



ISSUER RATING
LongTerm

OUTLOOK
Stable

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Rating Action and Rationale

EthiFinance Ratings (EFR) upgrades the Republic of Portugal's long-term rating from A- to A, with the outlook revised from Positive to Stable.

The upgrade reflects the strengthening of the sovereign's credit profile, supported by the cumulative reduction in public debt, the maintenance of a near-balanced budgetary position, and the continued improvement in the banking system's capacity to absorb shocks.

Although these factors strengthen the country's capacity to meet its financial obligations in full and on time, the current geopolitical uncertainty (war in Ukraine and Iran) is exerting upward pressure on inflation, primarily through energy prices. This, in turn, could weaken the external position and constrain fiscal flexibility to address future shocks.

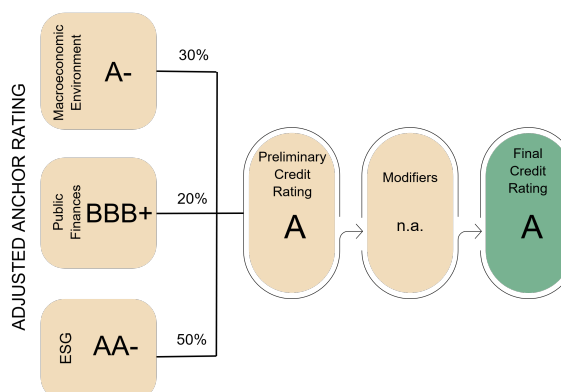
Public debt stood at 89,1% of GDP in 2025, compared with 94,9% in 2024. At EFR, we expect this downward trend to continue, with debt reaching 87,6% in 2026 and 86,0% in 2027. This favourable trajectory progressively reduces the sovereign's exposure to shocks to growth and financing conditions. Although the decline reflects both a reduction in the nominal debt stock and stronger nominal GDP growth, the still-high debt stock leaves the sovereign vulnerable to its reliance on market access for refinancing.

The budget surplus of 0,7% of GDP in 2025 provides further support. Although the European Commission forecasts a return to moderate deficits of -0,1% in 2026 and -0,4% in 2027, at EFR we expect their limited size, together with the improvement relative to the estimate in our previous report, to preserve the downward debt trajectory under our baseline scenario.

The continued strengthening of the banking system complements these developments. Lower levels of non-performing loans, earnings generation capacity, and capitalisation reduce the risk that a financial shock would give rise to extraordinary public support needs.

The rating combines a macroeconomic pillar of A-, a public finances pillar of BBB+, and an ESG pillar of AA-. The aggregate macro-fiscal assessment stands at A-, compared with BBB+ in our previous report. The two-way matrix does not constrain this outcome, and we have applied no additional modifiers.

Figure 1: Deriving the credit rating



Macroeconomic Environment Pillar

The macroeconomic pillar stands at A-, reflecting an economy that retains its capacity for growth and job creation, alongside a more resilient banking system. These factors partially offset the structural constraints associated with the size of the economy, population ageing, and the net external debtor position.

Real GDP grew by **1,9% in 2025**, and at EFR we expect growth of **1,9% in 2026** and **1,8% in 2027**. By component, private consumption, investment, and the recovery in exports helped sustain economic activity during the year, further supported by increased investment under the Recovery and Resilience Plan. Potential growth is estimated at 1,8% and 1,7% for 2026 and 2027, respectively.

Figure 2: GDP Evolution. Source: EFR

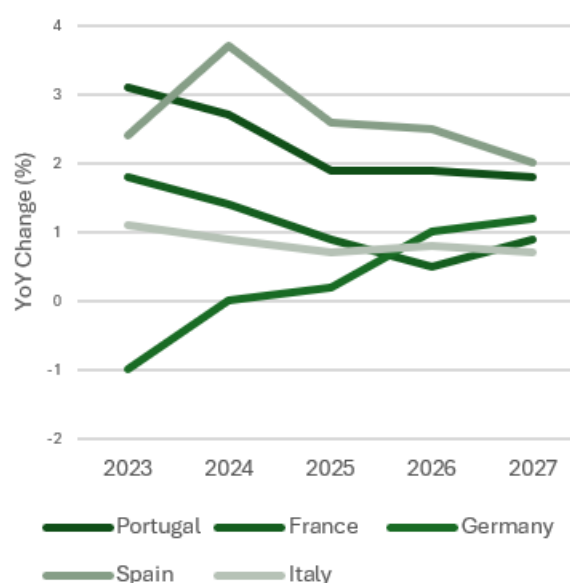
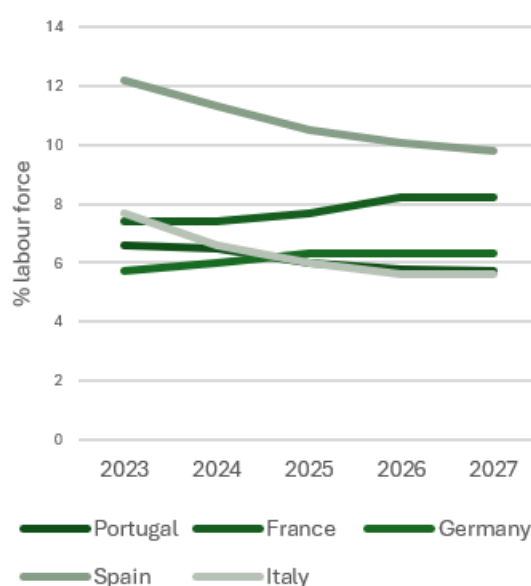


Figure 3: Unemployment rate. Source: EFR.



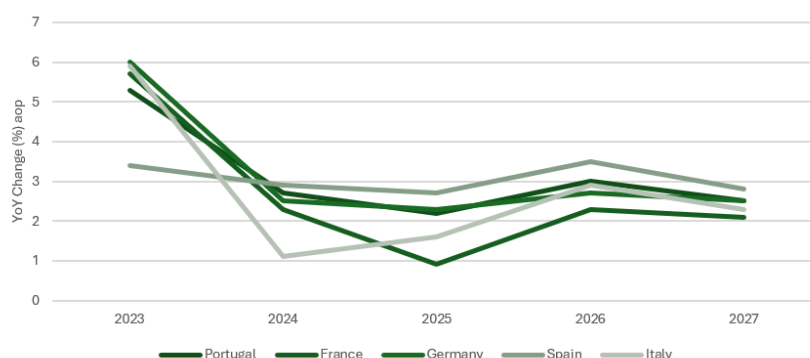
Nevertheless, downside risks persist, primarily due to higher energy costs associated with the conflict in the Middle East, with prices serving as the main transmission channel. Our inflation forecast for Portugal rises from **2,3% in 2025** to **3,1% in 2026** (2,8% in our previous report), before an expected moderation to **2,1% in 2027**. Although this

resurgence in inflation adversely affects households' real incomes and puts pressure on corporate margins, at EFR we do not expect significant second-round effects to materialise. We therefore view the shock as temporary in nature, with inflation expected to return to a path close to the ECB's target once the energy component dissipates.

The labour market provides a counterbalance to these pressures. Portugal's unemployment rate stood at **6,0% in 2025**, with forecasts of **5,8% in 2026** and **5,7% in 2027**. This trend supports tax revenues and social security contributions while limiting the need for unemployment benefits. Meanwhile, GDP per capita rises from **28.515 euros in 2025** to **29.525 euros in 2026** and **30.880 euros in 2027**.

In the external sector, the current account surplus declines from **1,2% of GDP in 2025** to a projected **0,3% in 2026** and **0,4% in 2027**. Continued surpluses remain favourable, reducing reliance on net external financing, but their narrowing limits the capacity to absorb further increases in import costs or weaker external demand. Diversification of goods and services exports is a mitigating factor, although the importance of tourism leaves the economy sensitive to income levels in tourist source markets, transport costs, and international confidence.

Figure 4: HCPI Evolution. Source: EFR.



Nevertheless, at EFR we highlight the cumulative improvement in the Net International Investment Position, which moved from **-58,3% of GDP in 2024** to **-52,7% in 2025**. Although the narrowing of this imbalance is positive, the country remains in a net debtor position.

The banking system continues to strengthen, providing greater capacity to absorb risks. Data for the first half of 2026 show a **non-performing loan ratio of 2,1%**, **return on assets of 1,36%**, and a **CET1 ratio of 18,0%**, compared with **2,3%**, **1,32%**, and **17,9%**, respectively, in 2025.

Public Finance Pillar

The public finance pillar stands at BBB+, reflecting a strong budgetary position, assessed at AA, and a weaker debt and liquidity profile, assessed at BB-. This distinction is central to understanding the rating: Portugal has improved its capacity to contain annual imbalances but retains accumulated obligations and contingent risks that constrain its flexibility under an adverse scenario.

The surplus of **0,7% of GDP in 2025**, compared with **0,5% in 2024**, reinforces fiscal policy credibility. However, projected deficits of **0,1% in 2026** and **0,4% in 2027** indicate that fiscal headroom remains limited. The baseline scenario remains consistent with declining debt but leaves less room to accommodate new permanent spending measures or revenue losses without offsetting adjustments.

Figure 5: Fiscal Balance. Source: EFR.

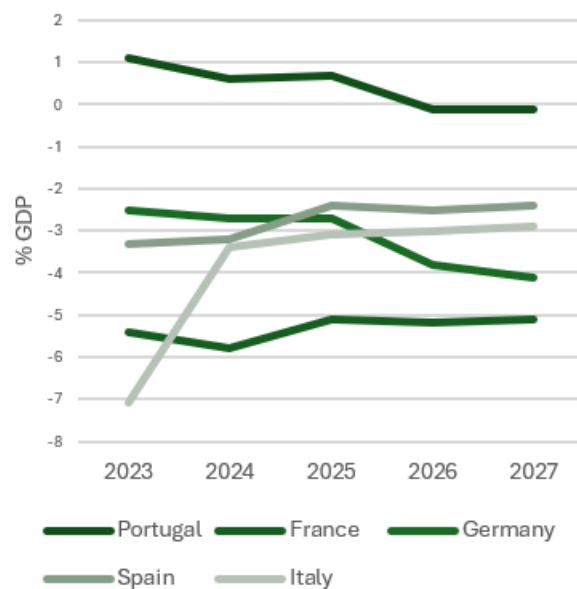
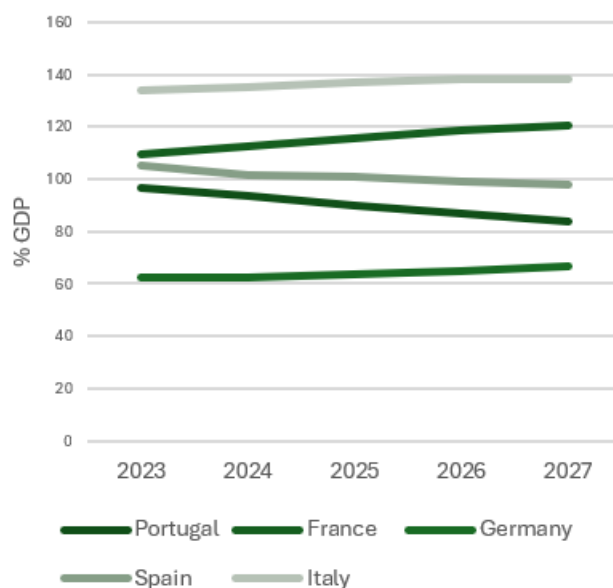


Figure 6: Public Debt. Source: EFR.



Current expenditure trends warrant close monitoring. Growth in current expenditure rises from **5,59% in 2025** to a

projected **7,64% in 2026**, before moderating to **3,04% in 2027**. The subsequent slowdown helps contain financing needs; conversely, persistently high expenditure growth would weaken the projected trajectory. Structural expenditure rigidity adds to these constraints, given the importance of social benefits and public sector compensation, which limit the scope for adjustment.

Public debt declines from **94,9% of GDP in 2024** to **89,1% in 2025**, with further reductions projected to **87,6% in 2026** and **86,0% in 2027**. The lower debt-to-GDP ratio reduces the sovereign balance sheet's sensitivity to rising financing costs. However, the sustainability of this trajectory continues to depend on fiscal discipline and nominal growth.

Our rating takes into account that the interest burden remains contained under the scenario used. Interest payments represent **4,64% of current revenues in 2025**, **4,65% in 2026**, and **4,97% in 2027**. Portugal's relatively stable ratio is a positive factor against a backdrop of sharply rising sovereign borrowing costs in Europe. Nevertheless, the expected slight increase in 2027 and, above all, uncertainty surrounding monetary policy and sovereign risk premiums warrant attention, as a sharp rise in borrowing costs would absorb a growing share of available resources and consequently put upward pressure on the fiscal deficit.

Market access and diversified funding sources are important rating strengths. Portugal's funding strategy combines market issuance, official financing, and retail savings, alongside a maturity management approach aimed at avoiding concentrations of debt repayments. These features provide flexibility, although they do not eliminate refinancing needs or the sensitivity of certain instruments to interest rate movements.

Environmental, Social and Governance (ESG) Pillar

The ESG pillar stands at **AA-**, supported by assessments of **AA for governance**, **AA- for the social component**, and **BBB+ for the environmental component**.

In governance, the institutional framework provides a basis for predictability in economic activity and the management of public obligations.

The presidential transition in 2026, with António José Seguro (with a moderate profile) taking office, provides a backdrop of institutional continuity but should not be equated with a new parliamentary majority or a guarantee that reforms will be approved. At EthiFinance Ratings, we consider that institutional strength can coexist with more limited political capacity to take difficult decisions due to the non-majority position of the Prime Minister in the Parliament.

This distinction also explains our cautious stance on structural reforms. Investment programmes and European funding offer an opportunity but do not replace the capacity to implement changes with lasting effects on productivity and spending efficiency.

In the social component, the **Gini index** declines from 31,9 in 2024 to **30,9 in 2025**, while the ratio of **female to male labour** force participation rates rises from **87% to 88%**. These trends support a more balanced distribution of economic opportunities and broader labour force participation. However, **vulnerable employment remains at 10,0%** in both years, limiting the extent to which the improvement in employment can be interpreted as a uniform improvement in job quality.

Population ageing represents another structural constraint. The demographic dependency ratio used in the analysis rises from **58,5% in 2024** to **58,7% in 2025**. Its credit relevance lies in potential pressures on pensions, healthcare, and care services, as well as the need to sustain the labour force and productivity.

In the environmental component, the share of renewables in energy consumption rises from **36,3% in 2024** to **36,7% in 2025**. This trend helps diversify energy supply and gradually reduce dependence on fossil fuels, although it does not eliminate the economy's exposure to oil and gas.

Exposure to physical risks and adaptation costs continues to constrain the environmental assessment. The storms and floods of 2026 highlight the need to restore housing, infrastructure, and economic activity. These events illustrate how physical risks can translate into extraordinary expenditure, guarantees, and liquidity needs. Progress in renewables is therefore a strength but is insufficient to conclude that the climate transition and adaptation entail no material fiscal costs.

Modifiers

The rating incorporates no additional modifiers. Risks related to the conflict in the Middle East, the property market, and weather events are reflected through their macroeconomic, financial, and budgetary transmission channels. The absence of a modifier does not imply the absence of these risks; rather, no separate additional adjustment is applied to the proposed rating outcome.

Main Figures

Indicator	2024	2025	2026F	2027F
Real GDP growth (%)	2,7	1,9	1,9	1,8
GDP per capita (€)	27.126	28.515	29.525	30.880
Average inflation (%)	2,7	2,3	3,1	2,1
Unemployment rate (%)	6,5	6	5,8	5,7
Current account balance (% of GDP)	2,2	1,2	0,3	0,4
Net international investment position (% of GDP)	-58,3	-52,7	—	—
Demographic dependency ratio (%)	58,5	58,7	—	—
General government balance (% of GDP)	0,5	0,7	-0,1	-0,4
General government debt (% of GDP)	94,9	89,1	87,6	86
Interest payments / current revenue (%)	5,1	4,64	4,65	4,97
Current expenditure growth (%)	9,8	5,59	7,64	3,04
CO2pc	4,80%	—	—	—
Consumption Renewable Energy	36,3	36,7	—	—
Protected Areas	22,8	—	—	—
Vulnerable Employment	10	10	—	—
Health expenditure pc	2971,04		—	—
Gini index	31,9	30,9	—	—
Female to male labor force	87	88	—	—

Fundamentals

Strengths

- Sustained reduction in public debt, supported by a near-balanced fiscal position and continued economic growth.
- Capacity to generate income and employment, supporting the tax base and limiting unemployment-related pressures.
- More resilient banking system, with lower non-performing loans, positive profitability, and capitalisation levels that enhance its loss-absorption capacity.
- Strong institutional and social profile, providing predictability, administrative continuity, and capacity to respond to shocks.
- Diversified access to funding, complemented by active debt management and support from European investment programmes.

Weaknesses

- Still-high public debt and limited fiscal flexibility, despite the cumulative improvement.
- Narrowing current account surplus and a net external debtor position, which maintain sensitivity to international shocks.
- Exposure to energy prices and the tourism cycle, with potential implications for real incomes, corporate margins, and economic activity.
- Property market risks and contingent liabilities, which could generate additional financing needs for the sovereign.
- Population ageing and constraints on the implementation of reforms, compounded by reliance on ad hoc parliamentary support.

Outlook

The Stable outlook reflects our expectation that Portugal's credit profile will remain consistent with the A rating over the next twelve months. Our baseline scenario envisages a continued reduction in public debt, moderate economic growth, and a near-balanced fiscal position, despite the anticipated return to small deficits. The strength of the banking system and institutional framework supports the sovereign's capacity to absorb shocks. These strengths and the expected improvement trajectory are already incorporated into the upgraded rating. Consequently, their materialisation would not, in itself, warrant a further upgrade.

At the same time, the outlook takes into account the constraints arising from the still-high level of public debt, expenditure pressures, and reduced external sector buffers. A prolonged energy shock, property market risks, and the potential materialisation of contingent liabilities could hinder the expected trajectory. Nevertheless, under our baseline scenario, we do not anticipate deviations of sufficient magnitude to materially affect the sovereign's debt-servicing capacity.

Sensitivity Analysis

Detailed below are the factors that, individually or collectively, could affect Portugal's rating:

Positive factors (↑).

A further upgrade could occur if the reduction in public debt and its associated budgetary burden sustainably exceeds the projected trajectory, supported by fiscal balances that remain resilient under less favourable economic conditions. Verifiable improvements in productivity and potential growth, a further reduction in external imbalances, and greater capacity to implement reforms and contain contingent liabilities would also support an upgrade. A decline in public debt below the level already achieved should not be regarded as an automatic trigger for an upgrade, as the projected trajectory for 2026 and 2027 is already incorporated into the current assessment.

Negative factors (↓).

Downward rating pressure could arise from a sustained reversal of the public debt trajectory, fiscal deterioration beyond expectations, or an increase in the interest burden that materially constrains fiscal flexibility. A prolonged energy shock, deterioration in the external sector, or the materialisation of banking sector losses and public commitments resulting in extraordinary financing needs would also be relevant. Institutional weakening that persistently hampers budget approval and implementation or the adoption of corrective measures would likewise constitute an adverse factor.

Rating Committee

The Rating Committee has agreed to upgrade Portugal's rating to A and revise the outlook to Stable. The main issues discussed during the Committee meeting included Portugal's macroeconomic situation in the current geopolitical environment, the expected evolution of public finances, and the domestic political situation, among other considerations.

Sources of information

The credit rating issued in this report is unsolicited. The main sources of information used are the following:

1. Public information from public access sources, mainly official statistics institutes, central banks, and other government sources, in addition to the OECD, Eurostat, World Bank, European Central Bank and International Monetary Fund, among others.
2. Own information of EthiFinance Ratings.

The information was thoroughly reviewed to ensure that it is valid and consistent, and is considered satisfactory. Nevertheless, EthiFinance Ratings assumes no responsibility for the accuracy of the information and the conclusions drawn from it.

Level of the rated entity participation in the rating process

Unsolicited Credit Rating	
With Rated Entity or Related Third Party Participation	NO
With Access to Internal Documents	NO
With Access to Management	NO

Additional information

- The rating was carried out in accordance with Regulation (EC) N°1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies. Principal methodology used in this research are :
 - Sovereign Rating Methodology : https://files.qivalio.net/documents/methodologies/CRA_157_V2_Sovereign-Rating-Methodology.pdf
- The rating scale used in this report is available at <https://www.ethifinance.com/en/ratings/ratingScale>.
- EthiFinance Ratings publishes data on the historical default rates of the rating categories, which are located in the central statistics repository CEREP, of the European Securities and Markets Authority (ESMA).
- In accordance with Article 6 (2), in conjunction with Annex I, section B (4) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009, it is reported that during the last 12 months EthiFinance Ratings has not provided ancillary services to the rated entity or its related third parties.
- The issued credit rating has been notified to the rated entity, and has not been modified since.

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