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PRESS RELEASE

STATEMENT BY THE EC, ECB AND IMF ON THE TENTH REVIEW MISSION TO PORTUGAL

Staff teams from the European Commission (EC), European Central Bank (ECB), and International Monetary Fund (IMF) visited Lisbon during December 4-16 for the tenth quarterly review of Portugal's economic adjustment program.

Further signs of recovery have emerged since the last review. Growth is broadly in line with projections, while unemployment has fallen by more than expected. External rebalancing has continued, although imports have picked up, reflecting stronger-than-expected domestic demand.

The program's fiscal targets have been confirmed. With tax collections performing well, the 2013 deficit target of 5.5 percent of GDP is achievable. The 2014 budget was approved by Parliament with only a few changes. It includes important steps towards rationalizing and modernizing public administration, improving the sustainability and fairness of the pension system, and lowering costs across ministries. If some of these measures are determined to be unconstitutional, the government has re-affirmed its commitment that it will then identify and implement compensatory measures of high quality to meet the agreed deficit target of 4 percent of GDP. Such measures, however, could heighten risks to growth and employment and reduce the prospects for a sustained return to financial markets.

The banking sector is stable, but low profitability signals that challenges remain. Capital buffers are broadly adequate and liquidity conditions are improving. However, profitability remains weak, and the corporate debt overhang is a source of vulnerabilities for the banking sector that must be addressed so as not to put a brake on medium-term growth prospects. Credit conditions remain challenging, notwithstanding recent improvements for lower-risk companies.

Continued structural reform efforts will have to be the centerpiece of a credible strategy for sustainable growth in the coming years. The Government has already made important progress in implementing challenging structural reforms, but more evidence of their impact on the functioning of the economy is needed. Accordingly, the implementation of reforms must be continuously evaluated to ensure that they deliver the desired results. Further efforts to facilitate a sustained rebalancing of the economy from the non-tradable to the tradable sector should focus on increasing competition and flexibility in product and labor markets, against the background of a more efficient and stream-lined public administration, so as to promote the flexible reallocation of resources. Articulating credible and time-bound reforms towards this end would reassure investors that improvements in Portugal's economic fundamentals are becoming entrenched.

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The program remains on track, and the authorities are determined to ensure continued program compliance. Market sentiment towards Portugal's sovereign debt has gradually improved, as also evidenced by robust demand for a debt exchange in early December, which reduced remaining financing needs in 2014. Public debt remains high but is sustainable provided program implementation and reaffirmed ownership remains resolute, thereby supporting the government's return to full market financing. Provided the authorities persevere with steadfast program implementation, euro area member states have declared they stand ready to support Portugal until full market access is regained.

Portugal's economic adjustment program is supported by loans from the European Union amounting to €52 billion and a €26 billion Extended Fund Facility with the IMF. The conclusion of the 10th review could take place in February 2014, subject to the approval of ECOFIN and EUROGROUP and of the IMF Executive Board. This would allow for the disbursement of €2.7 billion (€1.8 billion by the EU, and about €0.9 billion by the IMF) following the approval of the current review. The joint mission for the next program review is expected to take place in February 2014.

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