PORTUGAL REPUBLIC

Rating Analysis - 10/24/16

*EJR Sen Rating(Curr/Prj) BB+/ N/A
*EJR CP Rating: A3
EJR's 3 yr. Default Probability: 2.7%
Other NRSRO Rating: BB+

Portuguese economic growth has slowed down since the beginning of 2016. New governmental policies of the Socialist Government such as higher minimum wages and reversals of public sector pay cuts have put pressure on public accounts. Private consumption will rise due to higher minimum wages and other social initiatives. Job creation is expected to weaken as additional consumer spending expands. Weak bank conditions might impede additional investments in the economy.

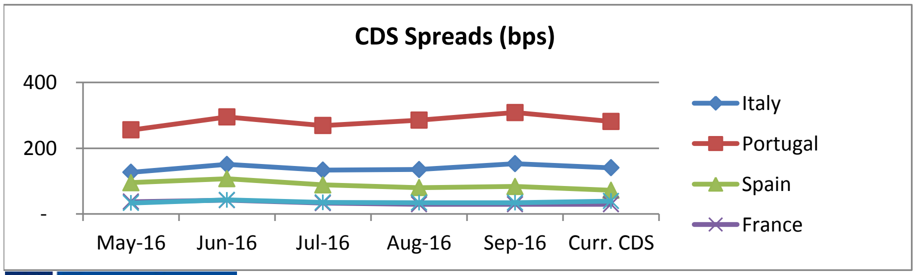
The Debt-to-GDP in 2015 was 129% as compared to 111% in 2011, a trend that is likely to continue. Distress in banking sector will adversely affect the economy, with the need for recapitalization for banking sector, thereby increasing Debt-to-GDP ratio. We have revised our sovereign indicative credit ratios based on the reduced funding costs and other EU support. We are upgrading to "BB+" with a developing watch.

Annual Ratios (source for past results: IMF)

CREDIT POSITION	2013	2014	2015	P2016	P2017	P2018
Debt/ GDP (%)	129.0	130.2	129.0	135.2	140.6	145.3
Govt. Sur/Def to GDP (%)	-5.6	-8.1	-5.1	-4.2	-3.4	-2.5
Adjusted Debt/GDP (%)	129.0	130.2	129.0	135.2	140.6	145.3
Interest Expense/ Taxes (%)	19.3	19.5	18.0	17.8	17.7	17.5
GDP Growth (%)	1.1	1.9	3.4	2.3	2.3	2.3
Foreign Reserves/Debt (%)	0.4	1.3	1.9	1.9	1.8	1.7
Implied Sen. Rating	BB+	BB+	BBB	BBB-	BB+	BB+

INDICATIVE CREDIT RATIOS	AA	A	BBB	BB	B	CCC
Debt/ GDP (%)	100.0	115.0	130.0	145.0	170.0	200.0
Govt. Sur/Def to GDP (%)	2.5	0.5	-2.0	-5.0	-8.0	-10.0
Adjusted Debt/GDP (%)	95.0	110.0	125.0	140.0	160.0	190.0
Interest Expense/ Taxes (%)	9.0	12.0	15.0	22.0	26.0	35.0
GDP Growth (%)	3.5	3.0	2.0	1.0	-1.0	-5.0
Foreign Reserves/Debt (%)	3.0	2.5	2.0	1.5	1.0	0.5

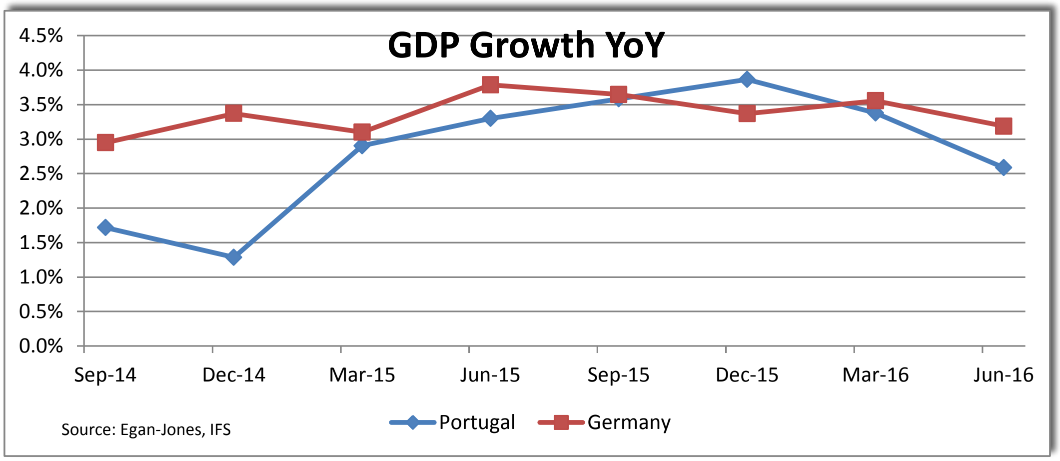
PEER RATIOS	Other NRSRO Sen.	Debt as a % GDP	Govt. Surp. Def to GDP (%)	Adjusted Debt/ GDP	Interest Expense/ Taxes %	GDP Growth (%)	Ratio-Implied Rating*
Federal Republic Of Germany	AAA	71.2	0.6	71.2	6.9	4.1	AA+
French Republic	AA	96.1	-3.4	96.1	6.9	1.9	A+
United Kingdom	AAA	89.2	-3.3	89.2	8.7	4.0	AA
Republic Of Italy	BBB-	132.9	-3.0	132.9	13.9	1.1	BBB-
Kingdom Of Spain	BBB	99.2	-5.3	99.2	13.7	2.1	A+



Country	CDS
Italy	141
Portugal	282
Spain	72
France	30
United Kingdom	39

Economic Growth

As can be seen in the below chart, Portugal's GDP growth improved in 2015, but has weakened recently. Due to policy uncertainty, high corporate debt and weak bank balance sheets, Portuguese GDP growth has slowed, and as a result, inflation has been subdued. The housing market is expected to remain soft until the domestic economy improves. Investments in the economy will probably rise during 2017 because of recovering oil market, increased demand from emerging markets and improved competiveness. Exposures to Germany and Spain needs to be taken into account since Portugal conducts a significant amount of business with both. Watch for tourist pressure from the UK's exit from the EU.



Fiscal Policy

The 2016 budget relies more on consumption taxes than income taxes. This change should aid growth. The incumbent socialist government has emphasized fiscal policy changes such as reversals of public sector pay cuts and higher minimum wages to stoke private consumption. They plan to raise taxes on consumer staples like tobacco and oil to finance the changes in fiscal policy. Also, the budget increases future social benefits. These initiatives are more likely to increase disposable income in particularly low-income households.

	Surplus-to-GDP (%)	Debt-to-GDP (%)	5 Yr. CDS Spreads
Portugal	-5.10	128.98	281.70
Germany	0.57	71.22	18.35
France	-3.35	96.15	29.57
United Kingdc	-3.31	89.24	39.00
Italy	-2.96	132.89	140.72
Spain	-5.32	99.17	72.05

Sources: Thomson Reuters and IFS

Unemployment

Labor market in Portugal is highly segmented. Low productivity and rising labor costs undermined Portuguese exports to the global market thus pressuring growth and unemployment. The unemployment rate has improved from 14.1% in 2014 to 12.6% in 2015. We estimate that the policies put in place to jolt domestic consumption along with moderate decrease in labor force will further improve the employment.

Unemployment (%)

	2014	2015
Portugal	14.10	12.60
Germany	6.70	6.01
France	10.30	10.40
United Kingd	6.14	5.33
Italy	12.65	11.89
Spain	24.50	22.10

Source: Intl. Finance Statistics

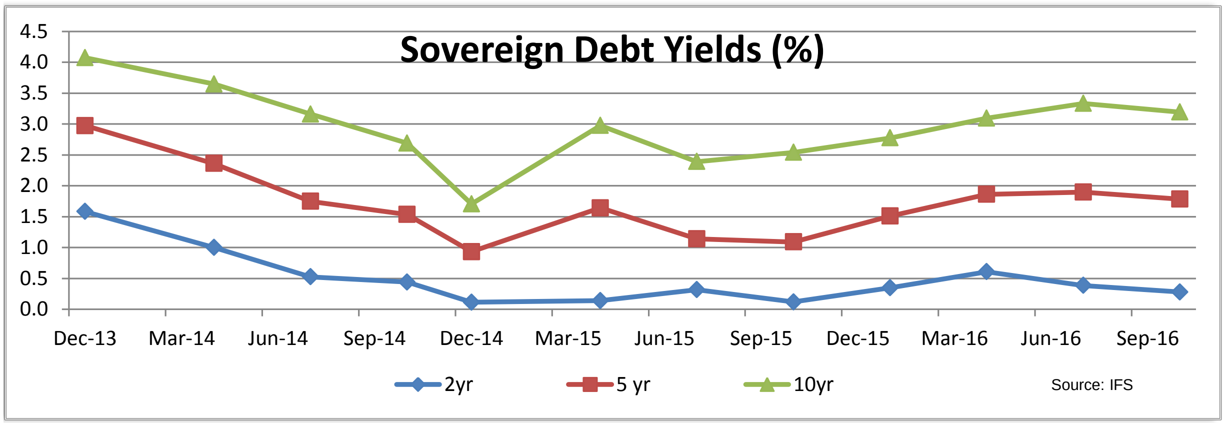
Banking Sector

History has shown that country and bank obligations are linked during times of economic distress. Although the overall size of top banks in Portugal is moderate, which accounts for about 64.4% of GDP, the banking sector is now facing a relatively weakened economy, rising level of non-performing loans and low profitability.

Bank Assets (billions of local currency)	Assets	Cap/ Assets %
Banco Comercial Portugues SA	74.88	1.34
Banco BPI SA	40.67	4.01
Total	115.6	
EJR's est. of cap shortfall at 10% of assets less market cap		8.9
Portugal's GDP		179.4

Funding Costs

Funding costs are high for Portugal as compared to Eurozone average. Current 5 year CDS spread is around 282 bps, which is high compared to Italy's CDS spread at 141 bps. Yields are bound to change as Portuguese debt is included in European Central Bank's sovereign debt purchase programme.



Ease of Doing Business

Major factors for growing the economy are the ease of doing business and the economic freedom; although not the sole factor for determining economic growth, a country which makes it easy for businesses to operate and provides a reasonably free environment to conduct business has a good chance for growth. The chart on the right indicates that with an overall rank of 23 (1 is best, 189 worst) is strong.

The World Bank's Doing Business Survey*	2015 Rank	2014 Rank	Change in Rank
Overall Country Rank:	**23**	**23**	**0**
Scores:			
Starting a Business	13	10	-3
Construction Permits	36	35	-1
Getting Electricity	25	26	1
Registering Property	27	26	-1
Getting Credit	97	90	-7
Protecting Investors	66	64	-2
Paying Taxes	65	65	0
Trading Across Borders	1	1	0
Enforcing Contracts	20	20	0
Resolving Insolvency	8	9	1

* Based on a scale of 1 to 189 with 1 being the highest ranking.

Economic Freedom

As can be seen below, Portugal is above average in its overall rank of 65.3 for Economic Freedom with 100 being the best.

Heritage Foundation 2015 Index of Economic Freedom
World Rank 65.3*

	2015 Rank**	2014 Rank	Change in Rank	World Avg.
Property Rights	70	70	0	42.2
Freedom from Corruption	62	61.1	0.9	41.9
Fiscal Freedom	61.1	60.1	1	77.4
Government Spending	28.8	26.8	2	61.7
Business Freedom	87.5	84.9	2.6	64.1
Labor Freedom	42.9	34.6	8.3	61.3
Monetary Freedom	82.8	79.3	3.5	75.0
Trade Freedom	88	87.8	0.2	75.4
Investment Freedom	70	70	0	54.8
Financial Freedom	60	60	0	48.6

*Based on a scale of 1-100 with 100 being the highest ranking.
**The ten economic freedoms are based on a scale of 0 (least free) to 100 (most free).
Source: The Heritage Foundation

Valuation Driver: Taxes Growth:
PORTUGAL REPUBLIC has grown its taxes of 4.5% per annum in the last fiscal year which is more than the average for its peers. We expect tax revenues will grow approximately 4.5% per annum over the next couple of years and 4.5% per annum for the next couple of years thereafter.

Valuation Driver: Total Revenue Growth:
PORTUGAL REPUBLIC's total revenue growth has been less than its peers and we assumed no growth in total revenue growth over the next two years.

Income Statement	Peer Median	Co. Avg.	Assumptions Yr 1&2	Yr 3,4,5
Taxes Growth%	4.1	4.5	**4.5**	**4.5**
Social Contributions Growth %	2.0	1.7	**1.7**	**1.7**
Grant Revenue Growth %	0.0	NMF		
Other Revenue Growth %	0.0	NMF		
Other Operating Income Growth%	0.0	(6.5)	**(6.5)**	**(6.5)**
Total Revenue Growth%	2.9	1.9	**1.9**	**1.7**
Compensation of Employees Growth%	1.0	(1.1)	**(1.1)**	**(1.1)**
Use of Goods & Services Growth%	2.3	5.2	**5.2**	**5.2**
Social Benefits Growth%	1.8	1.2	**1.2**	**1.2**
Subsidies Growth%	10.0	(3.1)		
Other Expenses Growth%	0.0			
Interest Expense	0.0	3.5	**3.5**	
Currency and Deposits (asset) Growth%	0.0	0.0		
Securities other than Shares LT (asset) Growth%	0.0	0.0		
Loans (asset) Growth%	(2.5)	4.2	**4.2**	**4.2**
Shares and Other Equity (asset) Growth%	0.9	2.9	**2.9**	**2.9**
Insurance Technical Reserves (asset) Growth%	0.0	0.0		
Financial Derivatives (asset) Growth%	0.0	(14.0)	**(5.0)**	**(5.0)**
Other Accounts Receivable LT Growth%	(0.2)	(0.5)	**(0.5)**	**(0.5)**
Monetary Gold and SDR's Growth %	0.0	0.0		
Other Assets Growth%	0.0	0.0		
Other Accounts Payable Growth%	0.0			
Currency & Deposits (liability) Growth%	5.4	20.5	**5.0**	**5.0**
Securities Other than Shares (liability) Growth%	2.4	9.4	**6.6**	**6.6**
Loans (liability) Growth%	0.0	(7.5)	**0.5**	**0.5**
Insurance Technical Reserves (liability) Growth%	0.0	0.0		
Financial Derivatives (liability) Growth%	0.0	(14.7)	**(5.0)**	**(5.0)**
Additional ST debt (1st year)(millions EUR)	0.0	0.0		

ANNUAL INCOME STATEMENTS

Below are PORTUGAL REPUBLIC's annual income statements with the projected years based on the assumptions listed on page 3.

ANNUAL REVENUE AND EXPENSE STATEMENT

(MILLIONS EUR)	2012	2013	2014	2015	P2016	P2017
Taxes	38,739	42,733	43,567	45,530	47,579	49,720
Social Contributions	19,142	20,449	20,371	20,718	21,070	21,429
Grant Revenue						
Other Revenue						
Other Operating Income	14,308	13,605	13,293	12,423	12,423	12,423
Total Revenue	72,190	76,787	77,231	78,671	81,072	83,572
Compensation of Employees	19,688	21,317	20,495	20,264	20,036	19,811
Use of Goods & Services	9,685	9,611	10,079	10,601	11,149	11,726
Social Benefits	33,010	34,785	34,106	34,517	34,933	35,353
Subsidies	1,018	1,031	1,210	1,172	1,172	1,172
Other Expenses				7,862	7,862	7,862
Grant Expense						
Depreciation	5,187	5,092	5,097	5,216	5,216	5,216
Total Expenses excluding interest	74,853	78,018	82,693	79,632	80,368	81,141
Operating Surplus/Shortfall	-2,663	-1,231	-5,462	-961	704	2,431
Interest Expense	8,214	8,258	8,502	8,192	8,482	8,782
Net Operating Balance	-10,878	-9,489	-13,964	-9,153	-7,778	-6,351

*EJR Sen Rating(Curr/Prj) BB+/ N/A
*EJR CP Rating: A3
EJR's 3 yr. Default Probability: 2.7%
Other NRSRO Rating: BB+

ANNUAL BALANCE SHEETS

Below are PORTUGAL REPUBLIC's balance sheets with the projected years based on the assumptions listed on page 3.

ANNUAL BALANCE SHEETS
(MILLIONS EUR)

Base Case

ASSETS	2012	2013	2014	2015	P2016	P2017
Currency and Deposits (asset)					814	814
Securities other than Shares LT (asset)	9,478	9,047	19	3,524	3,524	3,524
Loans (asset)	6,569	6,720	6,582	6,860	7,149	7,451
Shares and Other Equity (asset)	32,828	27,524	32,066	32,994	33,950	34,933
Insurance Technical Reserves (asset)					0	0
Financial Derivatives (asset)	397	-27	21,271	18,285	17,371	16,502
Other Accounts Receivable LT	11,895	10,123	10,312	10,255	10,199	10,143
Monetary Gold and SDR's						
Other Assets					2,558	2,558
Additional Assets	20,164	21,365	5,881	2,558		
Total Financial Assets	81,331	74,751	76,132	74,477	75,565	75,925

LIABILITIES						
Other Accounts Payable						
Currency & Deposits (liability)	13,688	14,748	19,350	23,319	23,319	23,319
Securities Other than Shares (liability)	111,471	112,067	123,528	135,187	144,119	153,640
Loans (liability)	87,196	95,571	100,912	93,313	101,091	107,441
Insurance Technical Reserves (liability)						
Financial Derivatives (liability)	1,200	1,017	1,537	1,311	1,245	1,183
Other Liabilities	20,268	19,438	19,044	16,497	16,497	16,497
Liabilities	233,822	242,841	264,371	269,627	278,492	285,203
Net Financial Worth	-152,491	-168,090	-188,240	-195,150	-202,928	-209,278
Total Liabilities & Equity	81,331	74,751	76,132	74,477	75,565	75,925

Comments on the Difference between the Model and Assigned Rating

SEC Rule 17g-7(a) Disclosure

Below are the disclosures as required by Paragraph (a) of Rule 17g-7.

1. The symbol in the rating scale used to denote the credit rating categories and notches within categories and the identity of the obligor, security, or money market instrument as required by Paragraph (a)(1)(ii)(A) of Rule 17g-7:
For the issuer PORTUGAL REPUBLIC with the ticker of 1174Z PL we have assigned the senior unsecured rating of BB+. There are three notches in our rating categories (e.g., A-, A, and A+) other than those deep into speculative grade; for CC, C, and D there are no notches.

2. The version of the procedure or methodology used to determine the credit rating as required by Paragraph (a)(1)(ii)(B) of Rule 17g-7:
We are using the methodology available in our Form NRSRO Exhibit #2 dated May 10, 2015 available via egan-jones.com under the tab at the bottom of the page "Methodologies".

3. The main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating as required by Paragraph (a)(1)(ii)(C) of Rule 17g-7:
The credit rating assigned reflects our judgement regarding the future credit quality of the issuer. Regarding the specific assumptions used, please refer to page 3 of this Rating Analysis Report.

4. The potential limitations of the credit rating as required by Paragraph (a)(1)(ii)(D) of Rule 17g-7:
Our rating pertains solely to our view of current and prospective credit quality. Our rating does not address pricing, liquidity, or other risks associated with holding investments in the issuer.

5. Information on the uncertainty of the credit rating as required by Paragraph (a)(1)(ii)(E) of Rule 17g-7:
Our rating is dependant on numerous factors including the reliability, accuracy, and quality of the data relied used in determining the credit rating. The data is sourced from publicly-available 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources. In some cases, the information is limited because of issues such as short operating histories, the lack of reported data, a delay in reporting data, restatements, inaccurate accounting, and other issues. Such shortcomings are not always readily apparent. EJR aims to identify such shortcomings and make adjustments using its best judgement.

6. Whether and to what extent third-party due diligence services have been used in taking the rating action as required by Paragraph (a)(1)(ii)(F) of Rule 17g-7:
EJR does not utilize third-party due diligence services.

7. How servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating as required by Paragraph (a)(1)(ii)(G) of Rule 17g-7:
Servicer or remittance reports normally pertain to structured finance issuers; this report does not pertain to a structured finance issuer (EJR is not an NRSRO for structured finance or sovereigns/ municipal issuers). Regarding surveillance, the minimum time period for corporation issuers is normally one year.

8. A description of the data that were relied upon for the purpose of determining the credit rating as required by Paragraph (a)(1)(ii)(H) of Rule 17g-7:
EJR uses 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources for ratings on publicly-traded issuers. In the case of private issuers, EJR relies on information provided mainly by issuers.

9. A statement containing an overall assessment of the quality of information available and considered in the credit rating as required by Paragraph (a)(1)(ii)(I) of Rule 17g-7: The information is generally high quality and readily avail.

10. Information relating to conflicts of interest as required by Paragraph (a)(1)(ii)(J) of Rule 17g-7:
This rating is unsolicited.

11. An explanation or measure of the potential volatility of the credit rating as required by Paragraph (a)(1)(ii)(K) of Rule 17g-7:
Our rating aims to assess the probability of the payment of obligations in full and on-time. Factors which affect such probability, and in turn our rating, include changes in the operating performance of the issuer, changes in capital structure, and merger and acquisition events.

12. Information on the content of the credit rating as required by Paragraph (a)(1)(ii)(L) of Rule 17g-7:
Regarding the historical performance of the credit rating, our rating transition matrix is available in our Form NRSRO, exhibit 1. The expected probability of default and the expected loss in the event of default is listed on the first page of this report.

13. Information on the sensitivity of the credit rating to assumptions as required by Paragraph (a)(1)(ii)(M) of Rule 17g-7:
Below is a summary of the impact of the 5 assumptions which independently would have the greatest impact on our "ratio-implied rating":

	Assumptions			Resulting Ratio-Implied Rating		
	Base	Optimistic	Pessimistic	Base	Optimistic	Pessimistic
Taxes Growth%	4.5	8.5	0.5	BB+	BB+	BB+
Social Contributions Growth %	1.7	(1.3)	4.7	BB+	BB+	BB+
Other Revenue Growth %		(3.0)	3.0	BB+	BB+	BB+
Total Revenue Growth%	1.9	0.1	3.9	BB+	BB+	BB+
Monetary Gold and SDR's Growth %	-	(2.0)	2.0	BB+	BB+	BB+

14. If the credit rating is assigned to an asset-backed security, a description of: (i) the representations, warranties, and enforcement mechanisms available to investors; and (ii) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities, as required by Paragraph (a)(1)(ii)(N) of Rule 17g-7:
This credit rating is not assigned to an asset-backed security.

ATTESTATION FORM

In compliance with the US Securities and Exchange Commission (SEC) Rule 17g-7(a), the Egan-Jones analyst who published the report is responsible for the rating action and to the best knowledge of the person:

1) No part of the credit rating was influenced by any other business activities,
2) The credit rating was based solely upon the merits of the obligor, security, or money market instrument being rated, and
3) The credit rating was an independent evaluation of the credit risk of the obligor, security, or money market instrument.

Analyst Signature: **Today's Date**

Mike Huang
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Mike Huang
Rating Analyst

October 24, 2016
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Reviewer Signature: **Today's Date**

Caroline Ding
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Caroline Ding
Rating Analyst

October 24, 2016
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Sovereign Rating Methodology (Non-NRSRO)

Scope and Limitations: Sovereign Issuer Credit Quality Ratings (CQR) are a forward- looking assessment of a sovereign's capacity and willingness to honor its existing and future obligations in full and on time. Sovereigns are assigned two CQRs: a Local-Currency CQR, which reflects the likelihood of default on debt issued and payable in the currency of the sovereign, and a Foreign-Currency CQR, which is an assessment of the credit risk associated with debt issued and payable in foreign currencies.

Key Rating Drivers: EJR's approach to sovereign risk analysis is a synthesis of quantitative and qualitative judgments. The quantitative factors EJR uses are:

- Debt in relation to GDP.
- Surplus or deficit in relation to GDP.
- Debt plus potential under-funding of major banks in relation to GDP.
- Interest expense in relation to taxes.
- GDP growth.
- Foreign reserves in relation to debt.

Debt levels for many sovereign issuers have increased at an accelerating rate over the past decade, affecting implied ratings. EJR also considers unemployment levels and funding costs. EJR recognizes that no model can fully capture all the relevant influences on sovereign creditworthiness, meaning that the its sovereign ratings can and do differ from those implied by the rating model. Some of the qualitative factors that impact its ultimate assessment of credit quality include the flexibility, stability and overall strength of the economy, efficiency of tax collection, acceptance of contract law, ease of doing business, trade balances, prospects for future growth and health and monetary policy, and economic freedom. These subjective and dynamic qualitative issues are not captured by the model but affect sovereign ratings

For additional information, please see Exhibit 2: Methodologies in EJR's Form NRSRO.