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OFF THE CLOCK

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Holding Steady

A year on from its bailout exit Portugal's economy continues to strengthen.

By Maria Jackson

In May 2014, Portugal took the brave decision to exit its €78 billion ($108 billion) rescue program without seeking a precautionary credit line from lenders. At the time the move looked risky: Portugal's debt levels were the third highest in the euro region in terms of percentage of gross domestic product (GDP), hovering at around €214 billion ($293 billion). Over a year later and the bold step looks to have paid off. In 2014, Portugal's economy grew by 0.9 percent, following a 6 percent contraction during 2011 - 2013. Importantly, growth continues to gain traction, with GDP expanding by 0.3 percent in the third quarter of 2014 and 0.5 percent in the fourth quarter, according to the National Statistical Institute of Portugal. In the first quarter of 2015 the Iberian country recorded its fourth consecutive quarter of growth and the consensus is that the country's austerity measures have been successful.

"Portugal is a very good example of a successful austerity program. There were significant doubts along the way, especially in the initial part of the program when it seemed like everything was going against us. However, 12 months after we exited the bailout program the indicators are very positive," says Duarte Garin, head of the Lisbon office at Iberian law firm Uría Menéndez. "GDP has increased

for several consecutive quarters; the unemployment rate has fallen to pre-program levels; the commercial trade balance is positive; and exports have significantly increased. It is a very good result."

TAKING ITS MEDICINE

Portugal's success has been hard-fought and its government deserves credit for efficiently managing to steer the country back towards the right course. Among the tough decisions taken following the bailout, Portugal committed itself to a far-reaching privatization program, raised taxes on a broad range of items and significantly reduced public spending. The government's substantial asset sale has helped to keep law firms busy, while distress in the banking sector has also led to a plethora of deals in that segment.

"During the last couple of years, large law firms in Portugal have benefitted from major M&A deals deriving from the aggressive privatization program resulting from the bailout," says Diogo Leónidas Rocha, partner in the Lisbon office of international law firm Garrigues. "The Banco Espírito Santo bankruptcy has also created exceptional workflow for large law firms, due to the substantial sale of assets of both the banking and the non-banking groups. As an example, Garrigues assisted Chinese company Haitong in the acquisition of BESI, the investment banking subsidiary of Banco Espírito Santo, and also assisted Banco Santander in the acquisition of Novo Banco, the transition bank resulting from the BES resolution measure."

Although still in its early stages, Portugal's recovery has been steady and is expected to continue on the back of recent key reforms. Indeed, the government forecasts that the economy will grow by 1.6 percent in 2015.

"Clearly, the structural reforms and measures taken by the Portuguese Government have been decisive in setting up the basis for recovery. These measures have had an impact in areas such as employment, competiveness, tax, insolvency and the public sector," says Carlos Rueda, resident partner of Gómez-Acebo & Pombo's Lisbon office. "As a result of this, Portugal has dynamized its labor market, reduced its indebtedness, facilitated the creation of enterprises and has seen its internal consumption increase."

The government's structural reforms were designed to promote competition across various areas of the economy and inject flexibility into the labor market, and the success of these reforms have been widely applauded by external agencies. According to the Organization for Economic Cooperation and Development (OECD)'s Going for Growth exercise, Portugal is considered among the OECD countries with the best recent track record of responsiveness to structural reform recommendations. Indeed, its reforms since 2009 are projected to raise productivity and potential GDP by at least 3.5 percent by 2020.

"Reforms in the labor market, the judicial system and the tax framework, among many others, have reshaped the face of the Portuguese economy, which is now more competitive, sustainable and investment friendly," says Tomás Pessanha, head of the Oporto office at PLMJ, which is Portugal's largest law firm. "As proof of this, Portugal has recently been considered as one of the very best countries to do business in Europe, ahead of the Netherlands, Belgium, Spain, France and Italy, just to mention a few of its illustrious European peers."

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FOREIGN INVESTMENT

The country's emphasis on boosting private investment has been particularly evident since the onset of its recession. On the employment side, Portugal has passed a raft of new legislative measures including making it easier for employers to hire and fire workers, reforming personal income tax and reducing severance pay. On the tax side, Portugal's Corporate Income Tax Code Reforms came into effect in January 2014, which aimed to simplify the existing tax environment and lighten the bureaucratic load. Among the key measures ushered in by the new tax regime were a reduction in statutory tax rates, the definition of a new international tax policy and a new participation exemption regime. In 2015, these reforms were followed up by a reduction in the corporate tax rate from 23 percent to 21 percent, along with several other measures.

"Foreign investors have clearly returned to the Portuguese market," says Rocha. "Recent tax reforms have been made with the intention of creating a more competitive environment for foreign companies to invest in the Portuguese market."

The statistics speak for themselves. According to the United Nations Conference on Trade and Development (UNCTAD)'s Inward FDI Performance Index, in 2013 inward FDI inflows to Portugal were worth $2,234 million but in 2014 that nearly quadrupled to $8,807 million.

In addition to the tax reforms, the country's high-profile Golden Visa Program has also proved a hit with foreign investors. In October 2012, Portugal launched the initiative as a fast track way for foreign investors from non-European Union countries to obtain a fully valid residency permit in Portugal and to travel freely within the majority of European countries. To obtain a Golden Visa, a foreign investor needs to fulfill one of the following criteria: make a property acquisition worth €500,000 (around $550,000) or more; make a transfer of funds above €1 million ($1.1 million); or create at least 30 jobs in Portugal.

"The Golden Visa Program and more recently the expat incentives (through the launching of a low-tax non-habitual residents scheme) has indeed attracted the interest of high-net-worth individuals and considerable investment, especially in real estate," says Pessanha. "For the sake of illustration, our Golden Visa Program has been widely recognized as one of the best in the world."

"Recent tax reforms have aimed to create a more competitive environment for foreign companies to invest in the Portuguese market."

—DIOGO LEÓNIDAS ROCHA, PARTNER IN THE LISBON OFFICE OF GARRIGUES

Data from the Portuguese Government shows that from October 2012 to June 2015 the program raised a total investment volume of around €1.5 billion (around $1.6 billion). Law firms report that investment into the program is originating mainly from Chinese individuals and this is borne out by government statistics that show China was home to 1947 investors into the program during the time frame outlined above. By way of contrast Brazil, which was the second most important investor country of origin, was home to 87 investors. Indeed, UNCTAD figures show that overall Portugal became the fourth favorite destination for Chinese FDI in the European Union in 2014.

DUARTE GARIN
URÍA MENÉNDEZ

DIOGO LEÓNIDAS ROCHA
GARRIGUES

A STRONG PIPELINE

Despite the current volatility in European markets brought about by the Greece crisis Portugal's outlook remains positive, with firms reporting that the deal market is looking robust.

"Exports, the industrial sector and tourism are key bright spots in the economy and the firm is booming in the M&A and real estate/tourism areas - we have seen a huge increase in activity in these sectors," says Garin. "On the real estate side particularly, we are having difficulty coping with the amount of sizeable projects being developed in Portugal. Generally speaking, Portugal is around 12-18 months behind Spain in terms of business trends and we are now seeing Spain's real estate boom spill over into Portugal."

Other firms are also quick to pinpoint the real estate sector as a continuing source of transactional activity going forward, with new legislation in the UCITS area being eyed as a potential deal driver.

"Recently Portugal revamped the tax landscape of UCITS (including real estate funds) and is scheduled to introduce a separate Real Estate Investment Trust (REIT) regime targeting non-UCITS fund structures for 2016 onwards," says Rocha. "Taking into account the continuous interest of foreign investors in Portuguese real estate it is expected that the broadening of legal structures available for real estate investments may bring further work in this field. Also, if this is confirmed, the creation of specific legislation for REITs in Portugal will also benefit from the momentum we are now witnessing in terms of real estate activity."

As foreign investment receipts grow and new sectors of the economy continue to strengthen, Portugal's uptick looks increasingly solid. In summary, it may be action stations for governments in other parts of Europe but Portugal continues to track a steady course towards economic recovery. ■