Lisbon School of Economics & Management
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ISEG Economic Outlook

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SUMMARY

According to the flash estimates of INE, Portugal's ***GDP*** *decreased in volume by 5.4% year-on-year and 3.3% in relation to the previous quarter during the 1st Quarter of 2021, which was affected by a lockdown for most of the period. Year-on-year Internal Demand was -3.4% during the Quarter, basically due to the behaviour of Private Consumption (-6.9%), with the contribution of Net External Demand (NED) being -2 pp.*

The Climate and Economic Sentiment indicators increased significantly in April and May, surpassing the pre-crisis levels. This resulted from the coming out of lockdown, the reopening of activities, and the progressive control of the health crisis. In the Euro Area, the evolution of the confidence and economic sentiment indicators has been similar, albeit slightly earlier overall than that verified in Portugal.

Based on the already-available data, and bearing in mind the year-on-year base, GDP is expected to grow year-on-year by between 14.5% and 15.5% during the 2nd Quarter of 2021, and between 4.2% and 5.1% in quarter-on-quarter terms.

0. THE EVOLUTION OF GDP AND ITS COMPONENTS DURING THE 1ST QUARTER OF 2021

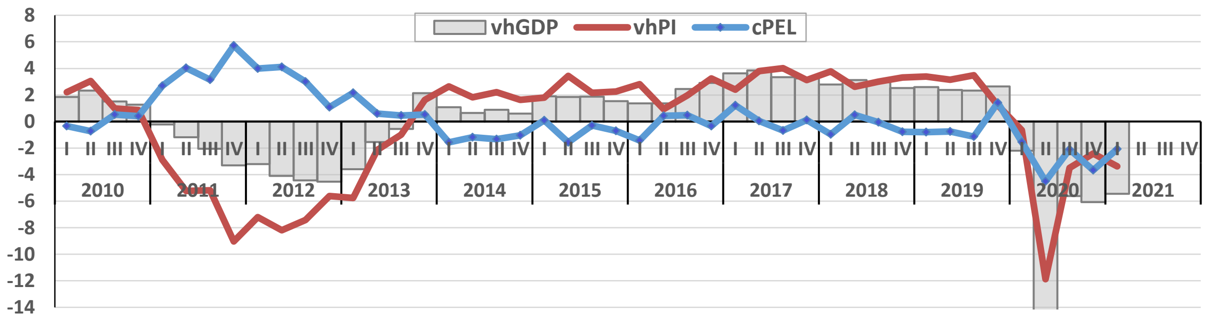
According to the INE Quarterly National Accounts, the preliminary forecast of 31/05/21, in comparison to the 4th Quarter of 2020 – which was characterised by a worsening of the pandemic and by a second, longer period of lockdown – the variation of GDP for the 1st Quarter of 2021 was -3.3%, which reversed the tendency of recuperation of the previous two quarters. The year-on-year variation in GDP was -5.4%, which was less negative than that registered during previous quarters, owing to the fact that the equivalent former base period had already already partially affected by the economic effects of the fight against the pandemic.

In terms of the components of demand, the year-on-year variation in Internal Demand (ID) of -3.4% was more negative that the previous quarter, as a result of the lockdown and its impact on the supply and consumption of certain types of goods, whereas the contribution of Net External Demand (NED) of -2.0 p.p. was less negative (see graph).

For ID, the larger year-on-year decrease in Private Consumption needs highlighting, as it fell from -4.6% during the last quarter of 2020 to -6.9% during the 1st Quarter of 2021. The contribution of Public Consumption was positive (with a growth of 2.8%) and was slightly greater than during the previous quarter. The contribution of Investment was also positive: registering growth of 3.7% during the 1st Quarter (especially for Construction and for Machinery and Equipment), in contrast to a growth of only 0.8% during the previous quarter.

With regards NED, in the light of a decrease in Exports and Imports, which was more accentuated on the Exports side, due to the fall in tourism demand, it can be seen that the contribution of NED to the year-on-year variation in quarterly GDP continued to be negative. However, the differential between the decrease in Exports and Imports narrowed during the 1st Quarter of 2021, with the year-on-year deterioration in the external balance being smaller and the contribution of NED being less negative than during the previous quarter (see graph).

Graph 0 | Year-on-year variation in GDP and the contributions of Internal Demand and Net External Demand



The year-on-year variation for all the EURO AREA (EA19) countries during the 1st Quarter of 2021 was -1.8%, with a variation of -0.6% compared to the previous quarter. Portugal was the country which registered the most negative cyclical variations among the AE19 during this quarter. Among the larger countries, Germany registered a year-on-year fall of 3%, Spain decreased by 4.3%, and Italy by 1.4%, while France increased by 1.5%.

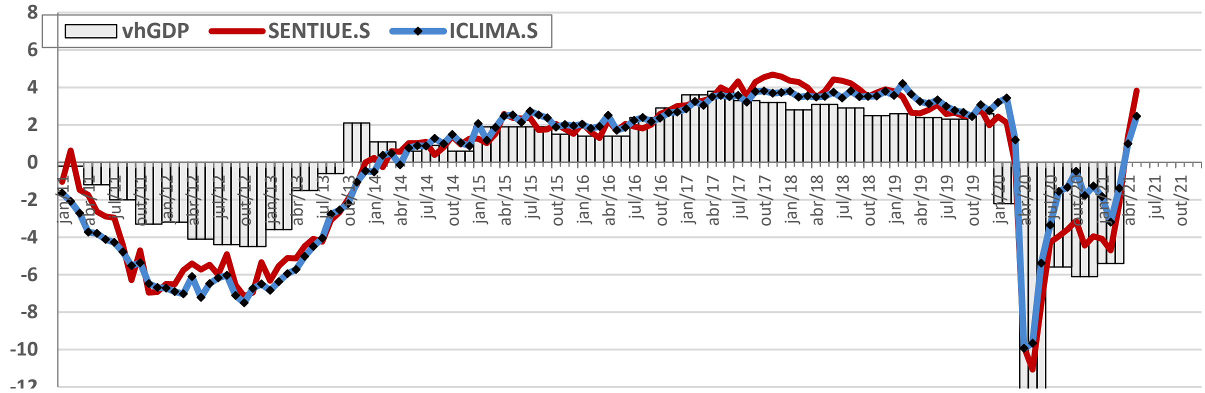
1. ECONOMIC CLIMATE AND CONFIDENCE - INDICATORS FOR MAY

In **May**, which saw an improvement in the progress of vaccination and the control of the sanitary crisis, both the **monthly Economic Climate Indicator** of the National Statistics Institute (ICLIMA.S, INE, which only includes businessmen's opinions) and the **Economic Sentiment Indicator** of EUROSTAT (SENTIUE.S, EUROSTAT, which includes the opinions of both businessmen and consumers) increased again in an impressive way, consolidating the recent positive evaluation. The current value of the Economic Climate indicator returned to mid-2019 levels and that of the Economic Sentiment indicator to pre-2019 levels (see graph 1[1]).

By **sectors of activity**, significant increases were registered for the **confidence indicators for the Industry sector** (with the highest levels since March 2018), **Commerce and Retail trade** (where the current level of confidence is still below the pre-March 2020 levels, but is greater that the post-crisis values), **Construction** (returned to levels last seen at the beginning of 2020) **and Services** (where the index surpassed pre-March 2020 values, but remains below pre-crisis levels).

Despite being slightly more negative when compared with the group of sectors of activity, the **Consumer confidence indicator** also increased significantly from February onwards, attaining values greater than those of March 2020 and since then, but not as large as the previous pre-crisis values.

Graph 1 | Economic Climate (ICLIMA.S) and Economic Sentiment (SENTIUE.S) indicators and year-on-year variation of GDP (vhGDP)



For all of the **Euro Area (EA19)** countries, the **Economic Sentiment** indicator also increased very significantly after February, attaining values in May close to the post 2010 maximum registered at the end of 2018. Among the countries with greater economic weight, the positive evolution of the indicators was generalised, with Germany being the country with the highest level. Among **consumers**, the confidence indicator for the Euro Area also increased appreciatively in March, April, and May.

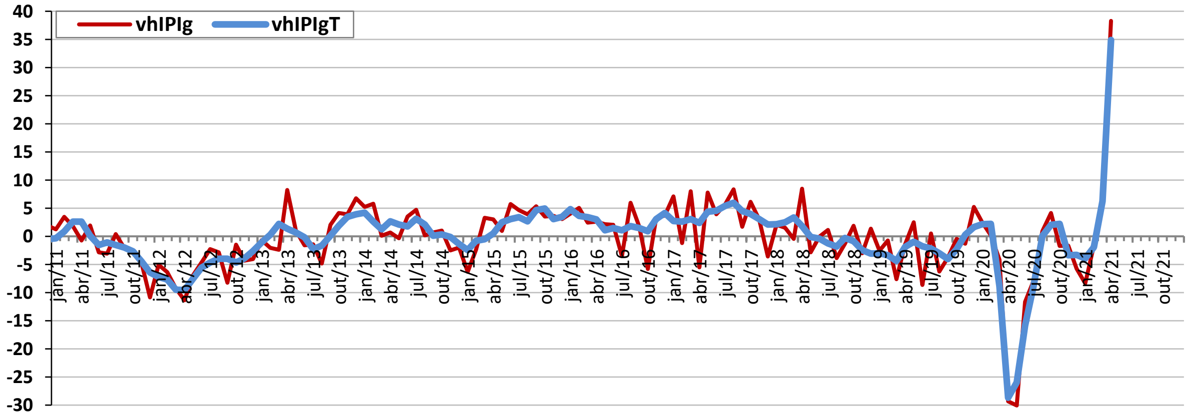
[1] In Graph 1, the original values of the Climate and Sentiment indicators were adjusted for the average and for the standard deviation of vhGDP during the period under analysis for calculating the ICLIMA.S and SENTIUE.S.

2. INDUSTRIAL PRODUCTION

In **April**, the **Industrial Production Index** (INE, gross values) registered a year-on-year variation of 38.3% (vhIPIg series in Graph 2). For the same month, the variation in Manufacturing was 45%. The dimension of these values is mainly the result of the lockdown base effect of the same period in 2020. Compared to 2019, with one extra working day, the year-on-year variation of the IPI for April was -2.2%. According to the surveys carried out by INE, the confidence indicator for Industry improved significantly in May, attaining its greatest value since the 1st Quarter of 2018.

Electricity consumption increased in April and May by 10.4% and 11.9%% respectively (adjusted values for temperature and working days), after a decreases of 13.7% and 13.2% in 2020 (in the same order).

Graph 2 | Year-on-year variation of Industrial Production

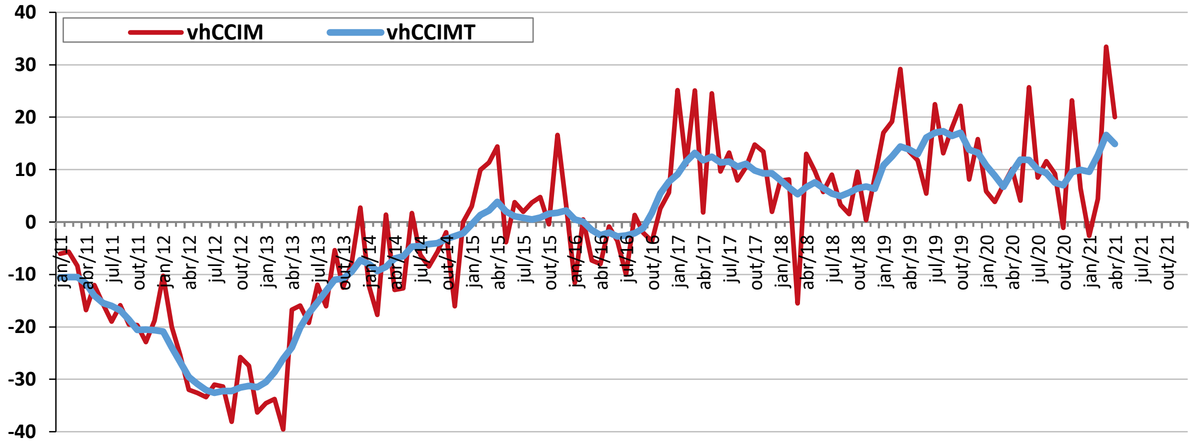


3. CEMENT CONSUMPTION AND CONSTRUCTION/PUBLIC WORKS

In **April**, the annual variation in cement sales was approximately 20%, after an increase of 12.4% during the 1st Quarter. The estimated trend of year-on-year variations (vhCCIMT, in Graph 3) increased to levels closed to 15%.

The confidence indicator for the Construction and Public Works sector also increased significantly.

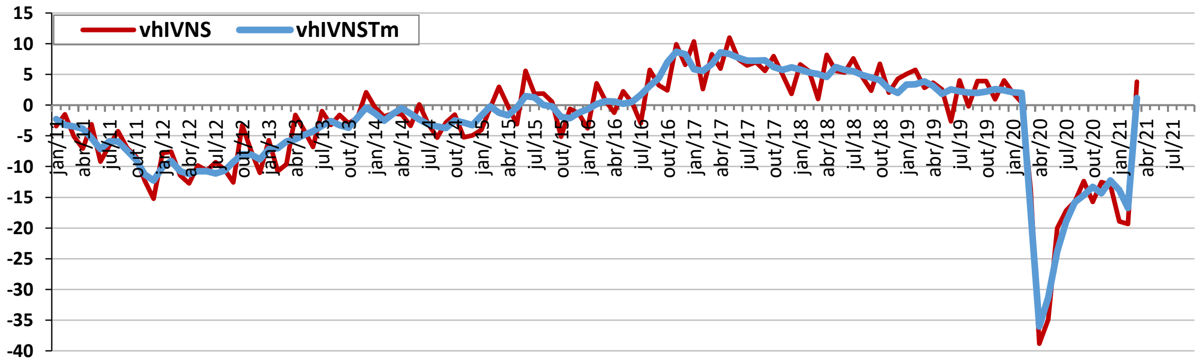
Graph 3 | Year-on-year variation of Cement Consumption



4. TURNOVER IN THE SERVICES SECTOR

In **March**, with one less working day, the **Services Turnover Index** (nominal series) registered a year-on-year variation of 3.8% (vhIVNS series, Graph 4, gross values), which, similar to other indicators, was inflated in April due to the base effect. The confidence indicator for this sector also registered significant improvements in April and May.

Graph 4 | Year-on-year variation for the Services Sector

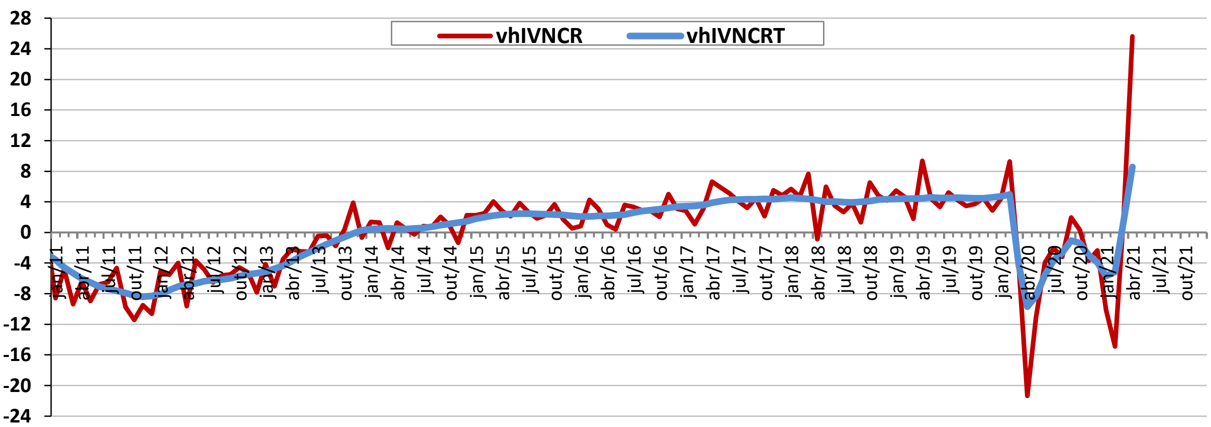


With regards the tourism sector, the number of **overnight stays** in tourist accommodation in **April** registered a year-on-year variation of 510% compared to 2020, which had virtually no activity, and -84.2% in relation to 2019 (INE, Tourism Activity, flash estimate). The year-on-year variation for *non-residents* was -93.5% compared to 2019.

5. RETAIL TRADE TURNOVER

In **April**, the **Retail Trade Turnover Index** registered a year-on-year variation of 25.6% (Graph 5, **deflated** gross values), as a consequence of the base effect caused by the lockdown of 2020. The year-on-year variations of *non-food products* – which was the most affected by the lockdown measures – was -45.6%, while the *food products* grouping registered an increase of 8.6%. In relation to 2019, the overall index decreased by 1.2%.

Graph 5 | Year-on-year variation in Retail Trade turnover



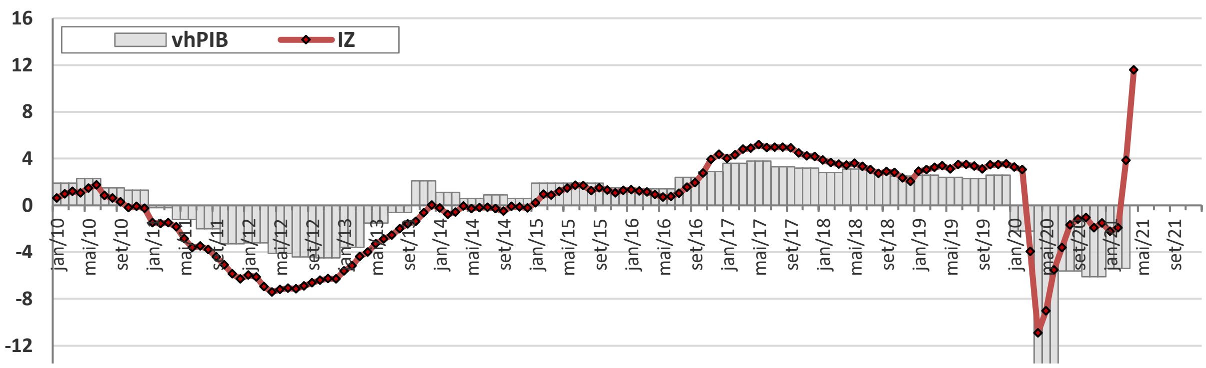
As a result of the lockdown and the year-on-year base effect, **car sales** increased by 3.7% when compared with 2020 for the period of March and April. However, the year-on-year variation was -28.2% when compared with 2019.

6. EVOLUTION OF THE TREND INDICATOR AND EXPECTATIONS FOR THE 2ND QUARTER

As can be seen in Graph 6, the **global activity trend indicator** (IZ), which is a summary of the sectorial indicators analysed above, increased substantially in March and April as a result of coming out of lockdown, the reopening of activities, and principally due to the base effect of the year-on-year comparison, as the 2nd Quarter of 2020 was the hardest hit by the decrease in economic activity brought about by the anti-Covid sanitary measures. The data already available for May reveal that these trends continued in May, and it is logically expected that they will continue to do so in June. Indeed, energy consumption (adjusted for temperature) registered a year-on-year variation of approximately 12% in May, and the value of payments and withdrawals made using the SIBS network increased by more than 30% up until the 30th of May, compared to the year-on-year period. Due to the improvement of both the health situation and the base effect, the question is not whether there will be strong year-on-year growth in GDP during the 2nd Quarter of 2021, but rather at what pace the recovery will continue later on, according to the evolution of the different components of demand, which are also distinctly affected by the base effect during this 2nd Quarter.

In terms of Internal Demand (ID), a substantial increase in Private Consumption is expected during this 2nd Quarter, which was previously negatively affected by the restrictions on supply during the lockdown and also the base effect. At this stage, Private Consumption will be the most dynamic component of demand, although Public Consumption and Investment are also expected to increase significantly in year-on-year terms. Nevertheless, the contribution of Net External Demand (NED) for quarterly GDP appears to be more uncertain, although it could be positive. It is most likely that the negative balance for Goods will increase with the recovery of internal demand, although the positive balance in Services should increase, even if the recovery in tourism is weak. It is thus possible that the overall deficit for the 2nd Quarter will be lower than that of the same period in 2020, and that the contribution of the NED will be positive. Should it be negative, the likely negative contribution of NED to the year-on-year variation in GDP will be lower than that of the previous quarters.

Graph 6 | Year-on-year variation in GDP (vhGBP) and the Z trend indicator



Based on the above, with the expected maintaining of the trend of information currently available and also due to the year-on-year base effect, it is expected that the year-on-year variation of GDP will be an increase of between 14.5% and 15.5% during the 2nd Quarter, and between 4.2% and 5.1% in quarter-on-quarter terms. Even counting with this growth, it is worth noting that the level of GDP during the 2nd Quarter will still be between 3.4% and 4.3% less than that of 2019.

Compiled with information available as of the 4th of June.