

## Portugal: moratoria, guarantees and the banks

- The Portuguese banking system is in a reasonably resilient position to tackle the COVID-19 crisis and contribute to the recovery.
- Containing credit risk is one of the key challenges ahead, especially if the moratoria and guarantees expire before the economic recovery is on track.

The Portuguese banking system faces the aftermath of the COVID-19 crisis with a more resilient position and greater room for manoeuvre in dealing with stress situations (see first table). There are several positive aspects which stand out: i) the solvency and liquidity indicators exceed EU average levels; ii) yield ratios were improving up until the outbreak of the pandemic and interest margins have remained stable despite low interest rates; iii) although the level of doubtful loans remains above the European average, in the years leading up to the pandemic it was improving, and iv) the coverage levels in the face of a potential impairment of these loans are higher than the European average.

However, in the context of significant contractions in economic activity as a result of the COVID-19 crisis, containing credit risk will be a major challenge for the sector going forward, especially if the credit moratoria and guarantees expire before the economic recovery is on track.

### The role of moratoria...

On the one hand, credit moratoria<sup>1</sup> temporarily mitigate the liquidity tensions that can occur when a reduction in income occurs, while they also provide protection for creditors in the event of defaults. Under the credit moratoria approved in Portugal, up until September 2021 affected households and firms can forego paying their

### Portugal: banking system indicators \*

|                                | 2011  | 2014  | 2016  | Q2 2020 | Q3 2020 | European Union ***<br>(Q2 2020) |
|--------------------------------|-------|-------|-------|---------|---------|---------------------------------|
| <b>Efficiency</b>              |       |       |       |         |         |                                 |
| Efficiency ratio               | 61.7  | 65.2  | 59.4  | 61.0    | 58.1    | 66.7                            |
| <b>Yield</b>                   |       |       |       |         |         |                                 |
| ROE                            | -4.0  | -17.3 | -3.9  | 0.9     | 1.7     | 0.5                             |
| ROA                            | -0.2  | -1.2  | -0.3  | 0.1     | 0.1     | 0.0                             |
| Interest margin                | 1.5   | 1.3   | 1.5   | 1.5     | 1.5     | 1.3                             |
| <b>Asset quality</b>           |       |       |       |         |         |                                 |
| Doubtful loans **              |       |       |       |         |         |                                 |
| Private sector                 | 7.5   | 11.9  | 17.5  | 6.6     | 6.2     | 2.9                             |
| Housing                        | 5.0   | 5.9   | 7.0   | 2.2     | 2.1     | 2.7                             |
| Consumption                    | 13.3  | 17.0  | 16.2  | 8.6     | 8.4     | -                               |
| Non-financial firms            | 9.7   | 19.0  | 29.5  | 11.1    | 10.6    | 5.1                             |
| Coverage ratio **              | 56.8  | 64.0  | 45.3  | 53.1    | 55.9    | 45.3                            |
| Cost of risk (CoR)             | 1.2   | 2.4   | 1.8   | 0.9     |         | 0.9                             |
| <b>Solvency</b>                |       |       |       |         |         |                                 |
| Capital ratio (CET1)           | 8.7   | 10.5  | 11.4  | 14.6    | 14.9    | 14.7                            |
| Leverage ratio                 | -     | -     | 6.6   | 7.6     | 7.6     | 5.1                             |
| <b>Liquidity</b>               |       |       |       |         |         |                                 |
| Loan to deposit ratio (LTD)    | 135.0 | 102.0 | 95.5  | 84.6    | 85.2    | 116.1                           |
| Liquidity coverage ratio (LCR) | -     | -     | 150.8 | 256.6   | 235.9   | 165.7                           |

**Notes:** \* More information on these financial concepts can be found at [https://www.caixabank.com/aula/recursos-de-formacion/conceptos-financieros\\_es.html](https://www.caixabank.com/aula/recursos-de-formacion/conceptos-financieros_es.html). \*\* New series from 2015 onwards.

\*\*\* The comparison between Portugal (based on Bank of Portugal data) and the EU (based on EBA data) is indicative, as there are technical calculation differences.

**Source:** CaixaBank Research, based on data from the Bank of Portugal and the EBA.

1. The public moratoria will be in force until 30 September 2021; the application deadline expires on 31 March 2021 and they apply to households and firms that are up-to-date with their tax obligations. The financial situation of the companies must obey certain rules, and they can request an extension or suspension of the payment of the capital, interest and guarantees assumed until 27 March 2020. In the case of households affected by the pandemic, the moratoria affect mortgages and loans for education. The private moratoria adopted by the banks encompass credit contracts that do not benefit from the public moratoria, such as personal, car and credit-card loans.

loan instalments,<sup>2</sup> without this resulting in their credit being classified as doubtful. Furthermore, the loan maturity date is deferred by the number of months for which the debtor benefits from the moratorium. This helps to contain default ratios, as it prevents debtors' temporary liquidity difficulties from translating into solvency problems.

As shown in the second table, in September moratoria affected 17.3% of household credit and 32.0% of business credit. That is, the total amount of credit under moratoria amounted to 45 billion euros, or approximately 23% of the stock of private sector credit and GDP. In addition, the Bank of Portugal estimates that up until September 2021 the cumulative sum of instalments that will have gone unpaid as a result of moratoria will amount to €13 billion: €2 billion for households and €11 billion for companies.

Indeed, Portugal has registered the third highest usage of moratoria in the euro area (22.2% of total credit according to data from the EBA up to June,<sup>3</sup> significantly above the European average of 7.5%). This is explained by a combination of factors: i) a level of indebtedness which, despite the deleveraging process of recent years, is still relatively high (among households it stands at 66% of GDP in Portugal, compared to 60% in the euro area as a whole, while among firms it is 101.4% versus 115% for the euro area, according to Eurostat); ii) a low savings rate, and iii) especially for firms and self-employed workers, the fact that the tourism sector, which accounts for a large part of GDP, has been one of the hardest hit.

Housing credit moratoria are particularly prominent (around 40% of private sector credit is subject to moratoria and 84% of credit to individuals with a moratorium is housing credit). Nevertheless, there are factors that help to mitigate this concern. On the one hand, the default rate among housing credit has historically been very low, reflecting households' strong commitment to honouring housing-related debts. It should also be noted that the rise in unemployment in 2021 is expected to be relatively moderate, so the increase in the default rate ought to be contained and should not tarnish the significant improvement achieved in the years leading up to the pandemic.<sup>4</sup> On the other hand, among the loans which have benefited from moratoria, Portugal has registered one of the lowest percentages of increased credit risk in these loans (see last chart).

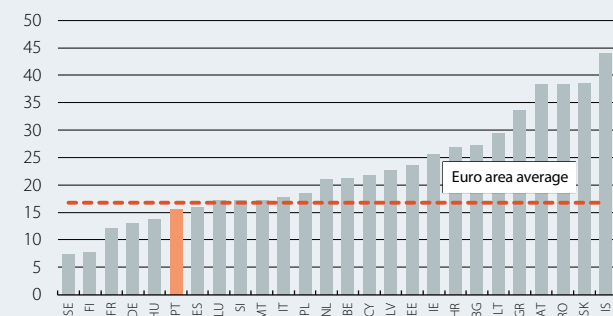
2. Moratoria are available to micro-enterprises and SMEs that have a reasonably compliant tax situation and have no payments more than 90 days overdue. Households are also required to have suffered a reduction in their income as a result of the COVID-19 crisis (reduction of hours worked, loss of employment, etc.).  
 3. EBA (2020). *First evidence on the use of moratoria and public guarantees in the EU banking sector*. Thematic note of November 2020.  
 4. Our projections suggest a 1-pp increase in the unemployment rate for 2021 as a whole, which would lead to an increase in defaults of around 0.08 pps, according to the historical relationships.

**Portugal: moratoria and credit lines with a state guarantee**

|  | EUR millions  | % of respective credit portfolio |
|--|---------------|----------------------------------|
| <b>Moratoria</b>   |               |                                  |
| <b>Individuals - Total</b>   | <b>21,272</b> | <b>17.3</b>                      |
| Housing  | 17,952        | 18.5                             |
| Consumption  | 3,320         | 17.2                             |
| <b>Non-financial firms - Total</b>   | <b>23,237</b> | <b>32.0</b>                      |
| Accommodation and catering   | 2,972         | 50.0                             |
| Consulting and industry  | 6,133         | 30.0                             |
| Construction   | 1,581         | 25.0                             |
| Retail   | 2,866         | 24.0                             |
| Transportation   | 1,075         | 22.0                             |
| <b>Loans with a guarantee granted to non-financial firms (March - September)</b> |               |                                  |
| Total new lending  | 7,029         | 40.0                             |
| <b>Breakdown:</b>  |               |                                  |
| to the hardest-hit sectors *   | 4,147         | 59.0                             |
| to SMEs  | 3,093         | 44.0                             |
| to large corporations  | 1,195         | 17.0                             |

*Note:* \* Accommodation, catering, retail, transportation, storage, artistic, entertainment and leisure activities, and industry.  
*Source:* CaixaBank Research, based on data from the Bank of Portugal.

**Portugal: loans that have suffered a significant increase in their credit risk (IFRS 9 stage 2) \* (% of loans with a moratorium that has not expired)**



*Note:* \* Under IFRS 9, a loan is considered to be in stage 2 when it has suffered a significant increase in its credit risk but it has not yet generated losses.  
*Source:* CaixaBank Research, based on data from the EBA.

**... and credit guarantees**

Another of the major tools introduced to cushion the blow of the COVID-19 crisis is the state-guaranteed credit lines.<sup>5</sup> These aim to maintain the flow of loans to the real economy, at a time when credit risk in the demand for credit has increased due to the economic impact of the pandemic. They are generally intended for SMEs, micro-enterprises and self-employed workers who are unable

5. The state guarantee amounts to as much as 90% in the case of micro and small enterprises, and up to 80% for medium-sized, Small Mid Cap and Mid Cap2 enterprises. It is granted to companies that were financially viable prior to the COVID-19 crisis, that have positive shareholders' equity, that have a compliant tax and financial situation and that were incorporated more than two years ago. The term of these loans can be up to six years and they come with an 18-month grace period.

to obtain bank credit. In Portugal, these secured credit lines accounted for around 40% of all loans granted to companies between March and September 2020 (€7 billion) and are largely concentrated in SMEs operating in the hardest hit sectors.<sup>6</sup>

Despite the risks associated with the granting of credit to companies in a weaker position, according to the Bank of Portugal the evolution of their risk profile is proving even slightly better than that of other loans, because of the conditions under which they are granted. On the one hand, these credit lines have an 18-month grace period. This means that the repayments will not begin until September this year, at which point economic activity is expected to be on the road to recovery. Moreover, the fact that these loans are mostly granted for terms of over five years reduces the potential for the borrowing firms to experience financial stress.<sup>7</sup>

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6. Accommodation and catering, retail, transportation and storage, artistic, entertainment and leisure activities and, to a lesser extent, manufacturing.

7. According to the EBA, 47.2% of the loans have a maturity of more than 5 years and 50.9% have a maturity of between 2 and 5 years.