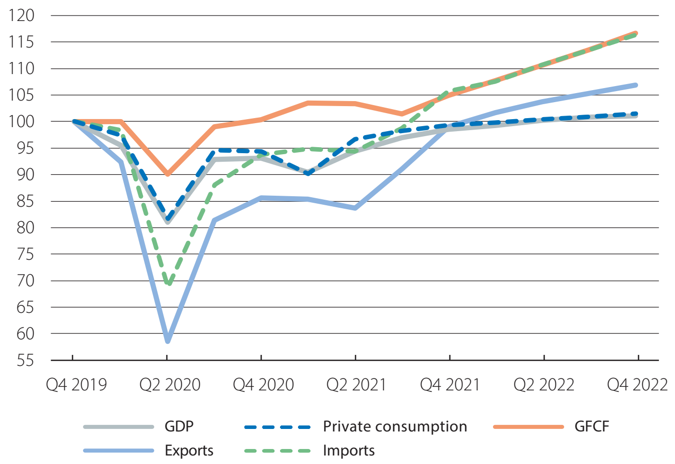
Portugal's buoyant economic activity is ruffled by the conflict in Ukraine

GDP grew by 4.9% in 2021, narrowing the gap compared to 2019 to 3.9%, while 2022 began on a relatively strong note. Growth benefited from the significant recovery in domestic demand, as well as from the contribution from exports (5 pps). Although indicators for 2022 are still scarce, those that are available show a positive trend. In an ordinary international context, this would suggest that the economy could outperform our initial expectations for this year (4.9% in 2022). For instance, the daily economic activity indicator grew by 3.7% year-on-year in the first half of the quarter. Similarly, electronic card payments in January were 9% higher than the levels of January 2020 (before the pandemic), while the sentiment indicators (the results are prior to Russia's invasion of Ukraine) registered significant improvements in February despite the blow from commodity and labour shortages. However, the outbreak of the conflict in Ukraine has introduced significant uncertainty, with downside risks, due to the rise in the price of energy products on the international market and the foreseeable cooling of economic activity in Portugal's main trading partners, especially in the case of central European countries. In this context, it is less clear in which direction we should revise our previous forecast of 4.9% GDP growth for 2022, so we opt to maintain this scenario and await a more complete picture of the consequences of the current situation.

Upside inflation risks. The first estimate of the February CPI confirms the upward trend of recent months: inflation reached 4.2% (3.3% in January). The rising energy prices and the transmission to other goods continue to be the main upside risk for 2022. As a result of Russia's invasion of Ukraine, Brent oil and gas prices have surged, at a time when supply chains have not yet returned to normal and issues in the supply of some commodities are cited among the main obstacles to industrial production.

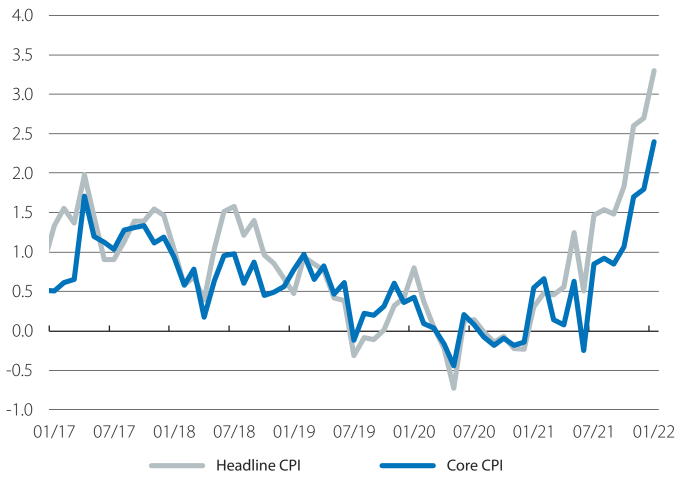
Very positive developments in the labour market in 2021, following the deterioration of the previous year. Employment ended 2021 with an increase of 148,400 people in work, while the number of unemployed people fell by 42,600 and the unemployment rate dropped to 6.3% from the 7.3% of the end of 2020. This represents an improvement on the pre-pandemic levels: there are 93,100 more jobs and 21,800 fewer unemployed than in Q4 2019. The increase in employment has spread to both the private and the public sector: private-sector employment at the 2021 year end exceeds the pre-pandemic level by 133,700 people, while public-sector employment remained some 14,600 people above pre-COVID levels, partly driven by the needs arising from the pandemic (e.g. health professionals).

Portugal: evolution of GDP and its components
Index (100 = Q4 2019)



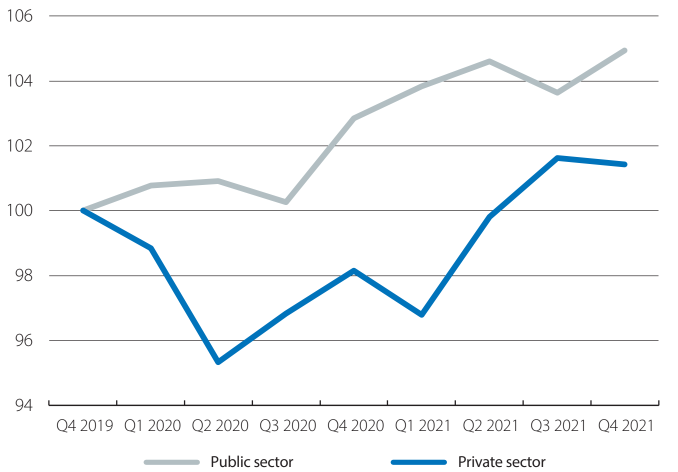
Source: *CaixaBank Research, based on data from the National Statistics Institute of Portugal.*

Portugal: CPI
Year-on-year change (%)



Source: *CaixaBank Research, based on data from the National Statistics Institute of Portugal.*

Portugal: employment in the public and private sectors
Index (100 = Q4 2019)



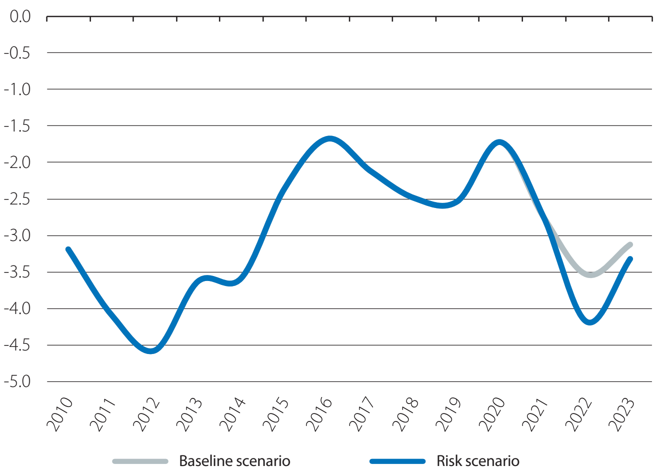
Source: *CaixaBank Research, based on data from the National Statistics Institute and the DGAEP of Portugal.*

Relatively stable current deficit in 2021. In the last year, the current account deficit amounted to 2,403 million euros (–1.1% of GDP), a deterioration of 265 million compared to 2020. By component, there have been notable improvements in the surpluses of the tourism balance (1,396 million more than in 2020) and the balance of secondary incomes (+1,245.5 million), as a result of the increase in European funds received. However, these improvements were not enough to offset the small deterioration in the balance of non-energy goods, the slight contraction in the surplus of non-tourism services and the significant deterioration in the energy deficit. The latter increased to 5,930 million euros (2,378 million more than in 2020) due to higher prices of imported energy goods, especially crude oil. The change in the quantities of fuel imports was just 1.9%, while the prices (unit value indices) of energy imports rose by around 60%.

Tourism: uneven recovery. Despite the strength of tourist numbers in 2021, with 40% growth over 2020, the recovery has not been uniform between regions and types of accommodation. In fact, the Lisbon Metropolitan Area (LMA) is the major loser. The revenues of tourist accommodation establishments is the LMA are the furthest from pre-pandemic levels (–61% compared to 2019), and the number of guests in 2021 was still 58% below 2019 levels, while for the country as a whole it was 46% below. These figures can be explained by two factors: (i) the greater relative weight of foreign tourists in this region compared to the rest and (ii) the fact that it is also the main region that resident tourists came from, and they chose to travel to less densely populated parts of the country that were also less affected by the pandemic. As for accommodation types, there are also marked differences: rural and family tourism was the star of 2021, registering only 5% fewer overnight stays than in 2019, well ahead of the hotel sector as a whole (–48% of overnight stays in the year as a whole compared to 2019).

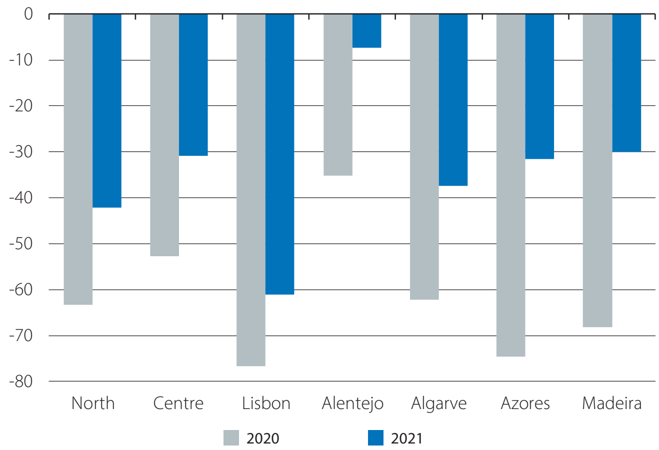
New lending to businesses fell in 2021 by 11.4% year-on-year. This decline was driven by new lending to businesses (–33.5%), in part due to the comparison effect in the face of the high volume of state-guaranteed credit facilities that were granted during 2020. Correcting for this impact, new lending to businesses fell by 9.9%. New lending for housing, meanwhile, remained buoyant (+34% compared to 2020), despite remaining far from the peak of 2007. On the other hand, the pandemic continues to have a negative impact on the indebtedness levels of the non-financial sector, which at the end of 2021 reached around 768,100 million euros (363% of GDP). This amount represents 42,745 million euros more than at the end of 2019, and over 60% of this increase is the result of the deterioration in the debt levels of the non-financial public sector due to the efforts to combat the pandemic. The stock of non-financial private sector loans, meanwhile, increased by 3.0% year-on-year in January.

Portugal: energy balance
(% of GDP)



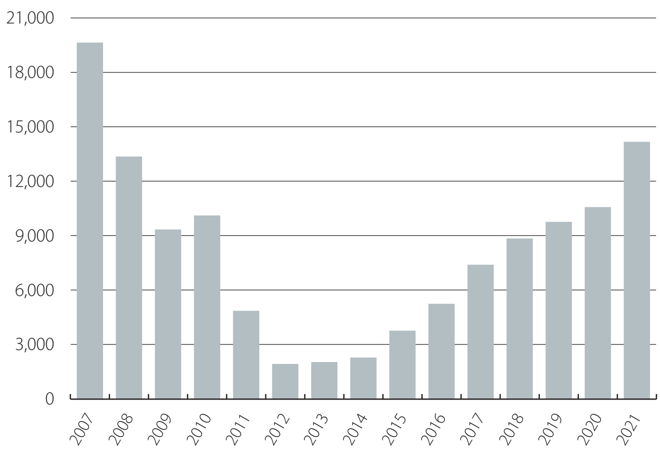
Source: *CaixaBank Research, based on data from the Bank of Portugal.*

Portugal: revenues of tourist accommodation establishments by region
Change versus *2019 (%)*



Source: *CaixaBank Research, based on data from the National Statistics Institute of Portugal.*

Portugal: new lending for housing
Year-to-date cumulative balance (EUR millions)



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