ISSN 1725-3209

EUROPEAN ECONOMY

Occasional Papers 124 | December 2012

The Economic Adjustment Programme for Portugal Sixth Review – Autumn 2012

Economic and Financial Affairs

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KC-AH-12-124-EN-N
ISBN 978-92-79-22930-5
doi: 10.2765/25406

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European Commission
Directorate-General for Economic and Financial Affairs

The Economic Adjustment Programme for Portugal
Sixth Review – Autumn 2012

EUROPEAN ECONOMY Occasional Papers 124

ACKNOWLEDGEMENTS

The report was prepared in the Directorate General Economic and Financial Affairs under the direction of Jürgen Kröger, Director and European Commission mission chief to Portugal.

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EXECUTIVE SUMMARY

A joint EC/ECB/IMF mission met with the Portuguese authorities in Lisbon between 12 and 19 November to assess compliance with the terms and conditions set out in the Memorandum of Understanding as updated following the Fifth Review of the Portuguese Economic Adjustment Programme. *The objectives of the Programme are to restore sound public finances, improve competitiveness and put Portugal's economy back on the path of sustainable growth and job creation. This report provides an assessment of compliance and summarises the findings of the mission.*

The mission concluded that the Programme is broadly on track. *External and fiscal adjustments continue to advance, adequate capital and liquidity buffers of banks have reduced financial stability risks, and structural reforms are proceeding. Keeping the fiscal adjustment path on target implies additional consolidation efforts in 2013 and 2014. Against this background, strong commitment and perseverance need to be maintained to bring the Programme to a successful completion.*

The macroeconomic outlook remains largely unchanged from the previous review, with real GDP expected to fall by 3 percent in 2012 and by 1 percent in 2013. *Following a strong decline in 2012, economic activity is projected to recover gradually during 2013, with moderate positive growth rates from the second half of 2013. The recovery is expected to gather pace in 2014, although due to carry-over effects from softer external demand headline growth has been revised downward from 1.2 to 0.8 percent. The rebalancing of the economy towards export-led growth is set to continue, supported by further improvements in competitiveness. Risks to the projections could come from a deteriorating outlook in the euro area which could weigh on export dynamics and economic sentiment more generally.*

Fiscal consolidation efforts are in line with the revised deficit targets of 5 percent and 4.5 percent of GDP for 2012 and 2013. *Revenue collection has been somewhat weaker than envisaged in recent months, partly offset by tight spending execution. The government has implemented additional measures to meet the 2012 target. However, risks to the achievement of the target remain, not least due to continued revenue shortfalls and uncertainties with regard to the statistical treatment of the planned sale of airport concessions. The target for 2013 is underpinned by a range of measures in the 2013 budget amounting to more than 3 percent of GDP. These include, on the expenditure side, further cuts in compensations of employees; a reduction in social transfers and subsidies including for the health care sector; curtailing intermediate consumption; and cuts in investment. On the revenue side, the budget foresees a restructuring of the personal income tax that reduces the number of brackets, increases the average tax rate and curbs tax benefits; a surcharge on taxable income above the minimum wage; a solidarity surcharge on the highest incomes; limiting the deductibility of interest costs from corporate taxes; and a reduction in the threshold for the highest surcharge on profits. Overall about 80 percent of the fiscal adjustment in 2013 will come from the revenue side. In view of the risks associated with the strongly revenue-based adjustment the authorities are preparing contingency measures, predominantly on the expenditure side, amounting to 0.5 percent of GDP. Going forward, the mission supported the authorities' intention to rebalance the adjustment effort toward permanent reductions in expenditure. To this effect, the authorities are carrying out an expenditure review and results will be presented at the Seventh Review.*

Structural measures to enhance control over government expenditure and improve revenue collection are progressing at a good pace. *The authorities are planning a comprehensive reform of the budgetary framework to bring it in line with best practices in budgetary procedures and management. The new commitment controls system is starting to show results but implementation needs to be monitored to ensure full effectiveness of the system. Budgetary risks in Madeira are being addressed with corrective measures. Local administrative reform is progressing as planned. Reforms in the central administration, which have already produced significant savings, will continue. The restructuring of revenue administration is close to completion and the authorities are enhancing monitoring and strengthening revenue compliance. The renegotiation of PPPs has started and significant savings are expected for 2013 and beyond. The government expects SOEs to reach operational balance by the end of the year at sector level. The schedule for privatisations has been re-confirmed. In the health care sector, policy implementation advances broadly in line with targets and starts to produce important savings.*

The resilience of the banking sector is improving, in spite of a difficult macro-economic situation. *Impaired loans are likely to rise further due to the weakening economy, especially in the construction and real estate segments. The demand for investment credit and house purchase remains weak. On the positive side, deposits remain resilient although the previously observed rapid deposit growth, which also contributed to the overall deleveraging process, has faded. Deposit remuneration came substantially down after supervisory action by the central bank. This will help Portuguese banks to start reducing their funding costs, which should translate, at some point, into lower lending rates. Also, the capital reinforcement exercise that took place throughout the summer and still continues in some banks has raised the sector's capacity to weather a longer than previously forecasted recession. Nevertheless, access to credit remains costly and difficult, in particular for small and medium-sized enterprises (SMEs). To address this issue, government action to ensure adequate funding is ongoing, including initiatives to improve information-sharing on SMEs and facilitate their access to capital markets.*

Fostering a more competitive economy remains imperative. *In addition to strengthening active labour market policies, the authorities are committed to reducing severance payments and promoting labour market flexibility and job creation. Judiciary reforms aiming at unclogging the court system are being finalised in the areas of civil procedures and court management. A reform of port labour and port governance, including the overhaul of port operation concessions, will lead to cost reductions and operational improvements in this part of the transport infrastructure critical for exports. Reforms aiming at cutting down context costs in energy and telecommunication are coming to conclusion. The powers of National Regulatory Authorities will be reinforced to enable them to efficiently protect customers through regulating natural monopolies and promoting competition. Furthermore, a comprehensive reform of the corporate income tax has been launched to foster investment and competitiveness whilst ensuring its compatibility with EU rules. A wide array of structural reforms are in the pipeline such as the liberalisation of the regulated professions, facilitating the provision of services and streamlining licensing of activities and need to be followed through with determination so as to introduce more dynamism into the economy.*

As part of its market re-entry strategy, the Portuguese Treasury has exchanged EUR 3.75 billion of bonds maturing in September 2013 into a bond maturing in October 2015 at a yield of 5.12 percent. *On top of it the government is optimising the cash reserves in the wider public sector which leads to savings in reserve holdings. As a consequence, the likelihood of Portugal being able to cover its financing needs in 2013 has strongly improved.*

The successful completion of the Sixth Review will release EUR 1.6 billion from the EU and EUR 0.9 billion from the IMF, bringing overall financing to EUR 64 billion (more than four fifths of the total envelope). *These disbursements could take place in January 2013 subject to the approval by ECOFIN and Eurogroup for the EU loans and the IMF Executive Board for the IMF loan. The government's program is supported by loans from the European Union amounting to €52 billion and a €26 billion Extended Fund Facility with the IMF.*

I. INTRODUCTION

1. The report assesses compliance with the terms and conditions set out in the Memorandum of Understanding as updated following the Fifth Review of the Portuguese Economic Adjustment Programme. The assessment is based on the findings of a joint European Commission (EC)/European Central Bank (ECB)/International Monetary Fund (IMF) staff mission to Lisbon from 12 to 19 November.[1] In accordance with the Council Implementing Decision amending Implementing Decision 2011/344/EU on granting EU financial assistance to Portugal[2], the mission assessed compliance with the conditionality associated with the seventh disbursement and progress towards the key objectives of the Programme of sound public finances, restoring competitiveness and putting Portugal's economy back on the path of sustainable growth and job creation. It also revised the specific policy conditionality while keeping unchanged its main objectives.

2. The Economic Adjustment Programme was agreed by the Ecofin Council on 17 May 2011 and by the IMF Executive Board on 20 May. The Programme, which covers the period 2011-2014, entails an external financing by the European Union, the euro-area Member States and the IMF of some EUR 78 billion[3], for possible fiscal financing needs and support to the banking system. One third will be financed by the European Union under the European Financial Stabilisation Mechanism (EFSM), another third by the European Financial Stability Facility (EFSF), and the remaining third by the IMF under an Extended Fund Facility.

3. A successful completion of the Sixth Review will pave the way for the release of the next loan instalment of around EUR 2.5 billion. This instalment will bring EU and IMF financing to around EUR 64 billion, representing more than 80 percent of total available financial assistance.

II. ECONOMIC DEVELOPMENTS AND OUTLOOK

MACROECONOMIC OUTLOOK

4. The macroeconomic outlook remains broadly unchanged, with real GDP expected to fall by 3 percent in 2012 and by 1 percent in 2013. In line with the projections of the Fifth Review, real GDP decreased by 0.9 percent in the third quarter of 2012 compared with the previous quarter. Accordingly, the projected profile of economic activity has been left unchanged, i.e. a strong decline in 2012 is expected to be followed by a gradual recovery during 2013, with moderate positive growth rates from the second half of 2013. The decline in economic activity in 2012 is driven by a marked 7 percent contraction in domestic demand, which is only partly offset by buoyant net exports. Amid continued weak business and household confidence, domestic demand is expected to trend further downwards in 2013, with the contribution of domestic demand to growth revised down from -2.7 in the last review to -2.9 percentage points in this review. This is balanced by an upward revision of the contribution of net exports from 1.8 to 2 percentage points, as slightly lower export growth is more than offset by a stronger fall in imports, in line with the evolution of domestic demand. HICP inflation decreased to 2.1 percent year-on-year in October 2012, falling below the euro area average rate for the first time since mid-2010. Inflation at constant taxes has been below the euro area average already since early 2011 (see Graph 1), with the latest reading standing at 0.8 percent. The forecast for price and wage developments in 2012-13 has been maintained. The outlook for unemployment has also remained unchanged, with the number of jobless expected to peak towards the end of 2013 at 16½ percent of the labour force.

5. The economic recovery is expected to gather pace in 2014. Despite some headwinds for domestic demand from further fiscal consolidation, economic activity is projected to expand on an annual basis starting from 2014 with the contributions of domestic demand and net exports becoming more balanced. Headline growth has been revised downward from 1.2 to 0.8 percent compared with the previous review due mainly to carry-over effects from softer external demand. Subdued domestic demand and the weak labour market should continue exerting downward pressure on wages and prices.

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[1] The cut-off date for the macro-economic and fiscal projections of this report is 19 November 2012.

[2] OJ L 269 of 14.10.2011

3 The IMF share of the Programme was set in Special Drawing Rights. Due to the lower Euro Exchange rate, since May 2011, the projected payout by the IMF in Euro has become higher, so the current projected Programme total is EUR 79.5 billion.

6. The rebalancing of the economy towards export-led growth is set to continue at a good pace. The external balance of goods and services is expected to become positive by the end of this year and to improve further over the forecast period, notwithstanding the expected cyclical rebound of domestic demand. The current account is set to turn around faster than previously expected due to lower-than-anticipated primary income deficits and is now projected to almost balance in 2014. Competitiveness as measured by unit labour costs relative to the euro area average has improved significantly over the last three years (see Graph 2), and further progress is expected for 2013 and 2014. However, the recent adjustment in unit labour costs was to a significant extent due to labour shedding and public sector wage cuts, part of which will be reversed by the reinstatement of a monthly salary in the public sector. In addition, the high level of foreign indebtedness accompanied by still increasing primary income deficits requires a further structural improvement in external competitiveness.

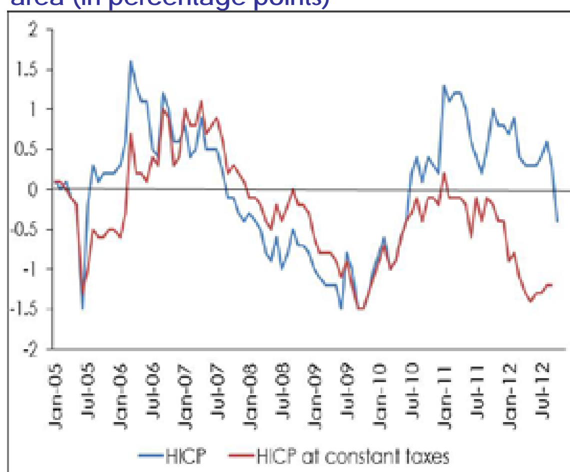
Table 1: Projections of main macroeconomic aggregates

	Nov 2012 (6th review)			Sep 2012 (5th review)			*Difference*		
	2012	2013	2014	2012	2013	2014	*2012*	*2013*	*2014*
				year-on-year volume change					
Gross domestic product	**-3.0**	**-1.0**	**0.8**	-3.0	-1.0	1.2	*0.0*	*0.0*	*-0.4*
Private consumption	**-5.7**	**-2.2**	**0.4**	-5.9	-2.2	0.2	*0.1*	*0.0*	*0.2*
Public consumption	**-3.5**	**-3.2**	**-2.0**	-3.5	-3.2	-1.5	*0.0*	*0.0*	*-0.5*
Fixed investment	**-13.7**	**-5.5**	**3.0**	-14.1	-4.2	2.7	*0.4*	*-1.3*	*0.3*
Exports of goods and services	**4.6**	**2.9**	**5.0**	4.3	3.5	5.5	*0.3*	*-0.6*	*-0.5*
Imports of goods and services	**-5.9**	**-2.1**	**3.8**	-6.5	-1.0	3.3	*0.6*	*-1.1*	*0.5*
				contributions to real GDP growth					
Domestic demand excl. inventories	**-7.0**	**-2.9**	**0.3**	-7.1	-2.7	0.2	*0.1*	*-0.2*	*0.1*
Change in inventories	**0.1**	**0.0**	**0.0**	0.1	0.0	0.0	*0.0*	*0.0*	*0.0*
Net trade	**3.9**	**2.0**	**0.6**	4.1	1.8	1.0	*-0.2*	*0.2*	*-0.4*
Employment (y-o-y change)	**-3.9**	**-1.6**	**0.5**	-3.9	-1.6	0.3	*0.0*	*0.0*	*0.2*
Unemployment rate (level)	**15.5**	**16.4**	**15.9**	15.5	16.4	15.9	*0.0*	*0.0*	*0.0*
HICP (y-o-y change)	**2.8**	**0.8**	**1.2**	2.8	0.7	1.1	*0.0*	*0.1*	*0.1*
Current external balance (% of GDP)	**-2.7**	**-0.6**	**-0.2**	-3.2	-1.9	-1.3	*0.5*	*1.3*	*1.1*

Source: European Commission

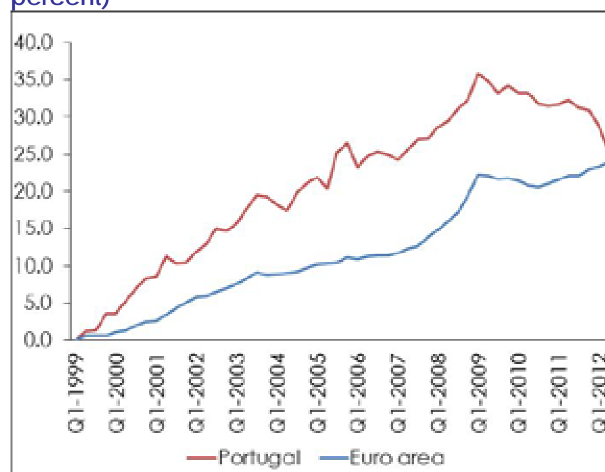
7. Risks to the macroeconomic outlook are tilted to the downside. A stronger-than-expected deterioration of the economic climate in the euro area would have serious spill-over effects on Portugal. Also, with recent business and confidence indicators having partly reached record lows, a further deterioration of economic sentiment could delay the recovery of domestic demand beyond 2013.

Graph 1: Inflation differential against the euro area (in percentage points)



Source: European Commission

Graph 2: Unit labour costs 99Q1-12Q2 (increase in percent)

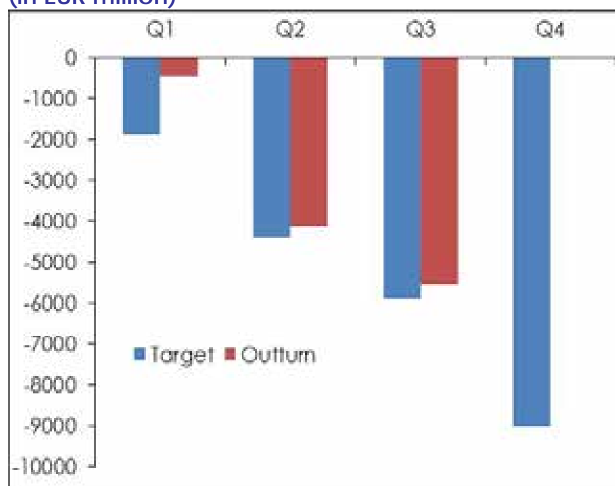


Source: European Commission

FISCAL DEVELOPMENTS

8. The third quarter target for the government cash balance of 3.5 percent of GDP was met. This was achieved despite an unfavourable evolution of tax revenues and social contributions, thanks to a tight execution of expenditures in the first nine months of the year. At the central government level, budgetary execution benefited in the last months from the suspension of some investment projects and a drawing down of budgetary buffers. Data up to September show that the operational balances of SOEs and budgetary developments in regional governments were less negative than projected whilst the surplus of local governments increased more strongly, mainly owing to a lower public wage bill. By contrast, social security deficits were higher than predicted due to unemployment rising faster than expected.

Graph 3. 2012 Quarterly Performance Criteria for General Government Balance – cash data (in EUR million)



Source: European Commission

9. In national accounts terms, the government deficit in the first half of 2012 was worse than the cash data suggests. At an estimated 6.8 percent of GDP, the government deficit in the first half of 2012 was 1.5 percentage points lower than in the same period of last year. The statistical difference with public accounts cash data, which according to the Performance Criteria show a deficit of 5 percent of GDP, is explained by time adjustments in the recording of taxes and social contributions, lags between interests accrued and paid, and a different delimitation of the general government perimeter.

10. State tax revenues have been shrinking amid weak macroeconomic developments. Tax collection until October fell by 4.6 percent compared with the same period of the year before, affecting both direct and indirect taxes. Corporate income taxes fell by 20 percent. Indirect taxes declined by 5.1 percent, as weak private consumption hit VAT revenues (-2 percent, including the effect of transfers to finance some social programmes) but also fuel taxes (-8.2 percent), vehicle taxes (-43.6 percent), tobacco taxes (-9.3 percent) and stamp duties (-9 percent, due to the decline of financial transactions). In recent months, the behaviour of tax revenue is largely explained by temporary factors, such as an unanticipated increase in reimbursements. Total tax reimbursements up to October increased by 3.1 percent on a year-on-year basis. However, gross collection before reimbursements or other transfers (which can be viewed as the best proxy for the tax base at a macro level) indicates that the declining trend of net collection could reverse once the temporary factors dissipate. Nevertheless, the fast decline in tax collection poses a downside risks to the attainment of the 2012 revenue target as included in the 2013 draft budget (which had already revised downward the initial estimate of the 2012 budget by 1½ percent of GDP).

11. Primary government expenditure has continued its downward trend over recent months, albeit at a slowing rate. Cuts in payroll costs and in investment were the main drivers of the fall in primary expenditure. Personnel expenses have decreased for all subsectors of the general government. For the State and Social Autonomous Funds, the wage bill fell by 13.7 percent year-on-year up to October. This is the result of both cuts in salaries (particularly the suspension of the summer bonus) and a reduced headcount. Until September, the reduction of public employees was twice as high as foreseen in the Adjustment Programme, mainly due to the layoffs in the education sector (5.1 percent compared with a 2 percent Programme target for the year). On current trends, the authorities expect an overall reduction of public employees by more than 3 percent for the year as a whole. Nevertheless, the attainment of the overall expenditure target is not without risks as there are indications that some payments that should have taken place earlier in the year have been delayed, which may raise expenditure in the last months of the year.

12. The social security balance fell by 0.5 percent of GDP over the first ten months of the year. On the one hand, social security contributions (which represent about half of the revenues of the social security sector) saw a year-on-year decline of 4.8 percent up to October as a consequence of falling employment and wages. On the other hand, unemployment benefits (which represent around 11 percent of the social security spending) increased by 23.4 percent compared with the same period last year, 14.6 percentage points higher than budgeted. Social

transfers have also moderately moved upwards, though the increase in pensions was mainly due to the payment of pensions transferred from the banking sector to the public system (financed by the State Budget).

Arrears

13. Latest data show that arrears have started to decline. In the health sector, the decline in the stock of arrears was particularly noteworthy due to the debt settlement programme worth EUR 1.5 billion, which was close to be completed by September. The decline in arrears of local governments will accelerate over the next months as the municipalities start benefitting from the Support Programme for Local Authorities (PAEL). By mid-November, the financial plans of about 80 municipalities that requested assistance under the programme had been assessed and first transfers are expected to take place at the end of 2012 or in early 2013. At the regional level, progress has been more muted. The central government is analysing a plan by the Autonomous Region of Madeira to pay arrears and benefit from some discounts in exchange of support from the Central Government in the form of guarantees.

14. The implementation of the commitment control law to prevent the accumulation of new arrears seems to be on track. The broadbased decline in arrears, although largely driven by the settlement of the stock, also appears to reflect a decline in the accumulation of new arrears (Table 2). However, the effectiveness of the new commitment control system will have to be closely monitored during the next few months to ensure that the indicative target of non-accumulation of arrears is met.

Table 2: Stock of arrears in 2012 (in EUR million)

	2012 (1)								(2)	(3)=(2)-(1)	
Subsector of the General Government	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Δ *Sep-Jan*	% total
Central Government excluding NHS	190	204	191	179	135	155	129	122	120	-69	3%
NHS classified in General Government	219	194	152	185	202	216	200	36	37	-182	1%
Reclassified entities	51	50	45	46	61	48	39	39	33	-18	1%
Local Government	1690	1711	1738	1760	1657	1597	1552	1531	1503	-188	38%
Regional Government	1185	1215	1287	1320	1261	1319	1304	1286	1267	82	32%
Total	3335	3373	3413	3490	3315	3334	3224	3014	2960	-375	75%
Total Consolidated	3219	3254	3289	3365	3200	3226	3117	2909	2855	-364	72%
Other entities outside General Government											
Enterprises excluding NHS	11	18	19	26	32	34	32	40	46	35	1%
NHS incorporated hospitals	*1695*	*1697*	*1856*	*1948*	*1996*	*1877*	*1806*	*1086*	*1044*	-651	26%
p.m.: health sector inside + outside GG	*1914*	*1891*	*2007*	*2132*	*2197*	*2093*	*2006*	*1122*	*1081*	-833	27%
TOTAL	4925	4969	5164	5339	5227	5137	4955	4034	3945	-979	
p.m.: percent of GDP	*3.0*	*3.0*	*3.1*	*3.2*	*3.1*	*3.1*	*3.0*	*2.4*	*2.4*		

Source: Ministry of Finance and Commission services
Note: Consolidated data concerns data net of intra-government sector arrears. Total amounts adjusted for arrears' settlement.

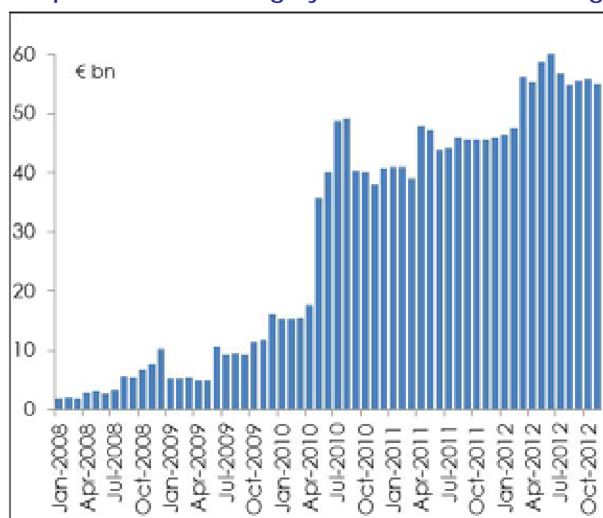
FINANCIAL MARKETS AND FINANCIAL SECTOR DEVELOPMENTS

15. The downward trend of bond yields has not continued in past months. Following the substantial fall in secondary market rates in the first eight months of the year, yields have been moving sideways without clear trend since. While the earlier decline in rates signalled increasing confidence in the success of the Programme in addition to the impact of ongoing initiatives at European level, the uncertainty created by the Constitutional Court decision to reinstate the cuts in public sector and pensioners holiday and Christmas bonuses have contributed to a temporary interruption in this trend. Encouragingly, rates have come down again recently which is likely to be a reflection of, amongst othe factors, returning political and social stability.

16. ECB lending to banks in Portugal decreased since the last review. Some banks reduced their lending from the ECB whilst others increased their borrowings marginally (Graph 4). A large share of the outstanding Eurosystem funding stems from the two long-term operations providing liquidity for 36 months, enhancing the stability of banks' funding.

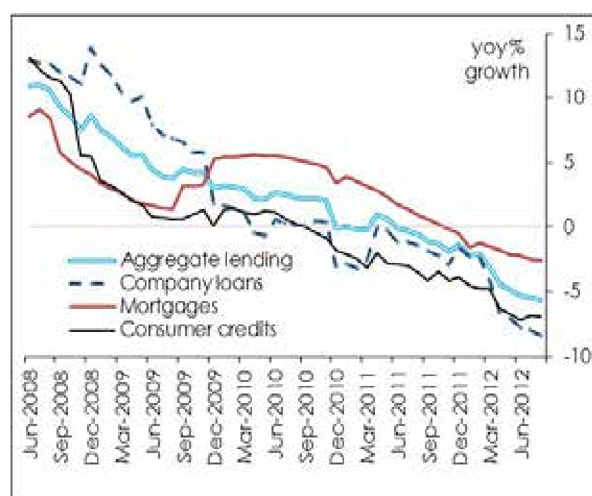
17. Deleveraging takes place in all loan sectors whereas new loans go mainly to the corporate sector. Whereas aggregate loans diminished by 5.7 percent between August 2011 and August 2012, sectorial developments differ substantially. The monthly amount of newly granted loans still reaches nearly ¾ of the past decade's average but, unlike in the years before the crisis, the lion's share (85 percent) goes to companies as the issuance of new mortgages has practically stalled. Nonetheless, given their fast roll-over, the stock of corporate loans fell by 6.5 percent between September 2012 and 2011. Corrected for the sale of loan portfolios the decrease is a more moderate 5.0 percent. Privately-owned companies saw their loan stock decrease by 7.3 percent whereas state-owned enterprises, whose share in total company loans is 5.3 percent, increased their loan stock by 10.4 percent. On the positive side, exporting companies were able to borrow 2.5 percent more than a year ago. Loans to the household sector, of which 82 percent are mortgages, decreased by 4.7 percent. Given the long maturities typical for mortgages, the stock of housing loans decreased by a mere 2.6 percent on a year-on-years basis in August (Graph 5). New mortgages amount to only 1/7 of the past 10 years' average. Loans to companies involved in the real-estate sector declined by 6.7 percent on an annual basis in the third quarter of 2012, reflecting depressed construction activity. In line with falling consumption, consumer credit decreased by 6.9 percent over the past 12 months. In early 2011, deleveraging occurred mainly through loan sales or disposing of foreign assets. Both operations have a limited impact on domestic loan supply. Given depressed prices and lesser assets on sale this two options came to a natural end. During the first 18 months of the Programme, deleveraging was largely achieved through better than expected deposit growth. With deposits now slightly diminishing, further improvements in the loan/deposit ratio will have to come from a shrinking loan stock. Because of the aforementioned movements the funding gap is closing fast (Graph 6).

Graph 4: ECB borrowing by banks located in Portugal



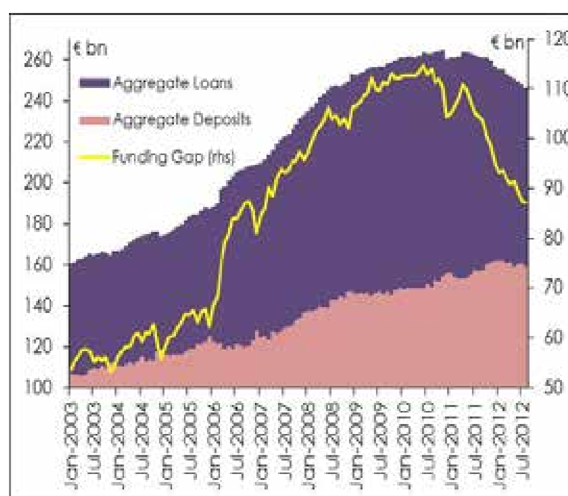
Source: Bank of Portugal

Graph 5: Trends in different loan segments



Source: Bank of Portugal

Graph 6: The funding gap is shrinking fast

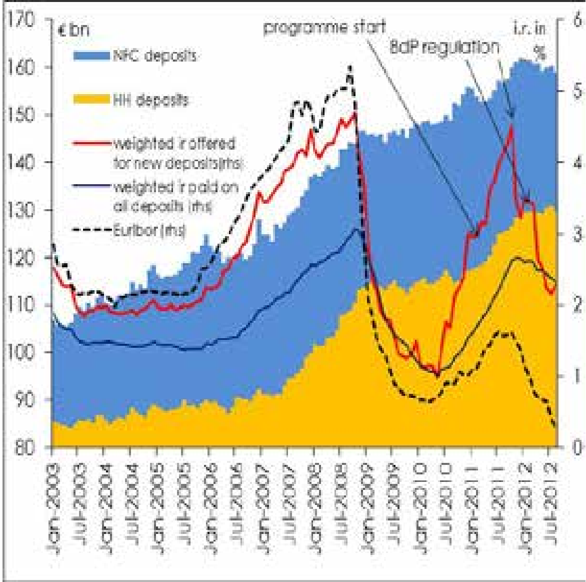


Source: Bank of Portugal

18. Aggregate deposits reach broadly the same level as one year ago. At the outbreak of the sovereign crisis in the second quarter of 2010, Portuguese banks saw themselves excluded from the interbank market and had to tap deposits as their primary funding source. In the process, banks competed for deposits by offering ever higher interest rates, which not only weakened their profitablitity but also put upward pressure on interest rates for bank loans to the non-financial sector. This development was successfully brought to a halt by a Banco de Portugal regulation on deposit remuneration, as a consequence of which the weighted interest offered for new

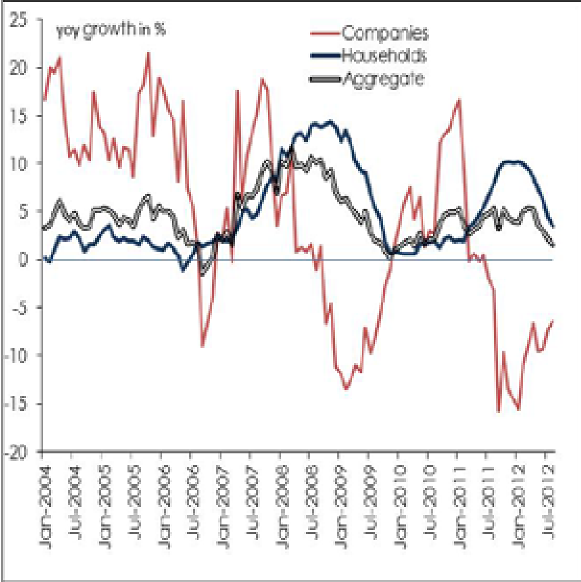
deposits has halved over the past 12 months (Graph 7). The impressive growth previously observed was mainly due to the transformation of securities placed with customers into deposits. This growth has stalled at the aggregate level, as total deposits oscillated around EUR 160 billion since November 2011, reflecting lower money demand in a context of declining economic activity and also a portfolio shift backwards into debt securities issued by banks and companies as the latter currently offer higher interest rates than banks' deposit remuneration on offer. In addition, companies ran down deposits as a substitute for difficult to obtain and expensive corporate credit. Compared with August 2011, companies' term and sight deposits fell by 6.4 percent (Graph 8). But the decline in corporate deposits seems to have slowed down somewhat in recent months. Household deposits, although also affected by the above mentioned factors, have proved quite resilient, increasing by 3.5 percent over the same time-span, which is a clear indication of the high degree of confidence in the Portuguese banking system.

Graph 7: Deposit remuneration came down thanks to the supervisory action



Source: Bank of Portugal

Graph 8: Deposit growth by segment



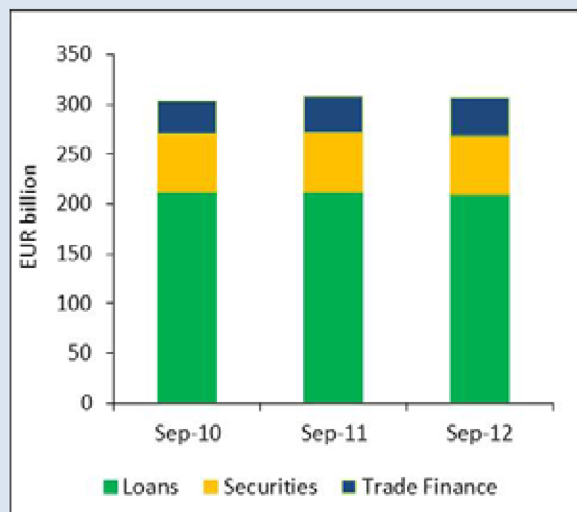
Source: Bank of Portugal

19. While bank credit to the corporate sector continues to contract, in particular to SMEs, progress towards diversifying financing sources was recorded. Total credit granted to non-fianancial private corporations (including lonas, debt securities and trade credit) has recorded only slightly negative year-on-year rates of change, due to the relaively favourable dynamics of non-domestic sources of financing. The recourse to non-domestic financing has been concentrated on large firms. The expansion of credit to large firms has also been supported by capital markets access, including in the domestic retail market, whereas loans by domestic banks to SMEs exposed to the non-tradable sector continued to contract. To mitigate the impact of banks' deleveraging strategies on their ability to finance the corporate sector, new avenues of financing are being pursued. The preparation of a pilot joint issue of corporate debt instruments for the capital market is under way. While some sort of public support may be envisaged at an initial stage, such as a capital guarantee, building on a diversified portfolio this market driven solution partially mitigates the credit risk of companies which, due to their size, are not in a position to access the capital markets individually. A detailed assessment of this measure, including an analysis of the suitable legal mechanisms, will be presented by end-January 2013. Initiatives to help mitigate risks to lenders by upgrading and promoting sharing information on SMEs are being considered. The supply of credit to microenterprises, including self-employment initiatives, is expected to increase, further to on-going applications by domestic credit institutions to the EIB Progress Microfinance Facility.

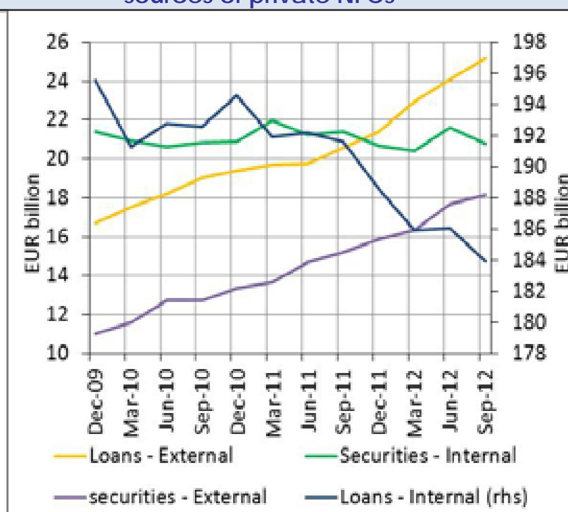
BOX 1: DEBT FINANCING TO THE CORPORATE SECTOR IN PORTUGAL

The Portuguese private corporate sector indebtedness is composed of a mix of loans, securities and trade credits. Over the last two years to September 2012, loans accounted for more than two thirds of the total outstanding indebtedness of private sector companies. The indebtedness structure was broadly stable during this period, although trade credits, which account for 13% of total debt sources, increased marginally, at the expense of the role of loans. The overall outstanding debt of private Non-Financial Companies (NFCs) is EUR 307 billion (September), 0.3% less than the year before, of which EUR 209.1 billion refer to loans, from both domestic and foreign sources (Graph I). The loans comprise mostly bank loans although a significant amount is not originating from the financial sector. Despite the overall stability of the indebtedness structure of private NFCs by source type, the overall figures mask a number of facts. Over the last year loans contracted 1.4%, the effect having been offset essentially by a 6.4% increase in trade credits. In the last quarter securities issuance increased 1.5%, which is explained by the issuance of retail bonds, essentially by listed companies. Credit originating from external (foreign) sources increased to an extent similar to the decrease observed in credit originating from internal sources. This substitution effect happened via both securities and through a substantial increase in external loans (22% yoy) (Graph II).

Graph I: Debt sources of private NFCs



Graph II: Internal vs. foreign debt sources of private NFCs



Source: Bank of Portugal

Although a number of large companies are able to access the debt market directly, or have access to external loans, smaller companies face difficulties in obtaining debt finance because of their high reliance on bank loans and more generally, domestic funding sources. Given that access by the corporate sector to bank credit is not normalised, SMEs are those facing the toughest financial constraints. SMEs absorb the bulk of corporate loans by financial institutions, having accounted for 77% of total EUR 110 billion of loans by financial institutions to NFCs[4]. Indeed, since December 2011, the amount of bank loans granted to NFCs recorded increasingly negative yoy changes, with a 6.5% decline in September. While these loans to SMEs declined 9%, those to large enterprises recorded a 2.8% annual increase (Graph III). Portuguese SMEs reported deterioration in the availability of bank finance since 2010[5]. The importance of "access to finance" as a concern increased for Portuguese SMEs, and despite declining turnover, the proportion of respondent SMEs who refer this topic as the most pressing concern reached a peak in September, and is amongst the five highest in the euro area. Also, the proportion of rejected demands for bank credit (24%) remains among the euro area highest, over the six months to September 2012. Only 40% of respondent SMEs report having received the full amount of credit asked to the bank. This behaviour should be read together with credit risk indicators observed. While large enterprises overdue loans account for 2.4% of total outstanding loans, small and medium enterprises display an equivalent ratio of 12.4%, 5 times higher (loans by the financial sector, BoP, September 2012). However, the relatively better credit risk record of large companies could to a certain extent reflect also a stronger impact of evergreening practices: banks have more incentives for renewing credit lines to large companies with which they already have significant exposures, to support their viability.

Loans extended to exporting companies by financial institutions, 13.6% of total NFCs loans, increased 2.5% (September, yoy). This is an improvement from June, though not as favourable 2011 developments.

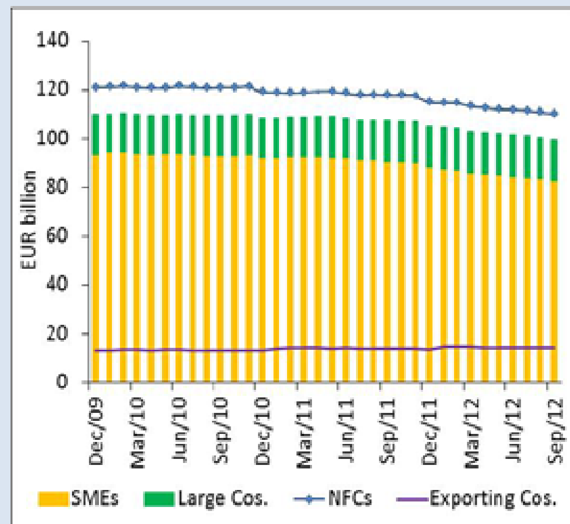
Trade credits data on average claim settlement periods also show the comparative difference between SMEs and large

[4] The disaggregation of financial institutions-related data refers to the whole corporate sector, i.e., including State-Owned Enterprises (SOEs), and not just to the private corporate sector. SOEs overall indebtedness decreased slightly in September (yoy), but the reduction of foreign funding sources is being compensated by internal sources (though not by resident financial institutions).

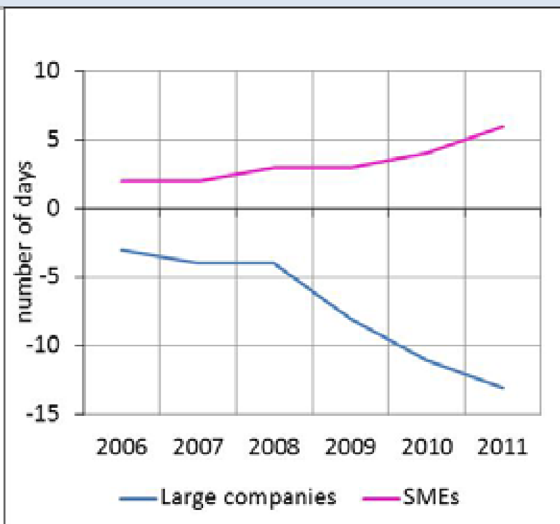
[5] ECB Survey on the Access to Small and Medium-sized Enterprises in the euro area, April to September 2012, November 2012.

companies. Structurally large companies receive their trade credits faster than SMEs and are able to settle their accounts payable sooner than SMEs, hence denoting a more agile financing structure. The most recent data record (2011) indicates that the average accounts receivable period of large companies was 52 days as opposed to 89 days for SMEs, while the average accounts payable period of large companies was 65 days and 83 for SME's. Graph IV depicts the performance of the time gap (in days) between the average accounts receivable period and the average accounts payable period. This indicator is understood here as a proxy for «trade finance needs» (if positive) or «trade finance resources» (if negative). Over the period 2006-2011 the indicator increased for SMEs, but was reduced for large companies, suggesting that SMEs have an increasing need to finance their working capital, while large companies increasingly use trade finance (usually with no explicit remuneration) as a financing source, thus optimizing their operations-derived financial flows.

Graph III: Loans from financial institutions to the corporate sector



Graph IV: Time gap between accounts receivable and accounts payable (days)



Source: Bank of Portugal
Notes: SMEs and large companies do not sum up to the total because holding companies are not classified according to their size. SMEs are companies with less than 250 workers and turnover inferior to EUR 50 million or total balance sheet assets of less than EUR 43 million (EC recommendation). Exporting companies are shown as an independent category, in addition to being included in the overall figures of NFCs.

There is no straightforward data that allows defining a clear border line between supply and demand factors affecting the quantity of credit extended to the corporate sector in Portugal. The analysis presented here points to a mix of both. However, on the supply side, risk aversion to an increasingly indebted corporate sector appears to be playing a role, leading banks to ask relatively high interest rates, both in historic euro era terms as in relation to other euro area members. In September the average rate for new loans offered by the resident financial sector to companies was 6.13%, 3.5 p.p. higher than in the euro area. Despite a reduction of ca. 50 bps from the year before, the gap with the euro area somehow widened. For smaller loans the equivalent rate is 6.8%. For companies to use credit at such high rates an equal or higher return on investment (ROI) is required, which did not happen in 2011 (ROI was more than 2 p.p. lower than the cost of debt) and mostly likely is not happening this year, given the more challenging economic environment. Consequently, exploring and implementing financing alternatives for companies is becoming increasingly necessary to respond to the financing needs of the most productive segments of the economy.

20. Credit lending standards and loan demand remained broadly unchanged throughout the third quarter of 2012. Banco de Portugal's latest bank lending survey confirms the bleak outlook for loan growth. In the third quarter, the declining investment credit demand is heavily affected by the weakening business confidence of the corporate sector. The drop in investment credit is, however, offset by the increasing financing needs associated with debt restructuring and related to inventories and working capital of Portuguese firms. High unemployment and fiscal consolidation dampen both consumer confidence and domestic demand affecting households' loan demand in the consumer and house purchase segments. The latter remains fragile also due to the bleak outlook for the housing market. These developments are generally expected to continue in the fourth quarter even though banks foresee keeping the criteria applied to household and business loans unchanged, in contrast to the first half of 2012. Some factors do however exert an increasingly tightening influence on banks' credit standards, with the weakening economic outlook, the deleveraging pressure, heightened rik aversion and the persistently high cost of funding coming on top of the list.

Table 3: Soundness indicators of the Portuguese banking system

	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1	2012Q2	2012Q3 (1)
Return on equity (2)	7.2	7.6	7.1	6.7	6.2	4.3	2.4	-3.8	6.3	1.0	-0.3
Gross income on assets	2.5	2.6	2.6	2.7	2.4	2.5	2.5	2.5	2.6	2.7	2.6
Cost to income ratio	57.7	57.1	57.2	57.6	59.1	58.3	59.0	61.4	56.1	52.9	56.5
Non-performing loans	5.4	5.5	5.8	5.2	5.5	6.2	6.9	7.5	8.2	9.0	10.1
Coverage ratio	63.2	62.9	60.8	61.5	60.7	57.7	55.3	56.7	53.0	51.9	49.6
Capital adequacy ratio (3)	11.3	10.9	11.0	11.1	11.4	11.0	10.1	10.7	10.7	12.3	12.3
Core tier 1 ratio (4)	7.8	7.8	8.0	8.1	8.4	8.7	8.5	9.6	9.6	11.2	11.3
Loan-to-deposit ratio	163.4	166.6	158.4	157.8	156.7	149.7	146.2	140.2	136.9	136.3	133.3

Source: Bank of Portugal
Notes:
(1) Preliminary data
(2) Income before minority interests /Average shareholders equity before MI.
(3) Excluding the banks in resolution (BPN until end 2011 and BPP).
(4) The Core Tier 1 ratio according to Programme definition and excluding the banks in resolution (BPN until end 2011 and BPP).

21. Bank profitability remains depressed by rising credit impairment, continued deleveraging and relatively high funding costs. Three quarters into the year, banks continue to struggle with bad credit impairment charges and a thin net interest margin. Against a background of general uncertainty, an increase in the non-performing credit portfolio and the squeeze in interest income due to the low level of the Euribor, the key reference rate for Portuguese mortgages, banks have shown a considerable capacity to adjust quickly as the sector as a whole achieved a positive result in the third quarter[6]. The domestic result is being helped by further loan re-pricing and cost cuts. Nonetheless, the international business remains the mainstay of earnings generation for the Portuguese banking groups[7], in particular from subsidiaries outside the Euro area.

[6] Excluding BCP's write-offs associated with Greek exposure
[7] With the exception of BCP's Greek subsidiary

III. PROGRAMME IMPLEMENTATION

22. The joint EC/ECB/IMF staff mission concluded that the implementation of the Programme is broadly on track.

Table 4: Summary of compliance with policy conditionality for the Sixth Review

	Status
Fiscal policy	The quarterly quantitative performance criteria on the general government cash balance and debt for Q3-2012 were met. However, amid weak macroeconomic developments, tax revenues and social security contributions are still lower than in the same period of last year. On the expenditure side, personnel expenses fell at solid rates up to October whilst interest payments have grown considerably in 2012. The 5 percent of GDP budget deficit target for 2012 remains valid, in spite of increasing risks, notably due to continued revenye shortfall and the statistical treatment of the ANA concession. The 2013 budget makes up for the slippages in 2012, the reinstatement of one month salary and 1.1 monthly pensions, and contains consolidation measures worth more than 3% of GDP, mostly on the revenue side. Contingency measures will be specified at the Seventh Programme Review drawing on the ongoing expenditure review.
Financial sector	The large Portuguese banks fully comply with the European Banking Authority capital standards. As part of its normal supervisory tasks, a follow-up of the on-site inspection programme has been completed focusing on the loan portfolio of the real estate and construction sectors. Despite the improvement, the recovery of the assets of BPN which have been transferred to the SPV remains low and the outsourcing of its management to a professional third party is delayed. As part of the regulation concerning bank resolution, both the recovery plans and bridge banks supervisory notices were adopted; the decree-law on the funding arrangements of the resolution fund is expected to be finalised shortly. The general and extraordinary regimes pertaining to the out-of-court debt restructuring of households was published in the Official Gazette. BdP continues their efforts to avoid banks' evergreening of loans and promote prompt restructuring of problem loans. The preparation of a pilot joint issue of corporate debt instruments for the capital market is underway. Initiatives to upgrade and promote sharing information on SMEs are being considered.
Fiscal-structural	Public finance management: The authorities are planning an ambitious reform of the Budget Framework Law. The Law will be amended by the end of this year to incorporate the new EU fiscal governance rules. An additional reform is announced for next year to improve budgetary procedures and principles, accountability, transparency and simplification. The process will be conducted in consultation with the relevant stakeholders. Arrears: The stock of arrears has been significantly reduced, particularly in the health sector and further declines are to be expected in the local administration by the beginning of next year. The implementation of the commitment control law to prevent the accumulation of new arrears needs close monitoring. Regional and local government reform: A draft version of the regional and local finance laws was discussed during the Sixth Review and the end-year target of submission to Parliament remains achievable. Local administrative reform is progressing as planned with the reduction in the number of parishes attaining its last stage and the elaboration of a new law defining competences at the local administration and the inter-municipal entities. Budgetary risks in Madeira require corrective measures. Public sector reform: The reduction of managers and administrative units according to PREMAC was completed. The new legislation on working time and geographical mobility was submitted to Parliament and a reform of the 'Special Mobility' scheme is expected in 2013 to support a broader public administration reform for a better allocation of human resources. SOEs, PPPs and privatisations: As a result of their ongoing restructuring, SOEs should reach operational balance by the end of 2012. Additional reforms are

	expected in the coming years to further improve the public companies' financial results. Privatisation plans are proceeding according to schedule, with the transaction of the health business of CGD signed and the privatisations of ANA and TAP expected to be signed before the end of the year. The renegotiation of PPPs has started and significant savings are expected already in 2013. Health: Policy implementation is continuing broadly in line with MoU's deadlines and is starting to produce important savings both in terms of pharmaceutical expenditure and hospital operational costs. Authorities are progressively increasing primary care provision and will now focus on hospital reform, including hospital reorganisation and changes to hospital financing and performance measurement. Additional reform steps are expected regarding public healthcare sub-systems. Revenue administration: Some major organisational reforms underway should be successfully concluded by the end of the year. Bottlenecks in the tax courts continue to be tackled by clearing high-value cases. The property revaluation process has accelerated in the last months. Authorities remain committed to put in place strategies to monitor and strengthen tax compliance.
Reform of labour, goods and services markets	Labour market and Education: Legislation to reduce severance payments to 12 days per year is expected by mid-December. The design of a fund and a possible date for its implementation is to be decided between the government and social partners. A Council of Ministers Resolution, in force since 1 November, sets new rules for the extension of collective agreements. Important progress has been made in the area of activation and active labour market policy (ALMP). The dual training system is being strengthened. On education, a tool for country-wide monitoring of educational outcomes by school has been presented; the number of proposals to conclude trust agreements with selected primary and secondary schools is already over 40; the formula to monitor the cost per student in every school and the full assessment of the new inspection model are expected by the end of the year. Energy: Implementation of the electricity costs reduction and tariff debt elimination by 2020 is on-going. For wind power capacity, an agreement with most of the producers was reached. For small-hydro power, negotiations are on-going. Final draft legislation for changing the CMEC[8] annuity discount rate in line with EC/ECB/IMF proposals should be approved in coming weeks. Negotiations concerning the Sines and Pego power plants are still on-going, with estimates of the total cost reduction ranging between EUR 1.3 and 1.4 billion in NPV terms. The legislation ensuring the financial and operational autonomy of the electricity regulator has not yet been adopted. Telecommunications and Postal: The process to designate the Universal Service Provider(s) started, thereby allowing market players to enter the universal service segment through an efficient, transparent and non-discriminatory public tender in compliance with the EU law requirements. The amended framework for the provision of universal service for postal services has not yet been adopted. Transport: The draft law on port work is expected to be adopted by the Parliament by the end of the year. The government is preparing a Decree Law on port operation; t(he draft is expected by the end of the year. Most cost reductions in ports (around 25 to 30 percent compared to the current situation) are expected to come from the revision of concessions. A reduction by 20 percent in tariffs levied by the port authorities (TUP Carga) has been approved. A Decree Law which sets the legal basis for the new transport regulator has been adopted. The report on the transfer of CP Carga terminals to another entity suggests that only two terminals generate sufficient movement to be viable options for privatisation. Services and professions: Progress on the adoption of legislative amendments to align the legislation with the principles of the Services Directive has continued, albeit at a modest pace. One third of the sector-specific amendments that are necessary to fully implement the Services Directive are still pending, although work on half of them is advanced. As regards professional services, the draft law deregulating three professions and the horizontal legal framework on professional services governed by professional associations were approved by the Parliament.

[8] Custos de Manutenção de Equilíbrio Contratual.

	To complete the recognition framework of professional qualifications, main legislative pieces have been adopted. A clear roadmap and work programme was presented to make the Point of Single Contact operational. Possible lack of human resources is a clear risk that could compromise the timely implementation of this reform.
Reform of framework conditions	Housing market: The government has adopted the complementary legislation of the law on the housing rental market. However, the late publication of these legal texts may further delay the actual implementation of the law. The revision of the cadastral value of the housing stock is expected to be completed by the first quarter of 2013. Judicial system: Reforms of the judicial system continue to advance on schedule. Progress has been made on the reduction of backlogged cases, the geographical reorganisation of the court districts, and the reform of the Code of Civil Procedure. Business environment: Financing alternatives for companies, including measures to stimulate a more equity-oriented culture in the corporate sector, are under consideration. In addition, the renewal of the existing guarantee line "PME Crescimento" of EUR 2 billion has been approved wigth the 2013 budget. Specific measures funded by the EU Structural Funds such as "QREN Investe" or incentives to SMEs are already operational. The system accelerating VAT exemptions for exporting firms, which enters into force at the beginning of the next year, will reduce the time required to provide all the necessary information from an average of more than 42 days to just 4 days. Strong commitment and fast progress are necessary to ensure the timely implementation of the Late Payments Directive by March 2013. Competition and sectorial regulators: The adoption of the Framework Law, setting out main principles for the functioning of National Regulator Authorities (NRA) is expected by the first quarter of 2013. The sale of the 1 percent share of CGD in Galp was completed on 27 November 2012.
Data submission	Requirements under the Programme have been observed. Work is ongoing to improve further data submission.

FISCAL POLICY

Budgetary execution in 2012

23. The budget deficit target of 5 percent of GDP for 2012 remains valid, but risks are non-negligible. Budget execution until October points to continued revenue shortfalls. Moreover, while budget execution on the expenditure side has been in line with projections, the implementation of additional measures worth 0.3 percent of GDP to cover for revenue shortfalls, as agreed at the Fifth Review, is not yet fully completed. The freeze of investment and of the acquisition of some goods and services has already been adopted and the necessary changes to high value property taxes are also in place, but the frontloading of some social security measures envisaged for 2013 is still pending. At the current stage it is difficult to judge whether the deficit target can be achieved because the full impact of these measures will only materialise in December. As a result, and despite the authorities' expectation that revenure shortfalls will fade out in the last months of the year, there are important risks to the revenue target. In particular, the statistical treatment of the sale of an airport concession is still being assessed by the statistical authorities and may not be accounted for as a deficit-reducing operation. This by itself could raise the headline deficit by 0.7 percent of GDP, but repercussions on the 2013 budget will be limited, if any, given the one-off nature of the operation.

Fiscal consolidation in 2013

24. The 2013 budget law includes discretionary measures of more than 3 percent of GDP to achieve the deficit target of 4.5 percent of GDP. On the expenditure side, the budget foresees a sizeable reduction in the public sector wage bill through lower employment coupled with a reduction in overtime payments and other compensations. Rationalisation efforts in the health sector, SOEs, PPPs will be deepened, while social spending will be further streamlined. On the revenue side, the budget foresees a restructuring of the Personal Income Tax (PIT) that will reduce the number of brackets and increase the average tax rate in line with European standards, while preserving progressivity and curbing tax benefits. In addition, a surcharge of 3.5 percent is imposed on the part of taxable income above the minimum wage and a solidarity surcharge of 2.5 percent on the income exceeding EUR 80 000 and of 5 percent on income above EUR 250 000. Corporate tax revenues are increased

by means of limiting the deductibility of interest costs, reducing the threshold for applying the highest surcharge on profits and changing the methodology for special prepayment to companies, among others. The budget also considers changes in indirect taxation by means of higher excises on tobacco, alcohol and natural gas, broadening the scope of property taxation after revaluation of properties and the creation of a financial transaction tax. In addition, social contributions will also rise as they will be also charged on supplementary payments for public employees and on unemployment benefits. Taking into account these measures, revenue increases will contribute 80 percent to the fiscal adjustment in 2013 while the remaining 20% will come from expenditure reductions. Going forward, the authorities plan to launch a comprehensive reform of corporate income taxation to make it more growth friendly without compromising tax collection.

25. Budgetary consolidation in 2013 needs to compensate for a negative primary balance drift of about 1½ percent of GDP and the dissipation of one-off measures amounting to 1 percent of GDP in 2012. The negative balance drift is caused by labour market developments and the shrinkage in tax revenue bases, linked to the downturn and the conintued rebalancing towards a less tax-friendly but more export-intensive economy. As the one-off measures that reduced the nominal deficit in 2012 also fade out, the deficit would rise by a further full percent of GDP in the absence of corrective action (Table 5). In addition, the budget needs to compensate the effect of the reinstatement of 1 monthly wage and 1.1 months of pension payments in the public sector following the Constitutional Court ruling (worth 0.8 percent of GDP). By contrast, the increase in interest payment is a relative modest 0.1 percent of GDP, which is less than assumed at the time of the last review. As the net result of these effects, the nominal deficit in 2013 is expected to improve by only 0.5 percent of GDP in spite of overall consolidation measures amounting to 3.9 percent of GDP.

Table 5: Arithmetic of the government deficit: from the deficit in one year to the next

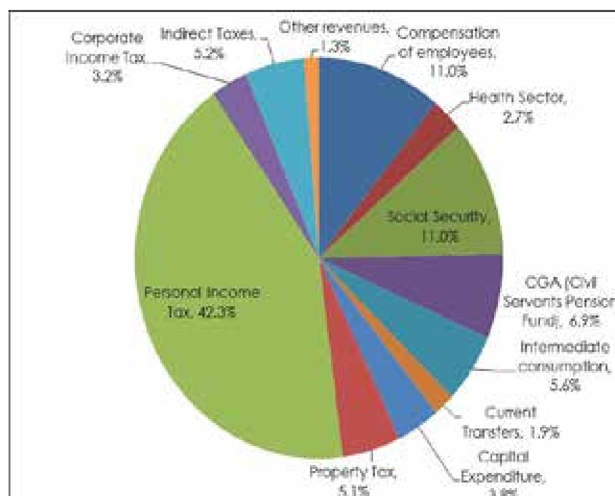
(+) means balance-improving impact; (-) means balance-reducing impact	% of GDP
2010 balance (observed)	**-9.8**
Primary balance drift in 2011	1.6
Change in interest expenditure	-1.1
Dissipation of one-offs and non-recurrent effects from previous year	0.7
New consolidation measures	4.3
2011 balance (estimate)	**-4.4**
Primary balance drift in 2012	-3.4
Change in interest expenditure	-0.2
Dissipation of one-offs and non-recurrent effects from previous year	-3.0
New consolidation measures	6.0
2012 balance (target)	**-5.0**
Primary balance drift in 2013	-1.6
Change in interest expenditure	-0.1
Dissipation of one-offs and non-recurrent effects from previous year	-1.0
New consolidation measures	3.9
Reinstatement of one salary and 1.1 pension	-0.8
2013 balance (target)	**-4.5**

Balance in year t equals balance in year t-1 plus nominal primary balance drift in year t, plus the impact of the change in interest expenditure in year t, plus the impact of the dissipation of the one-offs and non-recurrent measures from year t, plus the impact of new consolidation measures in year t.

The Primary Balance Drift includes the change in the balance level that would take place without discretionary measures. It includes the impact of economic activity on the balance, including the composition of growth, and the structural increase in expenditure in real terms, e.g., the increase in pension expenditure.

26. Risk to the attainment of the 2013 deficit target are elevated. The 2013 budget proposal contains a detailed fiscal risks assessment. Regarding macroeconomic risks, one scenario considers a fall in internal consumption leading to lower real GDP (1 percentage point less) which in turn would reduce tax revenues and social contributions and increase the deficit by 0.4 percentage points. Alternatively, higher-than-expected unemployment of 1 percentage point would raise the deficit by 0.3 percentage points. Other risks to public finances arise from the high SOEs indebtedness in a context of difficult access to finance, which is leading to an increase in State guarantees. Given the consolidation efforts which are to be achieved at regional and local level, risks to the general government budget also derive from this side although to a lesser extent than in previous years due to enhanced monitoring and control systems. The stronger reliance on revenue-based consolidation in 2013 poses additional risks as these measures are more directly related to macro-economic developments outside the control of the government. Finally, there is a general risk that some of the savings measures included in the 2013 budget may be challenged in the Constitutional Court.

Graph 9. Split of consolidation measures in 2013 Budget



Source: Commission Services

27. The authorities stand ready to implement additional measures in 2013 should slippages occur. With a view to addressing the risks to budgetary execution, the authorities are preparing contingency measures worth at least ½ percent of GDP. A large share of these measures consists of additional reductions in the wage bill and increased efficiency in the functioning of public administration. Moreover, budgetary appropriations will be adjusted in case budgetary execution risks materialise. The measures will be further specified once the comprehensive expenditure review currently underway (see below) is concluded.

Structural fiscal adjustment 2011-2014

28. Permanent consolidation measures of at least 1¾ percent of GDP will be implemented in 2014 to reach the deficit target of 2½ percent of GDP. A comprehensive expenditure review has been initiated with the objective of enhancing the efficiency and equity of public services, while generating targeted savings of EUR 4 billion. The identification, quantification and timetable of implementation of the measures will be fully defined by mid-February 2013 in time for the Seventh Review. The exercise aims at reducing redundancies across the public sector functions and entities and reallocating resources toward growth-friendly spending areas. The 2013 Stability Programme will further detail the results of this exercise and provide additional information on the medium-term fiscal consolidation plans. Overall, the cyclically-adjusted primary balance – net of one-off measures - is expected to improve by more than 9 percent over the period 2011-2014 (see Table 6). When including the EUR 4 billion to be identified in the expenditure review, over the whole Programme period expenditure will contribute 60 percent to the consolidation, while revenue will contribute the remaining 40 percent.

Table 6: Fiscal targets and structural adjustment 2011-2014

	2011	2012	2013	2014
Deficit targets	-4.4	-5.0	-4.5	-2.5
Budget deficit, net of one-offs	-7.4	-6.0	-4.6	-2.5
Structural balance	-6.1	-4.0	-2.6	-0.9
Primary balance	-0.4	-0.8	-0.1	2.1
Structural primary balance	-2.1	0.3	1.8	3.7
Fiscal adjustment	3.4	2.4	1.5	1.9
Fiscal effort (EDP definition)	2.2	2.2	1.4	1.6

Note: Fiscal adjustment measured as the difference between structural primary balances.
Fiscal effort defined as the difference between structural balances.

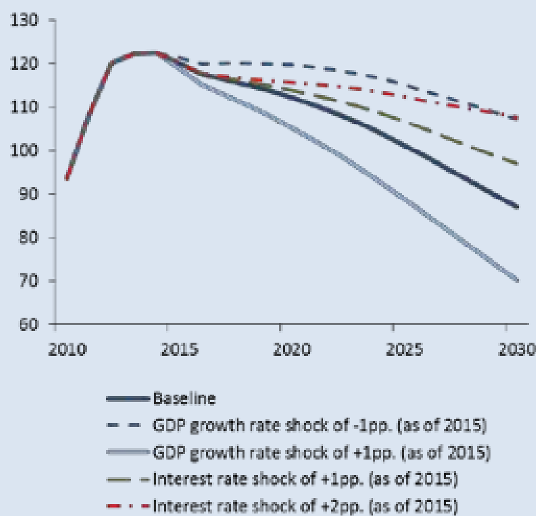
Box 2: Government Debt and Fiscal Sustainability in Portugal

Under the Programme scenario, government debt is projected to peak at 122.3 percent of GDP in 2014 and to gradually decline afterwards. The baseline long-term calculations shown below incorporate the Programme scenario up to 2016. The precise calculations for these figures are shown in Annex Table 7. The turning point is the result of achieving a primary surplus of about 3 percent of GDP, combined with a modest GDP growth. After 2016, it is assumed that: (i) the structural primary fiscal balance remains unchanged at a surplus of 3 percent of GDP;(ii) nominal interest rates are around 5 percent; (iii) nominal GDP growth stays close to 4 percent (2 percent growth in volume terms plus 2 percent inflation); (iv) ageing costs are taken into account according to the projections in the Commission's 2012 Ageing Report; and (v) the expected fiscal impact of PPPs costs and bank recapitalisation costs of EUR 12 billion over the Programme period is factored into the analysis.

Full observance of the Programme plans ensures a gradual decline of the debt ratio over the longer term. Nevertheless, for a large number of years the debt ratio would remain higher than before the current crisis. The graphs in this box present a sensitivity analysis with respect to macro-economic risks, the impact of different fiscal consolidation paths, and the potential impact of contingent liabilities such as reclassifications and other changes in the government perimeter.

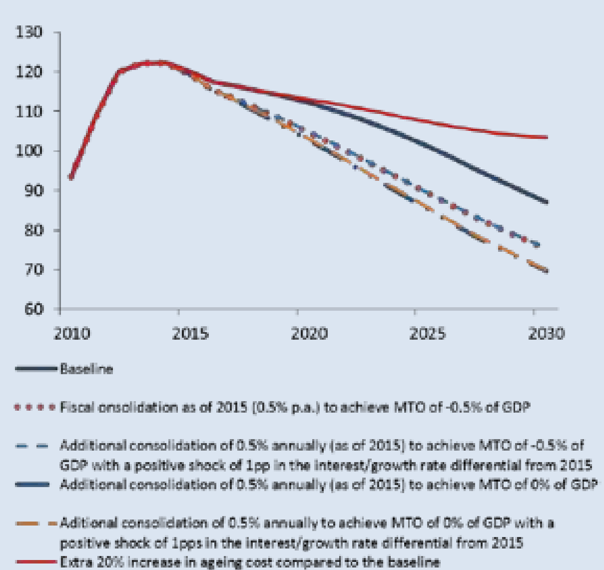
Graph I illustrates the sensitivity to macro-economic assumptions by considering a shock to real GDP growth and hikes in interest rates as from 2015. A lower GDP growth rate by one percentage point or a higher interest rate on maturing and new debt by one or two percentage points would significantly slow down the pace of debt reduction without jeopardising the declining trend over the medium-term. Conversely, a positive shock to growth in the medium-term on the account of the thorough structural reforms undertaken may result in visibly lower debt-to-GDP ratios and a higher pace of debt reduction.

Graph I: Macroeconomic risks-growth and interest rates (debt as % of GDP)



Source: Commission services

Graph II: Fiscal consolidation and ageing costs (debt as %of GDP)



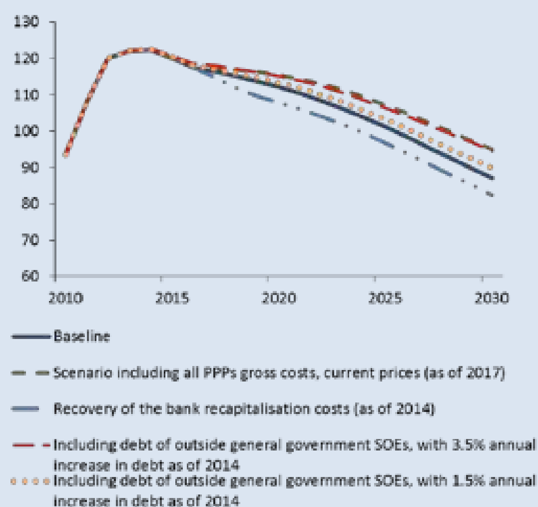
Source: Commission services

Additional fiscal consolidation beyond 2015 and the Programme horizon would clearly accelerate the debt reduction path (Graph II). Reaching the Medium Term Objective (MTO) of a structural deficit of 0.5 percent in 2015, would imply a fiscal effort of about 0.5 percent and a primary surplus of 3.5 percent. Maintaining the MTO over the longer term horizon will require primary surpluses of up to 4.4 percent in 2020 declining gradually to close to 3.0 a percent a decade later. Under these assumptions, the debt to GDP ratio will start declining already in 2015 falling below 100 percent at the beginning of the next decade and maintaining the sustainable downward path thereafter. Aiming at a more ambitious MTO of 0 percent would accelerate even further the debt decline. On the other hand, if ageing costs are allowed to rise significantly (simulated as a 20 percent increase), the fall in the ratio would be severely curtailed, stabilising at a high level in the absence of compensating fiscal consolidation.

Graph III illustrates the impact of changes in the government perimeter. The inclusion of all gross costs of PPPs and the debt of all state-owned enterprises (SOE) classified outside general government would lead to noticeable increase in government debt, especially if further increases in SOE debt are not reined in. The ongoing renegotiation of PPPs contracts will limit the cost of a reclassification scenario. Similarly, a far-reaching privatisation programme combined with the necessary reforms to reduce SOEs operational costs and a strategy to reduce their debt burden will also contain the risks stemming from SOEs. By the same token, a quick repayment of the bank recapitalisation funds to the government would quicken the adjustment towards lower debt-to-GDP ratios

Overall, the debt sustainability analysis reveals that the debt reduction path of the baseline is robust across a wide range of scenarios. Even in a setting which combines a number of adverse shocks, a solid reduction path is attainable if fiscal responsibility is maintained after the end of the Programme period.

Graph III: Changes in general government perimeter (debt as % of GDP)



Source: Commission services

29. Debt is projected to peak at slightly above 122 percent of GDP in 2014 and enter on a gradual downward path afterwards. The reduction in the debt ratio compared with the Fifth Review estimate (123 ½ percent of GDP in 2014) reflects the centralisation of cash holdings from the civil servants' and the general social security regimes at the debt management agency (IGCP), which amounts to EUR 1.3 billion already in 2012 and an additional EUR 0.5 billion in 2013. The assessment of debt sustainability remains broadly unchanged with a primary position of close to balance in 2013 and primary surpluses from 2014 onwards reflecting the recovery of the economy and the strength of the fiscal consolidation. Reaching the Medium Term Objective (MTO) of a structural deficit of 0.5 percent in 2015 would require a primary surplus of 3.5 percent. Maintaining the MTO over the longer term would require primary surpluses of up to 4.4 percent until 2020. Under these asumptions, the debt-to-GDP ratio would be on a firm downward path from 2015 onwards falling below 100 percent at the beginning of the next decade.

FISCAL STRUCTURAL REFORMS

Fiscal policy framework

30. The authorities are planning a comprehensive reform of the Budget Framework Law. A first phase, to be completed by the end of this year, consists of the transposition of the EU fiscal framework and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union ("fiscal compact"). A second phase, to be implemented in the course of 2013, will enhance budgetary procedures and principles of budgetary management, accountability, transparency and simplification. The process will be conducted in consultation with the relevant stakeholders. Although much has been done in the past couple of years to improve public financial management, the Portuguese system still suffers from several fragilities, such as budget fragmentation. With a view to overcoming these shortcomings, a three-year action plan has been prepared and published as an annex to the budget.

Revenue administration

31. Major organisational reforms are underway in revenue administration and should be successfully concluded by the end of the year. These include the key reform of the structure of the *Autoridade Tributária e Aduaneira* (AT); the establishment and clear definition of competences of an organisational unit to manage the tax affairs of the large taxpayers segment (Large Taxpayers Office); and the increase of enforcement capacities of the tax administration, that will hire about one thousand new tax auditors by an internal recruitment process. The authorities are committed to streamlining the revenue administration by reducing the number of local tax

offices. The process will lead to a closing of one half of the existing branches by the target date of June 2014. Although this revised plan implies some delays, due to the fact that it is being embedded in the overall framework of a rationalisation of all public services provided at local level, it is also more ambitious than the initial plan.

32. The property revaluation process has accelerated in recent months. The authorities expect to achieve the revaluation of about 4 million properties by the end of the year (out of the 4.9 million total) and to finalise the process by March 2013. The updated values of properties subject to revaluation will form the basis for the calculation of the 2013 property tax (Imposto Municipal sobre Imóveis).

33. Bottlenecks in the tax courts are being be tackled by targeting cases above EUR 1 million. The experience with the task forces of tax judges created to deal with high-value cases is considered positive and it is deemed desirable to extend their operations until June 2013 in order to gain more experience. The share of success cases for the State in all litigation cases is increasing.

34. Achieving the revenue target requires enhanced monitoring and a strengthening of compliance strategies. A new set of measures to fight non-compliance will enter into force in 2013, including a unified monthly return covering information on both social contributions and withholding taxes and the major reform of the VAT invoicing system. The government has also taken recently measures to fight fraud and evasion, notably changes in the regime of wealth signals triggering investigations and of tracking offshore transfers. Moreover, the authorities will launch an in-depth analysis of tax compliance by looking at the current revenue collection performance for different sectors and taxpayer sizes with a view to developing adequate response strategies. Furthermore, a new tax compliance management approach will be phased in over a three-year period, starting with the implementation of two pilot compliance improvement projects for key risk sectors, namely high net wealth individuals and self-employed professionals.

Regional and local governments

35. There is good progress in the revision of the regional and local finance laws to meet the end-year target of submission to Parliament. The current draft of the local finance law reflects the recommendations of the IMF/EC technical assistance mission in March 2012 but some elements still have to be defined. The draft law provides a broad framework of principles and rules together with the functioning of the Financial Coordination Council. Several key elements on the revenue side, notably the sources and size of own revenues and the calibration of transfers are still under discussion. Also, the role and financing of inter-municipal entities and the mechanisms of insolvency are not yet fully specified. The regional and local finance laws will adopt the principles of the budgetary framework law. Financial recovery rules have been inspired by the existing adjustment programme for Madeira. The definition of the fiscal rules, and in particular the debt rule, follows the model of municipalities by limiting the debt to 150 percent of net current revenues.

36. Budgetary risks in Madeira are being addressed with corrective measures. Underperforming revenues resulting from a more subdued performance of the regional economy and delays in curbing expenditure in some areas, such as investment, add up to an estimated deficit of about EUR 300 million, against a programme target of EUR 158 million. Therefore, the regional authorities have presented corrective measures, which the central government expects to bring the deficit to EUR 178 million by the end of the year. Overall, programme performance is mixed with some good results in curbing public expenditure to partly cover for revenue shortfalls.

37. Local administrative reform is progressing as planned. The reduction of the number of parishes by about 25 percent is in its final stage and expected to be concluded before the end of the year. The number of staff in local administrations declined by 3.8 percent overall in the third quarter of 2012 relative to end-2011. The elimination of one third of the positions of local administration managers is expected to be completed by the end of this year. A new framework law on the attribution and competences of local administrations and the statute of inter-municipal entities has been submitted to the Parliament. The purpose of the law is the transfer of responsibilities to the administrative level that can implement them most efficiently.

Public administration reform

38. The authorities are making significant advances in rationalising the central administration. The reduction of the number of managers and administrative units according to the PREMAC plan was concluded, with a few legal acts still pending publication. The new legislation on working time and geographical mobility

has been submitted to Parliament. The 'Special Mobility' scheme is being modified in the context of the 2013 Budget and a deeper reform is to be expected next year to support a broader public administration reform, addressing training and requalification for a better allocation of human resources. The aim is to simplify procedures, limit compensations and apply it to all sectors of the public administration. The reduction of personnel is progressing at a faster pace than initially foreseen with the overall annual reduction expected to be above 3 percent compared with a 2 percent target, according to the authorities' latest estimates. The implementation of shared services is progressing in line with the Programme schedule. A comprehensive study to review wage scales in the public sector relative to the private sector is expected to be available by the end of the year.

SOEs, PPPs and privatisations

39. The government expects SOEs to reach operational balance at sector level by the end of the year. On the expenditure side, cost reductions mostly arise from the wage cuts (suspension of the 13th and 14th salary) and the reduction in employment combined with efficiency-improving measures. On the revenue side, tariffs have been increased and exemptions reduced. Authorities are exploring ways to combat rising fraud which in past months contributed to revenues below expectations. In 2013, the reinstatement of the 13th salary will be compensated by further measures lowering employment, containing salaries, cutting current expenses and streamlining of investments while ensuring a strict implementation of the commitments control law. The schedule for privatisations as set out in the Programme has been confirmed, with the privatisation of the health business of CGD signed and the privatisation of ANA and TAP expected to be signed before the end of the year with a view to completion early next year.

40. The renegotiation of PPPs has started and significant savings are expected for the 2013 budget and beyond. The government is focusing its renegotiations efforts on road PPPs which represent 74 percent of all net public cost in net present value (NPV) terms. The first stage of negotiations, which focussed on a reduction of the scope of road sub-concession contracts still in a construction phase, was completed in October and aimed at savings of €1 billion NPV (permanent impact on state budget starting in 2014), higher than the initial target. A second stage of renegotiations will be carried out in compliance with the new legal framework for PPPs and will be led by the new PPP unit in the Ministry of Finance once it is fully operational. The goal is to revise the baseline scenario of all road PPPs, allowing for more private partner risk-taking and imposing a lower internal rate of return for shareholders. This should yield a significant positive impact on the public budget, while ensuring a sustainable reduction in government liabilities. Savings in the 2013 budget beyond the immediate effects of renegotiations include, amlongs other measures, operational measures in toll collection.

Healthcare sector

41. Policy implementation is continuing broadly in line with targets and starts to deliver significant savings. Revenues from co-payments are expected to double by the end of 2012, resulting in additional EUR 80-90 million by the end of 2012 compared with 2011. Authorities also aim to reinforce non-budget revenues by increasing payment collection from insurance companies and from cross-border care and care provided to foreigners.

42. The authorities are taking steps to transform existing primary care services into family care units (USFs). Improved coverage of primary care services is a means to ensure that the referral system to specialist and secondary care is more effective and to reduce unnecessary use of emergency care. Additional family care units (USFs) have been opened during 2012, bringing their number to 344 active USFs and 83 additional applications. An agreement with the medical association has increased the number of patients per family doctor from 1500 to 1900 and the patient registries for family doctors are being updated. These measures aim at reducing the share of patients not covered by family doctors, which currently amount to 17 percent. The system of electronic medical records has been finalised and is being rolled out through NHS facilities. This system will help improve safety of care and avoid the duplication or unnecessary use of services such as diagnostics. The revision of the co-payment system also contributed to increasing patients' use of primary care and reducing the use of emergency care.

43. Important savings have been realised in the hospital sector. Operational costs were lowered by 6 percent (EUR 314 million) in 2011 compared with 2010 and are expected to decline by an additional 9 percent (EUR 400 million) in 2012. The authorities aim for an additional reduction of about EUR 250 million in 2013, in part to compensate for the reintroduction of the 13th wage. These savings are in line with MoU targets (15 percent reduction over 2011-2013). Outsourcing of diagnostics and rehabilitation has led to savings in operational costs by 5 percent (EUR 38 million) in 2011 compared with 2010 and by an additional 10 percent (EUR 60 million) in

2012, notably by renegotiating/reducing prices paid to private providers and changing remuneration systems. In addition, the stock of arrears has been significantly reduced through the debt settlement strategy. About EUR 1.5 billion have been paid and the remaining stock of about EUR 1 billion will be reduced through a combination of additional settlements and increased efficiency in the sector.

44. The authorities confirmed their commitment to reorganising hospitals, changing hospital financing and introducing performance measurement. Several mergers/closures of hospitals and departments have already taken place since 2011, leading to a concentration of medical departments and laboratories, an elimination of about 1000 beds and a reduction in overtime. The authorities have presented the principles of the 2013 hospital reform which aims at further important savings through hospital reorganisation in 2013-14. The plan will be finalised by end November and will need to be implemented throughout 2013.

45. Progress has been made in centralising purchasing, but there is still room to extend its use. Several active substances and medical devices have been tendered or are now under tender procedures. In addition, centralised purchasing has been extended to service cars, IT services and outsourcing services. The authorities are planning to extend the use of centralised purchasing to other medical devices (following the continuous development of a uniform coding for medical devices) but also in relation to utilities (telecommunications).

46. Regarding pharmaceuticals, a wide set of measures are being implemented. Among these measures are the compulsory e-prescription and INN prescription, changes in pharmacies' margins, in the international reference price system and in the pricing of generics, the removal of administrative and legal hurdles to enhance the use of generics and prescription guidelines and regular monitoring of prescription behaviour and feedback to physicians. Overall, these measures will result in important savings in outpatient public spending (-10.3 percent year-on-year for the first three quarters of 2012). They also contribute to a reduction in private pharmaceutical spending (-12.9 percent year-on-year for the first 8 months of 2012). Savings on pharmaceuticals in hospitals have been slower to materialise (-1.3 percent year-on-year in the first half of 2012), though recent centralised tenders may lead to potential important savings. Together with the agreement made with the pharmaceutical industry (including a "clawback" clause up to EUR 300 million for 2012), these measures are likely to ensure that the target for 2012, i.e. lowering expenditure to 1.25 percent of GDP, will be achieved.

47. Regarding public healthcare sub-systems (ADSE, SAD, ADM), progress has been slow so far but the 2013 budget proposes some changes to the current situation. There has been some effort to align fees paid to private providers with those of the NHS and the 2013 budget proposes that a certain set of services and corresponding expenditure will be transferred to the NHS. However, the cut in contributions paid through state transfers (from 2.5 to 1.25 percent of the individual salary) has not yet been enactecd.

FINANCIAL SECTOR

48. The large Portuguese banks comply with the European Banking Authority (EBA) capital standards. The largest Portuguese banks were required to top up their capital levels up to a minimum of 9 percent Core Tier 1 (CT1) ratio calculated according to the EBA methodology. The EBA capital reinforcement process concerned four Portuguese credit institutions and was driven by the writing down of government bond holdings down to market prices. The capital injected was in total EUR 8.2 billion, with an impact on the CT1 ratio of EUR 7.9 billion. Out of this, EUR 4.3 billion were financed from the Programme's EUR 12 billion strong backstop facility in exchange for contingent interest bearing convertible bonds, which need to be repaid within five years. One major bank was able to accommodate its EBA additional capital needs through private means. In addition to the EBA-related capital reinforcement limited to the biggest lenders, all banks are required to observe the year-end 10 percent CT1 objective set by Banco de Portugal, enabling them to weather loan losses that have substantially risen amid the economic slowdown. This capital augmentation process is still on-going though most banks already comply with this requirement.

49. Progress was achieved in the implementation of the early intervention and resolution framework. The authorities were asked to conclude the measures pertaining to the funding arrangements of the recently created resolution fund. As part of the tools to allow the intervention by the central bank in a credit institution or an investment firm in financial distress, leading to the orderly wind-up of the institution, rules governing the setting-up up and operation of bridge banks were adopted through a supervisory notice. A supervisory notice on recovery plans, which set their respective content and associated requirements, was also adopted. The recently created resolution fund will be funded by the proceeds of a bank levy as well as contributions from the financial institutions. The latter will be set in a Decree-Law, which is due for approval by end-December, in accordance

with the MoU. The regulation on resolution plans will be adopted by the same date by means of a supervisory notice. Also, the government will submit to Parliament in early 2013 amendments to the law governing banks' access to public capital so as to allow the state, under strict circumstances, to exercise control over an institution and to perform mandatory recapitalisations. In making such amendments, an appropriate balance will continue to be struck between preserving the private structure of the banking system and safeguarding the use of public resources.

50. Banco Português de Negócios (BPN) legacy assets are a long way from being recovered. Further to the sale of troubled BPN in March to a foreign buyer, the authorities are managing the legacy assets of the bank which remained as property of the state, accommodated in three special purpose vehicles (SPV). These SPVs are so far operated by ex-BPN staff. *Parvalorem* holds an overwhelmingly (80 percent) non-performing loan portfolio with a nominal value of EUR 3.4 billion. *Parparticipadas* manages the legacy intragroup participations and *Parups* looks after the remaining financial and tangible assets. The financial participations and material assets accommodated in the SPVs are being either liquidated or sold. Caixa Geral de Depósitos (CGD) state-guaranteed claims will be gradually settled in cash and any net recoveries from the SPV will add to CGD's reimbursements, while BPN staff currently employed by the *PARs* will either find employment in the sold companies or will be made redundant.

51. The preparation of the tendering process aiming at mandating a third party to gradually recover the credits currently held by *Parvalorem* is nearing completion. The authorities concluded the technical specifications relating to the service contract, which will be awarded to a professional third party mandated to gradually recover the EUR 3.4 billion portfolio of non-performing loans of *Parvalorem*. The tendering process chosen for the contract award is a public tender limited by prior qualification and should be now launched until end-2012 with a view to award the contract before mid-2013. The incentive structure, predominantly based on success fees will serve as guarantee that NPLs are efficiently being recovered maximising the recovery amounts owed by debtors. Recoveries in 2012 add up to around EUR 70 million until October, denoting a better record than in 2011.

52. Further to the adoption of the legal framework for corporate and debt restructuring, the authorities are now focussed on their implementation, aiming at contributing to an orderly deleveraging while minimising the impact of defaults in banks' balance sheets. Further to proposals adopted in Parliament, the legal framework for financial institutions to engage in out-of-court debt restructuring for households was enacted by Decree-Law nº 227/2012 (general regime). The measures contained therein foresee *inter alia* banks to develop risk management systems to monitor and prevent the risk of default by households (PARI) and guidance on a standard negotiation procedure between the credit institution and the bank client aiming at non-litigious settlement of debts (PERSI). In addition, an existing network of consumer protection advisers will be put up to advise households under financial distress and prevent the recurrence of over indebtedness. A law containing an extraordinary regime to protect mortgage lenders in extreme difficult economic and financial situation was also passed (Law nº. 58/2012). These acts, which enter into force in January 2013, are an important further step to resolving the private sector indebtedness, coping with the rising levels of non-performing loans and ultimately, promote the soundness of the financial system.

STRUCTURAL REFORMS

Labour market

53. Severance payments will be reduced to 12 days per year worked, close to the EU average. The implementation of the third stage of the reform of the severance pay system is expected for mid-December 2012. A fund to finance dismissal costs will also be considered by the authorities and social partners. The design of the fund and possible date for its implementation is still to be decided between the government and social partners.

54. A Council of Ministers Resolution, in force since 1 November, sets new rules for the extension of collective agreements. Only if companies involved in the collective agreement employ at least 50 percent of workers in a sector can that agreement be extended to the rest of the sector. In addition, the request for extension must be requested by both unions and employers' associations. The quantitative criterion is waived when the request for extension concerns only firms that employ more than 249 workers. The new rules are minimum requirements. The government will also take into account the impact on competitiveness of non-signatory firms when considering extending collective agreements.

BOX 3: THE SUPPORT GROUP FOR PORTUGAL

Following a request by the Portuguese Government, the President of the European Commission, José Manuel Barroso, decided on 12 October 2011 to set up a Support Group (SGPT) to assist Portugal in the implementation of its Economic Adjustment Programme. The SGPT is under the authority of Vice-President Olli Rehn and supervised by the President. The SGPT is composed of a Lisbon-based team, a Brussels-based team and a network of correspondents in more than 15 Directorate-Generals of the European Commission.

The main objective of the Commission in setting up the SGPT was to create a flexible and small structure, which could support the overall implementation of the Programme for Portugal (for instance by identifying major bottlenecks and providing solutions to overcome difficulties, advising the Portuguese authorities on policies and legislation to strengthen growth and competitiveness or co-ordinating the internal work of the Commission services in a number of areas mentioned in the Memorandum of Understanding), help PT authorities in terms of absorption of current European Structural Funds and in the preparation of the next programming period. The SGTP has been instrumental in easing cooperation processes between Portugal and the Commission services. Furthermore, the SGPT is directly assisting on capacity building in the Ministry of Finance, particularly in the area of short term forecasting and modelling including the economic and budgetary impact of the Adjustment Programme.

The SGPT provides technical assistance in crucial areas of the Programme. Support is provided in areas such as public finance management (regional and local budgetary frameworks, tax administration), transports (ports and railway sector), energy, agriculture, internal market, judicial reform and education. The technical assistance actions include the financing of experts/consultants to directly assist Portugal authorities in the designated areas. Other sorts of interventions are the organisation of study visits and seminars, as well as the direct advice and short-term missions from Commission experts on a number of domains.

In addition, a number of conferences and workshops have been organised. For instance, the SGPT assisted the Portuguese authorities in a workshop on 'Structural change in the context of the Adjustment Programme', held in Lisbon in January 2012. The SGPT also supported a workshop on 'Judicial Reform' organised by the European Commission in Lisbon in April 2012.

Looking forward, the SGPT will continue to support the implementation of the Adjustment Programme, through an efficient liaison between the Portuguese authorities and the Commission services, especially DG ECFIN but also with all relevant Commission services, in order to ensure a smooth and timely implementation of the Programme.

The creation by the European Commission of the SGPT represents therefore a strong gesture of helping and easing the implementation of the Adjustment Programme in Portugal, aimed at pooling resources and building confidence to restore growth, competitiveness, jobs and social stability in the country.

55. Important progress has been observed in the area of activation and active labour market policy (ALMP). The authorities are on track in implementing a plan to reform the Public Employment Services (PES) and improving ALMPs. Participation in ALMPs has increased by 19.5 percent in the year, covering about 400,000 people. Considerable effort is being made on the activation of subsidised unemployed. About half of the recipients of unemployment benefits have been redirected to training measures. Here, the programme *Vida Activa*, which aims at developing high-employability training modules, is playing an important role. The programme *Impulso Jovem*, an initiative to tackle youth unemployment, is in an implementation phase. Since February, about 9,000 people were employed under the wage subsidy scheme *Estímulo 2012*.

56. The dual training system is being strengthened. The government has the intention of raising dual training positions from 30,000 in 2012 to 100,000 in 2020, following the increase by 9,000 between 2011 and 2012. This system targets employees younger than 25yearswith lower secondary education. 40 percent of the training is on-the-job, for which the government tries to recruit attractive firms and make the system more demand-driven.

Education

57. The implementation of the action plans on secondary school is overall progressing as scheduled. A tool for country-wide monitoring of educational results by school has been prepared. It includes an automatic monthly report for management purposes with data on public schools and private schools with contracts. In order to assess their performance, the results of every school will be compared with an 'expected value' developed on the basis of several socio-economic data of the school. It will be a valuable instrument to adapt educational policies to the actual needs of every school, including cost saving measures. A formula to monitor the cost per student in every school has not yet been provided. A Working Group is still working on the methodology but results are expected before the end of this year. The full assessment of the new inspection model is also expected by the end of this year. The number of proposals to conclude trust agreements with selected primary and

secondary schools is already over 40. These agreements, which are concluded between the government and the schools, provide significant autonomy to the schools in terms of pedagogical, curricular and organisational powers under certain performance criteria. It is expected that more than 80 trust agreement will have been signed by the beginning of the next school year 2013/2014.

58. The implementation of the action plan on vocational training has further advanced. The government has adapted the provision of educational training by focusing on exporting sectors. In addition to the programme of internships co-financed by the Structural Funds (Passaporte Emprego) presented at the Fifth Review, a reinforcement of the dual training system is under preparation (see above). The Government is also finalising the legal framework for the set-up of the professional schools of reference, with direct training offers into economic areas considered relevant to job creation, which will be fully operational by September 2013.

Housing market

59. The government has adopted the complementary legislation of the law on housing rental market. The new law entered into force on 12 November. Before that, the new regime for the determination of the gross annual income of the household (rendimento annual bruto corrigido do agregado familiar), which is an important element for the update of rents in open-ended contracts signed before 1990, was approved by the Council of Ministers. The legal text setting the Single Window for the rental market (Balcão do Arrendamento), which will be the competent body for the extra-judicial eviction procedure enshrined in the Law, was also adopted as well as the legal text setting the rules to determine the state of conservation of dwellings for the purposes of the rental market and renovation. However, as the publication of these legal texts is still pending, it may delay the actual implementation of the law. The revision of the cadastral value of the housing stock is expected to be completed by the first quarter of 2013.

Judicial system

60. Reforms of the judicial system continue to advance according to the agreed schedule. Progress has been made in the reduction of backlogged court cases, the reform of the judicial system, including the geographical reorganisation of the court districts, and the reform of the Code of Civil Procedure.

- Despite the challenges in addressing the backlog court cases, an additional 17 000 enforcement cases have been cleared, bringing down the total number by about 113 000 enforcement cases since November 2011. A decree law has been adopted with a set of urgent measures designed to combat the court case backlog. The inter-agency task forces have set quarterly targets for reviewing enforcement cases to be closed by mid-February 2013. To this end, the authorities have further stepped up their efforts by expanding the task forces to small claims court cases in specific courts.
- Tighter control and supervision of the enforcement agents by the Commission for the Efficiency of Enforcement Procedures (CPEE) resulted in an increase in disciplinary proceedings this year. In addition, a legislative proposal has been prepared to replace the CPEE as a supervisory body with a fully independent and better staffed organisation.
- Further advances have been made to improve the efficiency of the court system. A comprehensive judicial roadmap to reduce the number of courts, streamline the court structure and improve the management of courts has been submitted to parliament.
- The government has submitted to the parliament in accordance with the agreed timetable a proposal for an ambitious reform of the Code of Civil Procedure, including a number of measures to speed up judicial procedures. The proposal followed an extensive consultation with stakeholders and experts, including expert meetings held at the end of July with the IMF and EC technical assistance.

Business environment

61. The authorities envisage financing alternatives for corporations that aim at stimulating a more equity-oriented culture in the corporate sector. The draft budget 2013 foresees a legislative authorisation for the government to limit the tax deductibility of corporate interest costs to companies up to specific ceilings. Given that the envisaged ceilings are relatively high (financial costs up to EUR 3 million or 30 percent of EBITDA), the measure would only cover large companies, leaving smaller companies, notably SMEs, with no incentives to move to more stable and less risky financing structures privileging equity. The Ministry of Economy, in liaison with CGD, set up a state guaranteed quasi-equity financing line of EUR 500 million targeting SMEs. The financing instrument is expected to be up and running before end-2012. No progress was

recorded in the setting up of three EUR 30-million equity funds due by end-2012 to capitalise SMEs stemming from the conditionality of the public recapitalisation of banks. *Portugal Ventures*, the EUR 600-million assets private equity and venture capital management company created in June from the merger of three public entities has launched the *Ignition Programme*, a seed capital facility which will invest in scientific and technology-based projects. Portugal Ventures has EUR 140 million available to pursue its investment policy. The renewal of the existing guarantee line PME Crescimento to EUR 2 billion more is pending budget approval. Around EUR 2.3 billion of the current EUR 2.5 billion have already been executed. Guidelines on how to better ensure the credit flow from this line to exporting companies are under discussion. Specific measures funded by the Structural Funds such as QREN Investe or incentives to SMEs are already operational. The key challenge is the promotion of investment opportunities relying on private sector initiative while minimising fiscal risks.

62. The application to accelerate the request of VAT exemptions for exporting firms will be in place at beginning of next year. This application will allow exporters to provide full on-line proof of their operations. It will reduce the time required to provide all the necessary information from an average of more than 42 days to just 4 days so that the refund of VAT will happen much faster. Strong commitment and fast progress is necessary to ensure the timely implementation of the Late Payments Directive by March 2013. This is an important factor to alleviate the financing conditions of SMEs. Negotiations with municipalities to include all of them within the scope of the Simplex Programme are progressing as scheduled.

Sustainability of national electricity system

63. Electricity tariff debt elimination to ensure the sustainability of the system is on-going. Concerning wind power capacity, an agreement with about 98 percent of the capacity producers was reached. Draft legislation was shared with the mission setting the terms for the compensation after the existing feed-in tariffs For small-hydro power plants, negotiations are on-going. Final draft legislation for changing the CMEC annuity discount rate in line with EC/ECB/IMF comments should be approved still this year. This will be done in way that does not lead to an increase in the new established rate and ensures savings in Net Present Value (NPV) terms of EUR 120 million. Negotiations concerning the Sines and Pego power plants are still on-going, with uncertain outcomes. Estimates of the total cost reduction are in the range of EUR 1.3 to 1.4 billion in NPV terms, but the exact results depend on the success of ongoing negotiations with various stakeholders. As there is a need for a comprehensive assessment of the reform once all outstanding measures have been implemented the revised MoU updated some deadlines for the next review. The government presented elements of the preliminary report on the CMEC scheme and on the process for the extension of the concession of the public hydro resource to the former PPA hydro power plants.

64. A crucial step is still missing for the efficient functioning of the electricity and gas markets after their full liberalisation in January 2013. New draft legislation on the energy regulator (ERSE) bylaws including additional changes to the ones agreed in July is expected to be adopted soon. The law on the penalty system of ERSE has been in discussion at the Parliament's specific committee since 28 September. The law on the penalty system of ERSE has been generally approved in the Parliament on 28 September and is expected to be discussed in the specific committee on 5 December.

Telecommunications and postal service

65. A significant step has been taken in the telecommunication market.. The tender procedures for the designation of the universal service provider have been launched. According to the calendar of the tender process, the award of the service to one or more operator(s) is expected by Q2-2013; this has been reflected in the change of the MoU deadline. Concerning the negotiations with the incumbent operator and current universal services provider, the government reached an agreement on the terms for termination of the current contract. The amended framework for the provision of universal service for postal services has not been adopted yet.

Transport

66. The government reiterated its commitment to complete the reform of Portuguese maritime ports. The draft law on port work is expected to be adopted by the Parliament by the end of the year. The government is preparing a Decree Law on port operation. The draft shall be ready by the end of the year, too. Its goal is to increase efficiency of Portuguese ports by making the port operation concessions more performance-oriented, opening up the activity to new operators and ensuring that cost savings are passed on to port customers. A significant part of cost reductions in ports (around 25 to 30 percent compared to the present situation) are expected to come from the reform of concessions. The mentioned Decree Law will also set principles for a better

coordinated ports policy in the country. Finally, a reduction of 20 percent in tariffs levied by the port authorities (TUP Carga) has been approved. The overall port tariff framework will be reviewed to further rationalise the costs incurred by the Portuguese ports users.

67. Portuguese authorities presented further progress in reforming land and air transport. A Decree Law which sets the legal basis for the new transport regulator has been adopted. It merges the three former regulators (rail, ports and road) into a single one and sets a clear division between administrative and regulatory powers. The principles of functioning of this new regulatory entity for the transport sector will also depend on the Framework Law on National Regulators Authorities. Meanwhile, a number of low-cost airlines have been attracted to Portugal. Some additional low-cost flights have been recently attracted by Lisbon, though its airport is close to its maximum capacity. Montijo, a military airport, is considered the best alternative, though whether it will be developed will depend on the new owner of the airport operator ANA. The report on the transfer of CP Carga terminals to another entity was presented; it demonstrates that only two terminals (Lisbon-Bobadela and Leixões-Porto) have enough activity to make them viable for privatization. These two terminals account for more than 80 percent of the total cargo. The public service obligation contracts for the fluvial transport in Lisbon have been signed while those regarding urban transport services in Lisbon and Porto are expected to be concluded by the end of the year. The conditions for a Public Service Obligation of rail passenger transport (CP) and REFER are still under discussion.

Other services sectors

68. Progress on the adoption of legislative amendments to align legislation with the principles of the Services Directive has continued albeit at a modest pace. One third of the sector-specific amendments that are necessary to fully implement the Services Directive are still pending although work on half of them is advanced. A clear roadmap has been submitted and the government will adopt or, when relevant, present to parliament all remaining draft amendments required by Q4-2012. These amendments are needed to reduce barriers to entry and to facilitate the operation of businesses in 68 legal regimes of varying economic significance. The law proposal simplifying the regulatory framework for real estate activities has been discussed in the specific parliamentary committee since 28 September. Concerning the regulatory framework governing construction activity, the final draft laws on construction and reserves of activity have been sent for consultation to the Portuguese Committee on the Regulation of Professions (CRAP). This additional step before its validation by the Council of Ministers has delayed the legislative roadmap. In parallel, a report was recently submitted by the authorities on the functioning of the public institute governing construction activities (InCI, I.P.) and the fees it charges to businesses for granting various authorisations and certificates, which still needs to be assessed and justified in light of the real costs of the procedure. Minor amendments to the urban planning rules and procedures (RJUE), which are needed to complement this reform, will be discussed in the working group currently reviewing this legal regime under MoU measure 7.18.

69. Work on professional services is on-going. The law proposal on the deregulation of three professions and the horizontal legal framework on professional services governed by professional associations were approved in parliament. To complete the reform on highly regulated professions, one month following the publication of the horizontal law, professional associations shall have to present proposals for the amendment of their statutes and internal rules to bring them in conformity with the principles laid down in the law by removing requirements on the exercise of the profession that are not justified or proportionate. This is a decisive step in liberalising the exercise and activity of highly regulated professions. As regards deregulation of professions, a second phase of the review of regulated professions will be initiated by the government beginning of 2013, following analysis from the CRAP. This second phase shall seek to identify and ease requirements currently laid down to access the profession that may no longer be justified or proportionate.

70. Main legislative pieces have been adopted, which will improve the recognition framework of professional qualifications. The government has adopted two Executive orders (Portarias[9]) that identify competent authorities (such as for sports activities) and which complement amendments to the Law 9/2009[10] alongside with an Executive Order (Portaria 325/2012 of 16 October) with a simplified form for services provider's declaration. An exhaustive list of those professions that require prior checks of qualification to avoid

[9] Portaria 367/2012 of 6 November and Portaria 228/2012 of 3 August, *Official Gazette*
[10] Lei 41/2012, of 28 August, Diário da República, 1.ª série — N.º 166 —

risks of public health is being revised and will be published to increase transparency of the regulatory framework. In addition, information for professionals of their rights will be added to the Point of Single Contact.

71. Further improvements on the Point of Single Contact (PSC) are needed to enhance visibility of all simplification efforts to reduce the administrative burden for entrepreneurs and attract investment. A roadmap and work programme has been presented and will be updated on a monthly basis, which shows that efforts have been stepped up in this field. However, since September, all public institutes have to fulfil a specific procedure for recruitment and the authority responsible for administrative simplification (AMA) in charge of the PSC is still waiting for a strengthening of its resources. There is a risk that a lack of human resources could prevent AMA from keeping up the pace needed for this reform. However, priorities by the government have been clarified, showing political commitment, and this should ensure continuing progress on this measure and on the Zero licensing programme.

Competition and sectoral regulators

72. The government accomplished the sale of the 1 percent share of CGD in Galp. The Portuguese government has thus ended the long-lasting situation of maintaining special rights by the State in private sector companies.

73. A text of the draft Framework Law, which is meant to set the main principles of the functioning of the main National Regulator Authorities (NRA), was discussed with the Portuguese authorities. Some progress has been made compared to the first draft put forward in the Fifth Review. Further revisions will need to ensure that the law effectively guarantees the independence and autonomy of regulators and complies with provisions in existing EU law on these matter. The NRAs covered by this Framework Law have been consulted by the authorities. Further discussions will take place in subsequent reviews before submission to the Parliament by March 2013.

Licensing

74. In parallel with the implementation of the Services Directive, a significant number of legal initiatives to reduce excessive licensing procedures and other administrative burden are expected by the end of the year. Their overall objective is to significantly reduce the number of administrative and regulatory obstacles and the time required to obtain authorisations in order to facilitate the development of economic activities, especially in the case of SMEs. In the area of environment and territorial planning the forthcoming legal provisions include the revision of the Base Law of Soil and Territorial and Urbanism Planning, the legal regime of the Territorial Management Instruments, the requirements for the Environmental Impact Evaluation and the harmonisation of the Territorial Planning Regional Plans. The legal Regime for Urbanism and Building (RJUE) will be revised at the beginning of next year. Regarding industrial licensing, a set of ordinances will soon be adopted to make the Point of Single Contact (*Balcão do Emprendedor*) fully operational. The authorities are also proceeding to the revision of the legal regime of mining and ecological production. On tourism, a set of legal provisions will be adopted by the Council of Ministers by the end of the year. The overall approach is to transfer more management powers to the lower levels of government and to move from the current system of 'ex-ante' authorisations by the public administration to a new 'ex-post' control, in which the private operator bears more responsibility. In addition, an inter-ministerial group will be set up to carry out a full inventory and an analysis of the costs of all regulations in the economy at central, regional and local levels. This should be the basis for a possible roadmap for further regulatory simplification. The Government is also assessing the feasibility of fast-tracking applications for the licensing of planned investment projects which are left unresolved or undecided for more than 12 months and of setting a rule that prohibits at all levels of government the creation of a new regulation generating costs for businesses without the elimination of an existing regulation or regulations with an equivalent cost.

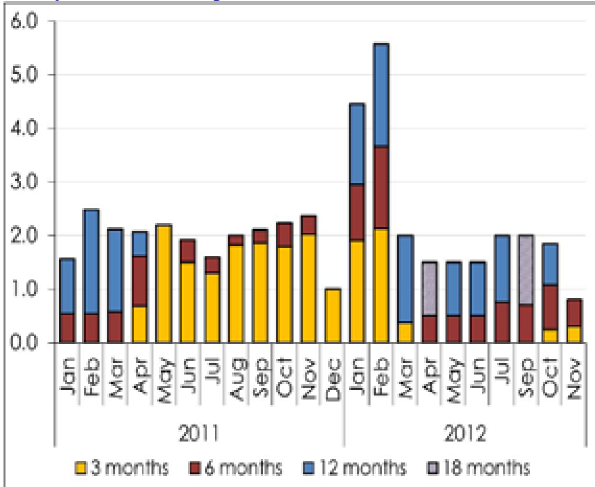
IV. PROGRAMME FINANCING

75. The Treasury enjoys strong demand for short-term debt. The Treasury regularly auctions three, six, twelve and eighteen month bills. The yields on short-term debt have significantly fallen compared with 2011. For some maturities, the Treasury could even raise funds at lower yields than other non-programme European sovereigns despite below-investment grade rating. The Treasury also started using more intensely other short-term debt instruments, such as CEDIC, where public companies can invest spare funds for a short period of time.

76. As part of the government's strategy to re-enter markets, the Treasury conducted a debt exchange operation. The Treasury successfully exchanged EUR 3.75 billion of bonds maturing in September 2013 (of a total of EUR 9.6 billion) into a bond maturing in October 2015 at a yield of 5.12 percent. The September 2013 bond is the first bond that Portugal needs to roll over without official help according to the funding plan of the Programme. As a result of this exchange, the Treasury will have to roll over only EUR 5.8 billion of bonds in 2013.

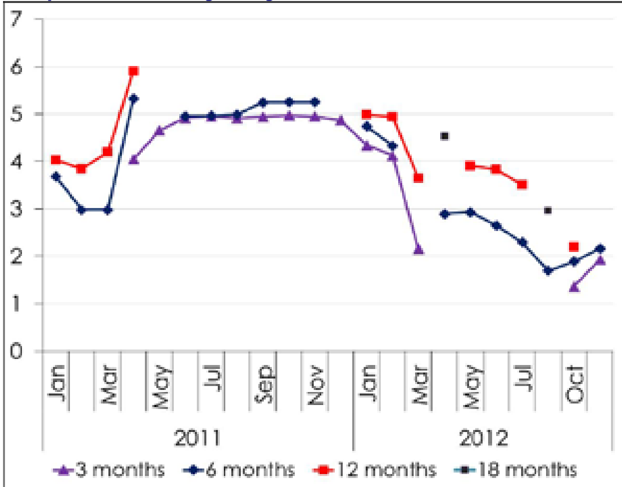
77. The Treasury actively seeks ways to broaden the investor base. The Treasury aims to revitalise relationships with retail investors. To that end, the Treasury increased interest rates on Saving Certificates, an investment product that enjoyed some popularity among domestic investors in the past, and intends to offer new products in 2013. The Treasury is also testing appetite for sovereign bonds by foregin investors. In autumn, the Portuguese authorities conducted several roadshows for investors in Europe and the US, which seemed to signal growing appetite for medium and long-term bonds. As the Treasury abstained from a new bond issuance, several investors acquired Portuguese bonds in the secondary market from domestic banks. Below-investment grade rating remains a serious hurdle to attract real money investors, though appetite from this class of investors is also increasing. The authorities will continue communication with investors and plan to visit several European countries still this year and Japan as well as the US at the beginning of the next year.

Graph 10. Treasury bill auctions



Source: Reuters

Graph 11. Treasury bill yields at auctions



Source: Reuters

Box 4: Euro Area and IMF Loans: Amounts, Terms and Conditions

The programme designed in spring 2011 foresaw a disbursement of EUR 78 billion to cover the financing needs of the Portuguese sovereign until mid-2014. According to the 2011 plan, the three lenders – European Financial Stabilisation Mechanism (EFSM), European Financial Stability Facility (EFSF), and the IMF – had to disburse EUR 26 billion each. For technical reasons and following political decisions these amounts have changed since the inception of the programme.

The IMF share for Portugal, equivalent to EUR 26 billion at the programme set-up, was expressed in SDR. In EUR terms, the IMF loan amount fluctuates subject to the SDR/EUR exchange rate. Since the start of the Programme, the SDR has appreciated versus the euro and, as a result, some of disbursements from the Fund were larger in EUR terms than originally envisaged. This may also apply for future IMF disbursements to Portugal, should the higher SDR exchange rate persist. According to the SDR/EUR exchange rate assumptions implied by the IMF's World Economic Outlook, the gross IMF disbursements to Portugal would equal EUR 27.8 billion, out of which 6.5 billion remain to be disbursed.

As regards the loans provided by the EFSF, lending modalities have been revised in line with changes to the Framework Agreement and the credit enhancement structure of EFSF. In the beginning of the programme, a loan specific cash buffer was deducted up-front and retained as credit enhancement by the EFSF. This was to compensate for the fact that at that time the over-guarantee percentage for the sovereign guarantees of EFSF bonds was limited to 120%. In the summer of 2011, this limit was increased to "up to 165%". Consequently, it was no longer necessary to deduct a loan-specific cash buffer for further disbursements to Portugal. Furthermore, in May 2012, following the signature of the Master Financial Assistance Facility Agreement the margin related to credit enhancement and the cash buffer were set to zero. The remaining amount to disburse is EUR 8.6 billion for a total Net Disbursement Amount of EUR 26 billion, as initially envisaged. Portugal's debt to the EFSF will amount to EUR 28.4 billion but Portugal will have to repay only EUR 27.5 billion (all costs included), due to the pre-payment of the loan specific cash buffer. This amount will be further reduced to approximately EUR 26.3 billion after taking into account the rebate mechanism agreed by the Eurogroup Working Group and the EFSF to compensate Portugal for a significant portion of the higher margin on the initial EFSF lending.

The EFSM loans to Portugal remain unchanged and will amount to EUR 26 billion. The EFSM charges no fees on its loans and passes on the interest rate at which it borrows to Portugal. Therefore the difference between the gross disbursements and net disbursements is minimal, originating from the difference between the issuance price (below par) and the nominal value of the corresponding bonds in the market as well as the need to cover the maintenance of the EMTN programme and the fees charged by the banks and rating agencies.

Loans received until Dec-2012

	Nominal value (EUR millions)	Net disbursed amount (EUR millions)	Nominal weighted average interest rate	"All in" costs [1]	Average maturity (years)
EFSM	22.1	22.0	2.9%	3.0%	12.4
EFSF [2]	18.7	17.4	3.1%	3.2%	14.4
IMF [3]	21.3	21.3	2.7%	4.7%	7.3
Total	62.1	60.7	2.8%	3.7%	11.2

[1] *IRR estimate, including all costs (interest, exchange rate and fees)*

[2] *The interest rate of EFSF loans obtained since May 2012 is variable and indexed to the EFSF funding pool.The IRR estimate takes into account the provisional EFSF funding program and interest rate forwards. On October 30, 2012 this rate stood at 2.0%.*

[3] *The base interest rate of IMF loans (in SDR) is refixed on a weekly basis (based on a basket composed by the Eurepo 3m, US Tbills, UK Tbills and JP Tbills rates) and available in: http://www.imf.org/external/np/fin/data/sdr_ir.aspx. In the week starting on October 22, 2012, the base rate stood at 0.08%. The cost of funding includes a remuneration rate of 100 basis points and a margin between 200 and 300 basis points, depending on the amount of funding and how long funding remains above a certain threshold (300 percent of country's IMF quota; outstanding for three years). The IRR for the entire period of the loan was estimated based on forward interest and exchange rates, applied to a tentative calendar of future payments.*

Sources: IGCP, IMF, Commission Services estimate.

The terms of all the official loans to Portugal are very favourable. In terms of maturity, the IMF loans have 7.3 years average maturity, i.e. the repayment period for an Extended Fund Facility is between 4.5–10 years (longer than for other IMF arrangements). The disbursed EFSF loans to Portugal have an average maturity of 14.4 years (the EFSF loans to Portugal can have a maximum average maturity of 15 years). The disbursed EFSM loans have an average maturity of 12.4 years, close to the established EFSM average lending maturity of up to 12.5 years.

The interest rates charged by all the official lenders differ but are very favourable in all cases. The IMF interest rate is a variable interest rate based on the SDR rate plus a remuneration spread and the margin, with the latter depending on the amount borrowed (relative to country's IMF quota) and the length of the outstanding loan. The IMF also applies service charges and fees according to its standard rules. The "all in" interest rate reported in the table below for the IMF is calculated by the IGCP, the Portugues public debt agency, and takes into account surcharges, expected changes in future interest and exchange rates. The IMF lends to Portugal in SDRs and the additional interest costs indicated in the table do not accrue to the IMF in full.

The interest rate charged on euro area loans depends on the rate at which the EFSF and the EFSM borrow in the markets. This rate is passed on to the beneficiary country. In addition, the EFSF charges fees, to cover its operational costs and to comply with the constitutional requirements of some guarantors. The EFSM charges no loan-specific fees, in other words the EFSM lending rate corresponds to the EFSM borrowing rate on financial markets. Hence, for both EFSF and EFSM, Portugal benefits almost fully from the high credit rating of the facilities and hence low interest rates.

78. The Treasury engaged in a more extensive use of internal resources. A large-scale cash centralisation is ongoing, bringing cash of several public entities under the single umbrella of IGCP, the national debt management agency. The Treasury aims at achieving several goals with this strategy, ranging from better control over the public entities' spending to economies of scale in cash reserve management.

79. Portugal's risk perception has improved substantially in early autumn on the back of the impressive external adjustment of the Portuguese economy and the ECB's announcement of outright market transactions. A more positive attitude was reflected in falling bond yields, declining CDS levels and their convergence in the 5- and 10-year segment, signaling that investors consider Portugal's long-term outlook more stable than before. The ECB's decisions as regards Outrigth Monetary Transactions (OMTs), while still being under discussion with respect of their applicability to Portugal, played an important role in improving market sentiment.

Graph 12. Government bond yields (percent)

Source: Bloomberg

Graph 13. Credit default swaps (basis points difference)

Source: Bloomberg

80. The successful completion of the Sixth Review will trigger the release of EUR 2.5 billion, out of which EUR 1.6 billion will come from the EU and about EUR 0.9 billion from the IMF.

ANNEXES

ANNEX 1: ASSESSMENT OF COMPLIANCE: MONITORING TABLE

	Actions for the sixth review (to be completed by end Q3-2012)	*Status*
Fiscal-structural	**[3.1]** Publish a comprehensive report on fiscal risks as part of the budget	**Observed.**
	[3.2] Publish a tax expenditure report as part of the budget.	**Partly observed.** An estimation of tax expenditures was prepared for the budget, yet additional efforts are still needed to develop and apply a clear methodology to evaluate tax expenditures.
	[3.3] Prepare a document assessing reform progress and specifying areas of action over the next three years in the area of public financial management, including the reduction of budget fragmentation.	**Observed.** The strategy was published as an annex to the 2013 Budget.
	[3.5] IGF will carry out inspections to verify compliance with the commitment control law and ensure a continued reduction of the stock of arrears in line with the strategy for the settlement of arrears.	**Observed.**
	[3.6] IGF will reinforce the verification of local government's arrears claims and commitment control systems. Disbursements under the PAEL will take place where IGF has certified the commitment control systems.	**Observed.** Disbursements under PAEL have not yet started.
	[3.11] Prepare a draft proposal to revise the regional finance law and the local finance law.	**Observed.** Although some elements of the laws are still under discussion, the end-year target for submission to Parliament remains valid.
	[3.12] Create a working group to prepare a proposal for common revenue forecasting guidelines for subnational governments.	**Delayed.** Available resources concentrated in the preparation of the local finance law in detriment of this measure. Given the importance of developing a common forecasting methodology, the measure has been delayed to the next local budget cycle in 2013.
	[3.13] Proceed with identifying data needs to support the revenue projections.	**Broadly observed.** An article that specifies the data to be transmitted from the central administration to the local authorities has been inserted in the draft local finance law.
	[3.14] Follow up of the Government's economic adjustment programme with the Autonomous Region of Madeira.	**Observed.** A progress report was discussed during the sixth review.
	[3.17] Enhance annual PPP and concessions report to provide information and analysis at sectoral level together with credit flows channelled through banks.	**Observed.**
	[3.18] Inform on progress towards achieving the operational balance target by the end of the year.	**Observed.**
	[3.19] Advance draft law on SOEs governance.	**Observed.** A draft law was submitted to Parliament.
	[3.20] Enhance the annual and quarterly SOEs report to include	**Observed.**

	information on operational results, debt, restructuring and governance at central and local level.	
	[3.23] Assess progress on an inventory of assets, including real estate, owned by municipalities and regional government, examining scope for privatisation.	**Ongoing.** The deadline for concluding the inventory is the end of the year. However, no progress was reported during the review, indicating a risk of a delay.
	[3.30] Present a final report on PREMAC.	**Observed.**
	[3.31] Based on the cost/benefit analysis decide to maintain, reduce or extinguish foundations.	**Observed.** The 2013 Budget contains special provisions regarding the amounts of transfers to foundations, where some savings are already expected. Further efforts at regional and local level are still possible.
	[3.33] Reorganise and reduce the number of the municipalities and parishes.	**On-going.** The proposals are currently being assessed in Parliament and a final decision will be taken before the end of the year.
Financial sector	**[2.3]** Ensure that the programme target CT1 of 10% is reached.	**Observed.**
	[2.12] Launch the competitive bidding process aimed at selecting a professional third party mandated to gradually recover the credits currently held by Parvalorem by end-October 2012 at latest, with a view to complete the process by end-March 2013.	**Not observed.** The procurement contract has been shared with the Troika. H owever there is some delay with starting the bidding process, which should be launched shortly.
	[2.13] The authorities were asked to conclude the implementing measures pertaining to the early intervention and resolution framework; in particular: adopt supervisory notices on recovery plans by end-October 2012 and adopt rules applicable to setting-up and operation of bridge banks in line with EU competitions rules by end-October 2012.	**Observed.** The supervisory notices on recovery plans and the rules governing the setting-up and operation of bridge banks have been published on 17 and 18 October.
Health sector	**[3.42]** Accelerate the plans to achieve a self-sustainable model for health-benefits schemes for civil servants.	**On-going:** the employer's contribution rates for ADSE or budget transfers in the case of specific ministries were not changed in the 2013 budget. However, according to 2013 budget provisions, the public health systems of the various ministries will move the provision of a set of services to the NHS together with the equivalent amount of financial resources. In 2013 authorities will re-evaluate the package of services covered by these systems and reduce the contribution rate to 1.25.
	[3.60] Implement the strategy to clear arrears and avoid their re-emergence.	**On-going:** the stock of arrears has been significantly reduced through the debt settlement strategy. EUR 1.5 bn have been paid and further payments may occur (including an additional 432 million payment through a second supplementary budget). In that case the stock of remaining arrears

		will be about EUR 400 million in 2013, to be paid through savings generated within the sector. The law on commitments is being implemented.
Labour market	**[4.3]** Draft legislation submitted to Parliament to align the level of severance payments to the EU average and consider the implementation of a compensation fund for severance payments.	**Delayed.** Draft legislation to be delivered by mid-December following the agreement between the Government and EC/ECB/IMF.
	[4.5 iii] Submit to Parliament a draft legislative proposal containing criteria and modalities for the extension of collective agreements.	**Observed:** The Council of Ministers Resolution 90/2012, in force since 1 November, limits extensions of collective agreements to those subscribed by employers' associations that employ more than 50 percent of workers in a sector. In addition, the request for extension must be asked by both unions and employers' associations. The quantitative criterion is waived when the request for extension concerns only firms that employ more than 249 workers.
	[4.8 i] Set up an operational management tool for schools.	**Observed:** A monitoring tool which will enable to monitor the educational results by school throughout the country has been presented. The authorities will continue to improve the tool in order to have it fully operational by Q2-2012.
	[4.8 ii] Implement the legislation to promote trust agreements with public schools, define and implement a simple formula-based funding framework and and present an assessment of the new inspection model.	**Partially observed:** Legislation has been published and the Government is taking action to conclude trust agreements with schools. While some preliminary information was provided, the funding formula and the assessment of the new inspection model have not been presented yet.
	[4.8 iii] Present a progress report on the involvement of businesses in the provisions of traineeships.	**Observed:** In addition to the programme of internships co-financed by the Structural Funds (*Passaporte Emprego*), plans for a reinforcement of the dual training system are ongoing. Their success crucially depends on further involvement of business in offering training possibilities.
Goods and services markets	**[5.1]** Adopt the the law on penalty system and new regulators' bylaws agreed in July 2012.	**Not observed.** Draft legislation on ERSE bylaws and the penalty system of ERSE have not been adopted yet.
	[5.2 i] Present proposals to harmonise the access tariffs to the interconnection networks.	**Delayed.** The awaited reform of the Spanish network tariffs is one of the necessary prerequisites.
	[5.4] Conclude the measures to reduce excessive rents and to address the sustainability of the national electricity system.	**On-going.** The government has not concluded all measures as some negotiations are still on going. Concerning wind power capacity, an agreement with about 98% of the capacity producers was reached. Draft legislations for CMECs and renewable energy are being finalized.
	[5.5] Conclude the measures to limit the policy costs embedded in CMECs and PPAs.	**On-going.** Draft legislation for changing the CMEC annuity discount rate was shared on 15-11. Negotiations concerning the Sines and Pego power plants are still on-going. Its outcome is very uncertain.
	[5.6] Present a report on the CMEC scheme.	**Delayed.** The report has been sent on 16 November, but not yet discussed.

	[5.7] Conclude the measures to limit the policy costs of renewables under the special regime.	**On-going.** Following agreement with the industry, draft legislation was shared with EC/ECB/IMF setting the terms for the compensation for wind producers, after the existing feed-in tariffs. For small-hydro, negotiations are on-going.
	[5.9] Annual report on revising downward the feed-in tariffs and ensuring that the tariffs do not over-compensate renewable producers.	**Observed.** Report submitted
	[5.10] Annual report containing an analysis in terms of costs and consequences for energy prices of future investments in renewables.	**Observed.** Report submitted
	[5.11] Renegotiate the telecommunication concession contract by reducing the scope of the services covered so as to exclude the universal service and launch a new tender to designate the universal service provider(s).	**On-going.** The tender has been launched (Executive Order 318/2012 published on 12th October and tender notices in Portuguese and EU official Journal) and an agreement in principle was reached on the terms for termination of the concession contract with the current universal service provider.
	[5.13] Further liberalise the postal sector by amending the decree-law and renegotiate the amendment with CTT.	**Delayed.** The draft provisions are close to completion.
	[5.16 iv] Ensure that the new railway Public Service Obligation (PSO) contracts concluded on rail passenger transport respect EU legislation including Regulation (EC) N° 1370/2007 and provide a detailed breakdown of state contributions for each line under PSO.	**Delayed:** The conditions of the PSOs contract for rail passenger transport (CP) are still under discussion.
	[5.17] Submit to Parliament a revised legal framework on port work	**Observed:** The draft law was submitted, though it has not yet been adopted by the Parliament.
	[5.20] Submit to Parliament of the remaining necessary amendment to the sector specific legislation to fully implement the Services Directive.	**On-going.** Internal work within the government on the preparation of the twenty reforms pending has been progressing and around half of them were shared and are being discussed with EC/ECB/IMF.
	[5.21] Approval by Parliament of the amendments in the areas of real estate.	**On-going.** The draft law is being discussed at specific committee in Parliament since 28 September. However, Parliament discussions of the 2013 state budget allowed little progress in this dossier.
	[5.21] Submit to Parliament amendments in the area of construction services.	**Delayed.** The final draft laws on construction and reserve of activity have been sent for consultation to the Portuguese Committee on the Regulation of Professions. This additional step towards its validation by the Council of Ministers was not foreseen and has delayed the legislative roadmap.
	[5.22] Improve the recognition of professional qualifications in particular through adoption of the executive order (portaria) on the services provider prior declaration following the adoption of amendment of Law 9/2009.	**Observed.** Executive Order 325/2012 published on 16 October in Official Gazette with a standard form for services provider prior declarations and Executive Order 367/2012 on sports regulated professions. A list of all those professions that require health and safety prior checks of qualifications (pursuant to Article 7.4 Professional Qualification Directive) will be made public via PSC and other websites.

	[5.23] Approval by Parliament of the law for professions where regulation does not involve a professional body.	**Observed.** The draft law was approved in Parliament on 29 November.
	[5.24] Approval by Parliament of the draft horizontal legal framework concerning the requirements affecting the exercise of regulated professions with professional bodies.	**Observed.** The draft law was approved in Parliament on 23 November.
	[5.25 i and ii] Extend on-line procedures in Point of Single Contact (PSC) to all sectors under the Services Directive and for each profession. Constantly adapt PSC to incorporate new legislation in order to reduce administrative burdens for firms.	**On-going.** Lack of sufficient human resources were mentioned as a reason for delays but the Agency for Modernization (AMA) has stepped-up its work with 28 online procedures under construction and some information content was updated and published online on the PSC.
	[5.26] Submit an updated detailed work programme of AMA.	**Observed.** A detailed work programme was submitted on 1 and 29 October, and presented on 15 November.
Competition, public procurement, and business environment	**[7.8]** Ensure that CGD alienates its participation in Galp.	**Observed.** The sale of 1 per cent share of CGD in Galp was completed on 27 November 2012.
	[7.11] Following up on the adoption of the executive order (portaria) concerning the transfers of payments from regulators to the Competition Authority and the report prepared under measure 7.12 (i), the financing model of the latter will be re-examined resulting in a technical proposal by **[Q1-2013] to** be implemented by [**Q2-2013**].	**On-going.** A new Executive Order (Portaria 383/2012, November 23) was enacted ensuring and further clarifying the financial model applicable during 2012 and 2013. Transfers from all NRAs are yet to be confirmed. The current financial model will remain as foreseen in the Competition Authority's by-laws.
	[7.11] Review with key stakeholders the conditions for the proper execution of the Competition Authority mandate	**On-going:** progress has been made but not all conditions are yet confirmed
	[7.15] Present an action plan with measures to facilitate access to finance and export markets for companies, in particular SMEs. Make operational the procedures for requesting VAT exemptions for exporting firms.	**Observed:** A set of possible measures to facilitate access to finance to SME has been presented.
	[7.2] Set quarterly targets for closing enforcement cases and prepare quarterly reports on implementation status, with the fourth report to be completed by mid-November 2012.	**Observed.**
Judicial system	**[7.4]** Refine by extensive consultation an initial draft bill on judicial reform.	**Observed.**
	[7.4] Submit a Bill to implement the judicial reform roadmap to Parliament by end-November 2012.	**Observed.** The bill was approved at the Council of Ministers of November 22 and submitted to Parliament by November 30.
	[7.5] Submit the Bill to improve the Justices for Peace regime to Parliament by end-November 2012.	**Observed.** The bill was approved at the Council of Ministers of November 22 and submitted to Parliament by November 30.
	[7.6] Refine by extensive consultation an initial draft of the new Code of Civil Procedure. Submit to Parliament the new Code of Civil Procedure by	**Observed.** The bill was approved at the Council of Ministers of November 22 and submitted to Parliament by November 30.

	end-November 2012.	
	[7.7] Publish quarterly reports on recovery rates, duration and costs of corporate insolvency cases starting from **[Q3-2011]**, within four months after the end of the relevant quarter.	**Observed.** The statistics for Q2-2012 were published on October 31

ANNEX 2: COMMISSION SERVICES MACROECONOMIC PROJECTIONS 2011-2016

Table 1: Use and supply of goods and services (volume)

Annual % change	2011	2012	2013	2014	2015	2016
1. Private consumption expenditure	-4.0	-5.7	-2.2	0.4	1.2	1.3
2. Government consumption expenditure	-3.8	-3.5	-3.2	-2.0	0.9	0.6
3. Gross fixed capital formation	-11.3	-13.7	-5.5	3.0	4.3	3.8
4. Final domestic demand	**-5.3**	**-6.7**	**-2.9**	**0.3**	**1.7**	**1.6**
5. Change in inventories	--	--	--	--	--	--
6. Domestic demand	**-5.6**	**-6.6**	**-3.0**	**0.3**	**1.6**	**1.6**
7. Exports of goods and services	7.5	4.6	2.9	5.0	5.5	5.5
7a. - of which goods	7.8	5.9	3.3	5.2	5.6	5.6
7b. - of which services	6.8	1.0	1.7	4.4	5.1	5.0
8. Final demand	**-2.7**	**-3.8**	**-1.3**	**1.7**	**2.8**	**2.8**
9. Imports of goods and services	-5.2	-5.9	-2.1	3.8	5.5	5.2
9a. - of which goods	-6.7	-6.4	-2.0	3.7	5.6	5.3
9b. - of which services	3.1	-2.8	-2.8	4.3	4.7	4.7
10. Gross domestic product at market prices	**-1.7**	**-3.0**	**-1.0**	**0.8**	**1.8**	**1.8**
Contribution to change in GDP						
11. Final domestic demand	-5.7	-7.0	-2.9	0.3	1.6	1.6
12. Change in inventories + net acq. of valuables	-0.4	0.1	0.0	0.0	0.0	0.0
13. External balance of goods and services	4.3	3.9	1.9	0.6	0.2	0.3

Table 2: Use and supply of goods and services (value)

Annual % change	2011	2012	2013	2014	2015	2016
1. Private consumption expenditure	-0.5	-3.5	-1.4	1.7	2.5	2.9
2. Government consumption expenditure	-8.1	-10.4	-0.8	-4.0	2.0	1.7
3. Gross fixed capital formation	-9.4	-11.5	-4.7	4.9	5.5	5.3
4. Final domestic demand	**-3.7**	**-6.2**	**-1.8**	**1.2**	**2.9**	**3.1**
5. Change in inventories	--	--	--	--	--	--
6. Domestic demand	**-4.1**	**-6.2**	**-1.9**	**1.1**	**2.9**	**3.1**
7. Exports of goods and services	13.3	6.4	4.2	6.6	7.0	7.0
8. Final demand	**-0.2**	**-3.0**	**-0.2**	**2.7**	**4.2**	**4.3**
9. Imports of goods and services	1.9	-3.9	-1.3	4.7	6.6	6.8
10. Gross national income at market prices	-1.4	-2.7	0.2	1.6	3.4	3.4
11. Gross value added at basic prices	-1.2	-3.6	-0.1	1.8	3.1	3.3
12. Gross domestic product at market prices	**-1.0**	**-2.7**	**0.3**	**2.0**	**3.2**	**3.3**

Table 3: Implicit price deflators

% change in implicit price deflator	2011	2012	2013	2014	2015	2016
1. Private consumption expenditure	3.6	2.3	0.8	1.3	1.3	1.5
2. Government consumption expenditure	-4.4	-7.2	2.5	-2.0	1.1	1.1
3. Gross fixed capital formation	2.2	2.6	0.8	1.8	1.2	1.4
4. Domestic demand	**1.6**	**0.5**	**1.1**	**0.8**	**1.3**	**1.5**
5. Exports of goods and services	5.4	1.7	1.3	1.5	1.5	1.5
6. Final demand	**2.5**	**0.8**	**1.2**	**1.0**	**1.3**	**1.5**
7. Imports of goods and services	7.5	2.1	0.8	0.8	1.1	1.5
8. Gross domestic product at market prices	**0.7**	**0.3**	**1.3**	**1.1**	**1.4**	**1.4**
HICP	**3.6**	**2.8**	**0.8**	**1.2**	**1.3**	**1.5**

Table 4: Labour market and cost

Annual % change	2011	2012	2013	2014	2015	2016
1. Labour productivity (real GDP per employee)	-0.1	1.0	0.6	0.3	1.2	1.4
2. Compensation of employees per head	-0.8	-2.9	1.5	0.5	0.8	0.8
3. Unit labour costs	**-0.7**	**-3.9**	**1.0**	**0.1**	**-0.4**	**-0.6**
4. Total population	0.1	0.0	0.0	0.0	0.0	0.0
5. Population of working age (15-64 years)	-1.3	-1.0	-0.5	0.0	0.5	0.5
6. Total employment (fulltime equivalent)	-1.5	-3.9	-1.6	0.5	0.6	0.4
7. Calculated unemployment rate - Eurostat definition (%)	**12.9**	**15.5**	**16.4**	**15.9**	**15.3**	**14.9**

Table 5: External balance

levels, EUR bn	2011	2012	2013	2014	2015	2016
1. Exports of goods (fob)	44.7	48.3	50.6	54.0	58.0	62.2
2. Imports of goods (fob)	57.0	54.6	54.0	56.5	60.4	64.6
3. Trade balance (goods, fob/fob) (1-2)	**-12.3**	**-6.3**	**-3.4**	**-2.5**	**-2.4**	**-2.4**
3a. p.m. (3) as % of GDP	***-7.2***	***-3.8***	***-2.0***	***-1.4***	***-1.4***	***-1.3***
4. Exports of services	16.0	16.3	16.7	17.7	18.8	19.9
5. Imports of services	10.2	10.0	9.8	10.2	10.8	11.4
6. Services balance (4-5)	**5.8**	**6.3**	**7.0**	**7.4**	**8.0**	**8.5**
6a. p.m. 6 as % of GDP	***3.4***	***3.8***	***4.2***	***4.4***	***4.5***	***4.7***
7. External balance of goods & services (3+6)	**-6.5**	**0.0**	**3.5**	**5.0**	**5.6**	**6.1**
7a. p.m. 7 as % of GDP	***-3.8***	***0.0***	***2.1***	***2.9***	***3.2***	***3.4***
8. Balance of primary incomes and current transfers	-4.8	-4.5	-4.5	-5.3	-5.3	-5.3
8a. - of which, balance of primary income	*-6.3*	*-6.3*	*-6.5*	*-7.2*	*-7.1*	*-7.1*
8b. - of which, net current Transfers	*1.5*	*1.8*	*1.9*	*1.9*	*1.8*	*1.8*
8c. p.m. 8 as % of GDP	*-2.8*	*-2.7*	*-2.7*	*-3.1*	*-3.0*	*-2.9*
9. Current external balance (7+8)	**-11.3**	**-4.5**	**-1.0**	**-0.4**	**0.3**	**0.8**
9a. p.m. 9 as % of GDP	***-6.6***	***-2.7***	***-0.6***	***-0.2***	***0.1***	***0.4***
10. Net capital transactions	2.6	2.7	2.8	3.0	3.1	3.3
11. Net lending (+)/ net borrowing (-) (9+10)	**-8.7**	**-1.8**	**1.8**	**2.6**	**3.4**	**4.1**
11a. p.m. 11 as % of GDP	***-5.1***	***-1.1***	***1.1***	***1.5***	***1.9***	***2.2***

Table 6: Fiscal accounts

	2011	2012	2013	2014	2015	2016
		% of GDP				
Indirect taxes	13.7	13.9	13.7	13.7	13.8	13.9
Direct taxes	9.9	9.3	11.3	11.2	11.3	11.3
Social contributions	12.2	11.7	12.0	12.0	11.8	11.7
Sales and other current revenue	4.7	4.4	4.7	4.7	4.7	4.5
Total current revenue	**40.5**	**39.3**	**41.7**	**41.7**	**41.5**	**41.3**
Capital transfers received	4.4	1.3	0.6	0.9	0.9	0.9
Total revenue	**45.0**	**40.6**	**42.3**	**42.5**	**42.4**	**42.1**
Compensation of employees	11.4	10.0	10.3	9.7	9.5	9.3
Intermediate consumption	4.7	4.7	4.5	4.1	4.0	3.9
Social transfers in kind via market producers	4.7	4.3	4.3	4.0	3.9	3.9
Social transfers other than in kind	17.3	17.9	18.3	18.0	17.8	17.7
Interest paid	4.0	4.2	4.4	4.6	4.7	4.6
Subsidies	0.7	0.8	0.7	0.5	0.5	0.6
Other current expenditure	2.6	1.9	2.2	2.0	2.0	2.0
Total current expenditure	**45.4**	**43.7**	**44.7**	**42.9**	**42.3**	**42.0**
Gross fixed capital formation	2.6	2.0	1.8	1.7	1.6	1.5
Other capital expenditure	1.4	-0.2	0.3	0.4	0.4	0.4
Total expenditure	**49.4**	**45.6**	**46.9**	**45.0**	**44.4**	**43.9**
General Government balance (EDP)	**-4.4**	**-5.0**	**-4.5**	**-2.5**	**-2.0**	**-1.8**
		% change				
Indirect taxes	1.0	-1.5	-0.6	1.8	3.9	3.7
Direct taxes	11.7	-8.4	20.8	1.5	3.6	3.4
Social contributions	-1.0	-7.4	3.2	2.2	1.5	2.1
Sales and other current revenue	8.4	-8.0	7.0	1.9	1.8	-1.2
Total current revenue	**3.6**	**-5.7**	**6.5**	**1.8**	**2.9**	**2.6**
Capital transfers received	63.2	-71.7	-50.0	36.1	2.8	2.7
Total revenue	**7.5**	**-12.2**	**4.7**	**2.4**	**2.9**	**2.6**
Compensation of employees	-7.9	-14.2	3.5	-4.8	1.0	1.1
Intermediate consumption	-8.3	-3.3	-3.5	-6.1	1.0	-0.1
Social transfers in kind via market producers	-5.8	-11.1	0.4	-4.1	1.0	3.2
Social transfers other than in kind	1.0	0.4	2.5	0.0	2.5	2.5
Interest paid	37.7	2.6	3.3	8.0	4.0	3.1
Subsidies	0.5	10.6	-8.7	-29.9	-2.4	26.7
Other current expenditure	-10.1	-29.7	19.3	-8.0	2.2	2.5
Total current expenditure	**-1.5**	**-6.2**	**2.5**	**-2.2**	**1.9**	**2.4**
Gross fixed capital formation	-28.8	-23.3	-10.0	-5.0	-4.5	-3.0
Other capital expenditure	-31.9	-114.3	-265.0	34.7	1.8	2.8
Total expenditure	**-4.7**	**-10.2**	**3.1**	**-2.0**	**1.7**	**2.2**
Nominal GDP, EUR bn	170.9	166.3	166.8	170.0	175.5	181.2

Table 7: Government debt developments

	2011	2012	2013	2014	2015	2016
EDP deficit (% of GDP)	**-4.4**	**-5.0**	**-4.5**	**-2.5**	**-2.0**	**-1.8**
EDP gross debt (% of GDP)	108.1	120.0	122.2	122.3	120.0	117.2
	levels, EUR bn					
EDP deficit	**-7.5**	**-8.3**	**-7.5**	**-4.3**	**-3.5**	**-3.2**
Gross debt	184.7	199.7	203.8	207.9	210.6	212.4
Change in gross debt	23.2	15.0	4.1	4.2	2.7	1.8
Nominal GDP	170.9	166.3	166.8	170.0	175.5	181.2
Real GDP	164.8	169.7	171.4	170.0	167.0	164.0
Real GDP growth (% change)	**-1.7**	**-3.0**	**-1.0**	**0.8**	**1.8**	**1.8**
Change in gross debt (% of GDP)	13.6	9.0	2.5	2.4	1.5	1.0
Stock-flow adjustments (% of GDP)	9.2	4.0	-2.1	-0.1	-0.4	-0.8
	% of GDP					
Gross debt ratio	**108.1**	**120.0**	**122.2**	**122.3**	**120.0**	**117.2**
Change in gross debt ratio	14.5	12.0	2.1	0.1	-2.2	-2.8
	Contribution to change in gross debt					
Primary balance	0.4	0.8	0.2	-2.1	-2.7	-2.9
"Snow-ball" effect	4.9	7.1	4.0	2.2	0.8	0.8
of which						
Interest expenditure	*4.0*	*4.2*	*4.4*	*4.6*	*4.7*	*4.6*
Real growth effect	*1.6*	*3.2*	*1.2*	*-1.0*	*-2.1*	*-2.2*
Inflation effect	*-0.7*	*-0.4*	*-1.6*	*-1.3*	*-1.7*	*-1.7*
Stock-flow adjustments	**9.2**	**4.0**	**-2.1**	**-0.1**	**-0.4**	**-0.8**
Implicit interest rate	*4.2*	*3.8*	*3.6*	*3.9*	*3.9*	*4.0*

ANNEX 3: INDICATIVE FINANCING NEEDS AND SOURCES

Table 8. Financing needs and sources (EUR billion)

	2011 Jun-Dec	2012 Year	2013 Year	2014 Year	2011-2014 Total
Public sector deficit	**11.3**	**15.8**	**13.0**	**4.8**	**44.9**
Treasury balance [1]	7.1	8.6	6.9	4.3	26.9
Other public sector cash needs [2]	4.2	7.2	6.0	0.5	18.0
Amortization	**9.5**	**26.6**	**5.9**	**14.6**	**56.6**
Medium- and long-term debt (incl debt exchange)	4.9	16.6	5.8	14.1	41.5
Other debt [3]	4.6	10.0	0.1	0.5	15.2
Banking support, net [4]	**1.0**	**7.4**	**2.0**	**0.4**	**10.8**
Financing needs	**21.8**	**49.8**	**20.9**	**19.8**	**112.3**
Market financing	**-6.4**	**9.6**	**5.2**	**14.1**	**22.5**
Medium- and long-term debt	0.0	4.9	0.0	14.1	19.0
T-Bills, net	-6.4	4.7	5.2	0.0	3.5
Own resources [5]	**-5.7**	**12.8**	**5.6**	**-2.4**	**10.3**
EU-IMF loan	**34.0**	**27.4**	**10.1**	**8.1**	**79.5**
EFSM/EFSF	21.0	19.2	6.5	5.3	52.0
IMF [6]	13.0	8.2	3.6	2.9	27.6
Financing sources	**21.8**	**49.8**	**20.9**	**19.8**	**112.3**

SOURCE: Portuguese authorities and Commission services' estimates.

1/ Calendar-year cash basis.

2/ Includes loans to state-owned enterprises and credit concessions to general government entities, contributions to the ESM, the economic adjustment programme for Madeira and repayment of arrears.

3/ Retail, repos, ECP, flows in cash collateral accounts and debt of other government entities managed by IGCP;T-Bills not included.

4/ From 2012 includes actual banking sector needs, including use of BSSF funds and loans for capitalization of Resolution Fund; for 2011 reflects payments to BSSF.

5/ Includes privatisation receipts, use of deposits, pension fund, Social Security and CGA assets.

6/ Numbers do not add up to EUR 26 bn due to changes in EUR-SDR rate compared to beginning of programme.

Table 9: Planned quarterly disbursements (EUR billion)

Review	Period covered by disbursement	Approximate disbursement period	Loan disbursements[1]	of which IMF [2] (⅓)	of which EU (⅔)
Approval	Jun-Sept 2011	Jun 2011	**18.5**	6.1	12.4
1	Q4-2011	Sept 2011	**11.6**	4.0	7.6
2	Q1-2012	Dec 2011	**8.1**	2.8	5.3
3	Q2-2012	April 2012	**14.9**	5.2	9.7
4	Q3-2012	July 2012	**4.0**	1.4	2.6
5	Q4-2012	October 2012	**4.3**	1.5	2.8
6	Q1-2013	January 2013	**2.5**	0.9	1.6
7	Q2-2013	April 2013	**2.0**	0.7	1.3
8	Q3-2013	July 2013	**2.8**	1.0	1.8
9	Q4-2013	October 2013	**2.9**	1.0	1.9
10	Q1-2014	January 2014	**2.8**	1.0	1.8
11	Q2-2014	April 2014	**2.6**	0.9	1.7
12	Q3-2014	July 2014	**2.7**	1.0	1.8
	TOTAL		**79.5**	27.5	52.0

ANNEX 4: PROVISION OF DATA (REPORTING REQUIREMENTS)

During the Programme, the following indicators and reports shall be shared with the European Commission, the ECB and the IMF by the authorities on the agreed periodic basis. Data for past periods should also be included in subsequent transmissions in case of revision. Other indicators may also be requested to and reported by the Portuguese Authorities.

	To be provided by the Ministry of Finance (or INE)	
1.	Data on cash balances of the State Budget. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published by the Ministry of Finance (MoF). Data on tax revenue should be decomposed in gross tax revenue received and tax reimbursements paid by the State (detailed per main individual taxes)	Monthly, 3 weeks after the end of the month
2.	Data on the cash balances of the other parts of General Government (Autonomous Funds and Services, Social Security and Other entities, including Incorporated State-owned enterprises (ISOEs) or extra-budgetary funds (EBF) not part of the State Budget, but which are, under the European System of Accounts (ESA95) and ESA95 Manual on Government Deficit and Debt rules, classified by the National Statistical Institute (INE) as part of the Central Government; [Regional and Local Governments (*Administrações Regionais and Locais*); Regional and local government-owned enterprises or companies, foundations, cooperatives, and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government, as defined in paragraph 4 of the TMoU) – progressively enlarged	Monthly, as soon as the data are available and no later than 7 weeks after the end of the month
3.	Accrual data on budget execution of the National Health System (NHS)	Monthly, 3 weeks after the end of each month
4.	Consolidated cash data on the General Government budget execution initially comprising the Central Government and Social Security and enlarging progressively the scope as in indicated in the TMoU, MoU and MEFP	Monthly, 7 weeks after the end of each month
5.	Publish information on: number of general government staff on a quarterly basis (no later than 45 days after the end of the quarter); stock and flows over the relevant period per Ministry or employment entity (i.e. new hiring, retirement flows, special mobility condition flows, and exit to other government service, private sector or unemployment); average wage, allowances and bonuses. The regional and local administration will transmit the necessary information. Information on employment in SOEs (central, local and regional) and other public entities and/or bodies will also be compiled	Quarterly, no later than 30 days after the end of the quarter (as of March 2012)
6.	Consolidated account on an accrual basis of the non-financial SOEs that are classified within the Central Government	Quarterly, 90 days after the end of the quarter (as of March 2012)
7.	Data on the past and projected financing needs of SOEs, including for the major SOEs details on the financing needs for the operational balance, capital expenditure, interest payments and debt principal repayments	Monthly, 4 weeks after the end of the month
8.	Data on arrears of: · the General Government, detailed by subsector · the incorporated (SOEs) government-owned hospitals that are not part of the General Government · other non-financial SOEs that are not part of the General Government	Monthly, 7 weeks after the end of each month (as of September 2011)

9.	Information on Public-Private Partnerships (PPP) related revenue and expenditure, for those PPP reclassified within the General Government (in line with paragraph 5.2 of the TMoU)	Monthly, 30 days after the end of the each month
10.	New guarantees granted by the State to SOEs, PPPs, banks and the non-financial private sector	Monthly, 30 days after the end of each month
11.	Detailed information on called guarantees of the State	Monthly, 30 days after the end of each month
12.	Data on proceeds from asset sales by the Central, Regional and Local Government	Monthly for Central Government Quarterly for Regional and Local Government 30 days after the end of reference period
13.	Quarterly data on General Government accounts as per the relevant EU regulations on statistics, showing also the main items of the transition from cash balances to the General Government balances in national accounts	Quarterly, 90 days after the end of each quarter
	To be provided by ESAME	
14.	Report on progress with fulfilment of economic policy conditionality on a quarterly basis. In addition, a short summary report should be sent on a monthly basis	Quarterly (report), two weeks after the end of each quarter. Monthly (short summary report) two weeks after the end of each month for which a report is not due.
	To be provided by the Debt Management Office	
15.	Accrual data on interest spending of the State	Quarterly, 7 weeks after the end of the quarter
	To be provided by the Ministry of Labour	
16.	Data on labour market as follows: a. layoffs by type b. collective agreements by type and number of collective agreements that are extended by the Ministry of Labour to non-signatory firms c. number of collective agreements that regulate the use of the Bank of Hours working time arrangement d. proportion of unemployed receiving unemployment benefits e. distribution of the unemployed in terms of amount of benefits received (mean of benefits received, median, number of unemployed receiving an unemployment benefit amount equal to the IAS and number of unemployed receiving the maximum amount of unemployment benefits allowed) f. unemployment duration	Every six months, 6 weeks after the end of each semester
	To be provided by Ministry of Justice	
17.	Publishing quarterly reports on recovery rates, duration and costs of corporate insolvency cases	Quarterly, starting in 2011 Q3, within four months after the end of each quarter.

ANNEX 5: PROGRAMME DOCUMENTS

PORTUGAL: LETTER OF INTENT

Lisbon, 20 December 2012

Mr Jean-Claude Juncker
President
Eurogroup

Mr Vassos Shiarly
Minister of Finance
Cyprus

Mr Olli Rehn
Vice President
European Commission

Mr Mario Draghi
President
European Central Bank

Dear Sirs,

The attached Memorandum of Understanding (MoU) describes the progress made in recent months towards the objectives laid out in our Programme. It also updates previous MoUs and highlights the policy steps to be taken in the months ahead.

We remain strongly committed to the programme's policies and objectives and expect the agreed 5 percent deficit target for 2012 to be achieved. The 2013 budget was approved by the Parliament, including a range of tax and spending measures that should ensure that the general government deficit of 4½ percent of GDP will be achieved next year. To advance with the additional fiscal adjustment that is required in coming years, we have initiated a comprehensive public expenditure review exercise to be completed early in 2013.

Consistent with our commitment to implement a multi-year strategic plan to strengthen fiscal discipline, we are intensifying our efforts to prevent the increase in the stock of existing domestic arrears. We are reforming the SOE sector, which has been brought to overall operational balance, as per our commitment, after many years of chronic deficits. We will continue this restructuring effort and actively manage their high legacy debt burden. Moreover, the privatisation is proceeding as scheduled and we are advancing our strategy to put the PPPs on a sustainable financial path.

Our policy efforts to preserve financial stability will continue, as banks are on track to meet the 2012 capital requirements, following the recent capital exercise. Banco de Portugal (BdP) continues on its supervisory effort to ensure adequate impairment levels, as evidenced by the successful completion of the latest on-site inspection. In addition, the recapitalisation and resolution framework will be further strengthened. The Portuguese authorities are preparing a proposal for the setting-up of a mechanism to securitise high-quality mortgage credit with a supranational guarantee. Moreover, we are exploring a new proposal to rationalise and redirect to the most productive segments of the economy existing government initiatives, including the setting up of a revolving mechanism to leverage EU structural funds. Finally, we will also continue consultations with the European Commission on the rate of remuneration of financial instruments used for recapitalisation purposes. In pursuing this route, we are motivated by concerns on local funding and lending conditions.

We have made important advances in many dimensions of our ambitious structural reform agenda, and will continue to press ahead with measures to improve the business environment and help spur investment. Measures to actively promote employment and improve education are being expanded. With the completion of the reduction of severance payments, to be soon submitted to the Parliament, we will have reduced the rigidity of labour contracts substantially. A landmark revision of the Ports Work Law in discussion in the Parliament will

increase efficiencies and help reduce costs for exporters. Going forward, we will continue to pursue a streamlined and more effective licensing and regulatory framework along with a reform in corporate taxation, as part of our strategy to attract more investment and boost competitiveness.

On the basis of the strength of the policies defined in this letter, and in light of our performance under the Programme, we request the completion of the sixth review under the Economic Adjustment Programme and the release of the seventh instalment under the Programme in the amount of EUR 1 600 million.

We remain confident that the policies described in the current and previous MoUs are adequate to achieve the objectives under the Programme. We stand ready to take additional measures should they be needed to meet the objectives of the Economic Adjustment Programme and will consult with the European Commission, the ECB and the IMF in advance of any necessary revisions to the policies contained in this letter and attached Memorandum.

This letter is copied to Ms Christine Lagarde.

Sincerely yours,

/s/	/s/
Vítor Gaspar Minister of State and Finance	Carlos da Silva Costa Governor of the Banco de Portugal

Attachments: Memorandum of Understanding (MoU); Memorandum of Economic and Financial Policies (MEFP); Technical Memorandum of Understanding (TMU)

PORTUGAL: MEMORANDUM OF UNDERSTANDING ON SPECIFIC ECONOMIC POLICY CONDITIONALITY

Sixth Update – 20 December 2012

With regard to Council Regulation (EU) n° 407/2010 of 11 May 2010 establishing a European Financial Stabilisation Mechanism (EFSM), and in particular Article 3(5) thereof, the sixth update of the Memorandum of Understanding on specific economic policy conditionality (MoU) details the general economic policy conditions as embedded in Council Implementing Decision 2011/344/EU of 17 May 2011 on granting Union financial assistance to Portugal.[1]

The first disbursement of financial assistance from the EFSM took place following the entry into force of the MoU and of the Loan Agreement.

The Council Implementing Decision specifies that the release of further instalments is conditional on a positive conclusion of the reviews of conditionality that will take place throughout the three-year duration of the programme. These reviews will assess progress made with respect to the policy criteria in the Council Implementing Decision and specified in the Memorandum of Economic and Financial Policies (MEFP) and in this updated MoU, as well as Council Recommendations in the context of the Excessive Deficit Procedure.

The sixth quarterly review was carried out in November 2012. It assessed compliance with the conditions to be met by end-October and the need and scope for additional policy steps. This sixth update of the MoU reflects the findings of the sixth review. The following reviews taking place in any given quarter will assess compliance with the conditions to be met by the end of the previous quarter or, where applicable, up to date of the mission.

If targets are missed or expected to be missed, additional action will be taken. The authorities commit to consult with the European Commission (EC), the European Central Bank (ECB) and the International Monetary Fund (IMF) on the adoption of policies falling within the scope of this updated Memorandum, allowing sufficient time for review. Staff of the EC, the ECB and the IMF will, in cooperation with the Portuguese authorities, monitor and assess progress in the implementation of the programme and track the economic and financial situation. Staff will also monitor whether the implementation and effects of measures taken by the Portuguese authorities fall short of the commitments of previous versions of the MoU; such commitments might be re-inserted. To this effect the authorities commit to provide all required information as soon as available. In areas where there are risks of significant delays in the implementation of policies under this programme the authorities in cooperation with the EC, the ECB and the IMF consider making use of technical assistance.

Prior to the release of the instalments, the authorities shall provide a compliance report on the fulfilment of the conditionality.

1. Fiscal policy

Objectives

Reduce the Government deficit to 5% of GDP in 2012, 4½ % of GDP in 2013 and 2½ % of GDP in 2014 by means of high-quality permanent measures and minimising the impact of consolidation on vulnerable groups. The fiscal consolidation over the medium-term up to a balanced budgetary position will be maintained, notably by containing expenditure growth. Growth-friendly tax policy will be pursued through, among others, a comprehensive reform of corporate taxation to promote investment and competitiveness.

[1] On 8 April 2011, Eurogroup and ECOFIN Ministers issued a statement clarifying that financial support of the EU (European Financial Stabilisation Mechanism, EFSM) and the euro-area (European Financial Stability Facility, EFSF) would be provided on the basis of a policy programme supported by strict conditionality and negotiated with the Portuguese authorities, duly involving the main political parties, by the Commission in liaison with the ECB, and the IMF. Further to the EU support from the EFSM, loans from the EFSF will contribute to the financial assistance. The Loan Facility Agreement on the EFSF financing contribution specifies that the disbursements thereunder are subject to the compliance with the conditions of this Memorandum.

Fiscal policy in 2012

1.1. The government will achieve a general government deficit of no more than EUR 8.3 billion (5 percent of GDP) in 2012 on ESA95 basis.[2] **[Q4-2012]**

1.2. Throughout the year, the government will rigorously implement the Budget Law for 2012, as amended by the Supplementary Budget. In addition, the government has adopted measures to confine the deficit to 5% of GDP in 2012 by freezing budget appropriations for investment projects not yet initiated, generating savings in intermediate consumption and raising stamp duties on high value properties and withholding tax rates on capital income. Within the year, progress will be assessed against the (cumulative) quarterly ceilings for the consolidated general government cash balance in the MEFP, as defined in the TMU, without prejudice to full-year ESA-95 deficit targets. **[Q4-2012]**

1.3. The authorities will frontload to 2012 some of the 2013 budget measures affecting social benefits to obtain savings worth at least 0.1% of GDP. These include, inter alia, cuts in reimbursements of funeral expenses, transfers in case of death, and dependency supplements.

Fiscal policy in 2013

1.4. The government will achieve a general government deficit target of no more than EUR 7.5 billion (4½ percent of GDP). **[Q4-2013]**

1.5. Throughout the year, the government will rigorously implement the Budget Law for 2013. Progress will be assessed against the (cumulative) quarterly ceilings for the consolidated general government cash balance in the Memorandum of Economic and Financial Policies (MEFP), as defined in the Technical Memorandum of Understanding (TMU), without prejudice to full-year ESA-95 deficit targets. **[Q1, Q2, Q3 and Q4-2013]**

1.6. Permanent consolidation measures of slightly above 3% of GDP have been proposed with the 2013 Budget Law to reach the 4 ½ % of GDP deficit target in 2013. The measures listed below will be detailed and carried out with the 2013 Budget Law **[Q4-2012]**, unless otherwise specified:

Expenditure

1.7. Reduce the public sector wage bill in gross terms by at least EUR 700 million by, among others:

i. decreasing the number of government employees by; (i) limiting staff admissions in order to achieve annual decreases at least of 2 percent (full-time equivalent) in 2013-2014 in the permanent staff of central, regional and local governments; (ii) a 50 percent reduction of fixed-term contracts; (iii) optimizing the allocation of resources as specified below under the section on the Public Administration/Human Resources, mainly as regards the special mobility scheme.

ii. other measures such as reducing over-time payments, enforcing private sector sickness benefit regime in the public sector and reducing compensation during extraordinary leave.

1.8. Savings in the national health service (at least EUR 180 million) by further rationalisation of available resources and pharmaceuticals' policy. Further savings, in particular in hospitals SOEs, are specified below under the section on the health-care system.

1.9. Reduce pension expenditure in a progressive manner by at least EUR 400 million.

1.10. Streamline social benefits expenditure by strengthening control and better targeting social support (at least EUR 450 million).

1.11. Reduce intermediate consumption (at least EUR 375 million) through efficiency gains in the general government administration and the renegotiation of PPP contracts.

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[2] In 2012, operations related to the banking sector support and restructuring strategy under the programme will not be considered for the assessment of compliance with the programme target for the general government deficit.

1.12. Reduction in transfers, among others to foundations and SOEs (at least EUR 120 million)

1.13. Reduce capital expenditure, particularly in SOEs (at least EUR 250 million)

Revenue

1.14. Amend the personal income tax (yielding at least EUR 3 billion) by:

i. reducing the number of tax brackets and increasing the average tax rate in line with European standards, while preserving progressivity of the tax and delinking social benefits from the tax structure;

ii. introducing a surcharge of 3.5 % on the part of taxable income above minimum wage, and a solidarity surcharge of 2.5% on the income of the top tax bracket and of 5% on the income exceeding EUR 250 000;

iii. increasing the tax rate on capital income;

iv. equalizing the tax rates on capital income between residents and non-residents;

v. lowering the basic personal deduction;

vi. reducing deductibility of mortgage interest payments;

vii. curbing some fiscal benefits.

1.15. Increase corporate tax revenues by at least EUR 200 million by:

i. limiting the deductibility of interest costs;

ii. curbing tax benefits;

iii. reducing the threshold for application of the highest tax rate on profits;

iv. amending the method for special prepayment applicable to companies under the regime for taxation of groups of companies.

1.16. Increase other indirect taxes (by at least EUR 685 million), such as:

i. excises by raising taxes on tobacco, alcohol and natural gas;

ii. property taxes by broadening the property taxation base after revaluation, and stamp tax surcharges for high-value properties;

iii. financial transaction tax.

1.17. Maintain the standstill rule for tax expenditures at central, regional or local level, except for the possibility of introducing additional tax benefits aimed at boosting investment.

1.18. Increase social contributions (at least EUR 270 million), by including supplementary payments to public employees and unemployment benefits in the social contributions' calculations.

1.19. Strengthen efforts to fight tax evasion, fraud and informality for various types of taxes inter alia by increasing means available for audits, increasing penalties for the most serious tax crimes and introducing a new VAT invoicing system.

1.20. With a view to addressing risks of budgetary execution in 2013 the authorities will prepare contingency measures worth at least ½ percent of GDP. Most of these will come from a frontloading of the measures of the comprehensive expenditure review and will be further specified at the seventh review. A significant share of these measures will consist in additional reductions in the wage bill and increased efficiency in the functioning of public administration, namely as regards working time organisation. Moreover, budgetary appropriations will be adjusted in case budgetary execution risks materialise.

Fiscal policy in 2014

1.21. The government will achieve a general government deficit of no more than EUR 4.3 billion (2½ percent of GDP) in 2014. **[Q4-2014]**.

1.22. A comprehensive expenditure review has been initiated with the objective to enhance the efficiency and equity of public policy, while generating spending savings of about EUR 4 billion in 2014. In the framework of this review, the identification, quantification and timetable of implementation of measures will be fully specified by mid-February 2013 in time for the **seventh review**. The exercise will aim at reducing redundancies across the public sector functions and entities, and reallocating resources toward growth-friendly spending areas. **[Q1-2013]** The fiscal consolidation plans for 2014-15 will be fully detailed in the 2013 Stability Programme. **[Q2-2013]**

1.23. Within the year, progress will be assessed against the (cumulative) quarterly ceilings for the consolidated general government cash balance in the Memorandum of Economic and Financial Policies (MEFP), as defined in the Technical Memorandum of Understanding (TMU), without prejudice to full-year ESA-95 deficit targets. **[Q1 and Q2-2014]**

2. Financial sector regulation and supervision

Preserve financial sector stability; maintain liquidity and support a balanced and orderly deleveraging in the banking sector; ensure adequate financing and working capital for the productive sectors; strengthen banking regulation and supervision; develop and implement solutions that provide financing alternatives to traditional bank credit for the corporate sector; optimise the process for recovering the assets transferred from BPN to the three state-owned SPVs; streamline state-owned Caixa Geral de Depósitos; complete the bank resolution framework and reinforce the Deposit Guarantee Fund and the Guarantee Fund for Mutual Agricultural Credit Institutions; complete the corporate and household insolvency frameworks and smoothen their implementation.

Maintaining liquidity in the banking sector

2.1. Encourage banks to strengthen their collateral buffers on a sustainable basis and to take full advantage of the broadening of the range of eligible collateral for the purpose of Eurosystem re-financing. The Banco de Portugal (BdP), in close cooperation with the ECB, will continue to monitor closely the liquidity situation of the banking system and stands ready to take the appropriate measures to maintain sufficient system liquidity. **[Ongoing]** A new platform for interbank unsecured lending has been put in place and the BdP is expected to extend it to secured interbank lending by the beginning of next year.

Deleveraging in the banking sector

2.2. The banking system should in the medium run eliminate its funding imbalances. Monitor the banks' implementation of the funding plans aiming at an indicative loan-to-deposit ratio of about 120% in 2014. It is important that the pace and composition of deleveraging should not jeopardise the provision of appropriate credit to finance productive investment and working capital in the private sectors of the economy, not least SMEs. Fiscal adjustment and an attendant reduction in the public sector's financing are crucial for reconciling potentially conflicting objectives. In addition, the BdP will implement the measures taken to discourage evergreening of doubtful loans with a view to facilitating an effective adjustment of bank balance sheets respecting EU state aid rules. In this context, banks are identifying and reporting recently restructured loans due to debtors' financial difficulties and the first report by the BdP is expected by end-November 2012. These steps will be taken without burdening or posing risks to public resources. Banks' funding and capital plans and broader credit developments will continue to be monitored closely. There is room for the necessary deleveraging to take place in an orderly manner and it is crucial that the pace and composition of the deleveraging remain consistent with the macroeconomic framework of the programme. **[Ongoing]**

Capital buffers

2.3. Ensure that the programme target of a Core Tier 1 ratio of 10% by **end-2012** target is reached including through the monitoring of the restructuring plans banks having received public capital support were requested to draw up, aiming at enhancing the banks' resilience.

2.4. BdP is closely monitoring compliance with the capital requirements for all banks, with a view to promptly take appropriate action if needed. **[Ongoing]**

2.5. Remain committed to provide further support to the banking system, if needed. Resources from the Bank Solvency Support Facility (BSSF) are available in line with state aid rules to further support viable banks, subject to strict conditionality. Avoid subsidizing private shareholders and prevent further migration of private liabilities to the public sector balance sheet. In the event new capital needs were to arise, banks are encouraged to seek private solutions. **[Ongoing]**

Caixa Geral de Depósitos (CGD)

2.6. Continue to streamline the state-owned CGD group.

Banking regulation and supervision

2.7. The BdP will continue to strengthen its supervisory organisation, optimise its supervisory processes and develop and implement new supervisory methodologies and tools. The field work of a new onsite inspections program (OIP) launched in May 2012 by the BdP has been completed in the major banking groups. The OIP findings are expected to be reflected in 2012 annual accounts of these institutions. This initiative is part of BdP regular supervisory activities, which are currently focused on assets classes that are more sensitive to existing market conditions.

2.8. In addition, the BdP is stepping up the monitoring of banks, including via ad hoc audits. **[Ongoing]**

2.9. BdP will remain committed to close coordination with home and host country supervisors, both within and outside the EU. **[Ongoing]**

Monitoring of bank solvency

2.10. The BdP will continue to monitor on a **quarterly** basis the banks' potential capital needs with a forward looking approach under stress conditions. In this context, banks will reflect the OIP findings in the implementation of the SIP recommendations on asset quality and stress testing methodologies by **end-December 2012**, with the update of the treatment of collective impairments expected to be finalized at the latest by **end-June 2013**.

Banco Português de Negócios

2.11. Gradually settle CGD's state guaranteed claim on the SPVs in cash, according to the schedule agreed with the EC, ECB and IMF. Any recoveries on the assets held by the three state-owned SPVs will also be used to promptly repay CGD. **[Ongoing]**

2.12. Outsource the management of the credits currently held by Parvalorem to a professional third party, with a mandate to gradually recover the assets over time. Select the party managing the credits through a competitive bidding process, to be launched by **end-2012,** at the latest, and with a view to complete it by mid**-2013**. Include proper incentives to maximise the recoveries and minimise operational costs into the mandate. Ensure timely disposal of the subsidiaries and the assets in the other two state-owned SPVs.

Bank resolution framework

2.13. The early intervention, resolution and deposit guarantee framework has been strengthened. The authorities are asked to conclude the implementing measures, In particular, the following actions will be taken: (a) the approval of a decree-law on the banks' contributions to the resolution fund by **end-2012** and (b) the approval of a

supervisory notice on the resolution plans by the same date, taking into account, to the extent possible in view of the deadline, the EBA recommendations and templates. The implementation of the recovery and resolution plans of the banks will give priority to those of systemic importance.

2.14. The legislator will closely follow the process of adoption of the EU Directive on resolution and revise the national resolution framework as soon as the Directive enters into force. **[Ongoing]**

Bank recapitalisation framework

2.15. The Government will, in consultation with the ECB, and the EC and the IMF staff, submit to Parliament by **[end-January 2013]**[3] amendments to the legal framework governing access to public capital to allow the State, under strict circumstances and in accordance with state aid rules, to exercise control over an institution and to perform mandatory recapitalisations.

Corporate and household debt restructuring framework

2.16. Implement the recently established framework for financial institutions to engage in out-of-court debt restructuring for households, smoothen the application of the framework for restructuring of corporate debt and implement an action plan to raise public awareness of the restructuring tools. **[Ongoing]**

Monitoring of corporate and household indebtedness

2.17. Continue the monitoring of the high indebtedness of the corporate and household sectors through the quarterly reports. **[Ongoing]**

Encouraging the diversification of financing alternatives to the corporate sector

2.18. The Ministry of Finance, the BdP, and other stakeholders, have put forward a set of preliminary proposals to encourage the diversification of financing alternatives to the corporate sector[4]**.**

i. develop and evaluate the different options put forward with a view to set priorities **[Ongoing]** and submit a detailed assessment on the proposal concerning the grouped issuance of corporate debt, in particular of SMEs, to obtain capital markets financing [**end-January**].

ii. consider in this exercise also the measures to facilitate access to finance for SMEs **[Ongoing]** and assess the effectiveness of EU-compatible government-sponsored export credit insurance schemes with a view to take appropriate measures to promote exports **[Q1-2013]**.

3. Fiscal-structural measures

Objectives

Improve the efficiency of the public administration by eliminating redundancies, simplifying procedures and reorganising services; regulate the creation and functioning of all public entities including SOEs, PPPs, foundations, associations; re-focus their activities to core public policy objectives and enhance their cost efficiency and fiscal sustainability; streamline the budgetary process, including by adopting new financing laws at regional and local level; strengthen risk management, accountability, reporting and monitoring of all parts of the general government. Government action will build on the recommendations provided by the IMF/EU technical assistance missions.

[3] Structural benchmark in the Memorandum of Economic and Financial Policies.
[4] Structural benchmark in the Memorandum of Economic and Financial Policies.

Public Financial Management framework

Reporting and Monitoring

3.1. Publish a comprehensive report on fiscal risks **each year as part of the budget**. The report will outline general fiscal risks and specific contingent liabilities to which the general government may be exposed, including those arising from Public-Private Partnerships (PPPs), SOEs and explicit guarantees to the banks. Technical assistance will be provided if necessary.

3.2. Publish a tax expenditure report **each year as part of the budget**. The report will define a clear methodology to estimate and to evaluate tax expenditures, in line with international best practices. The report will cover central, regional and local administrations.

3.3. Reduce the number of Serviços e Fundos Autónomos (SFA) in view of reducing budget fragmentation and improving efficiency in the general government. In particular, this reform will be deepened by reviewing the classification of own revenues to enlarge central government revenues. **[Q3-2013]**

Arrears

3.4. The stock of domestic arrears will be significantly reduced by the end of the programme period. A significant part of the existing arrears was reduced as laid down in the strategy for the settlement of arrears. The Inspeção Geral de Finanças (IGF) will carry out inspections throughout the process to verify compliance of the commitment control system through a risk-based approach. **[Ongoing]**

3.5. IGF will reinforce the verification of local governments' arrears claims and commitment control systems. Disbursements under the "*Programa de Apoio à Economia Local*" (PAEL) will only take place where IGF has certified the full functioning of the commitment control system. Transparency of the use of the credit line will be ensured through the monthly publication of the amounts lent, disbursed, and used to settle arrears and other liabilities by municipality in the framework of the PAEL. **[Ongoing]**

Budgetary framework

3.6. Publish a fiscal strategy document for the general government **annually in April**. The document will be in compliance with the requirements of the Stability and Growth Pact and will specify 4-year medium-term economic and fiscal forecasts and 4-year costs of new policy decisions. Budgets will include a reconciliation of revisions to the 4 year fiscal forecasts attributable to policy decisions and parameter revisions e.g. policy decisions, changes in the macroeconomic environment.

3.7. Review the Budget Framework Law to take account of the reinforced EU fiscal framework and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (fiscal compact). The revised law will also accommodate the developments in the regional and local financing laws. **[Q4-2012]** Conduct a review of the Budget Framework law to enhance budgetary procedures and principles of budgetary management, reinforce accountability, transparency and simplification. **[Q4-2013]**

3.8. Define in detail the characteristics of the medium-term budgetary framework, including medium-term fiscal strategy, decision-making and prioritisation process, carry-over rules, commitment controls, and appropriate contingency reserves and related access rules after modification of the Budget Framework Law. **[April-2013]**

Regional and local budgetary frameworks

3.9. The government will ensure that the measures to implement the new budgetary framework at central government level will also be applied at regional and local level. Adequate structures of monitoring, fiscal reporting, and commitment control will be put into place. **[Ongoing]**

3.10. The budgetary frameworks at local and regional levels will be considerably strengthened, in line with recommendations by the IMF/EC technical assistance mission of July 2011 and the new EU fiscal policy

framework. A draft proposal to revise the regional finance law and the local finance law will be submitted to Parliament by **[Q4-2012]**[5]. They will include the following main elements:

i. fully adapt the local and regional budgetary frameworks to the principles and rules in the revised Budgetary Framework Law, namely in what concerns (i) the inclusion of all relevant public entities in the perimeter of local and regional government; (ii) the multi-annual framework with expenditure, budget balance and indebtedness rules, and programme budgeting; and (iii) the interaction with the function of the Fiscal Council. The revision will also foresee that: (i) the Fiscal Council reviews regional governments own revenue projections and multi-annual fiscal plans (ii) a contingency reserve is included under the overall current expenditure envelope as a buffer against negative revenue surprises or erroneous expenditure planning, and (iii) the revised legal and institutional PPP framework is applied (see below);

ii. strengthen fiscal accountability, in particular by: (i) tighter financial requirements for regional and local SOEs and other regional and local public bodies; (ii) a revision of the regime of transfers between the State and the regions and the local authorities; (iii) strengthening the supervisory power from the State on budgetary execution and (iv) apply tighter debt ceilings combined with the adoption of a multi-tiered monitoring system as suggested by the July 2011 technical assistance mission. This reform should follow international best practices;

iii. limit the scope for lower tax rates in the Autonomous Regions vis-à-vis the rates applied in the mainland and ensure that the resulting additional revenues from increasing the regional rates are used as a priority for fiscal consolidation;

iv. strengthen the auditing and enforcement powers of the central tax administration to exercise control over the whole territory of the Republic of Portugal including currently exempt tax regimes;

v. include requirements for data provision to support the revenue projections, balancing the need to preserve tax secrecy and the elaboration of sound forecasts.

3.11. Create a working group with representatives from the Ministry of Finance, the Autonomous Regions and the local authorities to prepare a proposal for common revenue forecasting guidelines for subnational governments. **[Q2-2013]**

3.12. The Government's financial arrangement with the Autonomous Region of Madeira (RAM), which is in full compliance with the Memorandum of Understanding, will be implemented. The Portuguese Government will monitor progress of implementation by RAM and present the results on a quarterly basis in advance of the reviews of the Memorandum of Understanding **[Ongoing].**

Public Private Partnerships

3.13. Following the strategic plan presented by the government, PPP road contracts will be renegotiated in order to obtain substantial fiscal gains, notably in 2013, while ensuring a sustainable reduction in government liabilities. **[Ongoing]**

3.14. The government will further work towards implementing the PPP framework law and making the new technical unit in the Ministry of Finance fully operational by completing staffing and developing the tools for managing and monitoring all PPPs. No PPP will be launched until the institutional framework measures are fully effective. **[Ongoing]** Regions will be encouraged to design a similar framework for assessing fiscal risks derived from PPP, concessions and other public investments, as well as for monitoring their execution. **[Q4-2012]**

3.15. The annual PPP report will provide a comprehensive assessment of the fiscal risks stemming from PPPs and concessions. The report will provide information and analysis at sectoral level and an analysis of credit

[5] Structural benchmark in the Memorandum of Economic and Financial Policies.

flows channelled to PPPs through banks (loans and securities other than shares) by industry and an impact assessment on credit allocation and crowding out effects. This particular element will be done in liaison with the Banco de Portugal. The report will serve as input to the fiscal risks assessment for the budget. **[Q3-2013]**

State-owned enterprises

3.16. SOEs with commercial activity will reach operational balance from **end of 2012 onwards**. This will be achieved by substantially reducing operational costs and raising revenues. To this end the government is implementing the comprehensive SOEs strategy by reviewing the revenue structure and service provision of SOEs, with numerical targets on cost reductions, including measures to realign wages, reduce employment, and additional measures as appropriate. The government is further assessing options for managing the heavy debt load of SOEs, including Parpública. **[Ongoing]**

3.17. The government submitted to Parliament a draft law to strengthen the governance of SOEs in accordance with international best practices. It reviews the existing shareholder approach, giving the Ministry of Finance a decisive role in financial matters of the enterprises, including monitoring of local SOEs. This will enhance the monitoring powers of the central administration over all SOEs. In addition, the timing and content of financial and operational reporting will be defined. The decisions adopted at central level to improve the efficiency of the enterprises while reducing their financial burden will be implemented at all SOEs, taking into account their specificities. It will include the prohibition for SOEs within the general government to incur new debt with the private sector. No additional SOEs will be created until this law is adopted. **[Ongoing]**

3.18. Equivalent measures on operational results, debt, restructuring and governance will be taken at the local and regional levels, while respecting their administrative autonomy as foreseen in the law. The annual and quarterly SOEs reports will assess progress towards achieving these objectives for central and local SOEs. Each Autonomous Region will provide similar annual reports. These will serve as inputs to the fiscal risks analysis in the budget. **[Ongoing]**

Privatisation

3.19. The government is implementing its privatisation programme under the new framework law for privatisation. The privatisation plan targets front-loaded proceeds of about EUR 5 billion through the end of the programme. The sale of GALP and the small remaining stake in REN on the free market have been delayed until market conditions improve. The privatisation or concession of the cargo handling subsidiary of CP (CP Carga) will be concluded by the **[Q2-2013]**. The tenders for the privatisation of the national air carrier (TAP) and the airport operator Aeroportos de Portugal (ANA) were launched in the third quarter, with a view to final decisions by end-2012 and the financial completion of these transactions in **early 2013**. The privatisation of Correios de Portugal (CTT) will be launched, once changes underway in regulation of this sector have their full impact, in order to complete the sale in 2013. The sale or concession of a television channel and radio station belonging to RTP and concessions for transport operators in Lisbon and Porto upon completion of restructuring of the public transport firms in these cities are being considered. CGD's health insurance will be sold in 2012 and the process to sell its insurance arm (Caixa Seguros) to a final buyer is ongoing. The privatisation programme will be expanded to include additional companies and assets for sale or concession in 2013.

3.20. With a view to introducing private capital and management in the water company Águas de Portugal (AdP), a strategy will be prepared. This strategy will include considerations of the competitive and regulatory environment and organisational consequences. **[Q4-2012]**

3.21. The government is working together with the municipalities and regional governments in order to identify the scope for further privatisation, by preparing an inventory of their assets, including real estate. **[Q4-2012]**

Revenue administration

3.22. The Government will conclude the implementation of the undergone merger of the tax administration, customs administration and the information technology service (DGITA) in a single entity, *Autoridade Tributária e Aduaneira* (AT) by **Q4-2012**.

3.23. The reform of the AT will be deepened in **2013** by targeting a business function-type structure. In particular, the following elements will be implemented:

i. reduce the number of municipal offices by at least 25 per cent in 2013 **[Q4-2013]** and 25 per cent in 2014 **[Q2-2014]**;

ii. increase in the resources devoted to auditing in the tax administration to at least 30 per cent of the total staff, mostly through reallocations of staff within the tax administration and other parts of the public administration. The threshold should be attained by **Q4-2012**;

iii. publish quarterly reports on duration and costs of tax cases starting from **Q4-2013** within four months after the end of the relevant quarter.

3.24. To strengthen control and simplify compliance, exchange of information between the collection units of the Tax Authority and the Social Security administration will be significantly strengthened by means, among others, of a unified monthly tax return covering withholding information **[Q1-2013]** as well as a unified form on Independent Workers' annual revenue **[Q2-2013]**.

3.25. The government will address the bottlenecks in the tax appeal system by progressing with clearing cases worth more than EUR 1 million [**Q4-2012]** with the support of the tax court judges.

3.26. Also as part of the development of a modern tax compliance management framework, a fully-fledged Large Taxpayer Office (LTO) will be operational by **[Q4-2012]**[6].

3.27. With the aim of curving down fraud and evasion, a reform on the VAT invoicing system will enter into force on 1st January 2013. The reform implies mandatory invoicing across all sectors and transactions, a centralized VAT monitoring database, a system to electronically monitor goods in circulation and a tax incentive for final consumers to ask for invoices in hard-to-tax sectors. An evaluation report of the measures will be prepared **[Q2-2013]**.

3.28. The authorities will continue to focus on measures to combat fraud and evasion and strengthen taxpayers' compliance. To this end the authorities will:

i. prepare a report to analyse the current tax compliance situation, including a risk analysis of different economic sectors and categories of taxpayers by **the seventh review**. Following the results of the report, appropriate steps will be taken if necessary to reinforce tax compliance.

ii. continue building capacity in revenue administration by phasing in a more modern approach to managing compliance over a three-years period.

Public administration

Central, regional and local administration

3.29. The government will monitor and promote streamlining of foundations at the local and regional level. **[Ongoing]**

3.30. Review the regulation on the creation and the functioning of associations and observatories. The revised regulation will also facilitate the closure of existing associations and observatories and define the monitoring and reporting mechanisms to be put in place. **[Q2-2013]**

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[6] Structural benchmark in the Memorandum of Economic and Financial Policies.

3.31. Building on the study by the inter-ministerial working group for territorial issues, potential duplications of activities and other inefficiencies between the central administration, local administration and locally-based central administration services will be identified and the existing framework to eliminate the identified inefficiencies reformed. **[Q4-2012]**

Shared services

3.32. Develop the use of shared services in the central administration by fully implementing the ongoing projects and by regularly assessing the scope for further integration:

i. complete the implementation of the strategy of shared services in the area of financial resources (GeRFIP). **[Q1-2013]** GeRFIP will also be implemented in the Autonomous Region of Madeira and in the Autonomous Region of Azores **[Q4-2013]**;

ii. fully implement the strategy of shared services in the area of human resources (GeRHuP) in the Ministry of Finance's entities **[Q4-2012]**, with the exception of the Tax Authority for which this is scheduled for **end-June 2013**. Other Ministries will follow in 2013. The Autonomous Region of Madeira will implement GeRHuP gradually;

iii. rationalise the use of IT resources within the central administration by implementing shared services and reducing the number of IT entities in individual Ministries or other public entities in line with the "Overall Strategic plan to rationalise and reduce costs on ICT in Public Administration". **[Q4-2012]**

3.33. Reduce the number of local branches of line ministries (e.g. tax, social security, justice). The services should be merged in citizens' shops covering a greater geographical area and developing further the e-administration over the duration of the programme. **[Q4-2013]**

Human resources

3.34. Limit staff admissions in public administration to achieve annual decreases in 2012-2014 of at least 2 per cent per year (in full-time equivalents) in the staff of central administration and 2 per cent in local and regional administrations (in full-time equivalents); including a significant reduction of fixed-term contracts. The government will ensure the implementation of this measure at local administration level and will promote the initiatives needed so that each region will present its plan to achieve the same target. **[Ongoing]**

3.35. The government will present a comprehensive review of wage scales in the general government, to identify unwarranted differences in remuneration between the public and the private sector for similar types of qualifications. **[Q4-2012]** The comprehensive study of SOEs will follow in **Q2-2013**.

3.36. Accelerate the convergence of the system of social protection for staff that are in the Regime de Proteção Social Convergente (RPSC) to the rules of Regime Geral de Segurança Social. **[Q4-2013]**

3.37. The Special Mobility scheme will be reviewed aiming at being more oriented to support Public Administration Reform, addressing training and requalification for a better allocation of Human Resources. The existing Special Mobility Law need to be revised: (i) to ease/simplify the procedures for the management of the employees that can be targeted with this tool; (ii) to address the compensation that would be set to decline further over time and its duration; and (iii) to be applied to all sectors of Public Administration, including teachers and health professionals. **[Q2-2013]**

Health care system

Objectives

Improve efficiency and effectiveness in the health care system, inducing a more rational use of services and control of expenditures; generate additional savings in the area of pharmaceuticals to reduce the overall public spending on pharmaceutical to 1.25 percent of GDP **by end 2012** and to about 1 per cent of GDP in 2013; generate additional savings in hospital operating costs and devise a strategy to eliminate arrears.

The government will take the following measures to reform the health system:

Financing

3.38. The revision of NHS moderating fees (*taxas moderadoras*) and improvements in the billing and collection of payments from insurance companies and fees for the treatment of cross-border/foreign patients will result in additional revenues of EUR 150 million in 2012 and an additional 50 million in 2013. **[Q4-2012]**

3.39. In the light of the urgency and size of the savings needed in the health sector to address large arrears and budget limitations, plans to achieve a self-sustainable model for health-benefits schemes for civil servants will be accelerated. The current plan foresees that the overall budgetary cost of existing schemes - ADSE, ADM (Armed Forces) and SAD (Police Services) - will be reduced by 50 per cent of the employers contribution in 2013 through transfer of resources to the NHS in exchange for the provision of services by **Q4-2012**. The employer's contribution rate will be reduced to 1.25% in 2014 and will be accompanied by an adjustment in the scope of health benefits **[Q3-2013]**. The system would become self-financed by 2016.

Pricing and reimbursement of pharmaceuticals

3.40. Enact legislation which automatically reduces the prices of medicines when their patent expires to 50 per cent of their previous price. **[Q4-2012]**

3.41. The government implements an annual revision of prices of medicines and of countries of reference in order to achieve cost savings. Second price revision to be published in **January 2013**.

3.42. The government will monitor monthly pharmaceutical expenditures and ensure that the overall public pharmaceutical expenditure does not exceed the target of 1.25 per cent of GDP in 2012 and 1 per cent of GDP in 2013. **[Ongoing]**

Prescription and monitoring of prescription

3.43. Continue to improve the monitoring and assessment system of doctors' prescription behaviour regarding medicines and diagnostic in terms of volume and value and vis-à-vis prescription guidelines and peers. Feedback continues to be provided to each physician on a regular basis (e.g. quarterly), in particular on prescription of costliest and most used medicines. **[Ongoing]**

3.44. Continue to devise and enforce a system of sanctions and penalties, as a complement to the assessment framework **[Ongoing]**. Assess the possibility of establishing agreements with private sector physicians for the application of prescription rules as applied in the NHS.

3.45. Strictly monitor the implementation of the legislation making it compulsory for physicians at all levels of the system, both public and private, to prescribe by International Non-proprietary Name (INN) to increase the use of generic medicines and the less costly available product. An implementation report will be published by **December 2012**.

3.46. Continue to publish prescription guidelines with reference to medicines and the realisation of complementary diagnostic exams on the basis of international prescription guidelines, audit their implementation and integrate them in the electronic prescription system. A first set of guidelines is introduced in the e-prescription system by **Q2 2013.**

3.47. The government will produce a report assessing the effectiveness of the enacted legislation aimed at removing all effective entry barriers for generic medicines, in particular by reducing administrative/legal hurdles in order to speed up the use and reimbursement of generics. **[Q1-2013]**

3.48. The above measures should aim at gradually and substantially increasing the share of generic medicines to at least 30 per cent of all outpatient prescription (in volume) in 2012. In 2013 the target for NHS reimbursed medicines will be 45% of all outpatient prescription (in volume) and will increase to 60% in 2014.

Centralised purchasing and procurement

3.49. Reinforce the centralised acquisition of vehicles, utilities, external services and other cross functional goods and services by all entities included in the NHS, in order to reduce costs through price volume agreements and fighting waste. A detailed action plan will be published by **November 2012.**

3.50. INFARMED will continue implementing the uniform coding system and a common registry for medical supplies. **[Ongoing]**

3.51. Reduce by an additional 10 percent the overall spending of the NHS with private providers delivering diagnostic and therapeutic services (with particular reference to dialysis and rehabilitation). Regularly evaluate and if necessary revise (at least every two years) the remuneration paid to private providers with the aim of reducing the cost of more mature diagnostic and therapeutic services. **[Q4-2012]**

3.52. Implement the centralised purchasing of medical goods through the recently created Central Purchasing Authority (SPMS), using the uniform coding system for medical supplies and pharmaceuticals. Continue to implement the compulsory use of a formulary in all hospitals to monitor the stock and flows of hospital medicines and medical supplies and monitor compliance with central purchasing. **[Ongoing]**

3.53. Take further measures to increase competition among private providers and between private and public providers in relevant areas of service provision such as dialysis and the pharmacies sector in view of ensuring competition and fair prices in private markets. **[Q4-2013]**

Primary care services

3.54. As part of the reorganisation of health services provision and notably the concentration and specialisation of hospital services and the further development of a cost-effective primary care service, the Government reinforces measures aimed at further reducing unnecessary visits to specialists and emergencies and improving care coordination. **[Ongoing]** This will be done through:

i. increasing the number of USF (*Unidades de Saúde Familiares*) units contracting with regional authorities (ARSs) using a mix of salary and performance-related payments as currently the case. Extend performance assessment to the other primary care units (UCSPs). Make sure that the new system leads to a reduction in costs and more effective provision;

ii. setting-up a mechanism to guarantee the presence of family doctors in needed areas to induce a more even distribution of family doctors across the country;

iii. moving human resources from hospital settings to primary care settings and reconsidering the role of nurses and other specialties in the provision of services;

iv. updating patients' registration lists and the national register in order to increase by at least 20 per cent the maximum number of patients per primary care/family doctor for health centres and by 10 per cent for the USF.

Hospital services

3.55. Implement the strategy to clear arrears in the health sector, within the overall strategy for settling and avoiding the re-emergence of arrears. Ensure standardised and tight control procedures for all health sector entities to ensure expenditure commitments stay within the budget allocated to each entity and therefore prevent the re-emergence of arrears. **[Q4-2012]**

3.56. Hospital SOEs will change the existing accounting framework and adopt accounting standards and appropriate IT systems in line with the requirements for private companies and other SOEs. This will help improving the management of the enterprises and the quality of the financial oversight by the general government. **[Q4-2013]**

3.57. Implement measures aimed at achieving a reduction of at least EUR 200 million in the operational costs of hospitals **in 2012**. This is to be achieved through the reduction in the number of management staff, concentration and rationalisation in state hospitals and health centres with a view to reducing capacity. **[Q4-2012]**

3.58. Continue the publication of clinical guidelines and set in place an auditing system of their implementation. **[Ongoing]**

3.59. On the basis of the comprehensive set of indicators, produce regular annual reports comparing hospital performance (benchmarking). Establish a web-portal with publicly available information. The first report is to be published **by end 2012** and its results should be used to establish targets for less performing hospitals. **[Q4-2012]**

3.60. Continue work to ensure full interoperability of IT systems in hospitals, in order for the ACSS to gather real time information on hospital accounting and activities and to produce monthly reports to the Ministry of Health and the Ministry of Finance. **[Ongoing]**

3.61. Continue with the reorganisation and rationalisation of the hospital network through specialisation, concentration and downsizing of hospital services, joint management (building on the Decree-Law 30/2011) and joint operation of hospitals. The aim is to adjust hospital provision within the same health region, notably in the presence of newly established PPP hospitals, adjust the activity of some hospitals from curative care towards areas such as rehabilitation, long-term and palliative care and revise emergency and transplantation structures. These improvements aim at eliminating unnecessary duplication, achieving economies of scale and deliver additional cuts in operating costs by at least 5 percent in 2013 while improving the quality of care provided. A detailed action plan is published **by 30 November 2012** and its implementation is finalised **by end-2013**. Overall, from **2011 to 2013**, hospital operational costs must be reduced by at least 15 per cent compared to 2010 level. **[Q4-2012]**

3.62. Annually update the inventory of all health staff and prepare regular annual reports presenting plans for the allocation of human resources in the period up to 2014. The report specifies plans to reallocate qualified and support staff within the NHS. **[Q2-2013]**

3.63. Update the current legal framework applying to the organisation of working time of healthcare staff, including introduction of rules to increase mobility within and across Health Regions, adoption of flexible time arrangements and review of payment mechanisms for emergency work, the prevention regime and per call payments, notably by aligning overtime remuneration in the health care sector with the general legal framework recently adopted. In this context, overtime compensation should be reduced by 20% in 2012 and another 20% in 2013.**[Q4-2012].**

Regional health authorities

3.64. Improve monitoring, internal control and fiscal risks management systems of the Administrações Regionais de Saúde. **[Q4-2012]**

Cross services

3.65. Continue to develop the system of patient electronic medical records and ensure access to all relevant health care facilities. **[Ongoing]**

3.66. Reduce costs for patient transportation by one third compared to 2010. **[Q4-2012]**

4. Labour market and education

<u>Labour market</u>

Objectives

Revise the unemployment insurance system to reduce the risk of long-term unemployment while strengthening social safety nets; reform employment protection legislation to tackle labour market segmentation, foster job creation, and ease the transition of workers across occupations, firms, and sectors; ease working time arrangements to contain employment fluctuations over the cycle, better accommodate differences in work patterns across sectors and firms, and enhance firms' competitiveness; promote labour cost developments

consistent with job creation and enhanced competitiveness; ensure good practices and appropriate resources to Active Labour Market Policies to improve the employability of the young and disadvantaged categories and ease labour market mismatches.

Address early school leaving and improve the quality of secondary education and vocational education and training, with a view to raising the quality of human capital and facilitate labour market matching.

Reforms in labour and social security legislation will be implemented after consultation with social partners, taking into account possible constitutional implications, and in respect of EU Directives and Core Labour Standards.

Unemployment benefits

4.1. Following the reform of the unemployment benefit system (Decree-law 64/2012 and Decree-law 65/2012 of 15 March) - which introduces a declining profile for unemployment benefits, reduces the maximum monthly amount of benefits, reduces the maximum unemployment benefits duration and increases coverage by reducing the contribution period for eligibility and by extending the system to a clearly-defined category of self-employed - the government will prepare by **Q4-2012** an analysis on benefit dependency and long-term unemployment with a view to assessing whether further measures are needed to address possible deficiencies by **Q1-2013**.

Employment protection legislation

4.2. The government will carry out reforms in the employment protection system aimed at tackling labour market segmentation, fostering job creation, and easing adjustment in the labour market. **[Ongoing]**

4.3. Severance payments **[Ongoing]**. Following the entry into force of law n. 53/2011 concerning the reform in the severance payments for new hires in line with the MoU and the entry into force of law n. 23/2012, the government will further reduce severance payments. In consultation with social partners, the Government will:

- submit to Parliament by **mid-December** draft legislation aiming at aligning the level of severance payments with the EU average of 12 days, applied to all contracts while protecting accrued-to-date entitlements and maintain the cap of 12 month of pay;
- consider the implementation of a compensation fund for severance payments possibly allowing the severance pay entitlements financed from the fund to be transferable to different employers.

4.4. Following the changes to the dismissal rules as stated in law n. 23/2012, the government will prepare a report on the effects of these changes on relevant labour market indicators by **Q3-2013**.

Wage setting and competitiveness

4.5. The government will promote wage developments consistent with the objectives of fostering job creation and improving firms' competitiveness with a view to correcting macroeconomic imbalances. To that purpose, the government will:

i. commit that, over the programme period, any increase in the minimum wage will take place only if justified by economic and labour market developments and agreed in the framework of the programme review **[Ongoing]**;

ii. ensure wage moderation when deciding on the extension of collective agreements that fulfil the criteria set out in Council of Ministers Resolution 90/2012, by taking into account the implications of the extension on competitiveness of non-affiliated firms [**Ongoing**];

iii. prepare an independent review by **Q4-2012** on**:**

   - how the tripartite concentration on wages can be reinvigorated with a view to defining norms for overall wage developments that take into account the evolution of the competitive position of the economy and a system for monitoring compliance with such norms;

- o the desirability of shortening the survival (sobrevigência) of contracts that are expired but not renewed (art 501 of the Labour Code).

4.6. The Government will promote wage adjustments in line with productivity at the firm level. Following the implementation of the organised decentralisation (which creates the possibility for collective agreements to define conditions under which works councils can negotiate functional and geographical mobility, working time arrangements and remuneration) and the decrease of the firm size threshold to 150 workers for unions to delegate power to conclude collective agreements to works councils, the government will, by **Q1-2013,** assess in a report the effects of these measures and how they are being applied in collective agreements. If needed, an action plan will be prepared in consultation with the social partners by **Q2-2013** to ensure that works councils are given the possibility to negotiate wages at firm level.

Active labour market policies

4.7. The Government will ensure good practices and an efficient amount of resources to activation policies to strengthen job search effort by the unemployed and to other Active Labour Market Policies (ALMPs) to improve the employability of the young and disadvantaged categories and ease labour market mismatches. Following the preparation of a report assessing the effectiveness of ALMPs and the publication of the Council of Ministers Resolution n.20/2012, which sets a plan to improve ALMPs, including the role of Public Employment Services (PES) , the Government by **Q4-2012** will present a report:

i. detailing expenditures and sources of financing of the different ALMPs;

ii. assessing the role played by the job counselling/ job search assistance and activation/sanctions systems in facilitating the transition out of unemployment;

iii. reviewing the implementation of the Council of Ministers Resolution n. 20/2012 regarding the reorganisation of the PES and other ALMPs;

iv. proposing specific action to improve the effectiveness of training measures in light of the results of the report assessing the effectiveness of employment and training measures.

Education and training

4.8. The government will continue action to tackle low education attainment and early school leaving and to improve the quality of secondary education and vocational education and training, with a view to increase efficiency in the education sector, raise the quality of human capital and facilitate labour market matching. To this purpose, the government will:

i. set up an analysis, monitoring, assessment and reporting system in order to accurately evaluate the results and impacts of education and training policies, notably plans already implemented (notably concerning cost saving measures, vocational education and training and policies to improve school results and contain early school leaving). The tool should be fully operational by **Q2-2013;**

ii. in line with the action plan to improve the quality of secondary education the Government will: (i) continue to promote trust agreements with public schools and report about progress [**ongoing**]; (ii) define and implement a simple formula-based funding framework comprising performance evaluation criteria and accountability for public schools and schools under autonomy agreements [**Q4-2012**]; (iii) present an assessment of the new inspection model, including the planned follow up to recommendations of previous external evaluations [**Q4-2012**];

iii. in line with action plan on vocational and educational training (VET) the Government will report on: (i) involvement of businesses in the provisions of traineeships [**ongoing**]; (ii) action taken to reorganise modalities for the provision of VET, improve the quality and attractiveness of VET, and to enhance students' orientation and career guidance [**Q4-2012**]; (iii) the establishment of "professional schools of reference". **[Q1-2013]**

iv. present an assessment on the latest developments in the apprenticeship system. [**Q1-2013**]

5. Goods and services markets

Objectives

Reduce entry barriers in network industries and sheltered sectors of the economy such as services and regulated professions so as to increase competition and reduce excessive rents. These measures should help improving the competitiveness of the Portuguese economy by lowering input prices, raising productivity and improving the quality of the products and services provided. This should contribute decisively to the social balance of the programme by reducing unwarranted sector protection and rents so that all segments of the society participate in the burden sharing of the needed adjustment.

Energy markets

Objectives

Complete the liberalisation of the electricity and gas markets; ensure the sustainability of the national electricity system and avoid further unfavourable developments in the tariff debt; ensure that the reduction of the energy dependence and the promotion of renewable energies is made in a way that limits the additional costs associated with the production of electricity under the ordinary and special (co-generation and renewables) regimes; ensure consistency of the overall energy policy, reviewing existing instruments. Continue promoting competition in energy markets and to further integrate the Iberian market for electricity and gas (MIBEL and MIBGAS).

Liberalisation of electricity and gas markets

5.1. In order to fully transpose the Third EU Energy Package: a) adopt the law on the penalty system of the regulator and b) ensure the National Regulatory Authority's independence, autonomy and all powers foreseen in the package by adopting by **[November-2012]** the new regulators' bylaws agreed in July 2012, consulting the EC/ECB/IMF if changes are introduced. Ensure that the new bylaws are effective before end of year in time for the liberalisation of the electricity and gas market **[Q4-2012**].

5.2. Take measures to accelerate the establishment of a functioning Iberian market for natural gas (MIBGAS), through regulatory convergence and the harmonisation of the tariff structures in Portugal and Spain. In particular, in accordance with the roadmap of 30 September 2011 agreed with the Spanish authorities, the regulators of each country will:

i. present proposals to harmonise the tariffs for access to the interconnection networks taking into account the outcome of the public consultation conducted in January 2012 **[Q1-2013];**

ii. prepare a report analysing and developing options to improve the harmonised mechanism for capacity allocation and congestion management of cross-border flows with Spain, including the introduction of virtual reverse flows and other mechanisms allowing smaller players to make efficient use of the LNG Sines facility **[Q4-2012];**

iii. apply a harmonised allocation and congestion management mechanism to all the interconnection capacity between Portugal and Spain, in line with the EU network codes and guidelines in this respect **[Q1-2013].**

5.3. Clarify the national legal framework with respect to the scope of competencies of the logistics operator and define based on a cost-benefit analysis a way of convergence of the existing two platforms for electricity and natural gas. **[Q4-2012]**

Ensure sustainability of the national electricity system

5.4. Conclude the measures approved in the Council of Ministers on 17 May 2012 to reduce excessive rents and to address the sustainability of the national electricity system. Cost reduction measures address the following compensation schemes: power guarantee, special regime (renewables - excluding those granted under tender mechanisms – and cogeneration), CAE's (power purchase agreements) and CMECs, and will reduce policy cost

by at least EUR 1275 million in Net Present Value (NPV)[7] **[Q4-2012]**. The updated estimation of cost reductions that will be achieved as well as progress towards elimination of the tariff debt (dívida tarifária) by 2020 will be presented and assessed in the **seventh review**.

5.5. Conclude the announced measures to limit the policy costs embedded in CMECs and PPAs by **Q4 2012**. In particular, as an element in revising the rate of return to bring it in line with the cost of capital at the moment the CMEC compensation was defined plus, if warranted, a risk premium of the assets that the mechanism remunerates: (i) approve the pieces of legislation that reduce the CMEC annuity discount rate from 7.55% to below 5% in terms that do not allow the increase of the new established rate (yielding a NPV of EUR 120 million); and (ii) set a compensation for the extension of exploitation licences of the power plants in Sines and Pego[8] yielding NPVs of EUR 55-75 million and EUR 30-50 million respectively, providing details on the valuation methodology leading to these figures. The updated estimation of cost reductions that will be achieved will be presented and assessed in the **seventh review**.

5.6. Present a report on the CMEC scheme including the foreseen annual compensation amounts to each beneficiary and past payments since 2007 and the forecast of future payments. The report will also describe the process for the extension of the concession of the public hydro resource by the former CAE hydro power plants, its correspondent economic valuation, and the rationale for the direct award instead of a tender process. The report will assess and consider all the information available within the governmental and the official bodies (General Directorates, Regulator, State representative in the contracts). **[Q4-2012]**

5.7. Conclude the announced measures to limit the policy costs of renewables under the special regime - excluding those granted under tender mechanisms by **[Q4-2012]**. In particular (i) following the agreement in principle with wind power producers, approve the legislation to implement the compensation to be paid by the producers (yielding a NPV of EUR 110 million); and (ii) introduce a maximum duration for the feed in tariff in small hydro plants (yielding an NPV of EUR 200 to 250 million). The updated estimation of cost reductions that will be achieved will be presented and assessed in the **seventh review**.

5.8. Accelerate convergence to market-based pricing for co-generation operators in parallel with electricity market developments under the EU internal electricity and gas market legislation. The remuneration scheme for co-generation will be further revised to improve efficiency of the support system in ensuring continued guaranteed access of operators to electricity networks and markets with the calculation of explicit subsidies based on relevant price factors in the context of a competitive electricity market. The revision should ensure that the design of the support scheme allows a dynamic correlation between electricity market prices and the efficiency premium when the values of avoided externalities are not adequately reflected in electricity and other factor prices. This revision will be undertaken in line with the framework of the transposition of the energy efficiency directive **[Q1-2013]**. Ensure through annual audits that plants not fulfilling the requirements for co-generation do not receive the support, and report on the progress. **[Q2-2013]**

5.9. For new contracts in renewables, revise downward the feed-in tariffs and ensure that the tariffs do not over-compensate producers for their costs and they continue to provide an incentive to reduce costs further, through digressive tariffs. For more mature technologies develop alternative mechanisms (such as feed-in premiums). Report on action taken will be provided in **Q3-2013**.

5.10. Decisions on future investments in renewables, in particular in less mature technologies, will be based on a rigorous analysis in terms of its costs and consequences for energy prices. International benchmarks will be used for the analysis and an independent evaluation will be carried out. Report on action taken will be provided in **Q3-2013**.

Telecommunications and postal services

Objectives

[7] Computed using a discount rate of 7.55% back to June 2012.
[8] Pego power plant compensation will not be included when determining the reduction of the rate of return of the CMEC.

Increase competition in the market by lowering entry barriers; guarantee access to network/infrastructure; strengthen power of the National Regulator Authority.

Telecommunications

5.11. Ensure an efficient, objective, transparent and non-discriminatory mechanism for the designation of the universal service provider(s), in compliance with the Court of Justice ruling of 7 October 2010. Re-negotiate the concession contract with the undertaking currently providing the universal service, by reducing the scope of the services covered, so as to exclude the universal service and following the launch of a new tender process in October, proceed with the designation of universal service provider(s). **[Q2-2013]**

5.12. Following the corrective measures already taken, monitor the competitive situation in the telecommunications sector, in particular wholesale and retail broadband access, and mobile origination charges. **[Ongoing]**

Postal services

5.13. Following the transposition of the Third Postal directive, further liberalise the postal sector by amending the decree-law laying down the framework of the concession contract and renegotiating the amendment of said contract with CTT, in order to reflect the new law (Law 17/2012) transposing the Third Postal Directive; ensuring in particular that the current designation period for the universal service provision is shortened to 2020 and that investment needs and return on investment are taken into account when setting new designation periods. **[Q4-2012]**

Transport

Adopt a strategic plan to: rationalise networks and improve mobility and logistic conditions in Portugal; improve energy efficiency and reduce environmental impact; reduce transport costs and ensure financial sustainability of the companies; strengthen competition in the railways sector and attract more traffic; integrate ports into the overall logistic and transport system, and make them more competitive.

Strategic Plan for Transport

5.14. Implement the Strategic Plan for Transport for 2011-2015 **[Q4-2012]**, namely:

i. continue the reforms in the transport SOEs to achieve their EBITDA balance, by focusing efforts on the reduction of operational costs;

ii. reduce the forecast debt burden of Estradas de Portugal through the reduction of PPP contracts' scope still in the construction phase, revision of shadow-toll schemes and the adjustment of the CSR (Road Service Contribution) to the inflation level. Analyse additional measures to further reduce the forecast debt burden of Estradas de Portugal;

iii. focus the investment priorities in projects that present a positive cost-benefit ratio and contribute to the competitiveness of Portuguese exports, namely in the port and freight rail sectors;

iv. reform the transport and infrastructures' regulatory framework in order to improve the effectiveness, efficiency and independence of the entities regulating the transport sector. **[Q1-2013]**

5.15. Present a long term vision of the transport system and a list of actions to improve its efficiency and sustainability **[Q4-2012]**. It will specifically include an assessment of the existing rail, road and port networks and present a set of investment priorities for the 2020 and 2030 horizons, taking also into account TEN-T networks, with an estimate of the financial needs and the foreseen sources of financing **[Q2-2013]**.

Railways sector

5.16. Continue with the transposition of the EU Railway Packages and in particular:

i. ensure that the rail regulator enjoys the independence required under the EU rail Directives, in particular regarding the rules of appointment and dismissal of the director of the rail regulator. Strengthen the capacities of the railway regulator to fulfil its regulatory mandate effectively, including by exploring synergies with other transport regulators in the context of the revision of national regulatory agencies. **[Q1-2013]**;

ii. continue to implement the plans to bring the infrastructure manager to operational balance, in particular by reducing operational costs by at least 23 per cent in 2012 compared to 2010 **[Q4-2012]**. On the revenue side, track access charges for freight services should not be increased in order to prevent a deterioration of the competitiveness of rail freight services. Reintroduce incentives to REFER to reduce costs and access charges. Provide annual progress reports on the implementation of balancing revenues and expenditures **[Q2-2013]**;

iii. ensure that the new Public Service Obligation (PSO) contracts concluded on rail passenger transport respect EU legislation including Regulation (EC) No 1370/2007, and in particular provide a detailed breakdown of state contributions for each line under PSO. Develop administrative capacity for a stepwise introduction of competitive tendering of PSOs starting with some suburban services. Ensure that the awarding authority has the required level of independence and competence and guarantees fair conditions of tendering **[Q4-2012]**;

iv. extend the performance scheme on infrastructure charges to other operators **[Q4-2012]**;

v. review and render more effective the yield management on long-distance passenger ticket prices. **[Q1-2013]**;

vi. to prepare the privatisation of the freight branch of the state-owned rail operator, carry out an analysis for transferring part or whole of CP Carga's rolling stock to a rolling stock operating company **[Q2-2013]**;

vii. ensure that the main rail terminals currently owned by CP Carga are transferred to another entity that will guarantee non-discriminatory access to all rail freight operators. **[Q4-2012]**.

Ports

5.17. Adopt the revised legal framework governing port work as presented to Parliament by **[Q4-2012].** A review of the overall savings generated and the impact of the introduction of the law on port usage cost will be made by **August 2013**.

5.18. Take further steps to improve the governance model of the ports system with the objective to enhance the competitiveness and the efficiency of ports in line with the Strategic Plan of Transport 2011-2015. The Government will deliver and enforce policies that ensure strong integrated policy-making, strategic planning and surveillance functions common to all ports in the country. Moreover, policy decisions will be taken and enforced so that (i) efficiency gains and cost-savings are passed through to port customers; and (ii) concession-holders of terminals and land facilities in ports respect minimum performance criteria. **[Q4-2012]**

Road pricing

5.19. Adopt the necessary legislative amendments in order to achieve full compliance with Directive 1999/62/EC (Eurovignette Directive) and the EU Treaty and, in particular, to guarantee non-discriminatory application of tolling schemes to non-resident road users **[Q4-2012].** After the deadline of this measure, rebates in tolling schemes that pursue compelling reasons of territorial and social cohesion may only be applied if their compliance with the EU law is demonstrated.

Other services sector

Objectives

Eliminate entry barriers in order to increase competition in the services sector; soften existing authorisation requirements that hinder adjustment capacity and labour mobility; reduce administrative burden that imposes unnecessary costs on firms and hamper their ability to react to market conditions.

Sector-specific legislation of Services

5.20. Further to the adoption of a significant number of amendments to the sector specific legislation, complete the adoption of the outstanding sectorial amendments (such as construction, universities and higher education courses) necessary to fully implement the Services Directive and submit them to Parliament where necessary by **[Q4-2012]** in view of approval by **[Q1-2013]**. For those amendments already submitted to the Parliament (such as real estate) approval is expected by **[Q4-2012].**

Regulated professions

5.21. Review and reduce the number of regulated professions and in particular eliminate reserves of activities on regulated professions that are no longer justified, through adoption by the Parliament of the law for professions where regulation does not involve a professional body (Ordens or Câmaras) by **[Q4-2012]**. Following the final report by the Comissão de Regulação do Acesso a Profissões (CRAP), launch by **[Q1-2013]** a second phase investigation of the review of regulated professions to eliminate unjustified requirements by **[Q2-2013].**

5.22. Further improve the functioning of the regulated professions (such as accountants, lawyers, notaries) for which regulation involves a professional body (Ordens or Câmaras) by (i) carrying out a comprehensive review of requirements affecting the exercise of activity with a view to eliminating those not justified or proportional, such as those restrictions to the use of commercial communication (advertising) prohibited by the Services Directive, and (ii) by adopting measures to further improve the recognition of professional qualifications in compliance with the Professional Qualifications Directive To achieve the objectives referred to above the government has, following the public consultation, submitted a draft horizontal legal framework to Parliament in view of approval by **[Q4-2012]**. Upon enactment, the professional bodies will make the necessary changes in their statutes by **[Q1-2013]**.

Administrative burden

5.23. Continue the simplification reform effort by:

i. adapting the content and information available at the Point of Single Contact (PSC) for the 48 amended regimes to ensure conformity with the Services Directive and for those that have not required amendments so far by **[January 2013]** and make available online forms for the completion of procedures by **[Q1-2013]**. Constantly adapting the content and information available at the PSC to the remaining 20 sector-specific regimes that are about to be adopted to ensure conformity with the Services Directive (see 5.20 above) at the latest 1 month after the adoption of each sector-specific regime, clearly differentiating information on requirements applicable to established providers and to cross-border ones, and by making available online forms and extend on-line procedures for all sectors covered by the Services Directive no later than 2 months after adoption of the sector-specific regime;

ii. adapting the content and information available at the PSC for the 15 regimes approved to ensure conformity with the Professional Qualifications Directive by **[January 2013]** and online forms by **[Q1-2013]**. Constantly adapting the content and information available at the PSC to the new legislation to be adopted to ensure conformity with the Professional Qualifications Directive at the latest 1 month after the adoption of amendments, clearly differentiating information on requirements applicable to established providers and to cross-border ones, and by extending on-line forms and procedures for each profession no later than 2 months after adoption of amendments;

iii. making available in PSC on-line procedures for the registration, installation, modification, occupation of public space regimes, and closing up of restaurants, bars and other establishment for

the 5 municipalities (Porto, Águeda, Abrantes, Portalegre and Palmela) covered by "Zero Authorisation" pilot project (DL 48/2011) by **[Q4-2012]**. Foster collaboration from municipalities in providing the content for the working hours map for the stores and establishments services and advertisement regimes for which they have full competence to make the PSC operational **[Q4-2012]**; Identify and classify municipalities where the availability of those procedures through the PSC would have the most significant economic impact by **[November-2012]** to prepare for the extension of this tool to major municipalities by **[January-2013]**. Make fully operational the “Zero Authorisation” project that abolishes authorisations/licensing and substitute them with a declaration to the PSC for the wholesale and retail sector and restaurants and bars by **[Q2-2013]**. The platform will be available to all levels of administration, including all municipalities **[Q2-2013];**

iv. extending PSC to services not covered by the Services Directive **[Q4-2013]**;

v. extending the "Zero Authorisation" project to other services sectors of the economy **[Q4-2013]**.

5.24. Provide a monthly update of the detailed work programme of AMA to fulfil 5.23.

6. Housing market

Objectives

Improve access to housing; foster labour mobility; improve the quality of housing and make better use of the housing stock; reduce the incentives for households to build up debt.

Property taxation

6.1. The government will continue to step up the appraisal of the taxable value of the housing stock. In particular, the measures will: (i) ensure that the taxable value of the properties in **2012** is close to the market value and (ii) property valuation is updated regularly (every year for commercial real estate and once every three years for residential real estate as foreseen in the law).

6.2. The government will gradually rebalance property taxation towards the recurrent real estate tax (IMI) and away from the transfer tax (IMT), while considering the socially vulnerable. **[Q3-2013]**

Comprehensive review of the housing market

6.3. Following the adoption of the amendments to the New Urban Lease Act Law 6/2006 and the Decree Law which simplifies the administrative procedures for renovation, the government will undertake a comprehensive review of the functioning of the housing market with the support of internationally-reputed experts. The review will determine whether the new legal provisions adopted are sufficient to make the housing market more dynamic and, if necessary, will propose new policy measures. **[Q2-2013]**

7. Framework conditions

Judicial system

Objectives

Improve the functioning of the judicial system, which is essential for the proper and fair functioning of the economy, through: (i) ensuring effective and timely enforcement of contracts and competition rules; (ii) increasing efficiency by restructuring the court system, and adopting new court management models; (iii) reducing slowness of the system by eliminating backlog of courts cases and by facilitating out-of-court settlement mechanisms.

Court backlog

Recognising the urgency of the judicial reform to make the judicial system more efficient and more effective, the government will:

7.1. Aim to resolve the backlog of court cases by **Q2-2013.**

7.2. Implement targeted measures to achieve steady reduction of the backlogged enforcement cases. In particular, set quarterly targets for closing enforcement cases and prepare quarterly reports on implementation status, by inter-agency task forces with the fifth report to be completed by mid**-February 2013**.

7.3. Present a revised draft bill for enforcement agent's framework (i) strengthening the authority and financing structure of the oversight body and enhancing the accountability of enforcement agents, and (ii) to include a fee structure that incentivises speedy enforcement which will be approved by the government by **end-February 2013**.

7.4. Publish quarterly reports on recovery rates, duration and costs of corporate insolvency cases starting from **[Q3-2011]**, within four months after the end of the relevant quarter.

Competition, public procurement and business environment

Objectives

Ensure a level playing field and minimise rent-seeking behaviour by strengthening competition and sectoral regulators; eliminate special rights of the state in private companies (golden shares); reduce administrative burdens on companies; ensure fair public procurement processes; improve effectiveness of existing instruments dealing with export promotion and access to finance and support the reallocation of resources towards the tradable sector.

Competition and sectoral regulators

7.5. The Government shall take the necessary measures to ensure that the Portuguese State or any public bodies do not conclude, in a shareholder capacity, shareholder agreements the intention or effect of which hinder the free movement of capital or which influence the management or control of companies **[Ongoing]**. The Portuguese State will ensure that CGD alienates its participation in Galp. **[Q4-2012]**

7.6. Going beyond elimination of special rights of the State, the authorities also commit to ensure that obstacles to free movement of capital will not be created by their action. The authorities acknowledge that the discretion granted under the amended article 13(2) of the Framework Law of Privatisations (Law 11/90 amended by Decree 3/XII of the Parliament of 5 August 2011), if used, shall be restricted solely to the concrete privatisation operation and thus used in such a proportionate manner that privatisation's implementing laws will not set or allow holding or acquisition caps beyond the privatisation transaction**. [Ongoing]**

7.7. Monitor the inflow of cases and report on the functioning of the specialised court for Competition, Regulation and Supervision, assessing the situation in terms of risk of potential court backlogs. **[Q4-2012]**

7.8. Take the necessary actions to ensure the effective functioning of the Competition Authority financing model [**Q4-2012**]. Following the efforts made in order to guarantee the enlarged scope of action of the Competition Authority, report on the conditions for the proper execution of its mandate **[Q4-2012].**

7.9. Building on the independent report on the main National Regulator Authorities, the government will prepare a framework law for regulators in broad consultation with the Regulator Authorities. This law will establish a regulatory environment that protects the public interest and promotes market efficiency. The law will guarantee the Regulator's independence and financial, administrative and management autonomy to exercise their responsibilities, in full compliance with EU law. The law will also contribute towards the effectiveness of the competition authority in enforcing competition rules therefore supporting and complementing the effect of the recently adopted competition law. The framework law will be submitted to parliament by **[Q1-2013].**

Public procurement

The government will modify the national public procurement legal framework and improve public contracts award practices to ensure a more transparent and competitive business environment and improve efficiency of public spending. In particular, it will:

7.10. Submit a report analysing the effectiveness and impact of the amendments to the revised Public Procurement Code as well as of the enhanced role of the Court of Auditors in ensuring compliance with public procurement rules by **[Q1-2013]**.

Business environment

7.11. Make operational the procedures for requesting VAT exemptions for exporting firms and to simplify procedures associated with indirect exports as part of the "Simplex Exports" programme. **[Q4-2012]**

7.12. Following the plans presented at the sixth review, adopt measures to facilitate access to finance and to export markets for SMEs. A limited number of instruments should be sought, focusing primarily on SMEs, especially those in the most productive and innovative segments of the economy, while ensuring these initiatives will not pose significant fiscal risks. Progress will be reported by [**Q4-2012]**.

7.13. Promote liquidity conditions for business by timely implementing the New Late Payments Directive. **[Q1-2013]**

7.14. Continue reducing administrative burdens by including municipalities and all levels of public administration within the scope of the Simplex Programme. **[Q1-2013]**

Licensing environment

Objectives

The government is launching a new comprehensive programme to tackle excessive licensing procedures, regulations and other administrative burdens in the economy. These explicit and implicit barriers represent a major obstacle for economic growth in Portugal. Companies face substantial costs and uncertainty which affect investment decisions, thus limiting job creation. Furthermore, these barriers affect small and medium-sized enterprises in a disproportionate way because they have fewer resources to surpass these obstacles, deteriorating the competitive environment. Foreign investment is also affected disproportionally because national companies have information advantages. The various new initiatives laid out below cover all families of licenses and will have a substantial impact in the business environment. The reviews of the legal regimes of environment and territory planning and of industrial and commercial licencing aim at ensuring their mutual compatibility.

Regulatory simplification

7.15. To deal with the legacy of excessive licences procedures and other administrative burdens, carry out a full inventory and an analysis of the costs of all regulations in the economy (at central, regional and local levels). **[Q2-2013]** On the basis of the analysis the government will devise a roadmap for a regulatory simplification.

7.16. To prevent future growth in excessive licenses and regulations, study the feasibility of a rule that prohibits at all levels of government the creation of a new regulation generating costs for businesses without the elimination of an existing regulation or regulations with an equivalent cost. The feasibility of such rule will be decided by **[Q1-2013]** with a view of being in place by **[Q2-2013]**.

7.17. Create a working group to analyse and fast-track applications for the licensing of planned investment projects which are left unresolved or undecided for more than 12 months **[Q4-2012]**.

Environment and territory planning

7.18. In consultation with the relevant stakeholders, review the legal regimes at all levels of Government in the area of territorial planning, in order to increase and facilitate the establishment of investors while at the same time limiting urban sprawl. In particular, review the following legal regimes, in the area of territorial planning:

i. new Base Law of Soil and Territorial and Urbanism Planning (Lei dos Solos), that should be aligned with the new Industrial Licensing regime (measure 7.24 ii) **[Q4-2012]**;

ii. National Ecological Reserve/ Risks (REN): (1) Changes to Decree-Law 166/2008 (RJREN); (2) Publication of strategic orientations regarding modifications of REN's municipal delimitations; (3) Revocation of Ordinance 1356/ 2008 (Compatible REN actions); 4. Joint Dispatch of the Secretaries of State of Environment and Territorial Planning and of Internal Administration in order to determine the creation of Risk Sectorial Plan **[Q4-2012]**;

iii. review the legal regimes of the Territorial Management Instruments (RJIGT) and of the related regulations **[Q4-2012]**;

iv. diploma for the regularization of activities not in accordance with Territorial Management Instruments **[Q4-2012]**;

v. diploma for the harmonization of Territorial Planning Regional Plans – new generation **[Q4-2012]**;

vi. review the Legal Regime for Urbanism and Building (RJUE) , that should be aligned with, the new Industrial Licensing regime (measure 7.24 ii) **[Q1-2013].**

7.19. Increase a nationwide land registration system (registo cadastral) to allow a more equal (perequitativa) distribution of benefits and costs in the execution of urban planning. The government will:

i. implement a Legal Regime of Land Registration (registo cadastral) **[Q4 2013]**;

ii. create a diploma on Land Registration and Land Registration Experts **[Q4-2013]**;

iii. review the cartography for plans regime **[Q4-2013]**, and the diploma on Cartography **[Q4-2013]**;

iv. enforce the Council of Ministers Resolution 56/2012 by **Q4-2013**, to collect all land registration procedures, currently scattered in various departments.

7.20. Change the legal regime for Environment Impact Evaluation in order to increase the speed and effectiveness of this regulation and reduce associated monetary and time costs. **[Q4-2012]**.

Industrial Licensing

7.21. Implement the new Industrial Licensing regime by means of:

i. fully implement the approved Programme of Responsible Industry (“PIR - Programa da Indústria Responsável” **[Q2-2013]**;

ii. review the following legal norms and regimes that are crucial for a successful implementation of the approved System of Responsible Industry (“SIR - Sistema da Indústria Responsável”):

a. implement zero licensing procedures for Type 3 **[Q4 2012]** and Type 2 industries **[Q1 2013]** including fully integration of these procedures in the one-stop shop (“Balcão do empreendedor”). Implement fast-track procedures for Type 1 industries **[Ongoing]**;

b. define and establish the Zones of Responsible Enterprises (ZER – Zonas da Indústria Responsável) by **[Q1-2013]**, which will allow the installation of industries in areas previously licensed with all industrial, building and environmental provisions required by national and European law;

c. create and define standardized industrial licenses **[Q1-2013]**;

d. ensure that the new Industrial Licensing is aligned with, and strengthened by, the review of the New Base Law of Soil and Territorial and Urbanism Planning while at the same time limiting urban sprawl (measure 7.21 i) **[Q4-2012]**;

e. ensure that the new Industrial Licensing is aligned with, and strengthened by, the review of the Legal Regime for Urbanism and Building (RJUE - measure 7.21 vi) **[Q1-2013]**.

Commercial licensing

7.22. Review the commercial licensing regime. Approval of a new legal regime for commercial actives and establishment of the Program for the Competitiveness of Commerce and Services activities ("Programa para a Competitividade do Comércio e Serviços), which will simplify and condense in a single law more than 20 dispersed existing legal regimes **[Q4-2012].**

Geology

7.23. Reviewing the geological licensing regimes, including:

i. revision of the legal regime concerning the licensing of mining and geological production and investment in line with international best practices in this field **[Q4-2012]**;

ii. simplify the legal and bureaucratic procedures pertaining to mining and geological investments, especially in terms of assessment, search, development, and production activities **[Q4-2012]**.

Tourism

7.24. Review the Licensing in Tourism regime:

i. eliminate or transforming into a voluntary regime the mechanism of prior communication in the Regime for Urbanism and Building **[Q1-2013].** Simplify the legal regime for touristic establishments **[Q4-2012];**

ii. expand the range of ex post control mechanisms in urban operations, significantly reducing administrative procedures and costs for developers **[Q4-2012]**;

iii. simplified and transparent requirements on the classification of the several types of touristic establishments (number of stars) **[Q4-2012]**;

iv. review of the sanction legislation on the touristic establishments regime as a way to fight informal touristic economy, giving more powers to ASAE (Authority for Economic and Food Safety). **[Q4-2012]**

PORTUGAL: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

December 20, 2012

1. **Activity.** The outlook for growth and inflation remains broadly in line with the program framework. In the third quarter of 2012, real GDP contracted by 0.8 percent (over the previous quarter), somewhat smaller than the 1 percent assumed under the baseline. The main drag on growth remains the ongoing private sector deleveraging, ongoing fiscal adjustment, and, in more recent months, the marked slowdown in activity in the euro area. Looking ahead, we expect output to trough in the first half of 2013 followed by a gradual recovery in activity from the third quarter, limiting the contraction in output on average to 1 percent in 2013. The decline in investment is expected to slow down, as the strong export growth of recent quarters is expected to foster some increase in capacity utilization. The current account deficit is projected to continue narrowing from 6.5 percent of GDP last year to under 3 percent in 2012 and under 1 percent in 2013. The employment outlook unfortunately looks set to remain difficult, with projected average unemployment rates of 15½ percent this year and 16½ percent in 2013. Moreover, downside risks to both the output and employment outlook are significant, and avoiding still weaker outcomes will depend greatly on developments in the euro area.

I. Fiscal Policy

2. **Budget 2012**. Revenue performance has been somewhat weaker than envisaged in recent months. This is explained by macroeconomic developments (continued rebalancing of activity from domestic demand to net exports) and some temporary factors such as an unanticipated increase in tax reimbursements). Tight spending execution is being maintained, ensuring the end-September government cash deficit was met. While there are downside risks, the general government deficit objective of 5 percent of GDP for 2012 should be achieved reflecting our plans to sustain firm spending discipline. This is after the inclusion of revenue from the one-off sale of the ANA concession, which is expected to generate 0.7 percent of GDP. Overall, in 2012, the structural primary deficit is estimated to have improved by some 2½ percentage points of GDP.

3. **Budget 2013**. The 2013 budget was approved by Parliament on November 28. It includes a range of tax and spending measures: increases in personal income tax (PIT) rates and introduction of the streamlined PIT structure; increases in property and excise tax collection; changes to the corporate income tax to reduce debt bias; the streamlining of public services, and improved targeting of social transfers (see MEFP for the fifth review for a fuller description). Reflecting the discussions in the Parliament, we have been able to improve the composition of the adjustment, allowing us to reduce the surcharge on personal income tax by from 4 to 3½ percent, offset mainly by spending cuts. Overall, the measures adopted in the budget should ensure that the general government deficit to 4½ percent of GDP next year is achieved. As customary, we stand ready to take additional measures, if need be, to ensure this deficit objective is met.

4. **Expenditure Review.** To underpin the additional fiscal adjustment that is required in coming years, we have initiated a comprehensive public expenditure review exercise—to be discussed at the seventh review—with contributions from a broad range of stakeholders in the Portuguese society. Once the initial assessment is completed, we intend to initiate a consultation with social and political partners to ensure that this review has the broad-based support to reform the role and functions of the Portuguese state. The objective will be to refocus the role of the State in Portugal in order to ensure the sustainability, the effectiveness, and the equity of its social functions. This will allow generating spending savings of about €4 billion in 2013 and 2014. To this end, this exercise will aim at ensuring better value-for-money from the public sector. Furthermore, a crucial consideration will be to reallocate resources toward growth-friendly spending areas.

5. **CIT.** In parallel with the expenditure review we are launching a comprehensive reform of our corporate income taxation, so as to make Portugal a more attractive investment destination and boost competitiveness. We will analyze the competitiveness of the Portuguese corporate income tax system in comparison to peers—including its rates, tax expenditures, depreciation, loss-carryover rules, holding regimes, and group taxation rules. In addition, we will reform our tax policy in order to promote the internationalization of Portuguese groups and attract FDI, as well as the effectiveness of existing tax incentives schemes, particularly in tradable and high value-added sectors. The results of this analysis, which will be discussed during the 7th review, will help us devise strategic reform objectives for the CIT system. The 2013 budget foresees the possibility of broadening the scope of existing tax benefits aimed at boosting investment. We will ensure that any new initiative implemented under the budget provisions be fully consistent with our strategic reform objectives as well as EU State Aid rules, while assuring that this reform will be budget neutral.

II. Containing Fiscal Risks

6 **Public Financial Management**. We are committed to implement our 2013-2015 PFM Strategic Plan in order to strengthen fiscal accountability and transparency, reduce budgetary fragmentation, and build institutional capacity. To this end, we will proceed to transpose the new EU economic and fiscal governance framework by year-end and conduct a review of the Budgetary Framework Law in 2013, streamlining budget procedures. We will intensify our efforts to prevent the underlying increase in the stock of domestic arrears of the health sector, which still reflects commitments in excess of funding. We will work closely with the Autonomous Region of Madeira to ensure that the region's commitment control system is in full compliance with the new commitment control law. We are on track to submit the Regional and Local Finance Laws to Parliament by year-end (structural benchmark).

7. **Revenue Administration.** We will continue to strengthen our tax compliance strategy and to modernize the revenue administration. In particular, our VAT invoicing reform will enter into force on January 1st, 2013. We will also phase-in a new tax compliance management approach over a three-year period, with the implementation of two pilot projects on key risk sectors—the High Net Wealth Individuals and the Self-employed Professionals—by July 2013. The new approach will be guided by a comprehensive tax compliance report, including a risk analysis by economic sector and taxpayer size, to be discussed in the 7th review. We are on track to fully implement the Large Taxpayer Office by year-end (structural benchmark). The streamlining of the revenue administration's local offices will be completed by June 2014, aiming at closing down half of the existing branches. We are accelerating efforts to successfully conclude the property revaluation process and we expect to reach about 4 million properties by year-end. This far-reaching project will be finalized by March 2013. Finally, the tax administration has systematically improved its performance in tax courts' decisions.

8. **Public Administration.** Our public administration reform is advancing and we will continue to press ahead with the objective to shape a more efficient State. The PREMAC program, which reduced around 27 percent of management positions and 40 percent of administrative units across the central administration, was successfully concluded. The reduction in the number of public employees is projected at 3.5 percent in 2012, well above the 2 percent program target. Looking ahead, we remain committed to continue streamlining excess employment in a targeted way. We will also improve training and qualification of public employees and reinforce human resources management policies across all administrations. In this context, labor and social protection regimes will converge to private sector rules, increasing productivity and improving the quality of public services.

9. **State-Owned Enterprises.** We continue to make progress in restructuring the SOE sector. We have achieved our objective of restoring operational balance to the sector as a whole before the end of 2012.

Completion of cost cutting programs at firms still in deficit, consolidation of functions at merged firms, voluntary redundancies and efforts to raise non-core revenues will ensure this significant turnaround is sustained and deepened in 2013. We will continue to actively manage the high legacy debt burdens of these companies. Some small SOEs with non-essential functions are being wound down, and we are developing a strategy to sell or rent non-vital real estate assets.

10. **Privatization.** The privatization program remains on–track. We will accept final bids for the airport concession company ANA and the airline TAP soon, successfully meeting our development and financial objectives, with financial completion expected early in 2013. With the completion of this sale, 80 percent of the program objective to raise €5 billion will have been met. We will launch the privatization process for the postal company CTT in the second quarter of 2013, with a view to completing the process by the end of the year. The sale of the rail cargo firm CP Carga will be launched early in 2013, to be completed in the second or third quarter. A strategic plan for the water sector, which envisages the sale or concession of the waste management business, is being prepared.

11. **Public-Private Partnerships.** We are advancing our strategy to put the PPPs financial model on a sustainable path. The first stage of the road PPPs strategy has been concluded and is expected to lead to savings in excess of €1 billion, in NPV terms, starting in 2014. This will be reached by reducing maintenance costs of the sub-concessions contracts. However, a sustainable solution to the Portuguese road model will only be achieved after the completion of the ongoing second phase, which includes a gradual change in the risk matrix of some PPP projects, resulting in a significant reduction in the availability payments by the State starting in March 2013. The newly-created PPP Unit will technically support and monitor all phases of the renegotiation process.

III. Safeguarding Financial Stability

12. **Credit and Funding Conditions.** Reflecting both demand and supply factors, aggregate credit continues to decline. But within this overall picture, there are large differences between domestic and foreign sources of financing and among firms. Credit to large firms has continued to expand, supported by successful bond issuances in both the domestic and international markets, whereas loans by domestic banks to SMEs exposed to the non-tradable sector continued to contract significantly. Demand for credit by firms remains conditioned by the need to reduce the large debt burdens they face. The supply of credit is being affected *inter alia* by the banking system's need to move to a sustainable business model. In particular, very low rates on the legacy mortgage portfolios are proving a drag on banks' profitability, pushing up lending rates on new loans to companies, including in the more dynamic export sector. The combination of measures being taken by us and at the euro area level, including non-standard measures by the ECB to restore the proper transmission of monetary policy, have started to stabilize conditions. Tentative signs of progress include the recent issuance of a bond abroad by two commercial banks—the first such issuance since mid- 2010.

13. **Liquidity.** Exceptional Eurosystem liquidity support is playing a pivotal role in limiting liquidity pressures and mitigating the lingering risk of excessive credit contraction. Moreover, the eligibility of additional collateral has allowed Portuguese banks to reinforce buffers and is playing a critical role in supporting their resilience against potential adverse shocks. In parallel, to facilitate the functioning of the domestic interbank market, the BdP has launched a platform for interbank unsecured lending and is developing a new one for secured transactions, which is expected to be launched by in early 2013. Banks are expected to gradually reduce their dependence on the Eurosystem liquidity over the medium term, as the deleveraging process smoothly runs its course and collateral buffers are successfully strengthened on a sustainable basis.

14. **Orderly Corporate Deleveraging.** As the required corporate sector deleveraging process advances, it is also crucial that the most productive and innovative segments of the economy, notably among SMEs, are not subject to undue funding strains and can effectively support the economic recovery. To this end, the Ministry of Finance, together with BdP and other stakeholders, are developing a range of measures that seek to facilitate credit to productive firms, foster the diversification of firms' financing alternatives, and reduce information asymmetry and promote more efficient financing allocation. These could include the aggregation of SMEs' debt instruments to promote access to capital markets; initiatives to help mitigate risks to lenders by upgrading and promoting sharing of information on SMEs; the rationalization and redirection to the most productive segments of the economy of existing government initiatives. We will continue to ensure that these steps do not burden or pose risks to public finances.

15. **Private Sector Restructuring.** Private sector debt restructuring plays an essential role in the recovery of viable but financially vulnerable corporates and households. We continue facilitating a smooth application of the newly adopted or amended legal frameworks for corporate debt restructuring (such as the fast track in court restructuring tool, PER or SIREVE, mediated by IAPMEI). In particular, we continue raising public awareness about the new restructuring tools to promote early access by viable debtors in financial distress, while facilitating solutions to any remaining obstacles to their effective application. We will also evaluate the potential impact of the recently adopted household debt restructuring mechanisms on banks' balance sheets. These efforts are being supported by BdP's initiatives to avoid banks' evergreening and promote prompt restructuring of problem loans.

16. **Bank Supervision.** Efforts to strengthen the resilience of the banking system are continuing. The BdP's new onsite inspections program (OIP), launched last May and focused on assets related to the construction and commercial real estate sectors, has been completed, with the banks being expected to reflect the OIP findings in their 2012 annual accounts. This initiative is part of BdP regular supervisory activities, which are currently focused on assets classes that are more sensitive to existing market conditions. In parallel, the BdP has completed the next round of quarterly stress tests, while banks' implementation of the earlier recommendations on stress testing is progressing. Banks that have completed the capital augmentation exercise—including through successful private issuances—and despite higher impairment levels, are on track to meet the end-2012 capital targets under the program. The BdP continues to closely monitor compliance with the capital requirements, with a view to promptly take appropriate action if needed.

17. **BSSF Resources**. We remain committed to providing further support to the banking sector, if needed. We will continue to encourage banks to seek private solutions in the event new capital needs were to arise. Nevertheless, resources from the Bank Solvency Support Facility (BSSF) remain available to support viable banks if needed, in line with state aid rules and subject to strict conditionality, with the aim to avoid subsidizing private shareholders and preventing migration of private liabilities to the public sector balance sheet. The resources in the BSSF will solely be utilized to provide public support, if needed, to the banking system.

18. **Bank Recapitalization and Resolution Frameworks.** We will enhance the legal framework governing banks' access to public capital while continuing to strengthen the early intervention and resolution framework. The decree law on the banks' contributions to the resolution fund is expected to be approved by end-December, and the supervisory notice on resolution plans will be finalized by the same date. We will swiftly transpose the new EU Directive on bank resolution as soon as it enters into force. The government will, in consultation with the ECB, and the EC and the IMF, submit to Parliament by end-January 2013 (structural benchmark) amendments to the law governing banks' access to public capital so as to allow the State, under strict circumstances, to exercise control over an institution and to perform mandatory recapitalizations. Such

amendments will be in line with EU State Aid rules and will strike an appropriate balance between preserving the private structure of the banking system and safeguarding the use of public resources.

19. **BPN SPVs.** We are implementing the strategy for managing the distressed assets from Banco Português de Negócios (BPN). We are finalizing the terms of reference for the mandate of the professional third party that will manage the credits currently held by Parvalorem, with the aim to maximize recoveries while minimizing operational costs. The competitive bidding process to select the asset manager will be launched by end-2012, with a view to complete the tender process by mid-2013. We will also ensure timely disposal of the subsidiaries and the assets in the other two state-owned SPVs. CGD's state guaranteed claim will be gradually settled in cash, according to the schedule agreed with the EC, ECB, and IMF staff. Any net recoveries realized on the assets will also be applied towards the settlement of CGD's claim.

IV. Boosting Employment, Competitiveness, and Growth

20. **ALMPs.** We are delivering on commitments to support employment through Active Labor Market Policies and to improve education. The objective is to improve the employability of the young and disadvantaged categories and ease labor market mismatches. Continuous progress is being made in broadening the reach of *Vida Ativa*, our new targeted training initiative, and improving the role of public employment services. On the education front, we are focusing our efforts on the quality of secondary education and vocational training.

21. **Labor Market Institutions.** Significant steps have been taken over the past six months to make the labor market more dynamic and efficient—including the adoption of a new labor code, the reform of unemployment benefits and, more recently, the reform of the wage-setting mechanism. By mid-December 2012, we will submit to parliament a law to lower severance payments further to 12 days per year of service, bringing them in line with relevant comparators in the European Union. The law will be applied to all contracts while protecting acquired rights and maintaining the cap at 12 months of pay. Once this step is complete, the government will have reduced the restrictiveness of employment protection legislation significantly.

22. **Ports and Energy.** A landmark revision of the Ports Work Law, which was submitted to Parliament in September, substantially lowers wage costs and removes constraints to optimizing the use of labor. The Law is to be adopted by yearend. Follow-up measures to ensure the effective transmission of lower unit labor costs to end-users of port services include (i) encouraging price reductions under existing contract, (ii) revising incentives for port operators by adopting a new performance-based model for future concessions, and (iii) encouraging entry of new operators. Finally, responding to exporters' concern, we have reduced fees on port use (*TUP-Carga*) by 10 percent. Another 10-percent cut will be made effective in January. We are pursuing our efforts to cut energy costs, including by reducing excessive rents in the electricity sector.

23. **Business Environment.** Initiatives to tackle excessive licensing procedures, regulations and other administrative burdens—which are impeding the establishment, operation, and expansion of firms—are advancing in line with the sixth update of the Memorandum of Understanding (MoU).

24. **Regulation**. We are preparing a framework law for regulation that draws on the findings and recommendations of the recently completed expert report, benchmarking the responsibilities, resources, and independence of the main sectoral regulators against international best practices. The framework law, which will guarantee independence, as well as financial, administrative and management autonomy, and benefit from broad consultation with the regulatory bodies concerned, will be submitted to parliament by end-March 2013. While

this important law is being prepared, we are amending the statutes of the electricity regulator (ERSE) to give it the appropriate powers, independence, and autonomy ahead of full market liberalization in January 2013.

25. **Judicial.** We have further advanced the reforms to improve the efficiency of the judicial system, including by meeting the two end-November structural benchmarks on the judicial roadmap and the new Code of Civil Procedure. Moreover, despite the challenges in addressing the backlog court cases, an additional 17,000 enforcement cases have been cleared, bringing down the total number by about 113,000 enforcement cases since November 2011. We have adopted a decree law for a set of urgent measures designed to combat the court case backlog. The inter-agency task forces have set quarterly targets for reviewing enforcement cases to be closed by mid-February 2013. To this end, we have further stepped up our efforts by expanding the task forces to small claims court cases in specific courts. Finally, and in order to relieve civil courts from mandatory intervention to determine bad debt status for VAT purposes, a comprehensive reform of the VAT rules applicable to bad debts was approved in Parliament.

Table1. Portugal: Quantitative Performance Criteria
(In billions of euros, unless otherwise specified)

	Performance Criteria (unless indicated otherwise)									Indicative Targets
	Mar-12		Jun-12		Sep-12		Dec-12	Mar-13	Jun-13	
	Program	Actual	Program	Actual	Program	Actual				Sep-13
1. Floor on the consolidated General Government cash balance (cumulative)	-1.9	-0.45	-4.4	-4.1	-5.9	-5.5	-9.0	-1.9	-4.5	6.0
2. Ceiling on accumulation of domestic arrears by the General Government (continuous indicative target) 1/	0	Not met	0	Not met	0	Not met	0	0	0	0
3. Ceiling on the overall stock of General Government debt	182.0	171.2	175.0	170.9	177.5	174.2	180.0	182.2	185.3	186.8
4. Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by the general government (continuous performance criterion)	0	0	0	0	0	0	0	0	0	0

1/ Domestic arrears for the purpose of the program increased by €65 between end-July and end-September.

Table 2. Portugal: Structural Conditionality: Sixth Review Under the EFF

	Measure	Timing	Status
Structural Benchmarks			
A. Strengthen financial stability			
1	Make effective the amendments to the Corporate Insolvency Law to better support rescue of viable firms (after completing all necessary legislative and publication requirements)	Mid-June 2012	Met
2	Prepare a proposal for encouraging the diversification of financing alternatives to the corporate sector.	End-July 2012	Met
3	Submit to Parliament amendments to the law governing banks' access to public capital (MEFP ¶18).	End-January 2013	
B. Enhance competitiveness and address bottlenecks to growth			
4	Submit to Parliament draft legislation defining the criteria for extension of collective agreements (including a majority representation threshold) and the modalities for their implementation.	End-Sept 2012	Met with delay
5	Prepare a proposal to implement identified best international practices in order to reinforce the independence of the main sectoral regulators.	End-Sept 2012	Met
6	Submit to Parliament a new Code of Civil Procedure to streamline and speed up the court procedures.	End-Nov 2012	Met
7	Submit to Parliament the bill to implement the judicial roadmap to improve the court structure.	End-Nov 2012	Met
C. Strengthen fiscal institutions and reduce fiscal risks			
8	Develop a PFM strategy covering the next three years, to be attached to the 2013 budget.	Mid-Sept 2012	Met
9	Revise and submit to Parliament the draft regional and local public finance law.	End-Dec 2012	
10	Implement a full-fledged Large Taxpayer Office (LTO), to cover audit, taxpayer services, and legal functions concerning all large taxpayers, including the adoption of account managers.	End-Dec 2012	

PORTUGAL: TECHNICAL MEMORANDUM OF UNDERSTANDING

December 20, 2012

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the indicators subject to quantitative targets (performance criteria and indicative targets), specified in the tables annexed to the Memorandum of Economic and Financial Policies. It also describes the methods to be used in assessing the Program performance and the information requirements to ensure adequate monitoring of the targets. We will consult with the EC, the ECB, and the IMF before modifying measures contained in this letter or adopting new measures that would deviate from the goals of the Program, and provide the EC, the ECB, and the IMF with the necessary information for Program monitoring.

2. For Program purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "Program exchange rates" as defined below, with the exception of the items affecting government fiscal balances, which will be measured at spot exchange rate (i.e., the rate for immediate delivery) prevailing on the date of the transaction. The Program exchange rates are those that prevailed on May 5, 2011. In particular, the exchange rates for the purposes of the Program are set €1 = 1.483 U.S. dollar, €1 = 116.8390 Japanese yen, €1.09512 = 1 SDR.

3. For reporting purposes, the MoF and BdP will employ the reporting standards and templates considered to be appropriate given the transmission of data covered by this TMU, unless otherwise stated or agreed with the EC, the ECB and the IMF.

General Government

4. **Definition.** For the purposes of the Program, the General Government, as defined in the Budget Framework Law, Law No. 91/2001 of August 20, amended by Law 22/2011 of May 20, includes**:**

4.1. The Central Government. This includes:

4.1.1. The entities covered under the State Budget, which covers the budgets of the Central Administration, including the agencies and services that are not administratively and financially autonomous, agencies and services that are administratively and financially autonomous (*Serviços e Fundos Autónomos* – SFA).

4.1.2. Other entities, including Incorporated State-owned enterprises (ISOE), or extra-budgetary funds (EBF) not part of the State Budget, but which are, under the European System of Accounts (ESA95) and ESA95 Manual on Government Deficit and Debt rules, classified by the National Statistical Institute (INE) as part of the Central Government.

4.2. Regional and Local Governments, that include:

4.2.1. Regional Governments of Madeira and Azores and Local Governments (*Administrações Regionais and Locais*);

4.2.2. Regional and local government-owned enterprises or companies, foundations, cooperatives and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government.

4.3. Social Security Funds comprising all funds that are established in the general social security system.

This definition of General Government also includes any new funds, or other special budgetary and extra budgetary programs or entities that may be created during the Program period to carry out operations of a fiscal nature and which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE in the correspondent subsector. The MoF will inform the EC, ECB, and IMF of the creation of any such new funds, programs, entities or operations at the time of its creation or statistical re-classification or, in the case of Regional and Local Governments, at the time the Government acknowledges its creation.

The General Government, as measured for purposes of Program monitoring in 2012, shall not include entities nor operations (including pension funds) that are re-classified into the General Government during 2012, but shall include those reclassified in 2011.[1]

5. **Supporting Material**

5.1. Data on cash balances of the State Budget will be provided to the EC, the ECB and the IMF by the MoF within three weeks after the end of the month. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published by the MoF.

5.2. Data on the cash balances of the other parts of General Government as defined in paragraph 4[2] will be provided to the EC, the ECB and the IMF by the MoF within seven weeks after the end of the month. Data will include detailed information on revenue and expenditure items. Data will also include detailed information on PPP-related revenues and expenditures for those PPP reclassified within the General Government sector according to ESA 95, and called guarantees.

5.3. Data on domestic and external debt redemptions (securities), new domestic and external debt issuance (securities), change in the domestic and foreign currency assets and liabilities of the Central Government at the BdP and other financial institutions will be provided to the EC, the ECB, and the IMF by the BdP within 40 days after the closing of each month.

5.4. BdP will provide to the EC, the ECB, and the IMF detailed monthly data on the financing of the General Government, as defined in ESA95, within seven weeks after the closing of each month.

5.5. Data on the revenues, operating expenses, capital expenditure, remuneration of personnel, EBITDA, and number of staff will be provided for state-owned enterprises (SOEs) on a quarterly basis, within 7 weeks after the end of each quarter. Aggregate data for the SOEs within the perimeter will be provided, with company-specific information for REFER, Estradas de Portugal, Metro de Lisboa, and Metro de Porto. Furthermore data for Comboios de Portugal and Parpública (outside the perimeter) will also be provided.

[1] An operation refers to part of a legal entity that is involved in the production or delivery of goods and services—including government services provided on a nonmarket basis. As such, it does not include transactions relating to the assets or liabilities of an entity. For example, should an entity handle a number of PPPs, reclassifying only one PPP would be considered as reclassifying an operation. In contrast, taking over part of an entity's debt by the government would not qualify for the exclusion. On this issue, see also paragraph 13.

[2] In 2011, data exclude regional and local government-owned enterprises or companies, foundations, cooperatives and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government, i.e., entities referred in paragraph 4.2.2.

QUANTITATIVE PERFORMANCE CRITERIA, INDICATIVE CEILINGS, AND CONTINUOUS PERFORMANCE CRITERIA: DEFINITIONS AND REPORTING STANDARDS

A. Floor on the Consolidated General Government Cash Balance (Performance Criterion)

6. **Definition.** The consolidated General Government cash balance (CGGCB) is defined as the sum of the cash balances of the entities covered by the State Budget, the ISOE, the Regional and Local Governments, and the Social Security Funds, and other entities and EBFs, as defined in paragraph 4. Privatization receipts will be excluded from cash receipts. In 2012 and beyond, revenues from the reclassification of pension funds into the general government will not be accounted for as cash revenues for the purpose of the calculation of the consolidated general government cash balance. In 2012-13, the cash proceeds from the sale of the ANA airport concession will be accounted for as cash expenditure-reducing transactions. The net acquisition of financial assets for policy purposes, including loans and equity participation will be recorded as cash expenditures, except for transactions related to the banking sector support and restructuring strategy under the Program. Called guarantees (excluding those related to the banking sector support and restructuring strategy), where entities of the General Government make cash payments on behalf of entities that are not part of the General Government, will be recorded as cash expenditures.

6.1. **The Cash Balance of the State Budget.** The cash balance of the State Budget will be measured from above the line, based on budget revenues (recurrent revenue plus nonrecurrent revenue, including EU revenues, minus tax refunds) minus budget expenditures of the State Budget as published monthly on the official website of the DGO of the MoF, and in line with the corresponding line items established in the State Budget. Budget expenditures will exclude amortization payments but include salaries and other payments to staff and pensions; grants to Social Security Funds, medical care and social protection; operational and other expenditure, interest payments; cash payments for military equipment procurement; and EU expenses.

6.2. **The Cash Balance of the Regional and Local Governments, Social Security Funds, ISOE and Other Entities or EBFs.** The cash balance of each of these parts of the General Government will be measured from above the line, based on revenues minus expenditures as it will be provided by the DGO of the MoF in the monthly General Government budget execution report (see Para 5), and in line with the corresponding line items established in their respective budgets. All entities including ISOE that prepare accrual-based financial statements will submit monthly cash flow statement in accordance with form and content specified by the MoF. The reporting by Local Government will be phased as set out in paragraph 8 below.

6.3. **Adjustor.** The 2012 and 2013 quarterly floors on the consolidated general government cash balance will be adjusted for the cumulative amount of arrears settled in the context of the arrears clearance strategy: (i) health sector arrears (up to €1.95 billion), and (ii) local government arrears settled through the €1 billion credit facility created in May 2012. The targets will also be adjusted for the clearance of other arrears provided an agreement to this effect was reached with IMF staff.

Other Provisions

7. For the purpose of the program, the expenditure of the central government that is monitored excludes payments related to bank support, when carried out under the program's banking sector and restructuring strategy. However, any financial operation by central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to the EC, ECB, and IMF.

8. Quarterly consolidated accounts for the General Government on a cash basis will be reported for internal, EC, ECB, and IMF monitoring 7 weeks after the reference period, starting with the first quarter of 2012. The

reports will be published externally starting with December 2011 data. SOEs will be consolidated with the general government accounts starting with the first quarter 2012. The larger municipalities (defined as those with a population of 100,000 voters or more) are required to provide monthly reports under current arrangements, and their cash balance will be included in the calculation of the monthly cash General Government balance. The cash balance of the smaller municipalities, i.e. those with a population of under 100,000 voters, will be excluded until any necessary legal changes requiring them to provide monthly reports have been put in place. In this transitory period, the MoF will provide a monthly estimate of the cash balance of these smaller municipalities excluded from the General Government reports to the EC, the ECB, and the IMF.

9. **Supporting Material**

9.1. Data on cash balances of the State Government, ISOEs, Regional and Local Government and Social Security Funds will be provided to the EC, the ECB and the IMF by the MoF within seven weeks after the end of each month. The information provided will include general government net acquisitions of financial assets for policy purposes, including loans and equity participations, as well as called guarantees where entities that are part of the General Government make cash payments on behalf of entities that are not part of the General Government.

9.2. The MoF will submit quarterly data on General Government accounts determined by the INE in accordance with ESA 95 rules, showing also the main items of the transition from cash balances to the General Government balances in national accounts. The reconciliation will be accompanied by necessary explanatory materials for any indication of potential deviation of the annual general government cash target from the annual general government accrual target determined in accordance with ESA 95 rules.

B. Non-Accumulation of New Domestic Arrears by the General Government (Continuous Indicative Target)

10. **Definitions.** Commitment, liabilities, payables/creditors, and arrears can arise in respect of all types of expenditure. These include employment costs, utilities, transfer payments, interest, goods and services and capital expenditure. Commitments are explicit or implicit agreements to make payment(s) to another party in exchange for that party supplying goods and services or fulfilling other conditions. Commitments can be for specific goods and services and arise when a formal action is taken by a government agency, e.g., issuance of a purchase order or signing a contract. Commitment can also be of a continuing nature that require a series of payments over an indeterminate period of time and may or may not involve a contract, e.g. salaries, utilities, and entitlement payments. Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources (usually cash) embodying economic benefits or service potential. In relation to commitment, the liability arises when a third party satisfies the terms of the contract or similar arrangement. Payables/creditors are a subset of liabilities. For the purposes of the program payables/creditors exclude provisions, accrued liabilities. Arrears are a subset of payables/creditors. For the purposes of the Program domestic arrears are defined as payables/creditors (including foreigner commercial creditors), that have remained unpaid for 90 days or more beyond any specified due date (regardless of any contractual grace period). In case no due date is specified, arrears are defined as payables/creditors that have remained unpaid for 90 days or more after the date of the invoice or contract. Data on arrears will be provided within seven weeks after the end of each month. The continuous indicative target of non-accumulation of new domestic arrears requires that the total arrears at the end of any month are not greater than the corresponding total at the end of the previous month—based on the same perimeter with respect to the entities covered. This also includes arrears that are being accumulated by the SOEs not included in the General Government.

11. **Supporting Material.** The stock of arrears will be measured through a survey. Reports on the stock of arrears of the General Government are being published monthly. The MoF will provide consistent data on monthly expenditure arrears of the General Government, as defined above. Data will be provided within seven weeks after the end of each month and will include total arrears classified by the different constituent sectors of the General Government sub-sector as defined in paragraph 4, as well as the monthly amounts of (i) health sector arrears settled with the banks' pension funds transfers' resources, and (ii) local government arrears settled through the €1 billion credit facility created in May 2012.

12. **Adjustor.** The monthly change in the stock of arrears will be adjusted for any stock adjustment related to the arrears clearance strategy: (i) health sector arrears, as well as local government arrears settled through the €1 billion credit facility created in May 2012. This will allow monitoring the underlying flow of new arrears.

C. Ceiling on the Overall Stock of General Government Debt (Performance Criterion)

13. **Definition.** The overall stock of General Government debt will refer to the definition established by Council Regulation (EC) No 479/2009 of 25 May 2009 on the application of the Protocol on the Excessive Deficit Procedure annexed to the Treaty establishing the European Community. For the purposes of the Program, the stock of General Government debt will exclude: (i) debt contracted for bank restructuring, when carried out under the Program's banking sector support and restructuring strategy; (ii) IGCP deposits; and (iii) (from end-September 2011) the *'prepaid margin'* on all EFSF loans.

14. **Adjusters.** For 2012, the ceiling of the overall stock of General Government debt will be adjusted upward (downward) by the amount of any upward (downward) revision to the stock at end-December 2011 general government debt of EUR183.33 billion. From 2013 onwards, the ceiling of the overall stock of General Government debt will be adjusted upward (downward) by the amount of any upward (downward) reclassification of entities or operations that affects the stock at end-December of the previous year.

15. **Supporting Material.** Quarterly data on the total stock of General Government debt as defined in paragraph 12 will be provided to the EC, ECB and IMF by the BdP no later than 90 days after the end of each quarter, as reported to the ECB and the Eurostat. Monthly estimates will be provided to the EC, ECB and IMF by BdP no later than seven weeks after the end of each month.

D. Non-Accumulation of New External Debt Payments Arrears by the General Government (Continuous Performance Criterion)

16. **Definition.** For the purposes of the Program, the definition of debt is the same as in paragraph 12. An external debt payment arrear will be defined as a payment on debt to nonresidents, contracted or guaranteed by the general government, which has not been made within seven days after falling due (taking into account any applicable contractual grace period). The performance criterion will apply on a continuous basis throughout the Program period.

17. **Supporting Material.** Any external debt payment arrears of the General Government will be immediately reported by the MoF.

E. Bank Solvency Support Facility

18. The dedicated Bank Solvency Support Facility (BSSF) account will be maintained at the Bank of Portugal. As per previous review, resources for the BSSF will be agreed at each review and deposited in the dedicated account.

F. Overall Monitoring and Reporting Requirements

19. Performance under the Program will be monitored from data supplied to the EC, the ECB, and the IMF by the MoF and BdP. The authorities will transmit to the EC, ECB, and IMF any data revisions in a timely manner.

ANNEX 6: INDICATIVE TIMELINE

Indicative timeline of financial sector and structural measures in the Memorandum of Understanding on specific economic conditionality[1]

	Actions for the seventh review (to be completed by end Q4-2012)
Fiscal-structural	**[3.7]** Revise the Budget Framework Law to take account of the reinforced EU fiscal framework.
	[3.10] Submit to Parliament the draft proposal to revise the regional finance law.
	[3.14] Design framework for assessing fiscal risks derived from PPP, concessions and other public instruments.
	[3.16] Reach operational balance for SOEs.
	[3.16] Implement the SOEs strategy.
	[3.20] Prepare a strategy for Aguas de Portugal (AdP).
	[3.21] Prepare an inventory of municipalities and regional governments's assets including real estate.
	[3.22] Complete the implementation of the new structure that merges tax, customs and DGITA.
	[3.235 ii] Increase to 30% the number of auditors in the tax administration.
	[3.25] Clear cases above EUR 1 million with the support of the tax court judges.
	[3.26] Implement a full-fledged Large Taxpayer Office (LTO).
	[3.31] Reform the existing framework of central, local and locally-based administration services.
	[3.32 ii] Fully implement the strategy of shared services in central administration in the area of human resources.
	[3.32 iii] Implement shared services in IT.
	[3.35] Prepare a comprehensive review of wage scales.
Financial sector	**[2.10]** Reflect the OIP findings in the implementation of the SIP recommendations on asset quality and stress testing methodologies.
	[2.12] Launch the bidding process in order to select the party managing the credits currently held by Parvalorem.
	[2.13 a] Approve the decree-law on the banks' contributions to the resolution fund.
	[2.13 b] Approve the supervisory notices on recovery plans.
Health care system	**[3.38]** Additional revenue of EUR 150 million following the revision of NHS moderating fees.
	[3.39] The overall budgetary cost of health benefit schemes –ADSE, ADM, SAD-will be reduced by 50% of the employers contribution.
	[3.40] Enact legislation which automatically reduces the price of medicines when the patent expires to 50% of their previous price.
	[3.45] Publish implementation report of the legislation making compulsory the prescription by INN to increase the use of generic medicines.
	[3.49] Publish an action plan concerning the reduction of costs and fighting waste for all entities included in NHS.
	[3.51] Take measures to increase competition among private providers and reduce by 10% the overall spending.

[1] Square brackets identify paragraph numbers in the MoU as signed on 20 December 2012. Items that are Structural Benchmarks under the program are flagged with SB, and also identified by the MEFP paragraph number. Items that are Prior Actions under the program are flagged with PA, and also identified by the MEFP paragraph number.

	[3.57] Implement measures aiming at reducing the operational costs by at least EUR 200 million. **[3.59]** Set up a system for comparing hospital performance on the basis of a comprehensive set of indicators and regular reports. **[3.61]** Reduce hospital operational costs by at least 15%. **[3.63]** Adopt for all staff flexible time arrangements, to reduce by at least 20% spending on overtime compensation in 2012 and another 20% in 2013. **[3.64]** Improve monitoring, internal control and fiscal risks management systems of the Administrações Regionais de Saúde. **[3.66]** Reduce costs for patient transportation by 1/3.
Labour market	**[4.1]** Prepare an analysis on benefit dependency and long-term unemployment. **[4.3]** Submit to Parliament draft legislation aiming at aligning the level of severance payments with the EU average of 12 days. **[4.5 iv]** Prepare an independent review on defining wage norms that into account competitiveness and on the desirability of shortening the survival of contracts that are expired but not renewed. **[4.7]** Present a report on expenditure and financing of ALMPs, the role of job counselling and propose actions to improve the effectiveness of employment and training measures. **[4.8 ii]** Define and implement funding framework for public schools and schools under autonomy agreements. **[4.8 iii]** Reorganise modalities for the provision of VET, enhance students' orientation and career guidance.
Goods and services markets	**[5.1]** Adopt the new regulators' bylaws agreed in July 2012 and ensure they are effective before end of year. **[5.2]** Prepare a report for improving the harmonised mechanism for capacity allocation and congestion management of cross-border flows with Spain. **[5.3]** Clarify the national legal framework with respect to the scope of competencies of the logistics operator. **[5.4]** Conclude the measures aiming at reducing excessive rents and to address the sustainability of the national electricity system. **[5.5]** Conclude the measures to limit the policy costs embedded in CMECs and PPAs. **[5.6]** Present a report on the CMEC scheme. **[5.7]** Conclude the measures to limit the policy costs of renewables under the special regime. **[5.13]** Further liberalise the postal sector by amending the decree-law laying down the framework of the concession contract. **[5.14]** Implement the Strategic Plan for Transport for 2011-2015. **[5.15]** Present a long term vision of the transport system and a list of actions to improve its efficiency and sustainability. **[5.16 ii]** Reduce operational costs of REFER by at least 23% in 2012 compared to 2010. **[5.16 iii]** Ensure that the PSO contracts respect EU legislation and provide a breakdown of state contributions for rail lines under PSO. **[5.16 iv]** Extend the performance scheme on rail infrastructure charges to other operators. **[5.16 vii]** Ensure that the rail terminals (owned by CP Carga) are transferred to another entity guaranteeing non-discriminatory access to all rail freight operators. **[5.17]** Adopt the revised legal framework governing port work. **[5.18]** Deliver and enforce policies that ensure strong integrated policy-making, strategic planning and surveillance functions common to all ports in the country. **[5.19]** Adopt the necessary legislative amendments to achieve full compliance with

	Directive 1999/62/EC and EU Treaty. **[5.20]** Complete the adoption of the outstanding sectorial amendments to comply with the Services Directive. **[5.21]** Adopt the law for professions where regulation does not involve a professional body (Ordens or Câmaras). **[5.23 iii]** Make available in PSC on-line procedures for the registration of establishments covered by "Zero Authorisation".
Housing market	**[6.1]** Bring value of all property stock close to market value and ensure that property valuation is updated regularly.
Competition, public procurement, and business environment	**[7.7]** Monitor the inflow of cases and report on the functioning of the specialised court for Competition, Regulation and Supervision. **[7.8]** Report on the conditions for the proper execution of Competition Authority mandate. **[7.12]** Report on progress on the measures aiming at facilitating access to finance and to export markets for SMEs.
Judicial system	**[3.25]** Assess the need to establish special chambers within the tax tribunals to handle cases with value above EUR 1 million.
Licensing	**[7.17]** Create a working group to analyse the licensing of planned investment projects which are left unsolved or undecided for more than 12 months. **[7.18]** Review the legal regimes at all levels of Government in the area of territorial planning. **[7.20]** Change the legal regime for Environment Impact Evaluation to increase the speed and effectiveness of this regulation and reduce associated money and time costs. **[7.21 ii a]** Implement zero licensing procedures for Type 3. **[7.21 ii d]** Ensure that the new Industrial Licensing is aligned with the review of the New Base Law of Soil and Territorial and Urbanism Planning. **[7.22]** Review the commercial licensing regime. **[7.23]** Review the geological licensing regimes. **[7.24]** Review the licensing in tourism.

Actions for the eighth review (to be completed by end Q1-2013)	
Fiscal structural	**[3.32 i]** Complete the implementation of the strategy of shares services in the area of financial services (GeRFIP).
Health care system	**[3.41]** Publish second price revision for medicines (January 2013). **[3.47]** Produce a report assessing the legislation aimed at removing all effective entry barriers for generic medicines.
Labour market	**[4.1]** Assess if further measures are needed in relation with benefit dependency and long-term unemployment. **[4.6]** Assess in a report the effects of the organised decentralisation. **[4.8 iii]** Establish "professional schools of reference". **[4.8 iv]** Prepare an assessment on the latest developments in the apprenticeship system.
Goods and services markets	**[5.2 i]** Present proposals to harmonise the tariffs for access to the gas interconnection networks. **[5.2 iii]** Apply a harmonised congestion management mechanism to all the interconnection capacity between Portugal and Spain. **[5.8]** Undertake the revision of the co-generation remuneration scheme in line with the framework of the transposition of the efficiency directive. **[5.14 iv]** Reform the transport and infrastructure's regulatory framework. **[5.16 i]** Ensure that the rail regulator enjoys the independence required under the EU

Actions for the eighth review (to be completed by end Q1-2013)	
	rail Directives. **[5.16 v]** Review and render more effective the yield management on long-distance passenger ticket prices. **[5.20]** Approve the remaining required amendments to the sector specific legislation. **[5.25 i]** Adapt the content and information available at the PSC for the 48 amended regimes to ensure conformity with the Services Directive and make available online forms for the completion of procedures. **[5.25 ii]** Adapt the content and information available at the PSC for the 15 regimes to ensure conformity with the Professional Qualifications Directive. **[5.25 iii]** Prepare the extension of the PSC to major municipalities.
Competition, public procurement, and business environment	**[7.10]** Submit a report analysing the impact of the amendments to the revised Public Procurement Code as well as of the enhanced role of the Court of Auditors. **[7.13]** Implement the New Late Payments Directive. **[7.14]** Include all municipalities and all levels of public administration within the scope of the Simplex Programme.
Judicial system	**[7.2]** Prepare quarterly reports on implementation status of measures to achieve reduction of the backlogged enforcement cases.
Licensing	**[7.16]** Study the feasibility of a rule that prohibits at all levels of government the creation of a new regulation generating costs for businesses without elimination of an existing regulation. **[7.18 vi]** Review the RJUE that should be aligned with the new Industrial Licensing regime. **[7.21 ii a]** Implement zero licensing procedures for Type 2 and 3 industries. **[7.21 ii b]** Define and establish the Zones of Responsible Enterprises. **[7.21 ii c]** Create and define standardized industrial licenses. **[7.21 ii e]** Ensure that the new Industrial Licensing is aligned with the review of the RJUE. **[7.24 i]** Eliminate or transforming into a voluntary regime the mechanism of prior communication in Regime for Urbanism and Building.

Actions for the ninth review (to be completed by end Q2-2013)	
Fiscal structural	**[3.19]** Conclude the privatisation or concession of the cargo handling subsidiary of CP Carga. **[3.27]** Develop the plan to implement e-invoicing. **[3.30]** Review the regulation on the creation and the functioning of associations and observatories. **[3.37]** Review the Special Mobility Law.
Health care system	**[3.46]** Introduce in the e-prescription system a first set of guidelines. **[3.62]** Prepare annual reports on plans to reallocate qualified and support staff within the NHS.
Financial sector	**[2.10]** Finalise the update of the treatment of collective impairments expected to be finalised at the latest by end-June 2013.
Labour market	**[4.6]** If needed, prepare an action plan to ensure works council can negotiate wages at firm level. **[4.8 i]** Make operational an analysis, monitoring, assessment and reporting system.
Goods and services markets	**[5.8]** Ensure through annual audits that plant not fulfilling the requirements for co-generation do not receive the support scheme. **[5.11]** Proceed with the designation of universal service providers. **[5.15]** Assess the existing rail, road and port networks and present a set of investment

Actions for the ninth review (to be completed by end Q2-2013)	
	priorities for the 2020 and 2030 horizons. **[5.16 ii]** Provide annual progress reports on the implementation of balancing revenues and expenditures. **[5.16 vi]** Prepare the privatisation of the freight branch of the state-owned rail operator. **[5.23 iii]** Make fully operational the "Zero Authorisation" project. **[5.25 iii]** Make the "Zero Authorisation" platform available to all levels of administration, including municipalities.
Housing market	**[6.3]** Review of the impact of all housing market reforms.
Judicial system	**[7.1]** Eliminate the court backlog.
Licensing	**[7.15]** Carry-out a fully inventory and an analysis of the costs of all regulations in the economy (at central, regional and local levels). **[7.16]** If feasible, put in place the rule that prohibits at all levels of government the creation of the new regulation generating costs for businesses without the elimination of an existing regulation. **[7.21 i]** Fully implement the approved Programme of Responsible Industry (PIR).

Actions for the tenth review (to be completed by end Q3-2013)	
Fiscal structural	**[3.3]** Reduce the number of Servicos e Fundos Autonomos (SFA) in view of reducing budget fragmentation. **[3.15]** Provide annual PPP report on the risks stemming from PPPs and concessions.
Labour market	**[4.4]** Prepare a report on the effects of the changes to the dismissal rules on labour market indicators.
Goods and services markets	**[5.9]** Annual report on new contracts in renewables. **[5.10]** Annual report on new investments in renewables.
Housing	**[6.2]** Rebalance property taxation towards the recurrent real estate tax (IMT), while considering the socially vulnerable.

Actions for the eleventh review (to be completed by end Q4-2013)	
Fiscal-structural	**[3.25 ii]** Reduce the number of municipal tax offices by 25%. **[3.32 i]** GeRFIP to be implemented in the Autonomous region of Madeira and in the Autonomous Region of Azores. **[3.33]** Reduce the number of local branches of line ministries.
Health care system	**[3.53]** Take measures to increase competition among private providers and between public and private providers in relevant areas of service provision. **[3.56]** Change the existing accounting framework and adopt accounting standards and appropriate IT systems for hospitals SOEs.
Goods and services markets	**[5.27 iv]** Extend PSC to services not covered by the Services Directive. **[5.27 v]** Extend the "Zero Authorisation project" abolishing licenses to other sectors of the economy.
Licensing	**[7.19]** Increase a nationwide land registration regime to allow a more equal distribution of benefits and costs in the execution of urban planning.

KC-AH-12-124-EN-N

ISBN 978-92-79-22930-5