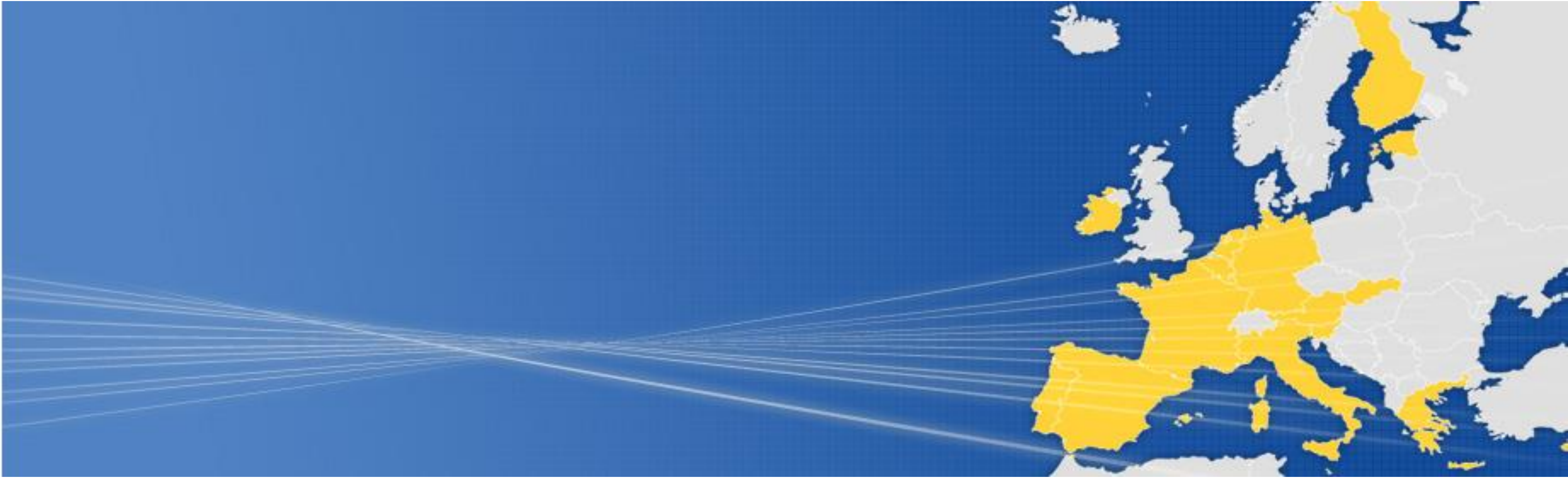


Conclusion of EFSF financial assistance programme for Portugal: an overview

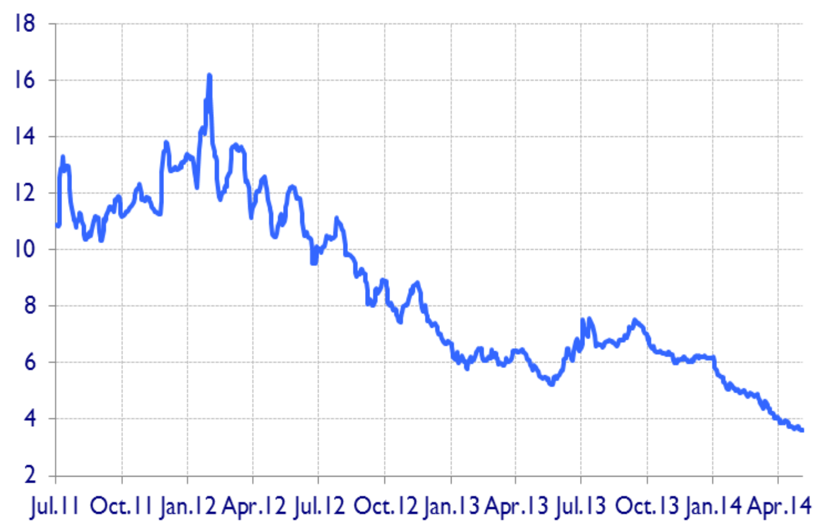
18 May 2014

European Financial Stability Facility
EFSF

Portugal's clean exit results from adequate crisis response

- Three years of sound policies and international support have laid the foundation for a correction of external and fiscal imbalances that is supporting a more sustainable **economic recovery**
- The fiscal deficit has been **significantly reduced**
- **Wide-ranging structural reforms** have improved Portugal's competitiveness, boosting exports and correcting the chronic external deficit
- Portugal's renewed credibility is confirmed by market participants through **low financing costs**

Yield on 10-year Portuguese government bond



Unit: %
Source: Datastream

The origins of Portugal's crisis

- **Low GDP and productivity growth** for over a decade before the crisis started
- **Weak competitiveness** due to decreasing productivity and structural inefficiencies
- High **external indebtedness**, leading to growing household and corporate debt
- **Public debt had been steadily increasing** with high structural budget deficits
- The **banking sector** was increasingly cut off from **international market funding**
- Concerns over **fiscal sustainability** pushed up sovereign spreads with access to markets gradually becoming restricted

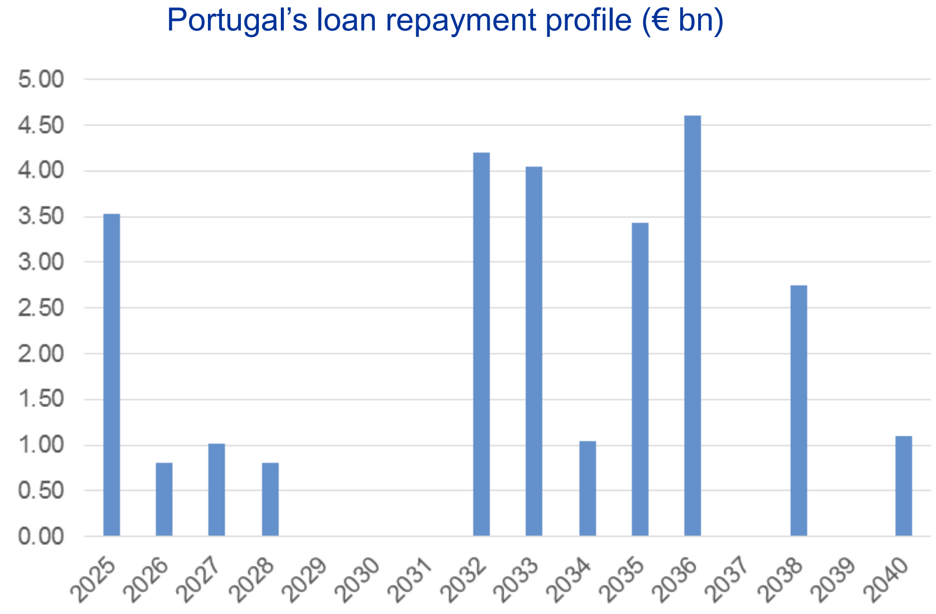
Financial assistance

- Portuguese authorities requested assistance from the EU and IMF in April 2011
- Reform package agreed in May 2011 by Eurogroup/ECOFIN
- Total financial assistance programme of €78 billion

	EFSF	European Commission (EFSM)	IMF	**Total**
€ billion	26	26	26	**78**

Financial assistance provided by the EFSF

- The EFSF disbursed a total of **€26 billion** from June 2011 to April 2014
- **Repayment** of loan principal by Portugal starts in 2025, ends in 2040
- **Average maturity of** loan tranches was initially nearly 14 years
- In April 2013 the Eurogroup decided to **extend** the average maturity by up to 7 years



Source: EFSF

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Key objectives of macroeconomic adjustment programme

- A **fiscal consolidation strategy** consisting of revenue-raising and expenditure reducing measures
- **Stabilisation of the financial sector**: strengthening banks' liquidity and capital, deleveraging, reinforcement of the supervisory and regulatory framework
- In-depth **structural reforms** to address external and internal imbalances and to raise potential growth (measures include labour market reforms, liberalisation of services, scaling down of direct involvement of government in the economy)

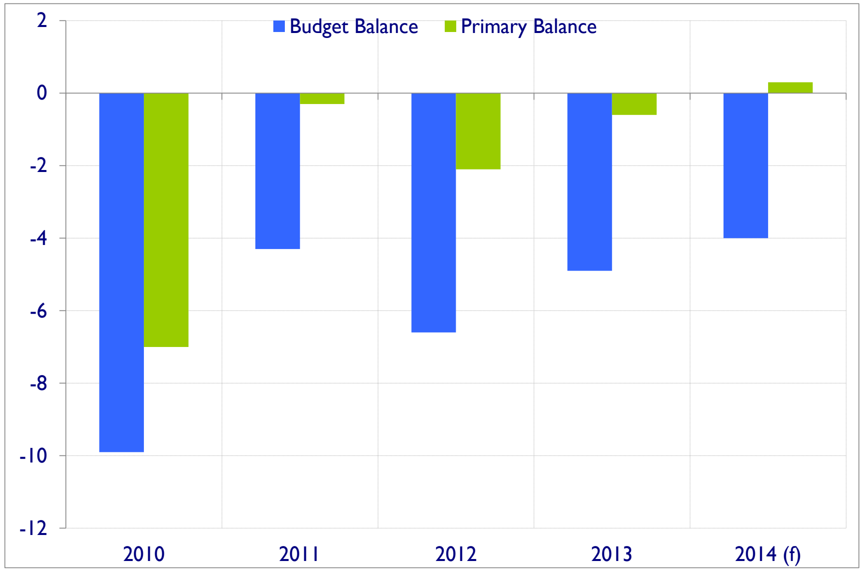
Programme conclusion: ‘clean’ exit

- **12 successful reviews** by European Commission, ECB and IMF
- Troika findings during 12th review (April/May 2014) confirm **achievements**
  - Economic recovery is broadening; GDP growth of 1.2% in 2014 and 1.5% in 2015 is predicted
  - Budget deficit targets of 4% in 2014 and 2.5% in 2015 have been reaffirmed
  - Current account surplus of 0.4% in 2013 was Portugal’s first in 20 years
  - Capitalisation of banks has been significantly strengthened
  - Long-term sovereign bonds yields have fallen to 3.6%
  - Portugal was able to build a comfortable cash buffer
- Decision of ‘**clean’ exit** supported by the Eurogroup and troika institutions

Fiscal adjustment helped to improve credibility

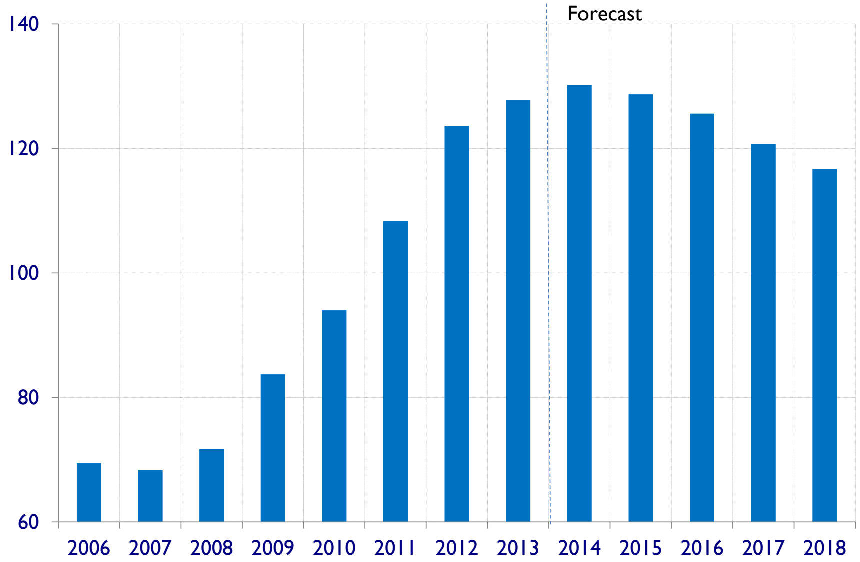
- **Budget deficit declined from 10% of GDP in 2010 to 4.9% of GDP in 2013.** According to the most recent forecasts, Portugal should reach a primary surplus in 2014
- **Government debt is expected to decline** after increasing at a slower pace due to smaller budget deficits
- **Fiscal adjustment should continue** in line with the commitments affirmed by the Portuguese authorities

Budget balance (% of GDP)



Source: European Commission

Government debt (% of GDP)



Source: Ministry of Finance

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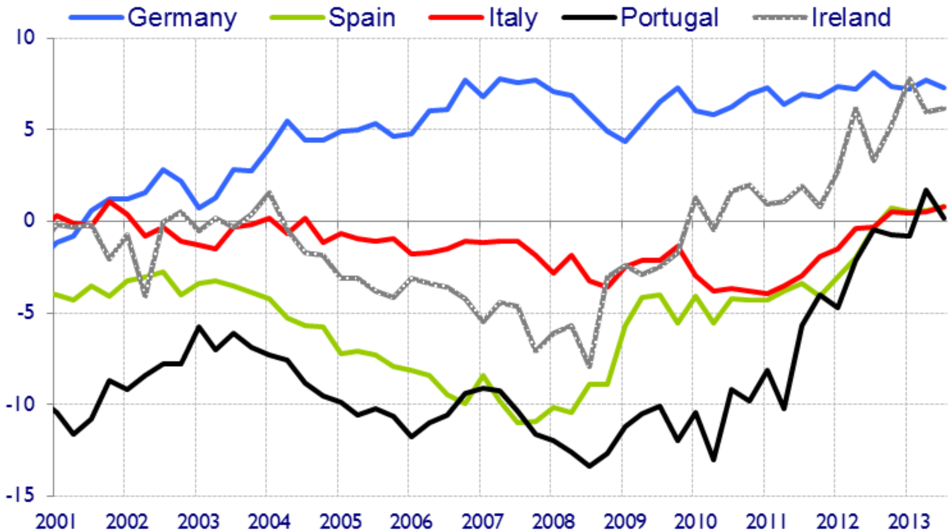
A remarkable external adjustment

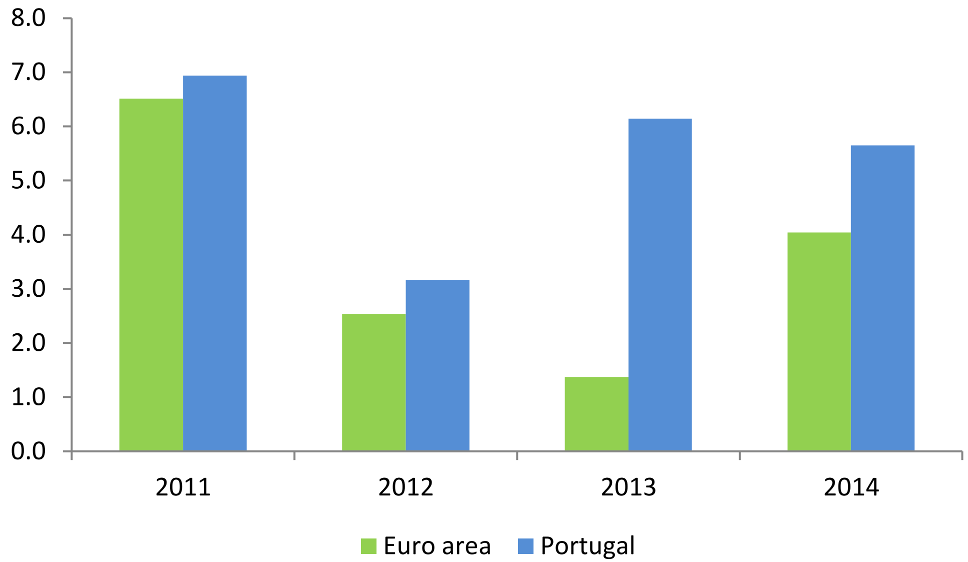
- Portugal's chronic current account deficit **turned into a surplus**, for the first time in 20 years …
- … on the back of a **strong performance of exports**, due to an **improvement in competitiveness** that resulted from the implementation of sound structural reforms

Current account balance (% of GDP)



Source: Bundesbank, Banco de Espana, Banca d'Italia and central statistical offices

Export growth (% y/y)



Source: Ameco

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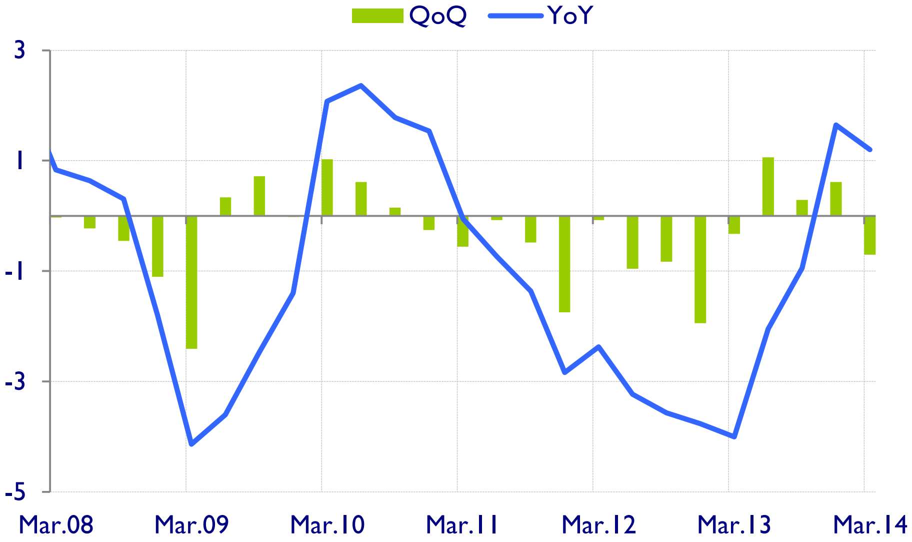
Back to growth

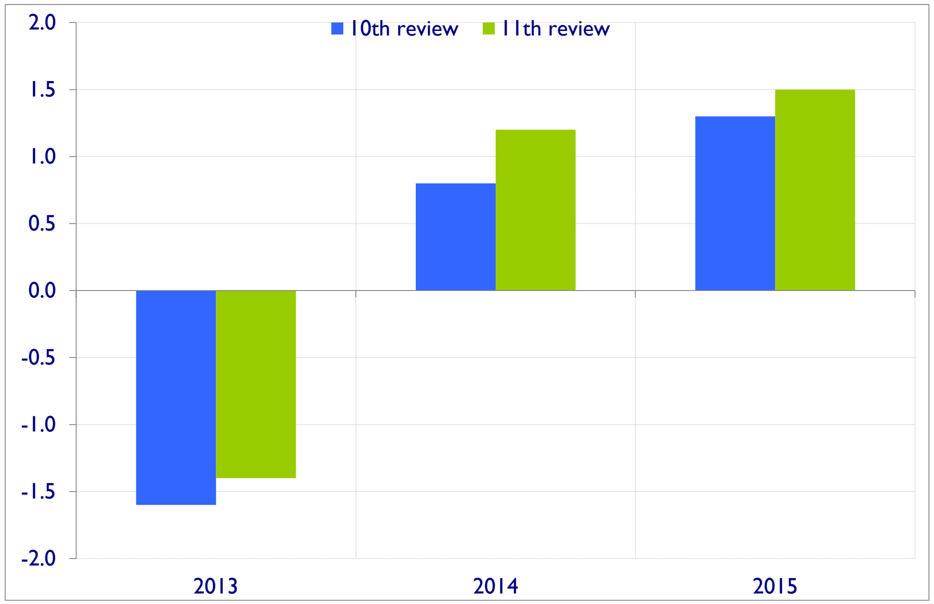
- **GDP expanded in three of the last four quarters** on the back of an improvement in domestic demand in tandem with a continuing increase in exports. Still, GDP contracted in Q1 2014 mostly due to a decline in exports
- **GDP growth is expected to be positive on annual terms:** it should expand by 1.2% in 2014 and 1.5% in 2015. The unemployment rate started to decline but remains high
- The effects of **structural reforms** should continue to improve potential GDP growth

GDP growth (% QoQ & % YoY)



Source: INE

GDP growth (% y/y)



Source: European Commission, IMF

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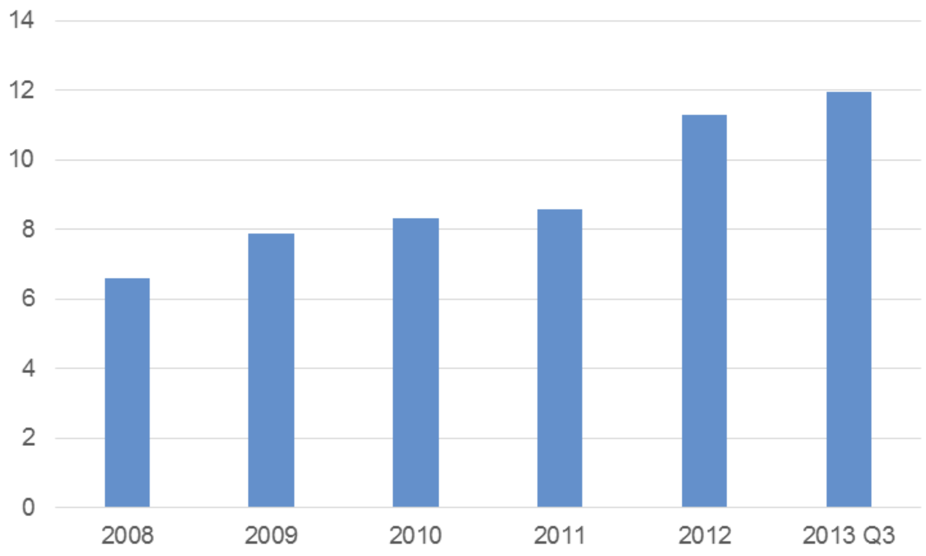
Banking sector developments

- **During the program 4 banks were recapitalised:** CT1 capital ratios are currently well above the Banco de Portugal's (BdP) requirement of 10%. Regulatory Tier 1 Capital ratio for the sector as a whole at 12% (2013Q3). The Bank Solvency Support Facility still has € 6.4 billion at its disposal in case of need
- **Strong deleveraging took place**: for the 4 major banks: -8.2% in total assets (2009-2013)

Regulatory Tier 1 Capital (%) in whole banking sector



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Next steps: Post-programme surveillance

- Euro area Member States exiting financial assistance fall under **post-programme surveillance** (based on EU's Two-Pack Regulation)
- These countries will remain subject to **enhanced surveillance** until they have paid back a **minimum of 75%** of the assistance received
- Post-programme missions will be carried out **twice a year** by the European Commission with the ECB , IMF and the ESM
- The ESM/EFSF will conduct its Early Warning System (EWS) until the end of the repayment of the loans, joining the European Commission in its missions

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Summary: The program was concluded but challenges remain

- Portugal's fiscal consolidation efforts and structural reforms have assured a successful return to funding in **financial markets**.
- The example of Portugal confirms the experience of other euro area countries: financial assistance combined with the implementation of necessary policy reforms is effective and allows countries to **restart economic growth and resume market financing**
- **Challenges remain beyond the end of the program**: high private and public debt/GDP ratio mean that deleveraging will continue
- **Reform efforts must continue** - both fiscal and structural – to allow for a continuing reduction of the fiscal deficit and improve potential GDP growth

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