



REYKJAVÍK ECONOMIC CONFERENCE 2024

MACROECONOMIC STABILISATION IN
SMALL OPEN ECONOMIES - CHALLENGES
AND LESSONS

PANEL: FISCAL
SUSTAINABILITY AND THE
CURRENT ACCOUNT

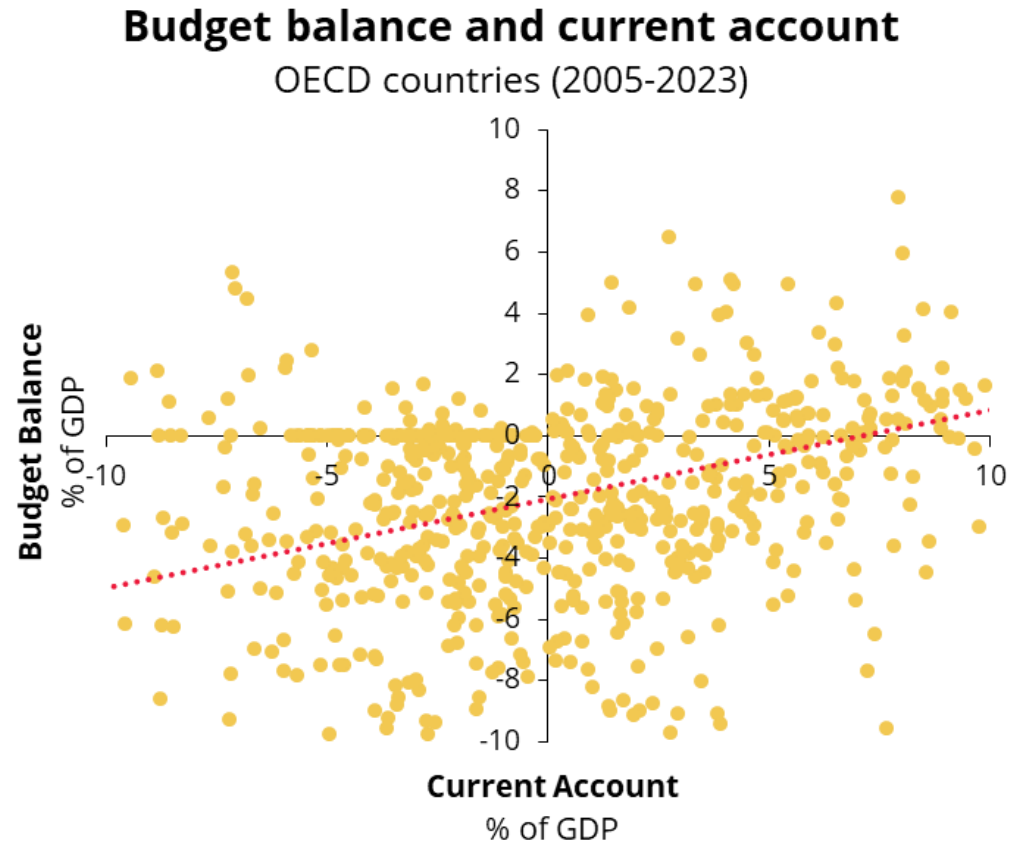
MÁRIO CENTENO, GOVERNOR

24 MAY 2024



BANCO DE
PORTUGAL
EUROSISTEMA

CURRENT ACCOUNTS & FISCAL POSITION: TWIN DEFICITS



Source: OECD and own calculations.
Note: Data truncated to the [-10;+10] interval.

EMPIRICAL DATA SHOW THIS RELATION IS NOT SIMPLE...



... institutions, policy content and coordination play a role.

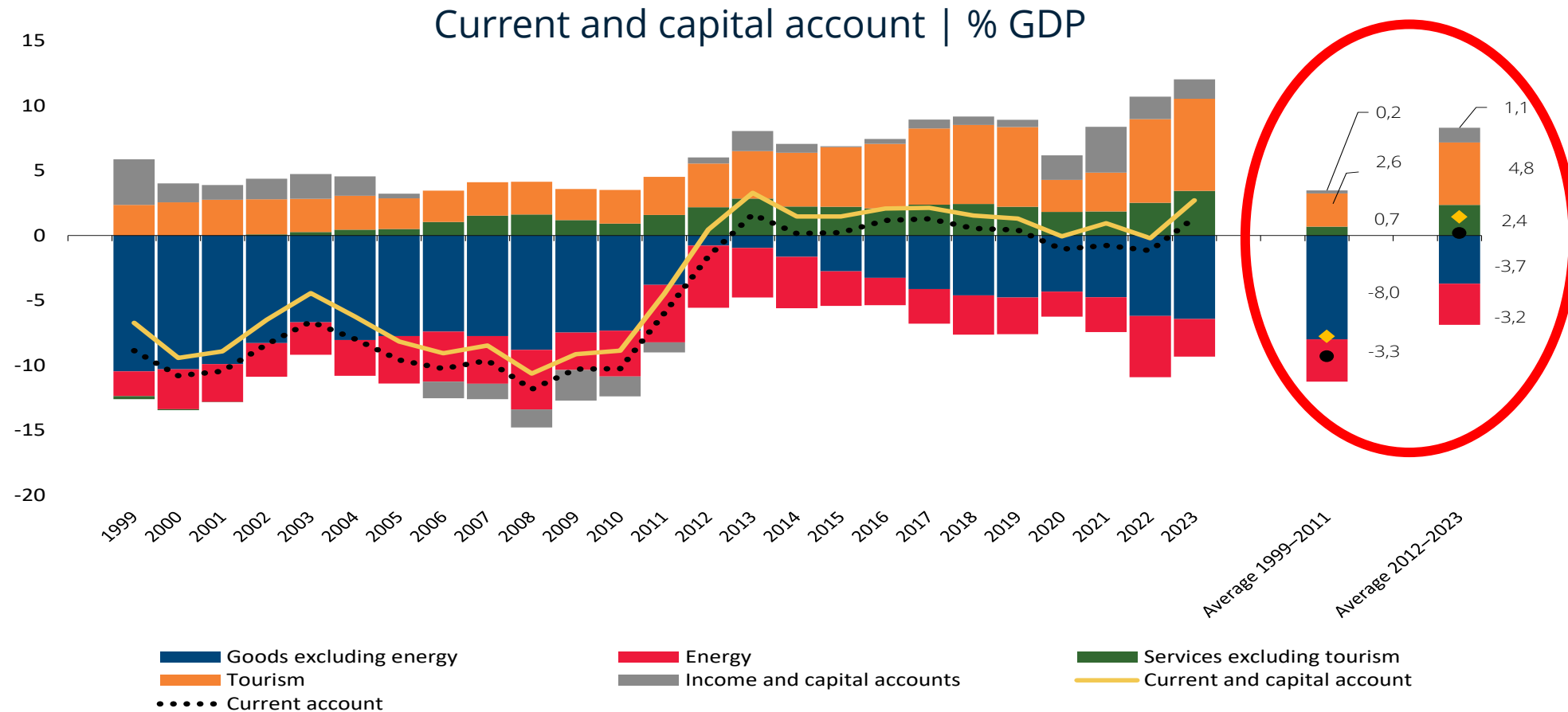
- **Economic context:** GDP growth, labor market stance, inflation rates, and interest rates.
- **Policy composition:** nature of the fiscal shock (tax changes, spending increases, or structural reforms).
- **Economic agents' behaviour:** type of economic agents (i.e. Ricardian or Keynesian).
- **Debt levels and fiscal health:** fiscal sustainability.
- **Policy coordination:** at both domestic and international levels.
- **Institutions:** monetary union; central bank independence; labor market.



THE PORTUGUESE ADJUSTMENT

No exchange rate: real adjustments to correct imbalances

Deep recession: a decrease in public and private consumption



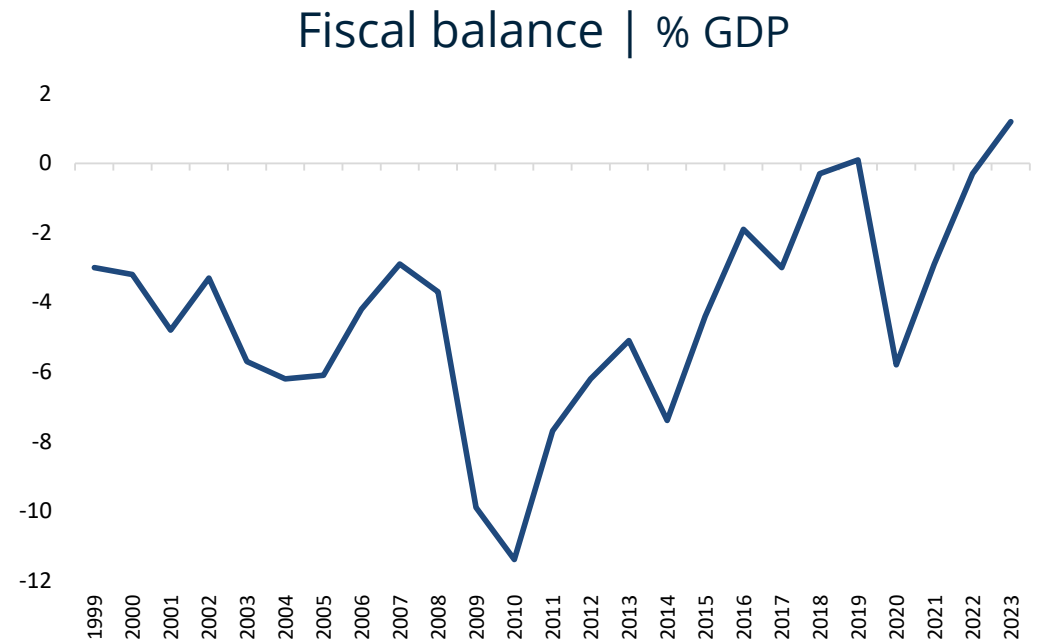
Sources: Balance of Payments (Banco de Portugal) and Statistics Portugal.



THE PORTUGUESE ADJUSTMENT

Fiscal sustainability

- Decrease in interest rates
- Upgrades of credit ratings
- Better financial conditions
- More investment
- Positive impact on firms' competitiveness



Source: Statistics Portugal.

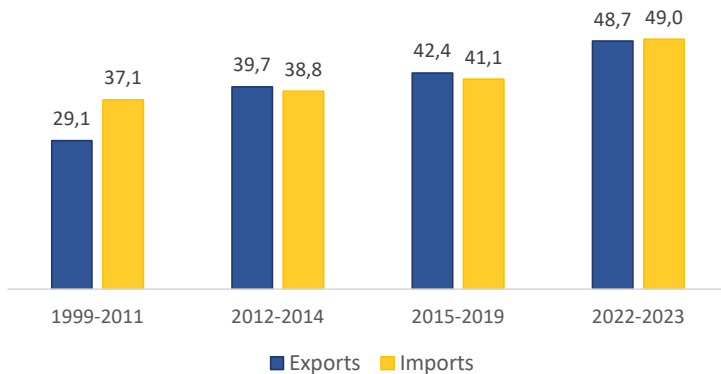


THE PORTUGUESE ADJUSTMENT

Firms looked for **other markets/products** (external demand), therefore:

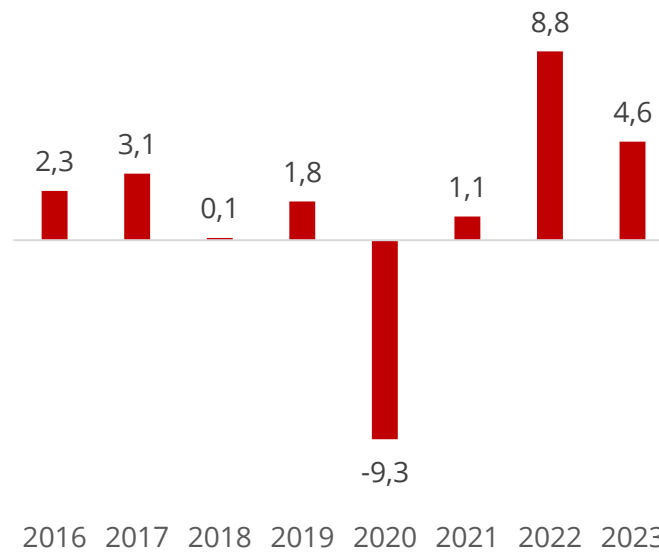
- Exports increased as % of GDP;
- More recently: market shares are increasing and more exports with higher value-added.

Exports and imports | % GDP



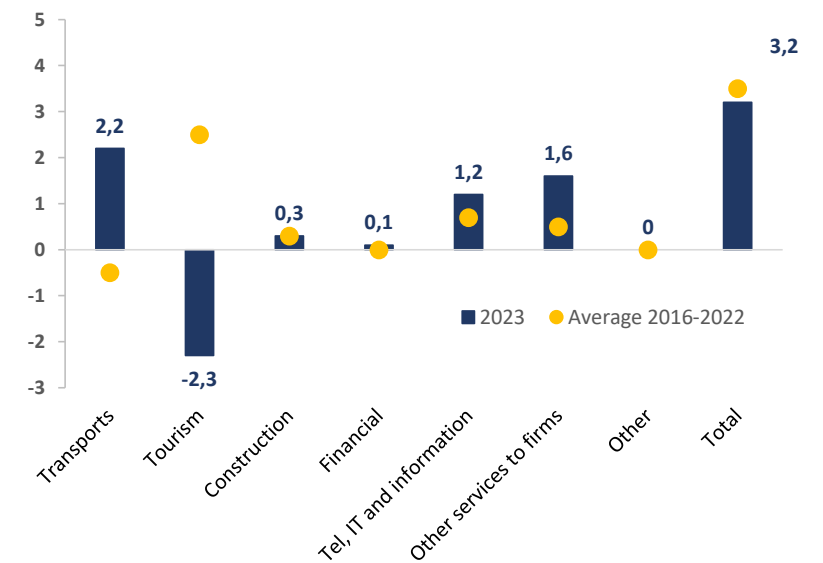
Source: Balance of payments, Banco de Portugal.

Market share | y-o-y (%)



Source: National Accounts, Statistics Portugal.

Market share effect - Services | Contributes, pp



Source: National Accounts, Statistics Portugal.

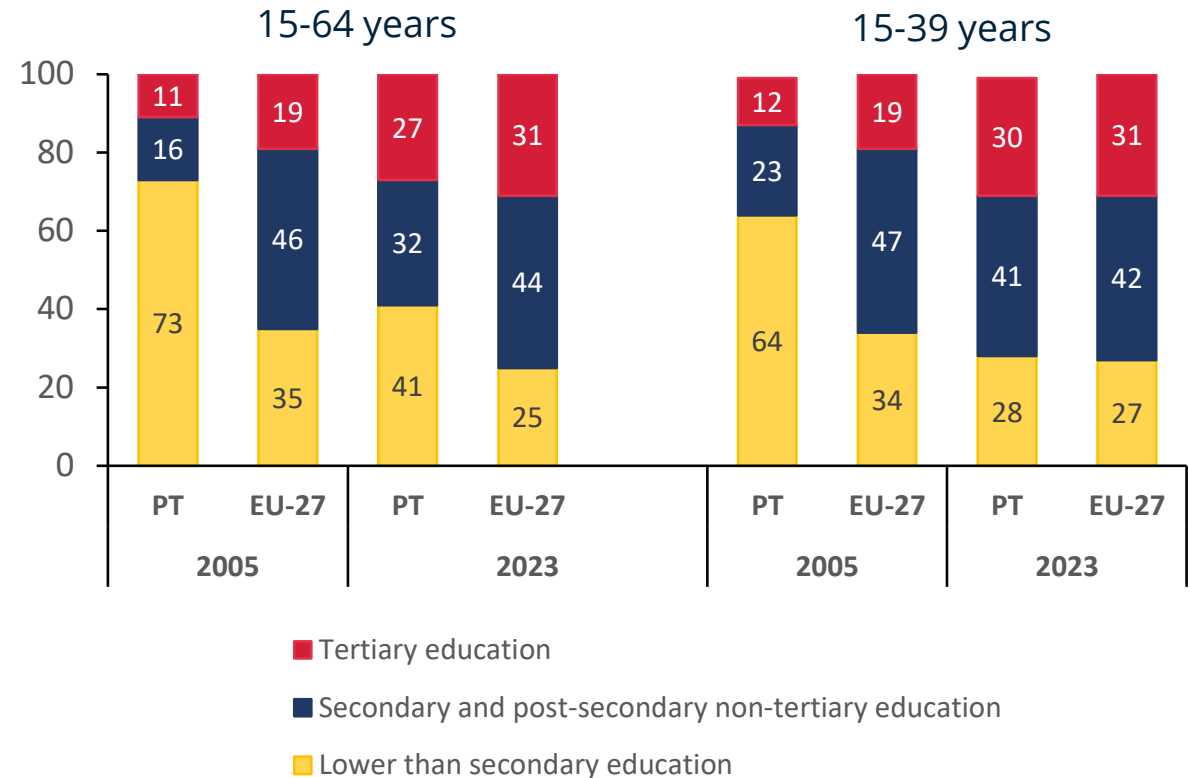


EDUCATION AND FINANCIAL STABILITY

Process benefited from other adjustments (that take time), namely in education: a **silent revolution**

- Over the past few decades, marked educational shift:
 - secondary and higher education schooling rates increased
 - better quality of education
- Strong increase in skills
- More productive labour

Population by education level | % of total



Source: Eurostat.



EURO AREA CONTEXT

- **Stronger EU institutional framework**
 - **Macroeconomic imbalances:** surveyed on a regular basis to better anticipate possible vulnerabilities.
 - **Fiscal rules:** to promote prudent fiscal behaviour.
 - **Risk reduction**
 - **Central fiscal capacity**
- **ECB** also played a central role in guaranteeing a more stable financial environment.





SOME FINAL REMARKS

- **ALL** policy actions must be credible: **credibility** is of the essence
- **Institutional landscape** is critical for **transmission channels**
- Gradual changes more effective than “game-changers”
- **Labor market** key to absorb shocks



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