PORTUGAL REPUBLIC

Rating Analysis - 12/26/18

*EJR Sen Rating(Curr/Prj) BBB-/ BBB-
*EJR CP Rating: A2
EJR's 3 yr. Default Probability: 2.3%

The Portuguese economy has move along on an expansionary path, at a pace of growth in line with that currently projected by the ECB for the euro area as a whole.

The economy continues to benefit from a favourable economic and financial environment, which is reflected in a strong domestic demand but GDP growth in Portugal is expected to slow down in 2019 and 2020 as net exports weaken. GDP growth is forecast to slow to 1.8% in 2019 and to 1.7% in 2020. Risks to the forecast appear broadly balanced as the uncertainty in external markets could be compensated by a more positive performance in domestic demand. The slight moderation seen in job creation points to some slowdown in household demand, which would be only partly offset by the expected increase in wage growth. Stronger investment, skills, and productivity will increasingly be the basis for sustainable income gains. Upgrading.
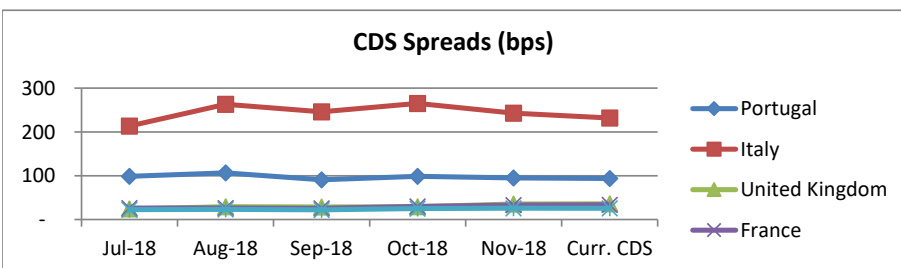
CREDIT POSITION		Annual Ratios (source for past results: IMF)				
	2015	2016	2017	P2018	P2019	P2020
Debt/ GDP (%)	128.8	129.9	125.7	125.5	123.9	120.8
Govt. Sur/Def to GDP (%)	-5.0	-3.3	-3.9	-2.6	-1.3	0.1
Adjusted Debt/GDP (%)	128.8	129.9	125.7	125.5	123.9	120.8
Interest Expense/ Taxes (%)	18.0	16.7	15.3	15.1	14.8	14.5
GDP Growth (%)	3.9	3.7	4.4	2.3	2.3	2.5
Foreign Reserves/Debt (%)	1.9	3.6	3.1	4.7	4.2	5.9
Implied Sen. Rating	BBB-	BBB-	BBB-	BB+	BBB-	BBB-

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	64.1	1.0	64.1	4.4	3.7	AA
French Republic	AA	97.0	-2.5	97.0	6.3	2.8	A
Kingdom Of Belgium	AA	103.1	-0.7	103.1	9.9	3.8	AA-
Republic Of Italy	BBB-	131.8	-3.0	131.8	13.1	2.1	BBB
United Kingdom	AA	87.4	-0.8	87.4	8.1	3.4	AA+

CDS Spreads (bps)

Country	CDS
Portugal	93
Italy	232
United Kingdom	36
France	34
Belgium	26

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Economic Growth

The Portuguese economy has grown over the past couple of years. The nominal GDP growth rate has fallen within the range from 3.3% to 4.7% since Sep 2016.

The Portuguese GDP growth rate increased from Sep 16 to the end of 2017. The nominal GDP growth rate reached 4.7%, which according to the Portuguese National Statistics Office has achieved its strongest growth since 2000. This was a result of positive eurozone economic situation in 2017. The growth in exports was strong with an increase in equipment exports. Exports of services were also boosted by a rise in the numbers of tourists. However, economic growth rate of Portuguese gradually slowed in 2018 due to a faster fall in exports compared to imports. We expect the economy will expand at a slightly weaker pace in the next year.

Source: IFS
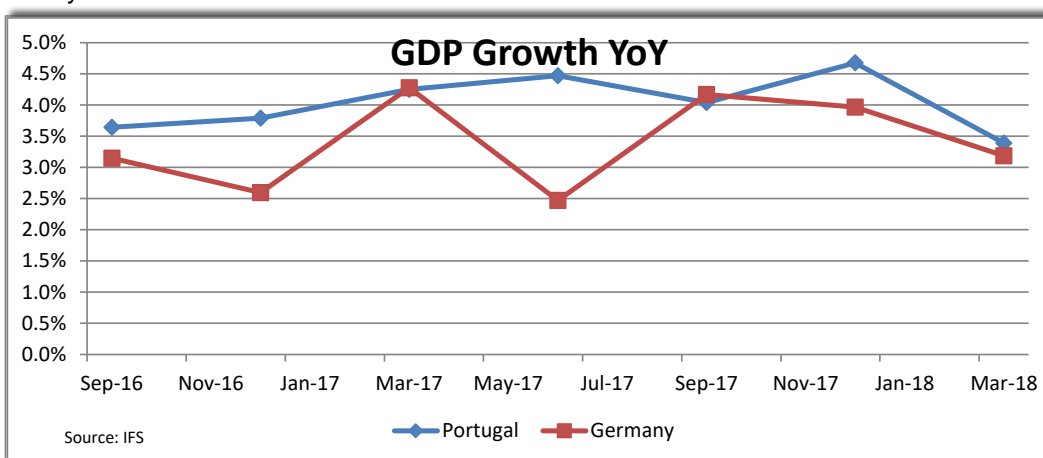
Fiscal Policy

Although the Portugal still has the third largest public debt in the European Union in 2017, the country has decreased their debt-to-GDP ratio slightly from 129.9% to 125.7% over the past couple of years. Portugal's excessive budget deficit also has been corrected in a sustainable and lasting way. Government of Portugal cut the budget deficit by more than half to under 2.1% of GPD in 2016, and kept the deficit well under 3%, which complied with the euro zone's fiscal rules.

	Surplus-to-GDP (%)	Debt-to-GDP (%)	5 Yr. CDS Spreads
Portugal	-3.92	125.70	93.42
Germany	1.02	64.10	13.36
France	-2.54	97.00	33.64
Belgium	-0.73	103.10	35.75
Italy	-2.96	131.80	232.05
United Kingdo	-0.79	87.40	25.59
Sources: Thomson Reuters and IFS			

Unemployment

Portugal's unemployment rate declined to 8.97% in 2017 from 11.18% in previous year, the rate reached a 14-year low at 6.7 percent in the Q2 2018. The employment growth has come from full time workers and employees rather than the part-time and the self-employed. The wages growth rate has fallen into the range from 2% to 8% since 2016, much higher than inflation rate in the same period, which fluctuated between 0.25% to 2%.

Unemployment (%)		
	2016	2017
Portugal	11.18	8.97
Germany	4.13	3.76
France	10.07	9.43
Belgium	4.91	4.40
Italy	11.68	11.23
United Kingd	7.86	7.16
Source: Intl. Finance Statistics		

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Banking Sector

The top 3 banks in Portugal have total assets that equals approximately 58.9% of the GDP. In spite of the improvement in the economic situation, the banking system remains fragile. The credit for many companies remains weak. Low profitability, as a result of the high level of non-performing loans, will continue to slow the internal recapitalization of the banks. This will prevent small and medium enterprises from having easier access to credit. High levels of corporate and household debt, weak credit, rising energy prices and uncertainties in the Eurozone still loom as risk factors for the Portuguese economy in 2019.

Bank Assets (billions of local currency)		
		Mkt Cap/
	Assets	Assets %
Banco Comercial Portugues SA	71.94	5.09
Banco BPI SA	29.64	7.20
BANIF BANCO INTERNACIONAL D	13.13	1.76
Total	114.7	
EJR's est. of cap shortfall at		
10% of assets less market cap		5.4
Portugal's GDP		194.6

Funding Costs

Portugal is a member of the European Union which has adopted the euro. Portugal's benchmark interest rate is set by the European Central Bank. The benchmark interest rate In the Euro Area was last recorded at 0 percent. The Portugal's 10Y Government Bond has a 1.795% yield, 10 Years vs 2 Years bond spread is 204.3 bp, which is high compared to most eurozone countries.

Sovereign Debt Yields (%)

Source: Thomson Reuters
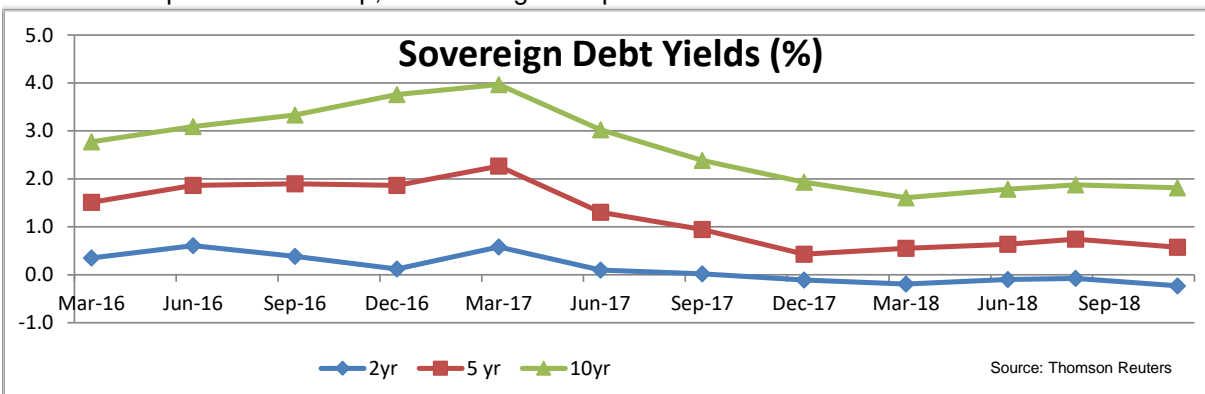
Ease of Doing Business

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 29 (1 is best, 189 worst) is strong.

The World Bank's Doing Business Survey*			
	2018	2017	Change in
	Rank	Rank	Rank
Overall Country Rank:	**29**	**25**	**-4**
Scores:			
Starting a Business	48	32	-16
Construction Permits	32	35	3
Getting Electricity	58	50	-8
Registering Property	28	27	-1
Getting Credit	105	101	-4
Protecting Investors	57	70	13
Paying Taxes	38	38	0
Trading Across Borders	1	1	0
Enforcing Contracts	19	19	0
Resolving Insolvency	15	7	-8
* 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 63.4 for Economic Freedom with 100 being best.

Heritage Foundation 2018 Index of Economic Freedom World Rank 63.4*				
	2018 Rank**	2017 Rank	Change in Rank	World Avg.
Property Rights	69.2	73.3	-4.1	51.5
Government Integrity	56.8	59.0	-2.2	42.1
Judical Effectiveness	70.1	68.9	1.2	46.9
Tax Burden	59.8	59.8	0.0	76.7
Gov't Spending	29.8	25.1	4.7	63.5
Fiscal Health	46.0	32.1	13.9	66.3
Business Freedom	83.2	86.4	-3.2	64.8
Labor Freedom	44.1	43.4	0.7	58.9
Monetary Freedom	85.3	85.9	-0.6	76.0
Trade Freedom	86.9	87.0	-0.1	75.9
*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				

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*EJR Sen Rating(Curr/Prj) BBB-/ BBB-

*EJR CP Rating: A2

EJR's 3 yr. Default Probability: 2.3%

Credit Quality Driver: Taxes Growth:

PORTUGAL REPUBLIC has grown its taxes of 5.0% per annum in the last fiscal year which is disappointing. We expect tax revenues will grow approximately 5.0% per annum over the next couple of years and 5.0% per annum for the next couple of years thereafter.

Credit Quality Driver: Total Revenue Growth:

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

Income Statement	Peer Median	Issuer Avg.	Assumptions Yr 1&2	Yr 3,4,5
Taxes Growth%	5.0	5.0	5.0	5.0
Social Contributions Growth %	3.2	5.1	5.0	5.0
Grant Revenue Growth %	0.0	NMF		
Other Revenue Growth %	0.0	NMF		
Other Operating Income Growth%	0.0	(2.4)	(2.4)	(2.4)
Total Revenue Growth%	4.1	3.9	3.9	3.5
Compensation of Employees Growth%	0.0	1.9	1.9	1.9
Use of Goods & Services Growth%	0.3	0.0		
Social Benefits Growth%	2.1	1.4	1.4	1.4
Subsidies Growth%	3.0	(11.2)		
Other Expenses Growth%	0.0			
Interest Expense	1.8	3.1	3.1	
Currency and Deposits (asset) Growth%	0.0	0.0		
Securities other than Shares LT (asset) Growth%	0.0	0.0		
Loans (asset) Growth%	1.7	(4.9)	(4.9)	(4.9)
Shares and Other Equity (asset) Growth%	0.0	0.0		
Insurance Technical Reserves (asset) Growth%	0.0	0.0		
Financial Derivatives (asset) Growth%	0.0	0.0		
Other Accounts Receivable LT Growth%	0.0	0.0		
Monetary Gold and SDR's Growth %	0.0	0.0	5.0	5.0
Other Assets Growth%	0.0	0.0		
Other Accounts Payable Growth%	0.0			
Currency & Deposits (liability) Growth%	0.0	76.9	5.0	5.0
Securities Other than Shares (liability) Growth%	0.0	0.0		
Loans (liability) Growth%	(2.0)	(13.1)	0.5	0.5
Insurance Technical Reserves (liability) Growth%	0.0	14.6	2.0	2.0
Financial Derivatives (liability) Growth%	0.0	0.0		
Additional ST debt (1st year)(millions EUR)	0.0	0.0		

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EJR's 3 yr. Default Probability: 2.3%

ANNUAL INCOME STATEMENTS

Below are PORTUGAL REPUBLIC's annual income statements with the
projected years based on the assumptions listed on page 5.

ANNUAL REVENUE AND EXPENSE STATEMENT
(MILLIONS EUR)

	2014	2015	2016	2017	P2018	P2019
Taxes	43,564	45,598	46,428	48,743	51,180	53,739
Social Contributions	20,458	20,784	21,609	22,705	23,840	25,032
Grant Revenue						
Other Revenue						
Other Operating Income	13,173	12,368	11,669	11,393	11,393	11,393
Total Revenue	77,195	78,750	79,706	82,841	86,413	90,164
Compensation of Employees	20,515	20,349	20,881	21,270	21,666	22,070
Use of Goods & Services						
Social Benefits	34,088	34,711	35,114	35,615	36,123	36,639
Subsidies	1,230	1,123	976	867	867	867
Other Expenses				19,892	19,892	19,892
Grant Expense						
Depreciation	5,088	5,238	5,266	5,341	5,341	5,341
Total Expenses excluding interest	82,676	79,467	78,076	82,985	83,889	84,809
Operating Surplus/Shortfall	-5,481	-717	1,630	-144	2,524	5,356
Interest Expense	8,482	8,211	7,760	7,475	7,703	7,939
Net Operating Balance	-13,963	-8,927	-6,130	-7,621	-5,179	-2,583

PORTUGAL REPUBLIC

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EJR's 3 yr. Default Probability: 2.3%

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ANNUAL BALANCE SHEETS

Below are PORTUGAL REPUBLIC's balance sheets with the projected years based on
the assumptions listed on page 5.

Base Case	ANNUAL BALANCE SHEETS (MILLIONS EUR)					
ASSETS	**2014**	**2015**	**2016**	**2017**	**P2018**	**P2019**
Currency and Deposits (asset)					5,300	5,300
Securities other than Shares LT (asset)	4,426	3,356	3,387	2,723	2,723	2,723
Loans (asset)	5,131	5,189	5,197	4,941	4,698	4,466
Shares and Other Equity (asset)						
Insurance Technical Reserves (asset)					0	0
Financial Derivatives (asset)						
Other Accounts Receivable LT					0	0
Monetary Gold and SDR's						
Other Assets					67,239	67,239
Additional Assets	65,815	64,578	70,604	67,239		
Total Financial Assets	75,372	73,123	79,188	74,903	79,960	79,728
LIABILITIES						
Other Accounts Payable						
Currency & Deposits (liability)	3,613	-9,447	-5,993	-10,600	-10,600	-10,600
Securities Other than Shares (liability)						
Loans (liability)	101,314	93,651	87,758	76,241	81,420	84,003
Insurance Technical Reserves (liability)	123,596	135,189	140,093	160,478	163,688	166,961
Financial Derivatives (liability)						
Other Liabilities	36,694	51,497	51,898	59,695	59,695	59,695
Liabilities	265,217	270,890	273,756	285,814	296,050	298,402
Net Financial Worth	-189,845	-197,767	-194,568	-210,911	-216,090	-218,673
Total Liabilities & Equity	75,372	73,123	79,188	74,903	79,960	79,728

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Comments on the Difference between the Model and Assigned Rating

In this case, there has been little change in the recent results and therefore we have used our best judgement in making adjustmer which are reflected in the results for the projected ratings. We have assigned a rating of "BBB-" whereas the ratio-implied rating for most recent period is "BBB-"; the median rating for the peers is significantly higher than the issuer's rating.

Changes in Indicative Ratios

We have not made any adjustment in the indicative ratios at this time.

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 BBB-. 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 Nov 5, 2018 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.

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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%	5.0	9.0	1.0	BBB-	BBB-	BBB-
Social Contributions Growth %	5.0	8.0	2.0	BBB-	BBB-	BBB-
Other Revenue Growth %		3.0	(3.0)	BBB-	BBB-	BBB-
Total Revenue Growth%	3.9	5.9	1.9	BBB-	BBB-	BBB-
Monetary Gold and SDR's Growth %	5.0	7.0	3.0	BBB-	BBB-	BBB-

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:
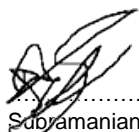This credit rating is not assigned to an asset-backed security.

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.

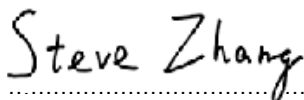**Analyst Signature:**   **Today's Date**

December 26, 2018

………………………………………..   ……………………………………
Subramanian NG
Senior Rating Analyst

Reviewer Signature: **Today's Date**

December 26, 2018

………………………………………..   ……………………………………
Steve Zhang
Senior Rating Analyst

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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.