Portugal

By Bruno Silva, DPEC - Departamento de Estratégia e Plano

IN A NUTSHELL

- → GDP growth slowed to 2.3% (6.8% in 2022), inflation fell to 5.3% (8.1%) and unemployment rose to 6.5% (6.0%).
- → The number of residential property transactions fell by 18.7% to 136,499 homes, after increasing 1.3% in 2022.
- → Non-resident participation continued to increase only 45% of purchases were financed by domestic lending.
- → Housing supply remains unable to match demand, with 22.8 td buildings licensed and 15.3 td completed (-7.7% and -1.8% y-o-y respectively).
- → Drivers of the 1.4% fall in mortgages were rates, repayments, and lower demand.
- → The Government approved additional measures to ease the burden on vulnerable borrowers' affordability.

MACROECONOMIC OVERVIEW

GDP grew by 2.3%, after 6.8% in 2022, the highest pace since 1987 and after the expansion of 5.7% in 2021 and the historic decline of 8.3% in 2020 – following the pandemic. Domestic demand was a positive contribution to growth, although less than previously, with a slowdown in private consumption and in investment. Net external demand also made a positive but lower contribution, with strong decelerations in volume of both exports and imports of goods and services.

This growth was accompanied by an increase in unemployment, from 6.0% in 2022 to 6.5% in 2023, and by a decrease in inflation – measured by the harmonised consumer prices index (HCPI) –, from 8.1% in 2022 to 5.3% in 2023. As in the Eurozone and elsewhere, after significantly higher inflation in 2022, it started to fall from the end of 2022. It also fell due to the VAT rate cut to 0% on several essential food items.

The budget balance had a surplus of 1.2% of GDP (0.3% deficit in 2022), with the public debt ratio decreasing of 13.3pps from 112.4% of GDP in 2022, to 99.1%.

The current account improved, from a deficit of 1.1% of GDP (as a result of the rise in prices of imported commodities, specifically energy) to a surplus of 1.4%.

The private savings rate dropped from 10.6% in 2021 to 6.3% in 2022 and then rose slightly in 2023 to 6.6%, partly exacerbated by rising inflation.

LOOKING AHEAD

For 2024, a further slowdown is expected, with GDP growing at around 1.8% (Banco Montepio projections; other forecasters range from +1.6% (OECD in May 2024) to +2.0% (Bank of Portugal in June 2024 and IMF in July 2024). The unemployment rate is expected to stabilize in 2024, in 6.5% (Banco Montepio projections; others range from 6.3% (OECD) to 6.5% (IMF and European Commission, in May 2024). Inflation is expected to decline in 2024, to 2.6% (Banco Montepio projections; with downside risks, another forecast from 2.2% (IMF) to 2.5% (Bank of Portugal).

As disclosed by BoP in March 2024, there are downside risks to economic activity – due to geopolitics, slowing external demand, financial tightening, uncertainty in economic policy and delays in the implementation of European funds – and balanced risks to inflation, where the risk associated with the energy markets will be mitigated by monetary policy.

Still highly restrictive monetary policy, inflationary pressures, the phasing out of public support for families and companies and the end of moratorium programs, will be challenges in 2024, with a potential negative impact on the mortgage and real estate market.

HOUSING MARKETS

According to the BoP's analysis, residential real estate prices continued to grow above the inflation rate in 2023, with signs of overvaluation of persisting. According to Statistics Portugal, the House Price Index (HPI) increased 8.2% in 2023, a slowdown compared to 2022 (+12.6%, the highest in the available series), having continued to grow since Q2 2015. The BoP considers that this growth is above the historical trend, and that signs of overvaluation have persisted since 2019, although these signs began to decrease in the 4th quarter of 2022.

According to Statistics Portugal, the number of residential property transactions fell to 136,499, for a total amount of EUR 28 bn. These were falls of 18.7% and 11.9% compared to 2022 (in number and value, respectively).

Participation of non-residents in the real estate market continued to increase. According to the BoP, non-resident buyers increased in the 1st half of 2023 (+2 pps) compared to the same period in 2022, to 12.7% (by value of transactions). However, the BoP recognizes that information tends to underestimate the relevance of foreigners, as many now have resident status (tax residence in the case of individuals). The European Commission estimated, in April 2024, that only 45% of residential real estate purchases in 2023 were financed by domestic lending.

Over the last 10 years, there has been an increase in non-resident buyers which, given the restricted supply, has had an impact on the resident population.

Supply has remained unable to meet demand. According to Statistics Portugal, 22.8 td buildings were licensed, and 15.3 td buildings were completed, decreases of 7.7% and 1.8%, respectively (-4.4% and -3.5%, in the same order, in 2022). In addition to licensing difficulties, disruptions to material supply chains, lack of labour and the increase in the cost of production were factors. In addition, higher interest rates tend to limit the construction of new buildings and the rehabilitation of used ones, and slightly more restrictive criteria for construction credit may exacerbate this.

According to the BoP, the limited supply of new housing and the lack of stock of homes mitigates the impact on prices of lower demand. The economy is now less dependent on the construction sector [construction fell from 9.2% of the economy's gross added value in Q3 2001 to 4.3% in Q4 2023 (at constant prices and without taxes) and the exposure of the banking sector to the construction sector is lower]. Construction costs have remained high, although slowing in recent months. Reflecting the construction/rehabilitation time of properties, the impact of increased construction costs on prices tends to be lagged, so they may continue to impact prices in particular for new buildings.

MORTGAGE MARKETS

Mortgage loans outstanding fell by 1.4% (EUR 1.4 bn) to EUR 99 bn (77% of total loans to households). This was mainly due to lower demand, with a decrease of 13% (EUR 1.9 bn) to EUR 12.6 bn in new loans (excluding restructuring decisions but including contract transfers between banks) to EUR 12.6 bn and increased early repayments (by 67% to EUR 10.7 bn, equivalent to 85% of the annual volume of new mortgage loans), due to higher interest rates, slow transmission of policy rates to deposit rates, as well as to the Government decisions to suspend fees on redemptions and allow the early reimbursement of Retirement and Education Savings Plans (PPR and PPR/E, article 6 of Law no. 19/2022, of 21 October), whose average monthly rate increased from EUR 70 mn, between Sep-19 and Sep-22, to EUR 100 mn since then.

As average interest rates charged on residential mortgage loans more than doubled, from 2.3% to 4.75%, debt service levels rose sharply, by an average of around EUR 400/month (a 33% increase vis-à-vis the previous year), leading to an increase in the weight of interest in instalments from 33% to 61%. Most new borrowers opted for mixed interest rates (a fixed rate period, usually 2 to 3 years, followed by a variable rate), whose weight in total new loans increased almost 4 times, from 16% in Dec-22 to 71% in Dec-23, leading to a decrease in floating rate loans outstanding by 10pp, from 90% to 80%, while the weight of mixed interest rate loans rose by almost 10 pps, from 6.4% to 16% in the same period.

The 2023 annual report of BoP macro-prudential measures stated that the recommendations regarding Loan-to-Value (LTV) ratios, Debt Service-to-Income (DSTI) ratios, and mortgage maturities are being followed. It also stated that borrowers' risk profile in new loans has improved significantly, with loans granted to low-risk customers (LTV ratio of 80% or less and a DSTI of 50% or less) increasing from 49% to 61%, between 2022 and 2023.The BoP underlined that "the better risk profile is a result of the increase since 2019 in the percentage of loans granted with LTV ratio equal to or less than 80% (from 48% in 2019 to 68% in 2023), while the distribution relative to DSTI ratio remained unchanged from 2022". Additionally, as in 2021 and 2022, 97% of new credit for housing and consumption had a DSTI ratio below or equal to 60%, with approximately 91% being below 50%, representing a decrease of 3 pps from the previous year (due to higher rates, BoP reduced interest rate shock used for the DSTI ratio from 3% to 1.5%, for contracts with a maturity above ten years, as of October 2023). The average maturity of new housing loans was 30.6 years in Dec-23, close to the 30.7 years in Dec-22, converging to the macroprudential recommendation of 30 years, although younger borrowers tend to opt for longer maturities.

The Government's set of measures to improve the access to affordable housing "Mais Habitação" ("More housing") and mitigate the impact of rising rates on households include (I) setting fixed monthly instalments for loans with variable rates, for a maximum of two years[1] (II) providing a temporary interest rate subsidy[2] and (III) extending the suspension of early repayment fees, only applied to variable rate mortgage loans, until December 31, 2024.

In November 2023, the BoP introduced a new requirement for banks that use internal ratings-based approaches to compute capital requirements for credit risk, corresponding to a systemic risk capital buffer of 4% over residential mortgages on Portuguese properties to be met by October 2024. This macroprudential tool aims to make institutions more resilient to systemic risk in the residential market, as Portuguese banks remain well capitalized (with an average CET1 ratio of 17% at the end of 2023, vs 14.8% in the previous year).

MORTGAGE FUNDING

Bank deposits continue to be the main source of funding accounting for more than 50% of banks' liabilities, higher than the average in the European Economic Area (EEA), which have been stable at around 30%. Moreover, debt securities issued represent only 6% of total liabilities, compared to an average of 20% among EEA banks.

Despite the reduction in total deposits by EUR 5.7 bn, to EUR 244 bn, the banking system's liquidity position remained robust, with the liquidity coverage ratio (LCR) at 243% (+19 pps compared to 2022 levels) and net stable coved ratio (NSFR) at 152%, both well above average EEA Banks (167% and 127%, respectively), while the loan-to-deposit ratio remained at 78%.

GREEN FUNDING

Under the Next Generation EU, Portugal has in place the Recovery and Resilience Plan (PRR) with a special focus on climate and environmental policies. Portugal's plan to support the green transition includes a public aid scheme for investment in the energy efficiency of residential buildings (up to EUR 300 mn) to (I) support a major wave of energy retrofits in residential buildings, (II) encourage resource and energy efficiency, (III) bolster energy production from renewable sources in the self-consumption regime, and (IV) combat energy poverty. Examples of such improvements include (a) installing heat-blocking insulation in walls, roofs, and windows; (b) installing climate control systems for home water heating and/or cooling (such as heat pumps); (c) installing renewable electrical energy generation systems under a community or self-consumption system for renewable energy; (d) water efficiency interventions, such as replacing outdated equipment with more energy-efficient models; (e) Interventions that promote the use of biomaterials, recycled materials and natural-based solutions.

ESG financing continues to improve in Portugal. As of December 23, total outstanding ESG bonds issued by resident entities amounted to EUR 10.7 bn (+47% y-o-y), of which 68% as green bonds. Non-financial corporations have the largest volume of debt securities classified as ESG, at EUR 8 bn. The financial sector issued the remaining EUR 2.7 bn.

Although the market is still improving, some banks offer mortgage loans with a discount on the interest rate or other benefits if the collateral has a higher Energy Efficiency Certificate grade.

[1] EBA Thematic note on moratoria and public guarantees, November 2020

[2] Growth expressed in domestic currency terms

	PORTUGAL 2022	PORTUGAL 2023	EU 27 2023
MACROECONOMIC VARIABLES			
Real GDP growth (%) (1)	6.8	2.3	0.4
Unemployment Rate (LSF), annual average (%) (1)	6.0	6.5	6.1
HICP inflation (%) (1)	8.1	5.3	6.4
HOUSING MARKET			
Owner occupation rate (%) (1)	77.8	76.0	69.2
Gross Fixed Investment in Housing (annual change) (1)	3.1	-1.1	-3.1
Building Permits (2015=100) (2)	366.8	391.1	94.0
House Price Index - country (2015=100) (2)	192.4	207.5	170.2*
House Price Index - capital (2015=100) (2)	n/a	n/a	165.1*
Nominal house price growth (%) (2)	11.3	7.8	3*
MORTGAGE MARKET			
Outstanding Residential Loans (mn EUR) (2)	101,700	100,370	6,782,375
Outstanding Residential Loans per capita over Total Population (EUR) (2)	9,824	9,589	15,114
Outstanding Residential Loans to disposable income ratio (%) (1) (2)	61.1	56.6	71.3
Gross residential lending, annual growth (%) (2)	5.8	34.0	-26.6
Typical mortgage rate, annual average (%) (2)	3.2	4.1	4.7

* Please note that this value is a simple average of the available values in 2023.

Sources:
(1) Eurostat.
(2) European Mortgage Federation - Hypostat 2024, Statistical Tables.

PORTUGAL FACT TABLE

Which entities can issue mortgage loans in your country?	Credit institutions (according to Decree-Law No. 349/98 of Nov/11 and within the limits established in articles 3 and 4 of DL No. 34/86, of Mar/3 for commercial and investment banks). The types of credit institutions and respective activities are defined by the Legal Framework of Credit Institutions and Financial Companies (articles 3 and 4).
What is the market share of new mortgage issuances between these entities?	In 2022, the largest credit institutions are expected to have continued representing the bulk of new mortgage production, with market shares generally reflecting the current market structure of the Portuguese banking sector (as per question three).
Which entities hold what proportion of outstanding mortgage loans in your country?	The seven largest institutions in Portugal are CGD, Santander Totta, Millennium BCP, BPI, Novo Banco, Banco Montepio and Crédito Agricola, which hold market shares ranging from c.4% of Crédito Agrícola to c.25% of CGD as of December 2022. *Source: Annual Reports; Banco de Portugal (Monetary and Financial Statistics).*
What is the typical LTV ratio on residential mortgage loans in your country?	Since 1 July 2018, new residential credit agreements should observe the following LTV limits: 90% for credit for own and permanent residence; 80% for other purposes than the latter; 100% for purchasing immovable property held by the credit institutions themselves and for property financial leasing agreements. In 2022, the bulk of new credit operations (99.7%) had an LTV ratio equal or below 90% (53,5% with LTV ≤80% and 46,2% with 80%<LTV≤90%). *Source: Banco de Portugal (Macroprudential measure within the legal framework of credit for consumers).*
How is the distinction made between loans for residential and non-residential purposes in your country?	Loans for residential purpose comprise (i) mortgage loans, which include credit agreements for the acquisition or construction of permanent, secondary or for-rental housing, and (ii) other related-mortgage loans, which comprise loans celebrated with individuals that are subject to the mortgage loans rules. *Source: Banco de Portugal (Bank Customer Website).*
What is/are the most common mortgage product(s) in your country?	The most common mortgage products are written with variable interest rate indexed to Euribor rate. As of December 2022, 89.6% of the mortgage contracts portfolio were written with variable interest rate, 6.4% with mixed rate and 4% with flat rate. Of the contracts written with variable interest rate, 43% were indexed to Euribor 12m, 32.4% to Euribor 6m, 22.2% to Euribor 3m and only 2.5% were indexed to other reference rates.
What is the typical/average maturity for a mortgage in your country?	Mortgage loans granted in 2022 had an average maturity of 30.7 years (32.5 years in 2021), 2.8 years lower comparing to the portfolio's (33.5 years as of December 2021, latest available data). *Source: Banco de Portugal (Retail Banking Markets Monitoring Report 2021; Recommendation on new credit agreements for consumers – progress report 1st quarter 2023).*
What is/are the most common ways to fund mortgage lending in your country?	From the banks perspective, retail and wholesale funding are the main sources of funding of the national banking system, with deposits becoming the main source (LTD ratio of 78.2% as of December 2022). From the point of view of customers, commercial banks are the most common providers of mortgage. *Source: Banco de Portugal, Portuguese Banking System: latest developments, 4th quarter 2022.*

What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?	There are bureaucratic charges related with the necessary procedures (at the Land Registry, Municipality Council and Notarial Office), and specific taxes related with house transaction, as the municipal taxes on real estate (IMI) and on onerous transfer of property (IMT). In purchases through loans, banks usually charge commissions related to the credit process (study and opening), which often include asset-evaluation costs.
What is the level (if any) of government subsidies for house purchases in your country?	Since September 2012 it is not possible to hire mortgages loans with a subsidised system scheme. Currently there are special conditions for disabled people with a disability grade greater than 60% and for family households in very difficult economic situation (Law 58/2012 of Nov/9). Following the increase of reference interest rates, a new decree law (Decree Law 20-B/2023 of Mar/23) entered into force in March 2023 that aims to concede temporary support to households with mortgage loans contracted before 15 March 2023. Borrowers eligible to benefit from this support may have temporary interest subsidy when the index of their credit contract is equal or greater than a threshold of 3%. This subsidy will be 75 or 50% (depending on the applicant household's income level) of the value of the interest corresponding to the difference between the index value determined contractually and the index threshold (3% or higher). Are eligible for this subsidy the households and contracts that meet the following conditions: (I) loans contracted before 15 March 2023; (II) have an initial contracted amount equal to or less than 250,000€; (III) are written with a variable interest rate regime or, in the case of mixed interest rate contracts, are in a variable interest rate period; (IV) have no overdue payments; (V) have a debt-service-to-income rate equal to or greater than 35% of their annual income (considering only the respective mortgage loan payments); (VI) have an annual income equal to or below 38,632€ (by reference to the last annual tax return) or, if above, that demonstrate that they have suffered a drop in income of more than 20% that places them below the limit of 38,632€; (VII) have no financial assets (which include deposits, financial instruments, capitalization insurance or savings or treasury certificates) with a total value greater than 29,786€ (by reference to the social support index). This support will be granted until December 2023.