Economic Adjustment Program

On December 19th, after the successful conclusion of the 10th review mission, the **Constitutional Court ruled against a measure on the alignment of the public pension scheme rules with the general scheme's**.

On January 9th, the Government presented substitute measures: a broadening of an extraordinary solidarity contribution on pensions and an increase in employees and retirees' contribution to the public health insurance scheme. Through this action, the **Government reaffirmed its commitment to achieve the 4% of GDP deficit target for 2014**.

The **11th review mission** is scheduled to begin on **February 20th**.

Monthly Economic Indicators

Recent data suggest positive y-o-y GDP growth in 2013Q4, as indicators continue to point to a recovery in economic activity.

The **industrial production index increased 7.2%** y-o-y in December (compared with 3.4% in November) and the **economic climate indicator continued to recover** in January. INE's press releases are available here and here.

External Adjustment

i. International Trade of Goods

Export performance continued to be positive. In November, **exports of goods increased** by 7.2% y-o-y, **accelerating relative to October** (4.5%), reflecting the performance of both intra and extra-EU trade. **Imports decelerated in November** (3.2% y-o-y from 3.9% in October), mainly due to extra-EU trade. INE's press release is available here.

ii. Balance of Payments

Banco de Portugal's data **for January-November 2013** show that **both the capital and the current account balances remain in surplus**. Balance of Payments statistics available here.

Financial Markets

On January 9th, **IGCP issued a 5-year syndicated tap of the OT due 14 June 2019**, raising €3.25Bn, at a yield of 4.657%, with a strong presence of buy-and-hold investors and increased geographical diversification. On January 15th, **IGCP issued €1.01Bn in 12-month T-bills at a yield of 0.869%, the lowest rate since 2009**.

Government bond yields showed a strong decline overall in January. On January 31st, the 10-year yield was close to 5% and about 100 basis points below the level at the end of 2013.

2013 Budget Execution

According to preliminary data from the Ministry of Finance (available here), the **Program deficit target for 2013 has been met with a comfortable margin** (the target was € 8.90Bn and the corresponding deficit amounts to € 7.15Bn). The results mainly reflect a **good performance of tax revenue and social security contributions** while **expenditure remained under control**.

State tax revenue (in net terms) **rose by 13.1% relative to 2012**, well above the targeted increase of 8.9% and around € 1.35Bn higher than foreseen in the second supplementary budget. The increases were particularly significant in terms of:

- **Personal Income Tax** (35.5% reflecting the increase in the average tax rate);
- **Corporate Income Tax** (18.8% increase).

The good performance of tax collection reflects **better than expected economic activity, as well as gains in fighting fraud, tax evasion and the shadow economy**. It is also **partly explained by tax revenues obtained through the Extraordinary Scheme for the Settlement of Tax and Social Security Debts (RERD)**, amounting to €1045M (above the €500M initially envisaged). However, after excluding this effect, **current tax revenue still increased 10.1%** relative to 2012.

Social security recorded a surplus in 2013. This is partly justified by the effect of transfers from the State Budget, but is also a result of the increase in social security contributions (2.5%). The **latter also partially reflects the results of the RERD, which raised a total of €234M** (slightly above the expected collection of €200M).

As for Central Administration expenditure, **the increase in compensation of employees** (10.4%) mainly **reflects the reinstatement of the 13th and 14th monthly payments** and higher **contributions of public entities to social protection schemes. Excluding these effects, compensation of employees would have declined by 4.2%** relative to 2012, mainly due to the reduction in the number of public servants.

The balances of Local and Regional Administration were strongly influenced by the payment of debt, including the settlement of arrears. Excluding these effects, the balance of Local Administration would be a €366 M surplus (vs. the unadjusted €42 M deficit) while that of the Regional Administration would be a surplus of €67m (vs. the unadjusted €825 M deficit).

An updated presentation on the Portuguese adjustment may be downloaded here.