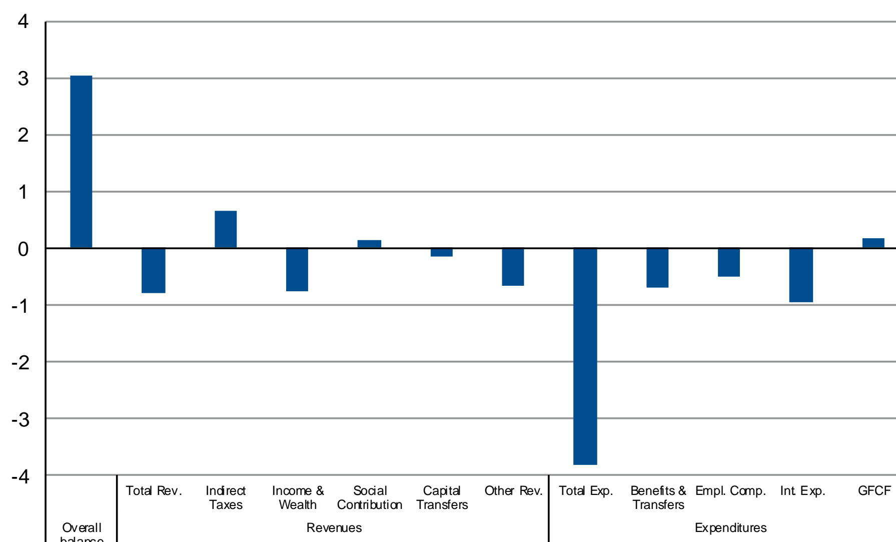
Still, Scope points out the mostly cyclical nature of the adjustment: around three-fifths of the 1.6pp decrease in the headline deficit was due to favourable economic conditions boosted by an improving labour market, resulting in lower benefits and the decline in interest charges stemmed from better market financing conditions and the early repayment of IMF loans[11]. Nonetheless, Scope is mindful of the contained primary expenditure growth and the fact that the spending review is gradually being expanded to new sectors including justice and internal affairs, in addition to education, healthcare, SOEs, public-sector real estate management, and centralised public procurement.

This restraint is also observed in an improving structural deficit, estimated at around 1% of GDP during 2017-19, which compares favourably to peers such as Italy (1.8%) and Spain (3.1%). Scope also notes positively that the steady decline in public investment, which stood at 1.8% of GDP in 2017, down from 5.3% in 2010, is expected to reverse, albeit modestly, over the coming years.

Going forward, Scope expects the government to stay well within the Maastricht deficit criterion of 3%, with the EC estimating deficits of 0.9% for 2018 and 0.6% in 2019, which include further banking support, specifically the activation of the Novo Banco contingent capital mechanism, estimated at 0.4% of GDP. Similarly, the IMF forecasts deficits to stay between 0.7% and 0.2% of GDP, along with primary surpluses close to 3.0% of GDP during 2018-20[12].

[11] http://www.cfp.pt/news/cfp-analyses-the-local-government-budget-outturn-for-2017/?lang=en#.Www-NkiFOUk
[12] http://www.imf.org/en/News/Articles/2018/05/29/ms052918-portugal-staff-concluding-statement-of-the-2018-article-iv-mission

Figure 11: Change in Portugal's budget balance, % of GDP, difference between average 2017-19F versus average 2014-16



Source: Haver, AMECO, Scope Ratings

Ongoing fiscal consolidation but debt levels still high

As a result, Portugal's general government debt level, which peaked in 2014 at 130.6% of GDP, has gradually declined to 125.7% in 2017, which is below Italy's (131.8%), but significantly above Spain's (98.3%) and the 60% Maastricht criterion. In Scope's opinion, this elevated debt burden constitutes a major rating constraint.

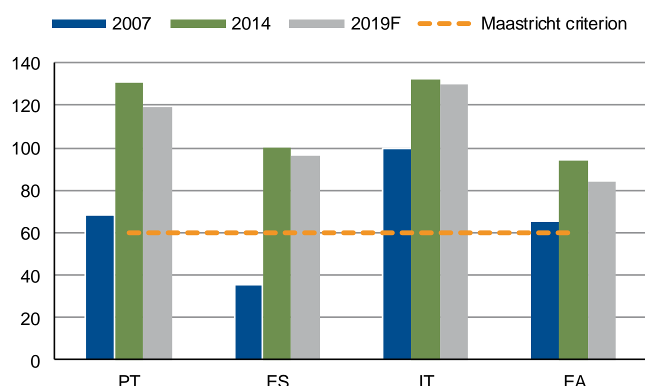
Moderate pension liabilities but elevated implicit healthcare liabilities

In addition, Scope highlights that, in line with peers, the ageing population is contributing to fiscal pressures in Portugal. Following several reforms which improved the long-term sustainability of the pension system – albeit, according to the IMF, via a backloading effort to protect current pensioners[13] – pension-related expenditure is expected to decrease slightly over the 2070 horizon, in line with those of Spain and Italy, according the EC's latest Ageing Report. Still, Scope notes that Portugal's 2016 pension spending of 13.5% of GDP was the fifth highest among the EU28 members. In addition, Portugal's healthcare expenditure is set to increase from 5.9% of GDP in 2016 to 8.3% by 2070, above the levels in Spain (6.4%) and Italy (7.0%) and the euro area average of 7.4%[14].

Using figures from the EC's previous Ageing Report for 2015 (which had similar results to the 2018 report) and applying a discount rate of 1% in excess of GDP growth, the IMF estimates the net present value of Portugal's pension spending during 2015-50 at 22.6%, with implicit healthcare liabilities at 74.3% of GDP[15]. Thus, adding Portugal's implicit future pension and healthcare liabilities to the expected 2018 general government debt level results in an obligation of around 218% of GDP, the highest among all euro-area members, significantly above the levels of Italy (169%) and Spain (155%).

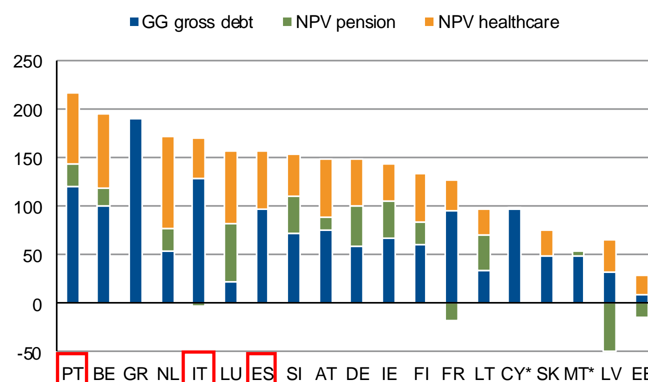
[13] IMF Article IV
[14] EC 2018 Ageing Report
[15] IMF Fiscal Monitor, April 2018

Figure 12: Debt levels, % of GDP



Source: Haver, EC, Scope Ratings

Figure 13: Implicit liabilities, % of GDP



Source: Haver, IMF 2018 Fiscal Monitor, Scope Ratings

Increasing hospital arrears have also led authorities to repeatedly release funds, which in 2017 amounted to EUR 400m, accompanied by capital injections into hospitals of EUR 500m in 2017 and again 2018. While the arrears have been caused by several underperforming hospitals, and not by the National Health Service as a whole, the pattern of periodic financial support points to the ongoing risk of further financial needs[16].

Contingent liabilities also stem from the financial sector, SOEs, and state guarantees. As previously noted, the 2018 budget already incorporates the activation of the Novo Banco contingent capital mechanism, estimated at 0.4% of GDP. Given past interventions, Scope believes further banking support beyond what is already expected to be unlikely. However, SOEs remain a source of vulnerability given their recurring, though decreasing, losses. Specifically, while SOEs' total net loss has improved from negative EUR 1.3bn in 2014 to negative EUR 0.5bn in 2017, losses are also expected in 2018 of around EUR 118m[17]. Finally, based on EC data, general government guarantees amount to 5.6% of GDP as of 2016, below those of Spain (7.7%) but above Italy's (2.4%).

Debt sustainability

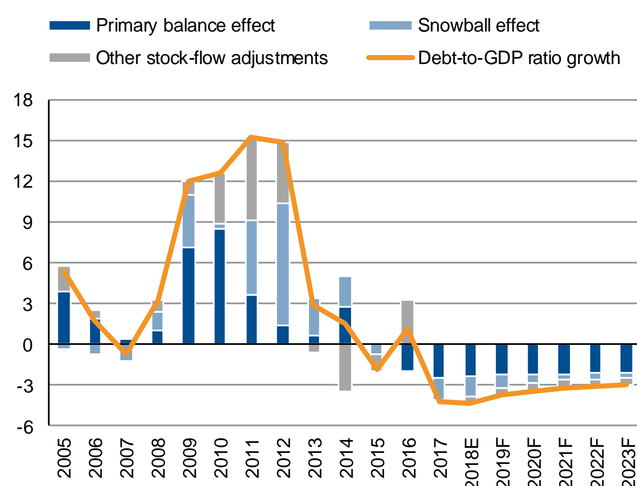
Challenging debt dynamics, even in an optimistic scenario

Scope's public-debt sustainability analysis, based on IMF forecasts and a combination of growth, interest-rate and primary-balance shocks, confirms that although Portugal's debt trajectory still faces significant risks given the sizeable debt burden and elevated gross financing needs, a gradual decline is expected in the near future. On the basis of Portugal's high debt level, an expected narrowing of fiscal deficits going forward, and more moderate growth rates, Scope's baseline scenario is for the debt-to-GDP ratio to fall to around 105% by 2023. This compares slightly more conservatively to the government which expects the debt-to-GDP ratio to fall to 102% by 2022. A more adverse scenario – assuming a combined 0.5pp shock to real GDP growth (lower), interest payments (higher) and the primary balance (lower) for each year over the forecast horizon – would lead to a debt-to-GDP of around 117% by 2023.

Despite this projected decline below the 130% peak of 2014 and Italy's debt level (131%), debt-to-GDP would remain high, markedly above Spain's (98%), the IMF's debt burden benchmark for advanced economies (85%), and the Maastricht criterion (60%). Portugal thus remains vulnerable to macroeconomic and financial market shocks, pointing to the need to maintain not only relatively high growth rates but also a significant level of fiscal consolidation over multiple years.

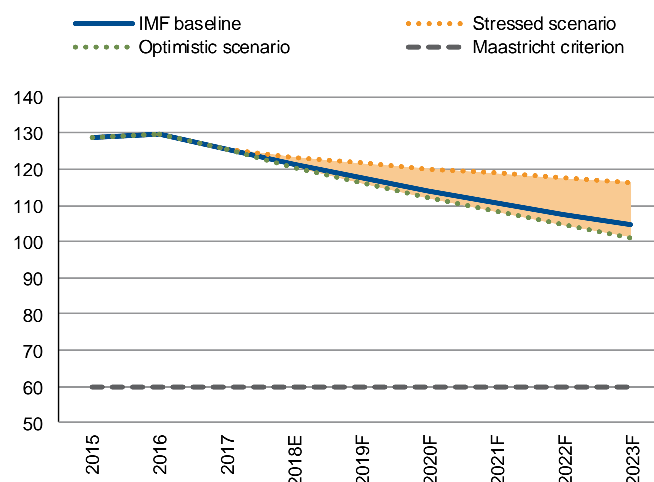
[16] EC, Post Programme Surveillance Report, Autumn 2017
[17] Ibid.

Figure 14: Contribution to gov. debt changes, % of GDP



Source: IMF, Scope Ratings. NB: Other includes stock-flow adjustments

Figure 15: Government debt, % of GDP



Source: IMF, Scope Ratings

Scenario	Time period	Real GDP growth avg. (%)	Primary bal. (% of GDP)	Real eff. int. rate (%)	Debt end period (% of GDP)
History	2013-17	1.2	0.2	1.5	125.6
IMF baseline	2018-23	1.5	2.2	0.9	104.7
Optimistic scenario		2.0	2.7	0.9	101.1
Stressed scenario		1.0	1.7	1.2	116.5

Source: IMF April WEO 2018, Scope Ratings

Market access and funding sources

Significantly smoother debt profile

While Portugal's debt level is expected to remain elevated over the medium term, Scope expects the country's gross financing needs in the coming years to remain below 20% of GDP, the IMF's vulnerability benchmark for advanced economies. Specifically, Portugal's active debt management – including accelerated early repayments to the IMF (EUR 10bn in 2017), bond buybacks and exchanges, and longer-term issuances – has smoothened the redemption profile. For the State, gross financing needs are estimated at EUR 18.8bn in 2018 (of which EUR 11.1bn has already been financed), EUR 15.3bn in 2019, and EUR 13.0bn in 2020. Only in 2021 are financing needs estimated to again rise to EUR 20.9bn. At the same time, the Treasury's cash buffer is projected to drop slightly from EUR 9.8bn last year to EUR 7.4bn in 2019 before rising to EUR 10bn in 2020 ahead of the high redemptions in 2021, when a EUR 5bn drawdown will lower the cash buffer to EUR 5bn. As a result, over 2018-20 the cash buffer will remain around 50% of the following year's gross financing needs before dropping to around 28% in 2021 (for expected needs in 2022)[18].

Against the backdrop of the current favourable financing environment, which has resulted in the cost of debt outstanding dropping from 4.1% in 2011 to 3.0% in 2017, the treasury's prudent debt-funding strategy extended the average life of debt outstanding from 5.3 years in 2012 to 6.4 years in 2017, excluding EU-IMF loans. Once these loans are included, the average maturity rises to 8.1 years, above that of Spain or the euro-area average (seven years)[19]. In Scope's opinion this favourable maturity structure of Portugal's public debt, combined with the treasury's solid cash buffer, limits the near-term

[18] https://www.igcp.pt/fotos/editor2/2018/Apresentacao_Investidores/IGCP_Investors_20180525.pdf
[19] Ibid.

risk of temporary market fluctuations or rising yields, especially once the ECB's asset purchase programme ends, expected in September this year.

ECB's purchases shift investor base

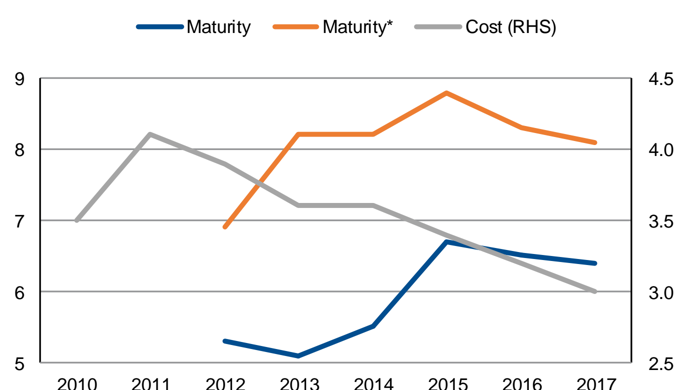
The number of non-residents holding Portuguese debt, in the majority before the crisis, has reduced markedly since then as a result of financial assistance and the ECB's public-sector purchase programme. As a first step, debt was substituted with bilateral loans from public creditors. Second, the Eurosystem, specifically the Bank of Portugal, has been purchasing debt securities on the market; as of March 2018, the Bank holds around EUR 28.2bn in Portuguese bonds, or around 19% of total issued debt. Consequently, the share of debt securities held by non-residents fell drastically to around 22.5% in Q1 2018 from around 60% in Q1 2008.

As the ECB's asset purchase programme comes to an end, Scope believes future demand is likely to come from domestic banks and possibly foreign central banks, two stable sources of funding. In addition, Scope notes that the recent increase in retail issuance is also an important development in diversifying sources of financing and providing an alternative vehicle for household savings[20].

ESM permanent regional financing arrangement

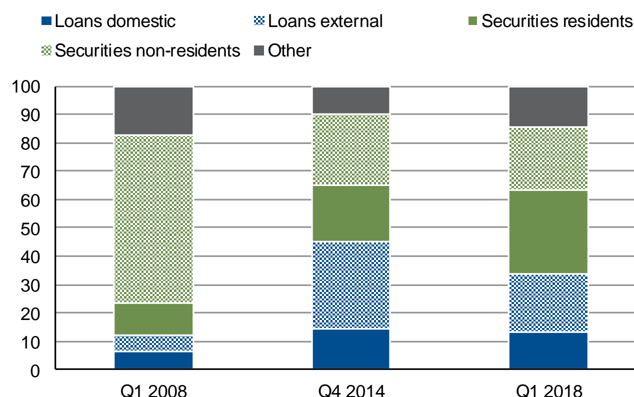
Finally, from an institutional perspective, Scope views positively the fact that the European Stability Mechanism has been established as a credible, conditional lender of last resort to all euro-area member states, which includes Portugal, further enhancing the resilience and sustainability of Portugal's market access.

Figure 16: Maturity (years) and cost (%) of outstanding debt



Source: IGCP; *Includes EU-IMF loans

Figure 17: Government debt holders, % of total



Source: Haver, Bank of Portugal, Scope Ratings

External economic risk

Current-account vulnerabilities

From external debtor to creditor

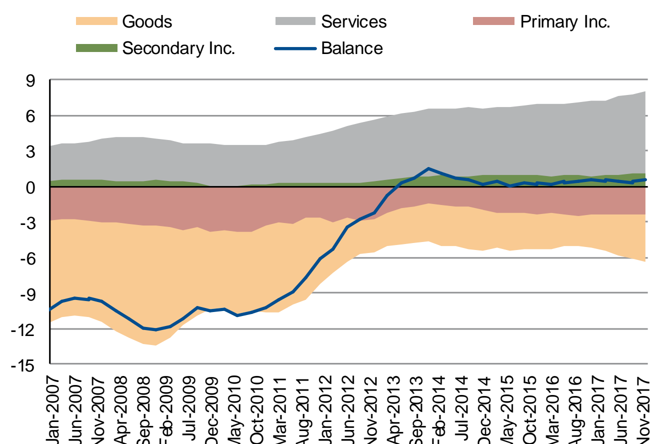
Portugal has recorded minor current-account surpluses since 2013, a significant turnaround after a deficit of 12.1% in 2008. This structural adjustment was driven by a strong performance for services exports, in particular tourism and transport, a declining negative goods balance, a mild decline in the primary balance due to lower interest rates, and a recent slight uptick in secondary income reflecting higher inflows from EU funds. During this rebalancing process, Portugal's economy has become much more open, with the proportion of exports of goods and services relative to GDP increasing from 27.2% in Q4 2009 to 44.1% by Q1 2018[21].

Scope expects this positive trend to continue over the medium term, due to cost-competitiveness gains as well as structural improvements to Portugal's export base,

[20] EC, Post Programme Surveillance Report, Autumn 2017
[21] Based on Bank of Portugal data.

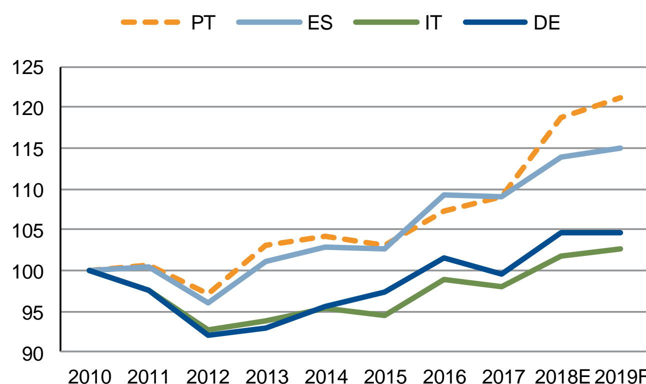
reflected in a broader diversification by sector and region. These improvements have increased Portugal's share of world merchandise exports in contrast to most euro-area peers. However, Scope notes that maintaining current-account surpluses for a sustained period is necessary to gradually improve Portugal's significant net debt position, which remains a source of vulnerability.

Figure 18: Sustained current-account surpluses, % of GDP



Source: Haver, Bank of Portugal, Scope Ratings

Figure 19: Share of world exports (incl. EU), 2010 = 100



Source: Haver, AMECO, Scope Ratings

External debt sustainability

Negative NIIP a credit vulnerability

Over the past few years, positive economic growth and current-account surpluses have led to a minor decline in Portugal's external debt and an improvement in the country's net international investment position (NIIP), which remains markedly below that of peers at around negative 106% of GDP as of Q4 2017. In addition, the reduction in Portugal's NIIP has been somewhat offset by valuation effects due to the increased market value of portfolio debt securities issued by Portuguese residents. Despite these positive effects, Portugal's NIIP remains far below the EC threshold of negative 35% of GDP, used in its macroeconomic imbalance procedure to identify external vulnerabilities. As a result, from a stock perspective, Portugal remains vulnerable to external crises[22].

High level of external debt…

While NIIP is a key measure for external sustainability and constitutes a current credit constraint for Portugal, the international balance sheet is also crucial for assessing external vulnerabilities. Specifically, the size, composition, and structure of the international balance sheet may exacerbate the risks stemming from NIIP. In this context, the size of gross external liabilities remains elevated, in Scope's opinion, with Portugal's total external debt standing at around 211% of GDP as of Q4 2017, slightly down since Q1 2010 (234%) but still above that of Spain (165%) and Italy (124%)[23].

…but improved composition…

Yet risks have abated given the change in the composition of external debt. Specifically, the government and central bank's share has increased from around 37% of total external debt in Q1 2010 to above 60% in Q4 2017, whereas the share held by financial institutions, in the context of ongoing deleveraging, reduced from 48% to around 14% over the same period.

…and debt-equity mix

In addition, the share of portfolio debt securities of Portugal's foreign liabilities, whose non-contingent nature may complicate the absorption of shocks, has fallen markedly from

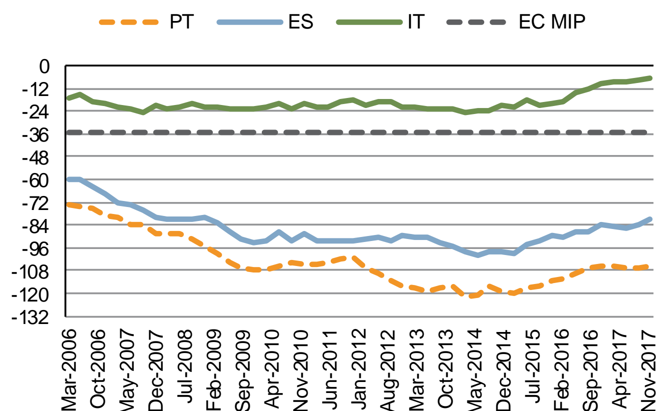
[22] Excessive net foreign liabilities are a common harbinger of external crises, which often lead to severe output losses. A standard early-warning model indicates that net foreign liabilities in excess of around 35% of GDP are associated with heightened risks of an external crisis. The risks become even more substantial at levels beyond 50% of GDP. https://www.ecb.europa.eu/pub/pdf/scpops/ecb.op198.en.pdf?dd48dc2fe1941f6f88e9c75eb4becc18

[23] However, Scope notes that Portugal's net external debt (obtained by excluding capital instruments and financial derivatives) declined by 2.1 p.p. of GDP, from 94.6% of GDP in 2016 to 92.5% in 2017, the lowest since March 2012.

around 32% in Q1 2010 to around 19% as of Q4 2017, which indicates an improvement in both the debt-equity mix and official loans, the latter of which is a stable source of external funding that reduces Portugal's external vulnerability.

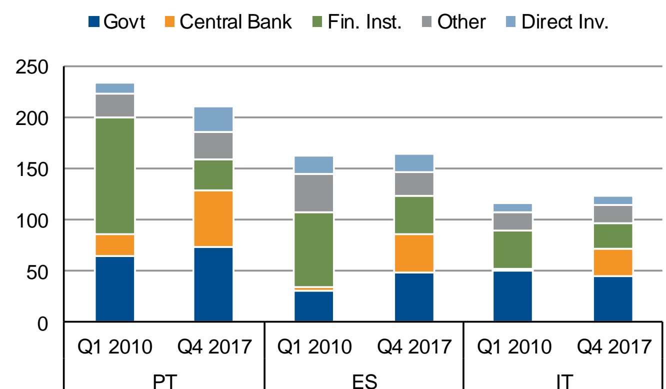
Finally, the NIIP burden – as measured by the investment income balance – is currently relatively light in Portugal, in line with other peripheral economies. This reflects a broad-based decline in aggregate yields during the post-crisis period, particularly for portfolio debt and 'other investment'[24]. While net payments associated with Portugal's external position could increase markedly if euro-area interest rates normalised, the expected gradual normalisation of the ECB's monetary policy along with the structural improvements in Portugal's external balance sheet should somewhat mitigate these risks, in Scope's view.

Figure 20: Net international investment position, % of GDP



Source: Haver, national central banks, Eurostat, Scope Ratings

Figure 21: External debt composition, % of GDP



Source: Haver, national central banks, Eurostat, Scope Ratings

Vulnerability to short-term external shocks

Limited vulnerability to short-term shocks

Portugal's still-negative NIIP is high at around 106% of GDP, exposing the sovereign to shocks or sudden shifts in market sentiment. However, it is Scope's opinion that the structural improvements in Portugal's external sector, combined with the strengthened euro-area architecture and the ECB's expansionary monetary policy stance, markedly reduce the country's risk to external shocks.

Scope expects Portugal's external imbalances, a legacy from the crisis, to gradually unwind. In this context Scope will monitor euro-area interest rates closely, which, if raised again towards pre-crisis levels, could heighten Portugal's external vulnerabilities.

Financial stability risk

Financial sector performance

Portugal's stronger economic performance, combined with recent capital increases in four of the six largest Portuguese banks amounting to EUR 7bn since Q4 2016, has resulted in a more resilient financial system overall. Banks are not only restructuring their business models, leading to a reduction in their distribution networks, but also disposing of non-core activities, helping to clean up balance sheets, which is gradually allowing them to perform credit intermediation[25].

[24] https://www.ecb.europa.eu/pub/pdf/scpops/ecb.op198.en.pdf?dd48dc2fe1941f6f88e9c75eb4becc18
[25] EC, Post Programme Surveillance Report, Autumn 2017

Better-capitalised banking sector with improving asset quality…

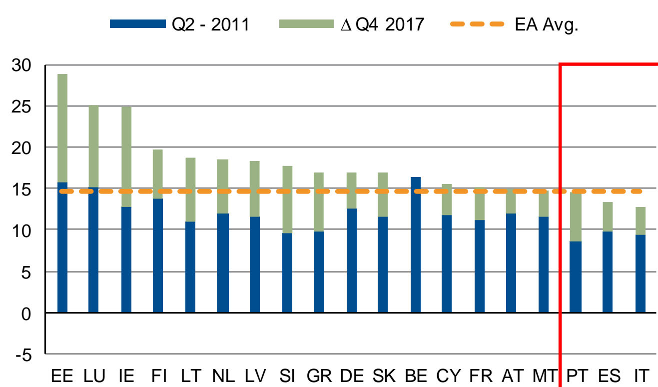
As a result, solvency and profitability have improved for most banks despite the low interest rates. Based on IMF data, capitalisation has increased due to recapitalisations as well as falling risk-weighted assets, with a Common Equity Tier 1 (CET1) ratio of 14.5%[26], slightly above Spain's (13.4%) and Italy's (12.8%) and in line with the euro area average of 14.6%. In addition, banking system profitability was positive in 2017 in contrast with the negative value in 2016, reflecting a significant reduction in the flow of impairments as well as an increase in total operating income with a system-wide return on equity of 3.5%. The Bank of Portugal estimates a cost-to-income ratio of 52.9%, or 54.4% excluding one-off restructuring processes.

The three-pillared strategy to deal with NPLs, in the form of legal and judicial reforms, prudential supervisory action and NPL management, is yielding results as expected, with the NPL ratio gradually declining to 13.3% of total loans in Q4 2017 from the 17.9% peak in Q2 2016 – a EUR 13.5bn reduction in the NPL stock. The NPL coverage ratio is also elevated at 49.3% as of Q4 2017[27].

…and ECB's fixed-rate full allotment until 2019 ensures ample liquidity

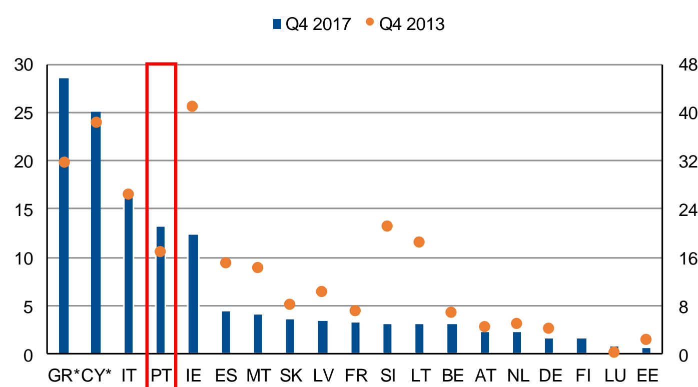
Banks are also benefiting from ample liquidity and cheap funding due to the ECB's targeted longer-term refinancing operations and asset purchase programme. Funding challenges are thus set to rise over the medium term as the ECB unwinds its unconventional monetary policies, potentially affecting both the liquidity and profitability of banks given their relatively large share of long-duration sovereign debt. However, the loan-to-deposit ratio has fallen markedly from 158.8% in Q2 2010 to 92.6% in Q4 2017 and, in addition, borrowing from the Eurosystem has also fallen from its Q2 2012 peak of EUR 60.5bn, to EUR 22.1bn as of Q4 2017, thus constituting only around 6% of banks' total liabilities. In addition, as the Eurosystem continues its regular one-week and three-month lending operations – which, as announced by the ECB in October 2017, will continue to be at a fixed rate with full allocation until at least the end of the last reserve maintenance period in 2019[28] – liquidity issues remain a limited risk in Scope's opinion.

Figure 22: Banking sector capitalisation, regulatory Tier 1 capital to risk-weighted assets, in %



Source: Haver, IMF, Scope Ratings; NB. If not Q4 2017 then latest available

Figure 23: Banking sector asset quality, NPLs to total gross loans, in %



Source: Haver, IMF; NB. *RHS. If not Q4 2017 then latest available

Despite the overall stabilisation of the Portuguese banking sector, Scope points out that challenges remain going forward, including the need of banking institutions to access the capital market to meet new requirements on own funds and eligible assets, which is within the scope of the bank resolution framework (MREL – Minimum Requirement for

[26] Based on Bank of Portugal data the CET1 ratio stood at 13.9% as of Q4 2017.
[27] Bank of Portugal; Portuguese Banking System: latest developments; 4th quarter 2017
[28] https://www.ecb.europa.eu/press/pr/date/2017/html/ecb.mp171026.en.html.

Own Funds and Eligible Liabilities), and the end of the phase-out period (in 2018) of some instruments which would previously have been included in regulatory own funds[29].

Financial sector oversight and governance

Oversight and governance shared between the Bank of Portugal and European institutions

The responsibility for the macro-prudential oversight of banks is shared between the Bank of Portugal and the ECB. As the national macroprudential authority, the Bank of Portugal defines and executes macroprudential policy and regularly analyses the financial system in order to identify vulnerabilities as well as existing and potential risks under baseline and adverse scenarios. The activation and deactivation of existing macroprudential instruments under the EU legal framework requires coordination at EU level; such coordination is ensured by several authorities, namely the European Systemic Risk Board (ESRB), the European Banking Authority (EBA), the European Commission and, within the scope of the Single Supervisory Mechanism (SSM), the ECB when performing its macroprudential tasks[30].

Use of macroprudential tools to strengthen banking sector

Against this background, the Bank of Portugal has identified four objectives to ensure macroprudential stability. These are aimed at mitigating and preventing excessive levels of credit growth, leverage, maturity mismatches and market illiquidity, as well as limiting direct and indirect exposure concentrations and incentives for excessive risk-taking by systemically important institutions:

- The Bank of Portugal has identified six banks as ‘other systemically important institutions’ (O-SIIs) which can be subject to **higher capital requirements**, between 0% and 2% of the total risk exposure amount. As of January 2018, the phase-in period of the O-SII capital buffer levels – ranging from 0.25% to 1% – has been extended by two years until 2020, upon which the additional capital required will gradually reach between 0.25% and 1% depending on the institution[31].
- The **countercyclical buffer**, which corresponds to an additional buffer of Common Equity Tier 1 capital to be built up when risks of system-wide stresses rise due to excessive credit growth (this can range between 0% and 2.5% of the total risk exposure), is set at 0% as of 1 April 2018[32].
- The **capital conservation buffer** aims to accommodate losses from a potential adverse scenario, allowing institutions to maintain a stable flow of funding to the real economy. This buffer is implemented gradually, from 0.625% of the total risk exposure in 2016 to 1.25% in 2017, 1.875% in 2018 and 2.5% in 2019[33].
- As of 1 July 2018, the Bank of Portugal recommends the following **lending limits**[34]: i) a maximum 90% loan-to-value ratio for own and 80% for non-permanent residential property; 100% if the property is for financial leasing agreements; ii) a 50% debt service-to-income ratio (DSTI)[35]; iii) a maximum 40-year maturity for mortgages and 10 years for consumer loans; and iv) for new loans, the requirement of regular payments of interest and capital. The Bank of Portugal notes that since the limits apply only to new credit agreements, their effects on the stock of credit will be gradual.

[29] https://www.bportugal.pt/en/page/o-sii-capital-buffer
[30] https://www.bportugal.pt/en/page/macro-prudential-policy?mlid=1144
[31] Caixa Geral de Depósitos (1.0%), Banco Comercial Português (0.75%), Novo Banco (0.5%), Santander Totta, SGPS (0.5%), Banco BPI (0.5%), Caixa Económica Montepio Geral (0.25%). https://www.bportugal.pt/en/page/o-sii-capital-buffer
[32] https://www.bportugal.pt/en/page/countercyclical-capital-buffer
[33] https://www.bportugal.pt/en/page/capital-conservation-buffer
[34] https://www.bportugal.pt/en/page/ltv-dsti-and-maturity-limits
[35] Unless the total amount of credit granted by the institution in each year is less than 20% (5%), then a 60% (no limit) DSTI applies

Overall, in Scope's opinion, the introduction and application of these measures is an appropriate regulatory response in light of four bank failures in Portugal over the past decade.

Macro-financial vulnerabilities and fragility

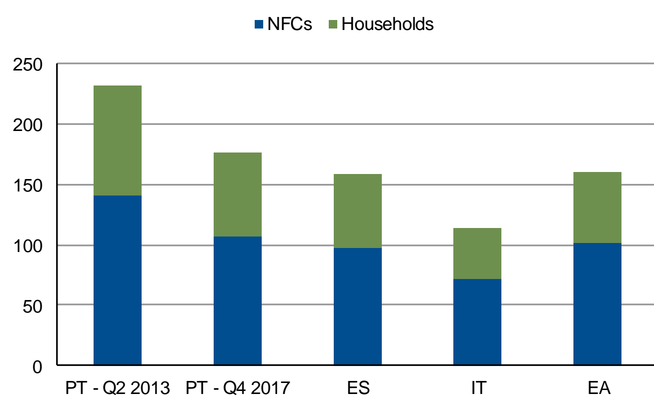
Ongoing private-sector deleveraging

Over the past few years, the Portuguese private sector has significantly reduced its indebtedness to levels similar to those of euro-area peers. NFCs have reduced liabilities by around EUR 30.9bn since Q1 2013. On the other hand, households have reduced liabilities more gradually, given that most loans are long-term mortgages, but still by around EUR 16.8bn over the same period. As a result, corporate sector indebtedness fell from 141.5% of GDP in Q1 2013 to 106.8% as of Q4 2017, slightly above the euro-area average of 101.7%, while household indebtedness decreased from 90.0% to 69.4%, just above the euro-area average of 58.0%. This marked decline in liabilities – and vulnerabilities along with it – has so far been compatible with investment and private consumption given the increase in confidence, employment, and economic stability, which is a development Scope expects to continue over the medium term.

Slowing deleveraging process alongside a pick-up in credit growth

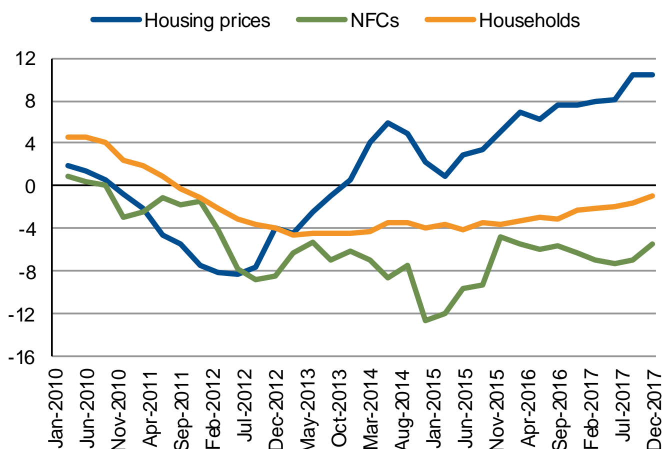
The significant deleveraging process has resulted in weak demand for credit despite declining lending rates. However, while overall credit growth to corporates and households remains negative, the contraction is slowing, and going forward Scope expects deleveraging to be driven mainly by real GDP growth along with a pick-up in credit growth, particularly among the most solvent and productive corporates, contributing to the investment recovery.

Figure 24: Private-sector debt, % of GDP



Source: Haver, ECB, Scope Ratings

Figure 25: Housing prices and credit, %, YoY growth



Source: Haver, ECB, Scope Ratings

Finally, Scope notes that labour market improvements and the prevailing low interest rate environment have led to an increase in consumer demand, which, based on ECB data[36], is up 11.9% year on year. However, the savings rate of Portuguese households, measured as gross disposable income, has dropped to 5.4% (down from 10.5% in 2009), which is below the euro-area average of 12%. In Scope's opinion this limits the potential increase in credit demand for mortgages over the medium term. It is in this context that Scope assesses increases in housing prices, which have steadily recovered since Q4 2013 and now exceed the pre-crisis level by 12%. However, the stock of mortgage loans continues to decline, which dampens the upward pressure on house prices and is evidence that the price rebound is not generated by debt accumulation. Moreover, the

[36] ECB. Portugal: MFI Consumer Loans to EA Households.

price increases are concentrated in tourist areas, particularly in Lisbon, and the growing supply from new construction, which increased around 23% in Q3 2017, is likely to moderate price increases going forward[37].

Overall, the Portuguese economy is in a low phase of the financial cycle, along with a gradual economic recovery that limits vulnerabilities stemming from credit and real estate prices. However, Scope highlights the vulnerabilities caused by the still-elevated debt burden of the non-financial private sector and extreme events in the financial markets.

Institutional and political risk

Perceived willingness to pay

Portugal joined the EU in 1986 and has fully adopted the EU's regulatory framework, providing an anchor for institutional stability and predictability. In Scope's view, Portugal is as likely as any EU member to honour debt obligations in full and on time. Portugal's request for an EU-IMF financial assistance package in May 2011, its clean exit from the programme in June 2014, and the subsequent successful post-programme monitoring reviews speak to Portugal's willingness to repay its creditors on time.

Recent events and policy decisions

Expected policy continuity beyond next year's elections

Since November 2015 Portugal has been governed by the minority centre-left Socialist Party (PS), led by Prime Minister António Costa. The government benefits from an alliance with three left-wing parties: the radical Left Bloc, the Portuguese Communist Party, and the pro-communist Greens.

The government has managed to balance demands around the reversal of austerity measures, including increases in the minimum wage and pensions, and an unfreezing of public-sector career progression while ensuring a growth-friendly consolidation process.

In Scope's opinion this also reflects the Portuguese authorities' constructive relationship with its official creditors. Despite exiting the EU-IMF programme, Portugal will remain under the EU's post-programme surveillance, which allows the EU Council to recommend corrective actions until at least 75% of the financial assistance has been repaid, thus at least until 2026.

In this context, Scope points to the expected policy continuity, also after the next elections set for late 2019 and which, based on current polls, are likely to lead to another PS-led government. In Scope's opinion, political stability and policy continuity are essential to further implement reforms to raise Portugal's growth potential and ensure fiscal discipline over a multi-year period to reduce the elevated debt burden.

Geopolitical risk

Portugal has been a member of NATO since 1949 and is not engaged in any bilateral conflicts. Thus, in Scope's opinion, Portugal is as likely as its European partners to be affected by geopolitical threats.

[37] EC, Post Programme Surveillance Report, Autumn 2017

Methodology

The methodology applicable for this rating and/or rating outlook, Public Finance Sovereign Ratings, is available at www.scoperatings.com.

Historical default rates from Scope Ratings can be viewed in Scope's rating performance report at https://www.scoperatings.com/#governance-and-policies/regulatory-ESMA. Please also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA) at http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope's definition of default and definitions of rating notations can be found in Scope's public credit rating methodologies at www.scoperatings.com.

The rating outlook indicates the most likely direction of the rating if the rating were to change within the next 12 to 18 months. A rating change is not automatically ensured, however.

I. Appendix: CVS and QS results

Sovereign rating scorecards

Scope's Core Variable Scorecard (CVS), which is based on the relative rankings of key sovereign credit fundamentals, provides an indicative 'BBB' ('bbb') rating range for the Portuguese Republic. This indicative rating range can be adjusted by up to three notches on the Qualitative Scorecard (QS) depending on the size of relative credit strengths or weaknesses versus peers based on analysts' qualitative findings.

For the Portuguese Republic, the following relative credit strengths have been identified: i) economic policy framework and ii) market access and funding sources. Relative credit weaknesses are: i) macroeconomic stability and sustainability. The combined relative credit strengths and weaknesses generate no adjustment and indicate a sovereign rating of BBB for the Portuguese Republic. A rating committee has discussed and confirmed these results.

Rating overview	
CVS category rating range	bbb
QS adjustment	BBB
Final rating	BBB

To calculate the rating score within the CVS, Scope uses a minimum-maximum algorithm to determine a rating score for each of the 24 indicators. Scope calculates the minimum and maximum of each rating indicator and places each sovereign within this range. Sovereigns with the strongest results for each rating indicator receive the highest rating score; sovereigns with the weakest results receive the lowest rating score. The score result translates to an indicative rating range that is always presented in lower case.

Within the QS assessment, analysts conduct a comprehensive review of the qualitative factors. This includes but is not limited to an economic scenario analysis, a review of debt sustainability, fiscal and financial performance, and policy implementation assessments.

There are three assessments per category for a total of 15. For each assessment, the analyst examines the relative position of a given sovereign within its peer group. For this purpose, additional comparative analysis beyond the variables included in the CVS is conducted. These assessments are then aggregated using the same weighting system as in the CVS.

The result is the implied QS notch adjustment, which is the basis for the analysts' recommendation to the rating committee.

Foreign- versus local-currency ratings

The Portuguese Republic has almost no foreign-currency-denominated public debt. Consequently, Scope sees no reason to believe that Portugal would differentiate between any of its contractual debt obligations based on currency denomination. Furthermore, the recent history of sovereign defaults does not provide a strong justification for a rating bias in favour of either local-currency or foreign-currency debt.

II. Appendix: CVS and QS results

CVS

Rating indicator	Category weight
Domestic economic risk	**35%**
Economic growth	
Real GDP growth	
Real GDP volatility	
GDP per capita	
Inflation rate	
Labour & population	
Unemployment rate	
Population growth	
Public finance risk	**30%**
Fiscal balance	
GG public balance	
GG primary balance	
GG gross financing needs	
Public debt	
GG net debt	
Interest payments	
External economic risk	**15%**
International position	
International investment position	
Importance of currency	
Current-account financing	
Current-account balance	
T-W effective exchange rate	
Total external debt	
Institutional and political risk	**10%**
Control of corruption	
Voice & accountability	
Rule of law	
Financial risk	**10%**
Non-performing loans	
Liquid assets	
Credit-to-GDP gap	
Indicative rating range	**bbb**
QS adjustment	**BBB**
Final rating	**BBB**

QS

Maximum adjustment = 3 notches

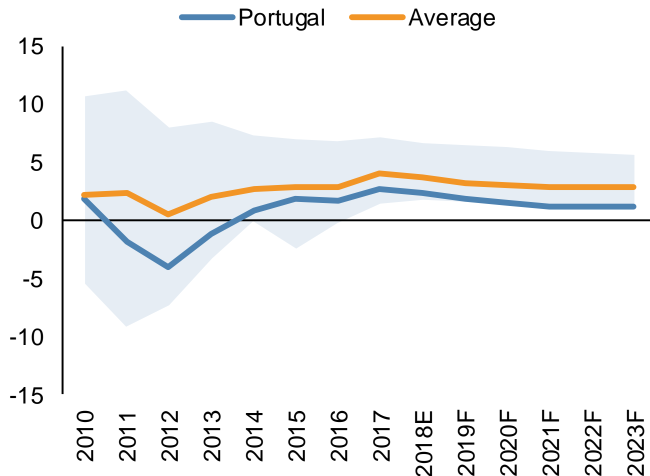
	+2 notch	+1 notch	0 notch	-1 notch	-2 notch
Growth potential of the economy	○ Excellent outlook, strong growth potential	○ Strong outlook, good growth potential	◉ Neutral	○ Weak outlook, growth potential under trend	○ Very weak outlook, growth potential wel under trend or negative
Economic policy framework	○ Excellent	◉ Good	○ Neutral	○ Poor	○ Inadequate
Macro-economic stability and sustainability	○ Excellent	○ Good	○ Neutral	◉ Poor	○ Inadequate
Fiscal policy framework	○ Exceptionally strong performance	○ Strong performance	◉ Neutral	○ Weak performance	○ Problematic performance
Debt sustainability	○ Exceptionally strong sustainability	○ Strong sustainability	◉ Neutral	○ Weak sustainability	○ Not sustainable
Market access and funding sources	○ Excellent access	◉ Very good access	○ Neutral	○ Poor access	○ Very weak access
Current account vulnerability	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
External debt sustainability	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
Vulnerability to short-term external shocks	○ Excellent resilience	○ Good resilience	◉ Neutral	○ Vulnerable to shock	○ Strongly vulnerable to shocks
Perceived willingness to pay	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
Recent events and policy decisions	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
Geopolitical risk	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
Banking sector performance	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
Banking sector oversight and governance	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate
Financial imbalances and financial fragility	○ Excellent	○ Good	◉ Neutral	○ Poor	○ Inadequate

*** Implied QS notch adjustment = (QS notch adjustment for domestic economic risk)*0.35 + (QS notch adjustment for public finance risk)*0.30 + (QS notch adjustment for external economic risk)*0.15 + (QS notch adjustment for institutional and political risk)*0.10 + (QS notch adjustment for financial stability risk)*0.10**

Source: Scope Ratings GmbH

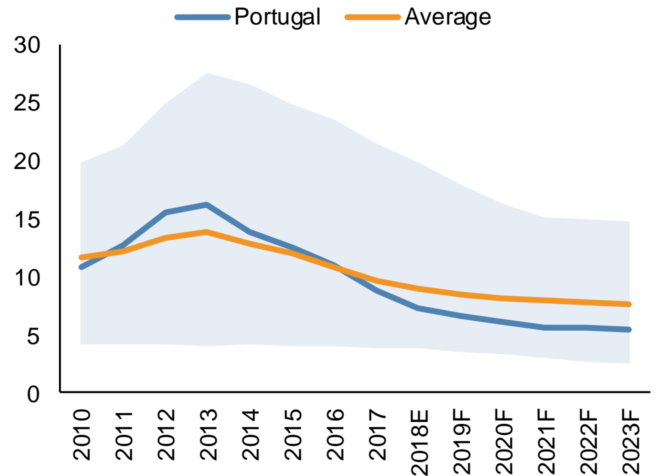
III. Appendix: Peer comparison

Figure 26: Real GDP growth



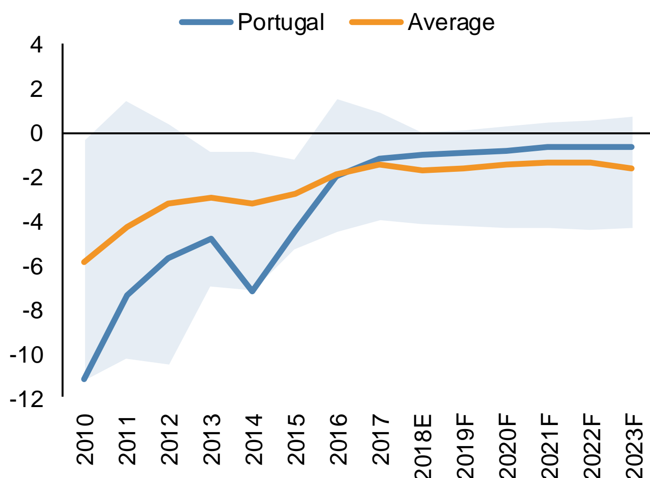
Source: IMF, Calculations Scope Ratings GmbH

Figure 27: Unemployment rate, % labour force



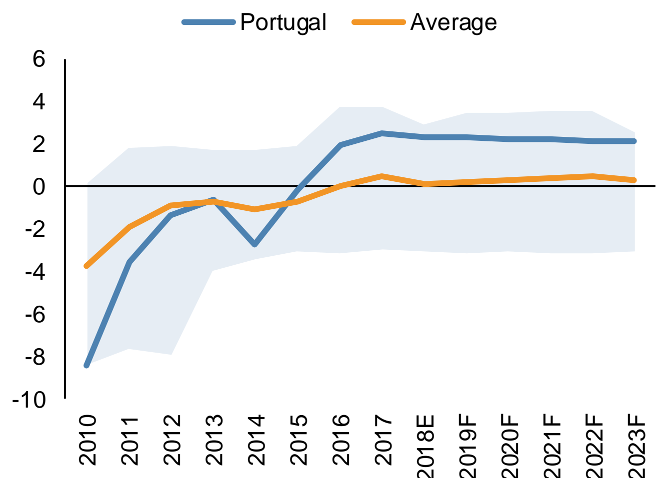
Source: IMF, Calculations Scope Ratings GmbH

Figure 28: General government balance, % of GDP



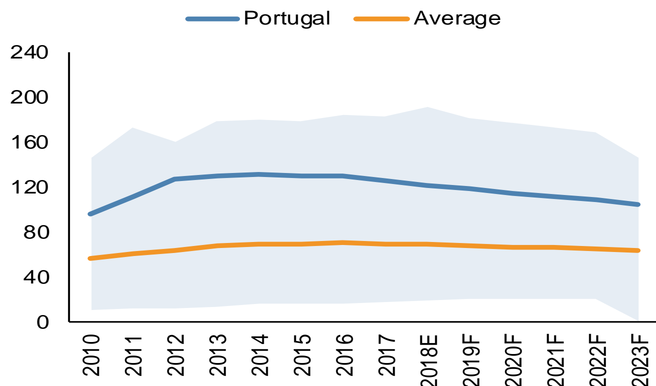
Source: IMF, Calculations Scope Ratings GmbH

Figure 29: General government primary balance, % of GDP



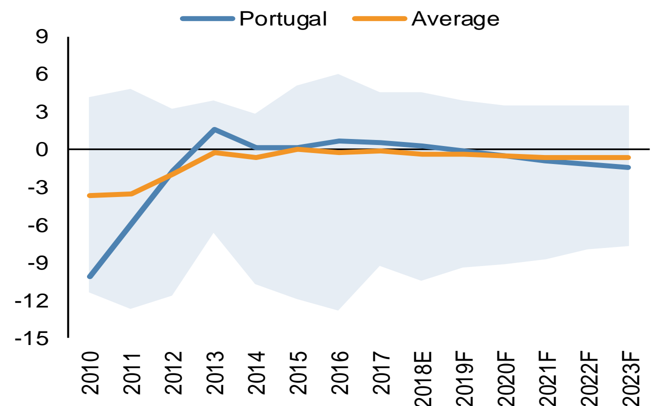
Source: IMF, Calculations Scope Ratings GmbH

Figure 30: General government gross debt, % of GDP



Source: IMF, Calculations Scope Ratings GmbH

Figure 31: Current account balance, % of GDP



Source: IMF, Calculations Scope Ratings GmbH

IV. Appendix: Statistical tables

	2013	2014	2015	2016	2017	2018E	2019F
Economic performance							
Nominal GDP (EUR bn)	170.3	173.1	179.8	185.5	193.1	200.8	207.6
Population ('000s)	10,457.0	10,401.0	10,358.0	10,326.0	10,305.0	10,269.0	10,234.0
GDP per capita PPP (USD)	27,899.5	28,746.7	29,532.4	30,658.6	-	-	-
GDP per capita (EUR)	16,282.3	16,640.5	17,359.3	17,964.7	18,740.9	19,549.6	20,287.6
Real GDP, % change	-1.1	0.9	1.8	1.6	2.7	2.4	1.8
GDP grow th volatility (10-year rolling SD)	2.3	2.2	2.3	2.3	2.3	2.4	2.2
CPI, % change	0.4	-0.2	0.5	0.6	1.6	1.6	1.6
Unemployment rate (%)	16.2	13.9	12.4	11.1	8.9	7.3	6.7
Investment (% of GDP)	14.6	15.3	15.8	15.5	16.3	17.1	17.9
Gross national savings (% of GDP)	15.3	15.4	15.9	16.1	16.8	17.4	17.8
Public finances							
Net lending/borrow ing (% of GDP)	-4.8	-7.2	-4.4	-2.0	-1.2	-1.0	-0.9
Primary net lending/borrow ing (% of GDP)	-0.6	-2.8	-0.1	1.9	2.5	2.3	2.3
Revenue (% of GDP)	45.1	44.6	43.8	43.0	43.1	43.0	42.8
Expenditure (% of GDP)	49.9	51.8	48.2	44.9	44.3	44.0	43.7
Net interest payments (% of GDP)	4.2	4.4	4.3	3.9	3.6	3.3	3.2
Net interest payments (% of revenue)	9.3	9.8	9.7	9.1	8.4	7.7	7.4
Gross debt (% of GDP)	129.0	130.6	128.8	129.9	125.6	121.2	117.5
Net debt (% of GDP)	107.3	111.9	113.1	112.3	108.1	105.2	102.6
Gross debt (% of revenue)	286.1	292.8	294.0	302.3	291.3	281.8	274.6
External vulnerability							
Gross external debt (% of GDP)	226.9	235.9	222.0	215.3	211.1	-	-
Net external debt (% of GDP)	99.6	104.3	100.7	94.5	92.5	-	-
Current-account balance (% of GDP)	1.6	0.1	0.1	0.6	0.5	0.2	-0.1
Trade balance [FOB] (% of GDP)	-	-4.7	-4.5	-4.3	-5.2	-5.5	-5.8
Net direct investment (% of GDP)	-1.7	-1.5	-0.7	-1.8	-4.3	-	-
Official forex reserves (EOP, EUR mil)	825.0	2,776.0	4,574.0	9,063.0	7,276.0	-	-
REER, % change	0.2%	-0.5%	-2.8%	1.6%	0.6%	-	-
Nominal exchange rate (EOP, USD/EUR)	1.4	1.2	1.1	1.1	1.2	-	-
Financial stability							
Non-performing loans (% of total loans)	7.8	13.6	14.4	14.4	-	-	-
Tier 1 ratio (%)	12.2	11.4	12.6	11.7	-	-	-
Consolidated private debt (% of GDP)	202.4	190.5	179.4	170.3	163.5	-	-
Domestic credit-to-GDP gap (%)	-16.0	-30.4	-42.0	-48.8	-49.7	-	-

Source: IMF, European Commission, European Central Bank, Bank of Portugal, World Bank, Haver Analytics, Scope Ratings

V. Regulatory disclosures

This credit rating and/or rating outlook is issued by Scope Ratings GmbH.

Rating prepared by Alvise Lennkh, Lead Analyst

Person responsible for approval of the rating: Dr Giacomo Barisone, Managing Director

The ratings/outlook were first assigned by Scope as subscription rating in January 2003. The subscription ratings/outlooks were last updated on 30.06.2017.

The senior unsecured debt ratings as well as the short term issuer ratings were last assigned by Scope on 30.06.2017.

The main points discussed by the rating committee were: i) Portugal's growth potential; ii) macroeconomic stability and sustainability; iii) fiscal consolidation, contingent liabilities, public-debt sustainability, debt structure and market access; iv) external debt sustainability and vulnerability to external shocks; v) banking sector performance and private-sector deleveraging; vi) political developments; and vii) peers.

Solicitation, key sources and quality of information

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The following material sources of information were used to prepare the credit rating: public domain and third parties. Key sources of information for the rating include: Ministry of Finance of Portugal, the Bank of Portugal, the BIS, the European Commission, the European Central Bank, Instituto Nacional de Estatística Portugal, Portuguese Treasury (IGCP), the Statistical Office of the European Communities (Eurostat), the IMF, the OECD, and Haver Analytics.

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