REPUBLICA DE PORTUGAL

PT SOVEREIGN

A- ISSUER RATING
Long term

OUTLOOK
Stable

Initiation date 18/01/2019
Rating Date 25/04/2025

Contacts

Lead analyst
Antonio Madera Del Pozo
antonio.madera@ethifinance.com

Committee chair
Brianda Torres
brianda.torres@ethifinance.com

Rating Action and Rationale

Ethifinance Ratings affirms the Republic of Portugal's unsolicited long-term rating at A-, maintaining its Stable outlook.

The rating is based on i) the sustained economic trend and its projected continuation over the medium term; ii) the consolidation of a prudent fiscal policy with projected budget surpluses; iii) a further improving external position; and iv) a sound and resilient banking system. These strengths are further supported by a robust ESG profile, particularly in the area of governance. However, the rating is constrained by the high level of public debt, exposure to external risks such as international trade tensions, and rising political instability, which creates institutional and fiscal uncertainty in an increasingly complex geopolitical environment.

Figure 1: Deriving the credit rating

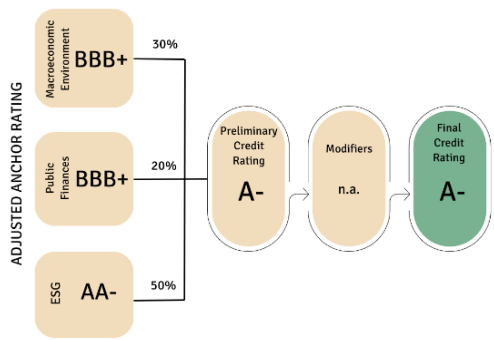
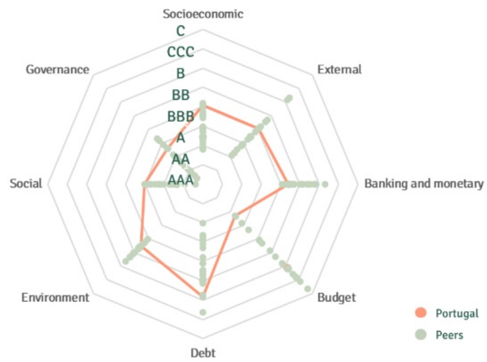


Figure 2: Anchor rating by sub-pillar.



Macroeconomic Environment Pillar

The anchor rating of BBB+ assigned to this pillar is based on Portugal's favorable macroeconomic environment, which continues to outperform most other European economies.

In this context, we project **GDP growth** of 2.3% in 2025 and 2.0% in 2026, in line with forecasts from the Bank of Portugal. This positive trend is supported by strong private consumption, a dynamic tourism sector, rising foreign direct investment, and the effective implementation of EU recovery and resilience funds.

However, downside risks persist. In April 2025, the United States announced 10% global tariffs and 20% on EU goods, with some metal products facing tariffs of up to 25%. This adds uncertainty to the economic outlook, with potential negative spillovers on Portuguese growth due to its integration in European value chains.

The United States is Portugal's largest non-EU trading partner, accounting in 2024 for 1.9% of GDP in goods exports and 2.1% in services exports. Portugal's exposure ranks mid-level among EU peers. The most exposed industries include i) Textiles and apparel (11.9% of total exports); ii) Non-metallic mineral products (11.5% of total exports), and iii) Beverages (9.6% of total exports).

According to the Bank of Portugal, cumulative effects of trade tensions could reduce GDP by up to 1.1% over three years. To cushion this impact, the government has launched a support package exceeding €10 billion, targeting export-oriented and vulnerable sectors.

On the labor front, Portugal maintains a strong performance. Our rating assumes an unemployment rate of 6.3% in 2025 and 6.1% in 2026. Nonetheless, the projected GDP per capita of €28,643 in 2025 remains below the EU average, reflecting an unresolved structural gap in economic convergence.

Externally, Portugal enjoys an improving position, with a current account surplus of 1.6% of GDP expected for both 2025 and 2026. This supports further improvements in the net international investment position (NIIP), which improved from -102% of GDP in 2020 to -56% in 2024, enhancing resilience to external imbalances.

In the financial sector, the banking system continues to strengthen. The non-performing loan (NPL) ratio fell to 2.4% in 2024, down from 2.7% in 2023, while the return on assets (ROA) rose to 1.38%, nearly double the previous year. These gains reflect increased efficiency and profitability, aided by sustained high interest rates and the ongoing deleveraging of the private sector, with household and corporate debt down to around 170% of GDP in 2024—well below the peak of over 200% in May 2021.

Finally, the rating incorporates the ongoing convergence of inflation toward the ECB's 2% target. Inflation is expected to end 2025 at 2.3%, moving closer to target in 2026. Recent ECB rate cuts, including the latest on April 17 bringing the deposit rate to 2.25%, and the prospect of further easing to 2.0%, provide monetary stimulus expected to support medium-term economic growth.

Public Finance Pillar

The BBB+ anchor rating for this pillar reflects the improving outlook for Portugal's public finances, though this remains constrained by high public debt levels.

EthiFinance Ratings has revised its budget balance forecast upwards, now projecting a fiscal surplus of 0.4% of GDP in 2025 and 0.3% in 2026. This supports the ongoing fiscal consolidation process, driven by a prudent budgetary framework and disciplined public spending execution.

However, public debt projections have slightly deteriorated. The European Commission has revised the 2025 debt-to-GDP ratio to 92.9%, up from a previous 91.5%. This increase reflects, among other factors, additional fiscal efforts to counteract geopolitical shocks. Nevertheless, the Portuguese government remains committed to reducing public debt to below 80% of GDP by the end of the decade—an ambitious target that would place Portugal in a stronger position than peers such as Italy (142%), France (124%), Belgium (119%), Spain (97%), and Austria (81%).

Financing costs remain contained, contributing to sound debt management. Interest payments are expected to stay just above 5% of current revenues in both 2025 and 2026, reflecting a well-structured debt profile with low short-term sustainability risks. Although debt redemptions exceed €21 billion in 2025, mostly in medium-to-long-term bonds and Treasury bills, refinancing risks are moderate given Portugal's favorable rollover profile compared to other EU countries.

The 2025 budget includes structural tax reforms aimed at fostering inclusive growth. Key measures include personal and corporate income tax cuts, investment and innovation incentives, a minimum wage hike to €870 (accompanied by an income tax exemption for recipients), an average 3.85% pension increase, and expanded social programs. These reforms are pursued alongside moderate structural spending growth and a firm commitment to increase defense spending to 2% of GDP, in line with NATO commitments, while maintaining a fiscal surplus.

Environmental, Social and Governance Pillar

The AA+ anchor rating is underpinned by Portugal's strong ESG profile, marked by solid governance and social inclusion, and a maturing environmental strategy aligned with the EU energy transition goals.

On the Environmental Subpillar, Portugal faces challenges from high greenhouse gas emissions intensity, particularly in transport and industrial sectors. Nonetheless, the country remains committed to climate neutrality targets through a gradual energy transition strategy. Public planning allocates increasing resources to green projects, including infrastructure, urban mobility electrification, and expansion of renewable energy capacity—especially solar and wind. Despite the gradual pace, the strategic direction remains aligned with the European Green Deal and the National Energy and Climate Plan, although effective implementation will depend on institutional stability and the continuity of fiscal and regulatory incentives that ensure long-term decarbonization viability.

On the Social Subpillar, Portugal maintains a favorable track record in cohesion and wellbeing, supported by public policy frameworks enhancing social coverage and equity. The 2025 budget measures reinforce this through expanded social transfers, stronger youth employment support, and targeted tax relief for low-income households, reinforcing an inclusive welfare model.

On the Governance Subpillar, Portugal has historically benefitted from strong institutions, a well-established rule of law, efficient public administration, and a functional and predictable judiciary. However, political instability resurfaced in Q1 2025 with the collapse of Prime Minister Luís Montenegro's government following a failed confidence vote. This led to parliamentary dissolution and snap elections scheduled for May 18, marking the third national election in just three years and highlighting continued political fragmentation.

Modifiers

For this credit analysis, we have not applied any modifiers as no extraordinary situations with immediate impact on the sovereign credit situation have been identified.

Main Figures

	2020	2021	2022	2023	2024	2025E
Real GDP (% change)	-8.2%	5.6%	7.0%	2.5%	1.9%	2.3%
GDP per capita (current, €)	19,473	20,987	23,530	25,733	27,613	28,643
CPI (annual change, %)	-0.1%	0.9%	8.1%	5.3%	2.6%	2.3%
Unemployment rate (% labor force)	7.1%	6.7%	6.2%	6.5%	6.5%	6.3%
Dependence ratio (<19 and >65 y/20-64 y)	56.6%	57.3%	57.9%	58.3%	-	-
NPLs	4.9%	3.7%	3.0%	2.7%	2.4%	-
ROA (financial sector)	0.1%	0.5%	0.7%	1.3%	1.38%	-
Current Account Balance (% GDP)	-1.0%	-0.8%	-1.1%	1.4%	2.2%	1.6%
NIIP (% GDP)	-102.1%	-99.2%	-87.6%	-76.0%	-58.3%	-
Fiscal Balance (% GDP)	-5.8%	-2.9%	-0.3%	1.2%	0.6%	0.4%
Public Debt (% GDP)	134.9%	124.5%	112.4%	99.1%	95.7%	92.9%
CO2 emissions per capita	5.3	5.0	5.3	-	-	-
Consumption of Renewable Energy	33.9%	33.9%	34.7%	-	-	-
Human Development Index	86	86	87	-	-	-
Gini Index	31.2	33.0	32.0	33.7	-	-
World Governance Indicators	81.7	80.9	80.1	80.1	-	-

Fundamentals

Strengths

- Solid macroeconomic fundamentals supported by strong consumption, tourism, and EU fund execution.
- Fiscal discipline with projected budget surpluses in 2025 and 2026.
- Robust ESG profile with strong institutions and a credible climate transition strategy.
- Strengthening banking sector with lower NPLs, higher profitability, and private sector deleveraging.

Weaknesses

- Moderate exposure to external shocks including US trade tariffs.
- Public debt remains elevated despite consolidation efforts.
- The persistent income gap vs. EU peers reflects incomplete economic convergence.
- Recent political instability undermines policy continuity and predictability.

Outlook

Our Stable outlook is based on our expectation that the rating fundamentals will remain broadly unchanged over the next 12 months. There are several areas with positive trends, particularly fiscal metrics, with the country achieving budget surpluses and a declining debt ratio. In addition, steady economic growth and resilient employment levels reinforce Portugal's socioeconomic profile. However, there are potential global developments which could lead to renewed upward pressure on inflation.

Sensitivity Analysis

Detailed below are the factors that individually or collectively would impact Portugal's rating:

Positive factors (↑).

The credit rating and/or outlook could be upgraded if economic growth exceeds expectations, surpassing its potential rate over 2.2% in the medium term and facilitating convergence of GDP per capita toward the EU average. Additionally, sustained inflation around the ECB's 2% target would further support an upgrade. On the fiscal front, maintaining fiscal surpluses that reduce debt levels closer to the 60% threshold would be a positive factor. Finally, continued political cohesion, with agreements among different political parties to help ensure the implementation of key measures and maintain government stability, would also bolster the rating.

Negative factors (↓).

The credit rating and/or outlook could be downgraded if the risk factors - such as a renewed rise in inflation- leading to sustained below-potential growth and negatively affecting other key rating fundamentals like the labor market, external sector, and public finances - intensify. Moreover, any move away from fiscal responsibility, with the return of deficits in the fiscal balance that lead to the debt level rising above 100% of GDP, could also negatively impact the rating.

Rating Committee

The rating committee agreed to confirm the rating and maintain the outlook. The main issues discussed by the Committee were the GDP projections for the coming years in the light of the complex macroeconomic scenario, the evolution of the external sector and the fiscal situation. The impact of the early elections was also reviewed, among others.

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.