Washington, October 17, 2012

In response to media queries on Portugal, IMF mission chief Abebe Aemro Selassie issued the following statement in Washington today:

The Fund's advice on fiscal adjustment remains pragmatic and consistent: it is necessary in countries with high debt burden and limited recourse to financing -- the situation in which Portugal finds itself now. These countries need to undertake fiscal adjustment, paying heed as much as possible to the impact on growth and other macroeconomic variables. But country circumstances are important. As IMF Managing Director Christine Lagarde put it recently, "a fiscal adjustment program over a period of time cannot be one size fits all. It has to be adjusted based on the parameters of each country, it depends on its pace of growth, it depends on the market pressure upon it, and it depends on the weight of debt that is upon it, as well, and therefore it has to be adjusted very specifically to each country."

During the 5th review, in light of the large revenue shortfalls and, higher unemployment in 2012, and in order to avoid too strong an impact on growth in 2013, the government argued for the deficit targets under the program to be relaxed.

The government's case for such a relaxation was strong. First, financing conditions had improved markedly, with yields on government bonds at the bottom end of their trading range over the past year. Second, even with the relaxed targets, the debt trajectory would remain contained, with debt peaking in 2014 and declining steadily thereafter. As a result, it was agreed to ease the budget deficit target for 2013 from 3 to 4½ percent of GDP—a larger deficit than initially envisaged.

From the IMF side, we also felt that the revision of the targets would be consistent with findings that higher fiscal multipliers might be at work in countries in circumstances similar to Portugal's. This work was subsequently published in the WEO. But it is very important to stress that findings from cross-country regressions such as this cannot be used to determine precisely the appropriate size of the multiplier for an individual country.

Relatedly, we also do not see a need to revise the GDP growth forecasts, including for 2013, which were agreed with the government during the fifth review discussions in Lisbon. It effectively assumes a higher fiscal multiplier being at work. The IMF Executive Board will have the opportunity to discuss this and other aspects of the program next week as it considers the fifth review.

A great deal has been achieved in Portugal over the past 18 months in terms of structural reforms and fiscal consolidation, with great sacrifices and determination of the Portuguese authorities and the Portuguese people. But debt remains high, and to ensure full recovery the country needs to contain it. Portugal also needs to ensure that it can finance itself again at reasonable rates. This means that fiscal adjustment is imperative and needs to continue.