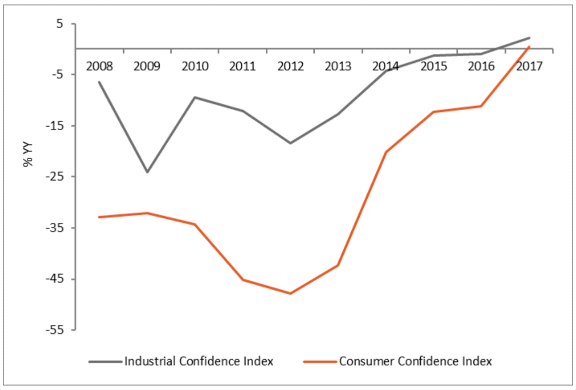
## Beginning of a new year – recapitulating 2017 and looking what's ahead

- First year-end data publications allow for performance analysis 2017 – robust recovery of labor market and price levels
- Funding conditions have remained supportive in the first month 2018, further retracements on longer maturity bonds (20Ys and 30Ys)
- Portugal has accumulated highest state cash buffer (%GDP) in whole Eurozone, expected to considerably reduce only as from 2021
- ECB reaffirmed current monetary policy stance, no definite end of asset purchase program announced

## Macroeconomics – First full year results 2017

### Sentiments and Confidence levels follow hard data recovery

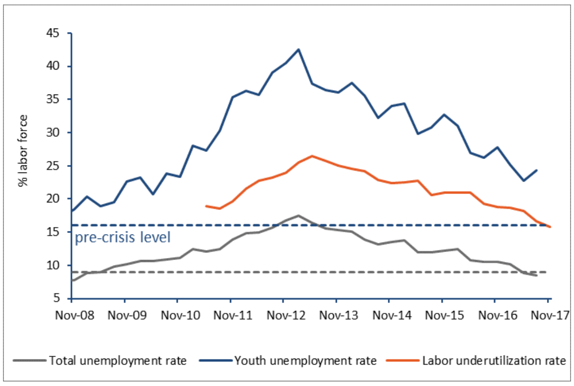
While GDP growth has started recovering since 2014, investors, producers and consumers only gradually regained confidence in the Portuguese economy and financial market along the past one and a half years. Only in the past 12 months consumer confidence levels for the first time since its record start in 1997 started increasing. 2017 further marks a turning point for the country's sovereign debt market. Investors' confidence in the Portuguese debt market has grandly been re-established, allowing the country to cut its borrowing costs (10 Y yield levels) in half in 2017.




Source: INE, OECD

### Robust recovery in labor market, pre-crisis levels reached

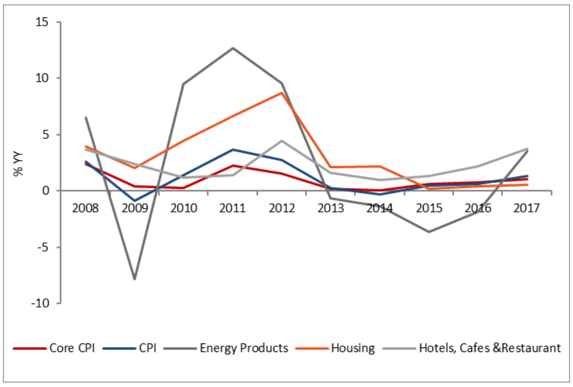
Unemployment has reached pre-crisis level this year. The annual unemployment rate is estimated at around 9% for 2017, 2 percentage points lower than in 2016 (11.2%). New employment has primarily been created in sectors characteristic for lower-skilled, lower-income job profiles (service sector, production of durable consumer goods, construction), therefore only resulting in moderate increases in wage levels. Youth unemployment has slightly improved along the year, estimated at 22.1% in December 2017 (26.2% in December 2016).




Source: INE, BiG Research

### Significant pick-up in domestic price pressure

The annual inflation rate increased from 0.6% in 2016 to 1.4% in 2017, core inflation (excluding food and energy prices) increased from 0.7% to 1.1%. Apart from considerable price increases in energy products (3.5% YY), tourism and real estate further contributed significantly to domestic price pressure. Prices in *Hotels, Cafes & Restaurants* increased by 3.7% YY in 2017. The price development in Portugal is in line with the moderate pick-up of inflation in the Euro area. The annual HICP inflation for 2017 is measured 0.1 percentage points above the annual HICP inflation rate of 1.5% for the whole Euro area.




Source: INE

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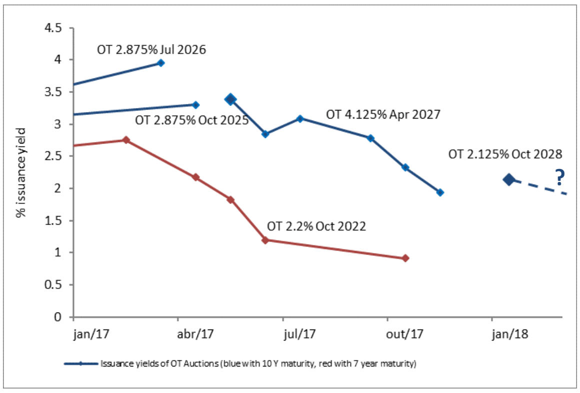
## Primary Market - January

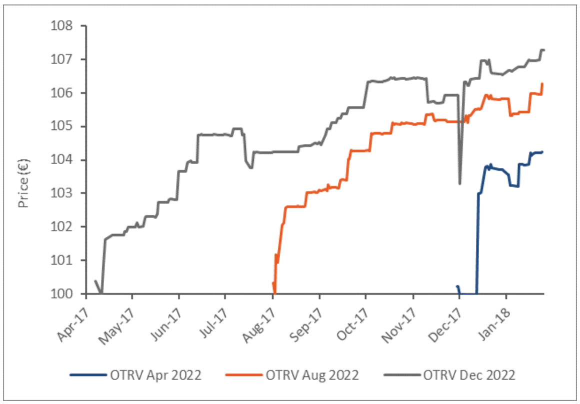



Source: IGCP, BiG Research

### Beneficiary financing conditions continue in early 2018

A new 10-year maturity OT line *Oct 2028* has been placed through a € 4 bn syndicated issuance, with a coupon of 2.125% and a re-offer yield of 2.137%. Biggest investor demand came from the UK (35%), followed by France, Italy and Spain (30.4%) and Portugal (12.4%). A further treasury bill auction achieved the lowest rates for short-term debt ever issued. Additionally, Portugal has settled further € 800 mn repayments of the most expensive outstanding tranches of its IMF loan. The outstanding € 4.6 bn IMF loans hold an average maturity of 4.5 years with considerably lower interest rates.

## Secondary Market - January

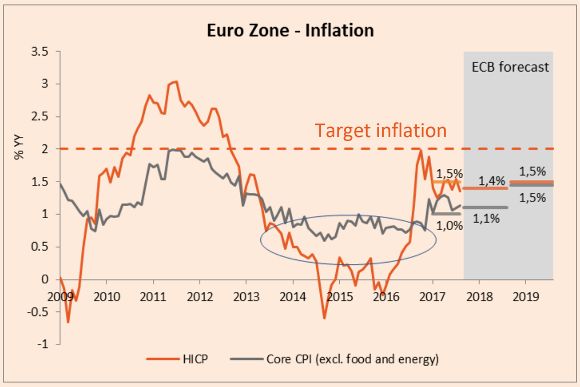



Source: Reuters

### Longer-term maturity bond yields fall, OTRVs gain of popularity

The Portuguese 10 Y yields have closed the first month of the year below the psychological 2% level, continuing to trade below Italy's. Longer-term maturity bonds (20Ys and 30s) have experienced further yield retracements, evident for the broadening of Portugal's investors' base given its re-establishment of investment grading. The 10 Y PGB/Bund spread compressed by around 25 bps, primarily due to higher Bund yield levels reflecting the gradual end of the ultra-loose ECB monetary policy and that have not translated into perceived higher periphery risk (yet). OTRV series trade above their nominal value on the secondary market, given their increasing popularity as a domestic savings alternative.

## ECB Governing Council Meeting – January 25th




Source: ECB Projections December 2017

### No further information on ending of asset purchase program

The ECB left its monetary policy stance unchanged this month, confirming to let its asset purchase program (at a current monthly volume of € 30 bn) run until September, "or beyond, if necessary". The Euro area annual inflation rate HICP was measured at 1.4% in December 2017, the development of prices remains subdued, forecasted to remain below its price stability target of 2% in the coming two years. Key interest rates are stated to remain at their present levels, "well past the horizon of (the) net asset purchases". We do not expect rate hikes earlier than in the first or second quarter of 2019.

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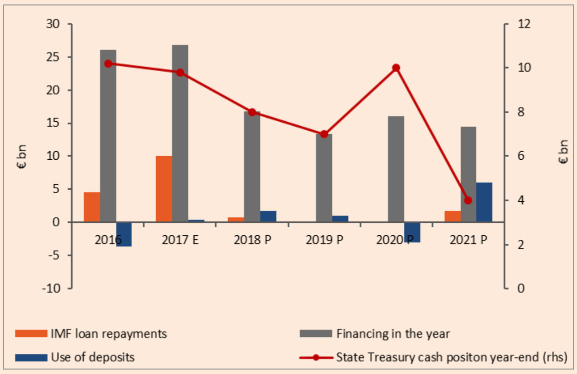
## State Treasury Cash Position 2018




Source: IGCP Investors Presentation January 2018

### Portugal holds highest cash buffer (%GDP) in Euro zone

Portugal has accumulated a considerable cash buffer (excluding gold) from € 1.3 bn in 2008 to currently more than € 10 bn, corresponding to 5.3% of GDP - currently the highest share of GDP in the Euro zone area. Spain holds cash reserves worth 4.2% of GDP, Italy 2.4% of GDP, Germany 1.7%, Greece 1.4%*. The Portuguese Treasury and Debt Management Agency (IGCP) scheduled to decrease Portugal's cash buffer from year-end € 9.8 bn in 2017 to € 8 bn by the end of 2018 – allowing for a € 1.8 bn "negative surplus variation", corresponding to 0.6 percentage points of GDP. A considerable reduction in its cash buffer is however only intended as of 2021 (€ 4bn).

## Outlook – February

### Catalonia – "Political limbo" remains

Spanish courts have ruled out for Mr. Puigdemont to be elected as leader of the new Catalan government. Still fugitive in Brussels and facing charges of sedition and rebellion in Spain, Puigdemont was unable to attend "physically" the new regional government's elections – a legal requirement to become elected president. The election of the new government has been postponed for an indefinite period. Should the pro-independence parties not be able or willing to propose an alternative leader, re-elections are the only alternative – implying further (unnecessary) uncertainty for Spain and the European integration progress as a whole.

| Event Outlook - February | |
|---|---|
| **Date** | **Event** |
| 7-Feb | Unemployment rate (Q4 2017) |
| 9-Feb | Global trade balance (Dec 2017) |
| 12-Feb | Consumer price index (Jan) |
| 14-Feb | GDP growth (Q4 2017) |
| 21-Feb | Current Account Balance (Dec 2017) |
| 21-Feb | Reopening 3m & 11m T-Bills |
| 27-Feb | Business Confidence (Feb) |
| 27-Feb | Consumer Confidence (Feb) |
| 28-Feb | Unemployment rate (Jan) |

### Data Publication:

- **Annual GDP growth rate 2017**

BiG Research estimates an annual growth rate of 2.6% for 2017, in line with the annual growth estimates from the Ministry of Finance, the IMF and Banco de Portugal. The Portuguese Public Finance Council - usually known for its prudent projections - represents the most optimistic forecast of 2.7% growth in 2017.

### Treasury and Debt Management (IGCP):

- Feb 21st: Auction of 6 months and 11 months BTs (reopening), indicative amount set between € 1 bn and € 1.25 bn

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| MACROECONOMIC DEVELOPMENT | | | BiG Research | | Forecasts 2018 | |
|---|---|---|---|---|---|---|
| | | | Projections | Assessment | IMF** | Ministry of Finance |
| | 2015 | 2016 | 2017 P | Development 2017 | 2018 P | 2018 P |
| **Real Economy (YoY, % change)** | | | | | | |
| GDP | 1.8 | 1.5 | 2.59 | ↑ | 2.0 | 2.2 |
| Private Consumption | 6.4 | 0.9 | 2.13 | ↑ | 1.8 | 1.9 |
| Public Consumption | 6.1 | 4.1 | -0.21 | ↓ | 0.5 | -0.6 |
| Investment (GFCF) | 2.1 | 2.1 | 8.85 | ↑ | 5.7 | 5.9 |
| Imports | 8.5 | 4.1 | 7.37 | ↑ | 5.2 | 5.2 |
| Exports | 2.7 | 1.6 | 7.47 | ↑ | 5.1 | 5.4 |
| **Fiscal Account (%GDP)** | | | | | | |
| Primary balance | 0.2 | 2.2 | 2.5 | ↑ | 2.7 | 2.7 |
| Budget balance | -4.4 | -2.0 | -1.4 | ↑ | -1.4 | -1.0 |
| Public debt | 128.8 | 130.2 | 124.85 | ↑ | 122.5 | 123.5 |
| **External Accounts (%GDP)** | | | | | | |
| Current Account | 0.1 | 0.7 | 0.51 | → | 0.5 | 0.1 |
| NIIP | -112.0 | -104.7 | -103.96 | → | | |
| Gross External Debt | 222.3 | 215.8 | 213.65 | → | | |
| **Labour market (YoY, %change)** | | | | | | |
| Unemployment Rate | 12.4 | 11.1 | 9.13 | ↑ | 9.0 | 8.6 |
| ULC | 0.9 | 2.6 | 1.45 | ↑ | | |
| Labor Productivity | 0.4 | -0.1 | -0.40* | ↓ | | |
| **Sentiment Indicators** | | | | | | |
| Consumer Confidence Indicator | -12.6 | -11.7 | -0.10 | ↑ | | |
| Industrial Confidence Indicator | -1.2 | -0.9 | 2.26 | ↑ | | |
| **Financial Sector** | | | | | | |
| Tier 1 Ratio | 11.3 | 11.5 | 12.96 | ↑ | | |
| Return on Equity | 0.5 | -3.2 | -0.19 | ↑ | | |
| Share of NPLs (NFC; % of total loans) | 15.9 | 16.0 | 15.16 | → | | |
| **Monetary/FX** | | | | | | |
| Inflation, HICP (YoY, % change) | 0.50 | 0.64 | 1.55* | ↑ | | |
| PGB 10Y-Bund Spread (Bps) | 213.9 | 238.1 | 373* | ↑ | | |
| EUR/USD | 1.1 | 1.1 | 1.08* | | | |
| Real effective exchange rate (1999=100) | 87.0 | 89.2 | 90.46* | → | | |

Source: INE, Banco de Portugal, ECB, Reuters, DG ECFIN, OECD

*Full-year data 2017 already available, no projection

**IMF Article IV country report projections, ***Ministry of Finance projections as accounted for/published in the State Budget 2018

**Cross-Country Bund Spreads**

| Bps | France | Spain | Italy | Portugal | Greece |
|---|---|---|---|---|---|
| 2y | 16.3 | 30.2 | 30.3 | 42.8 | 197.2 |
| 5y | 17.3 | 43 | 72.8 | 85.4 | 288.2 |
| 10y | 29.7 | 72.3 | 132.8 | 126.4 | 304.1 |
| 30y | 45.1 | 118.7 | 172.5 | 160 | 660.6 |
| **Δ 1M** | | | | | |
| 2y | -2.1 | -9.8 | -17.2 | -9.8 | -43.4 |
| 5y | 2.7 | -19.7 | -18.4 | 22.1 | -83.5 |
| 10y | -6.4 | -41.9 | -24.6 | -24.4 | -65.4 |
| 30y | -5.4 | -41.5 | -24 | -32.8 | -6.6 |

Source: Reuters, retrieved on January 31st, 2018

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