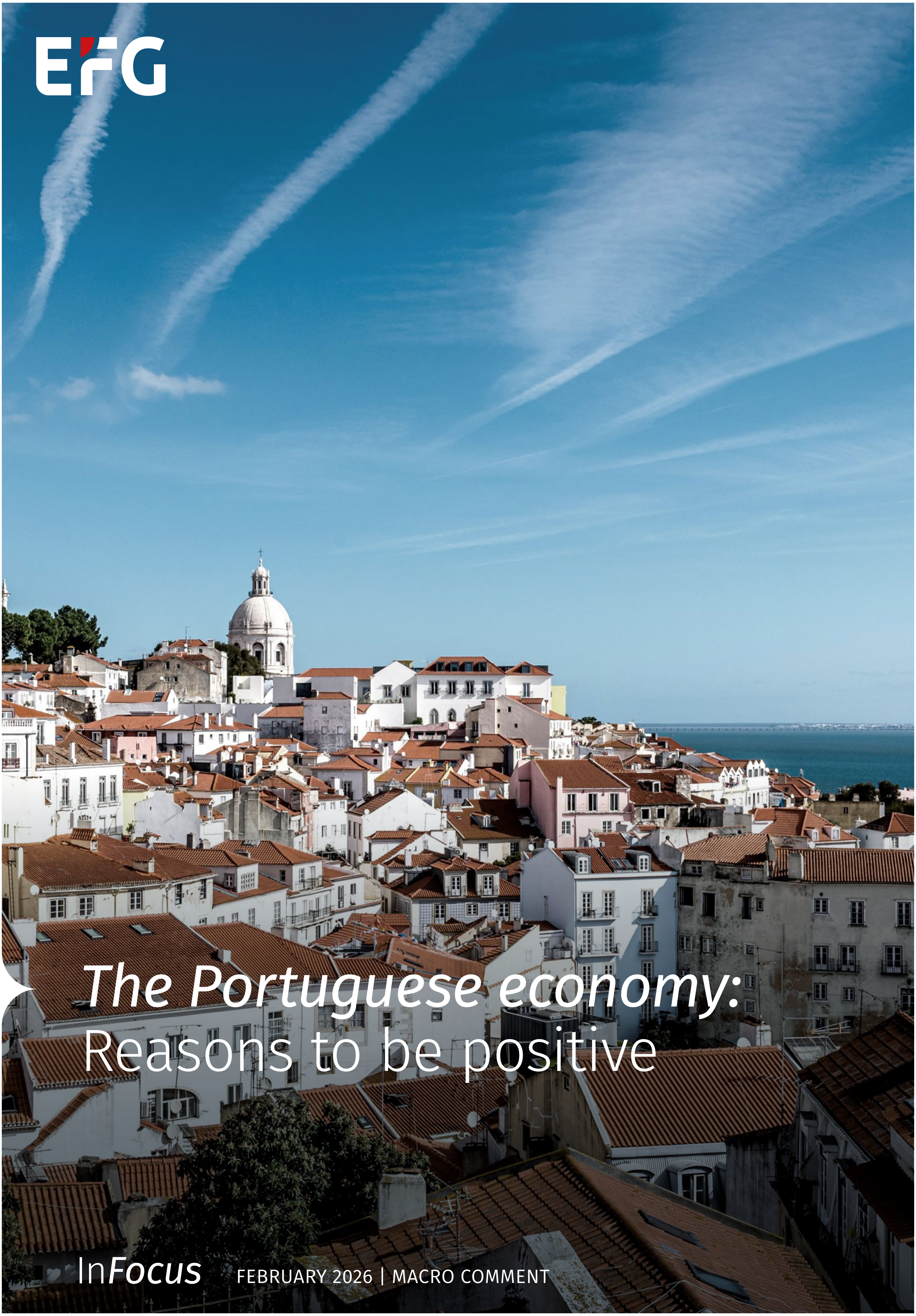

The Portuguese economy: Reasons to be positive

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The Portuguese economy: Reasons to be positive

Stefan Gerlach
Chief Economist

Portugal's economy has come a long way since the eurozone debt crisis, transforming over the last decade. The recently published OECD Economic Survey for Portugal provides a positive assessment. In this edition of InFocus, Chief Economist Stefan Gerlach examines the key drivers behind Portugal's economic strength while weighing up structural constraints.

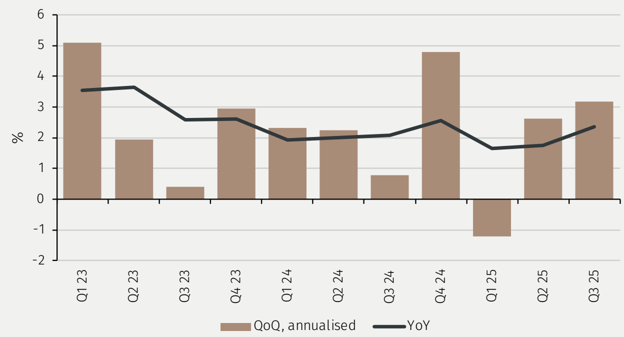
Key Statements

- The OECD projects growth of roughly 1.9% in 2025 and 2.2% in 2026, pointing to a stable expansion rather than a cyclical boom.
- The economy has historically low unemployment, inflation close to 2% and markedly improved fiscal and external balances.
- Maintaining prudent fiscal policy and prioritising productivity enhancing public investment will therefore be crucial to sustain the declining debt trajectory.

Portugal's recovery from the fiscal crisis a decade ago remains impressive. The OECD's recently released Economic Survey for Portugal highlights a resilient economy with solid growth, historically low unemployment, inflation close to 2% and markedly improved fiscal and external balances, despite a challenging European environment.[1] At the same time, the OECD emphasises that structural constraints, including labour shortages, an ageing population and weak productivity, may weigh on medium-term growth.

Chart 1.

Real GDP growth



Source: ECB. Data as of 18 February 2026.

Activity has remained resilient, with real GDP growth running at about 2% in both year-on-year and quarter-on-quarter annualised terms. The OECD projects growth of roughly 1.9% in 2025 and 2.2% in 2026, pointing to a stable expansion rather than a cyclical boom. Growth is supported by rising real incomes, strong employment and the continued implementation of EU funded investment programmes, with domestic demand as the main driver and external demand somewhat softer amid weaker European growth and global uncertainty.

Chart 2.

A steady decline in the unemployment rate

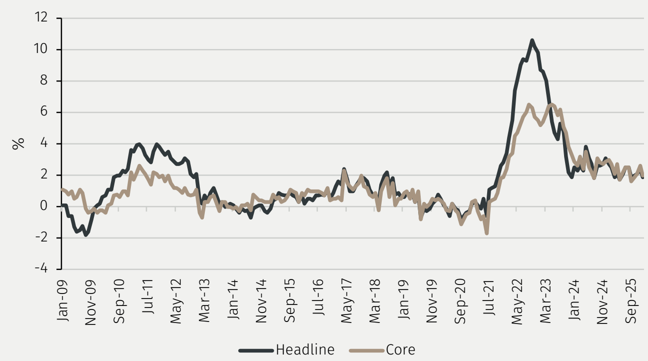
Source: ECB. Data as of 18 February 2026.

The labour market is the clearest pillar of strength. Unemployment, which peaked at 18.3% in early 2013, declined steadily to 5.6% in December 2025, the lowest level in roughly a quarter of a century. This reflects sustained job creation and strong labour demand across sectors.

High employment supports household income, consumption and fiscal revenues. The OECD notes that employment has reached record highs, although firms increasingly report labour shortages and difficulties recruiting skilled workers. This suggests that the labour market is not only strong cyclically but also becoming constrained structurally.

Chart 3.

Inflation close to the ECB target

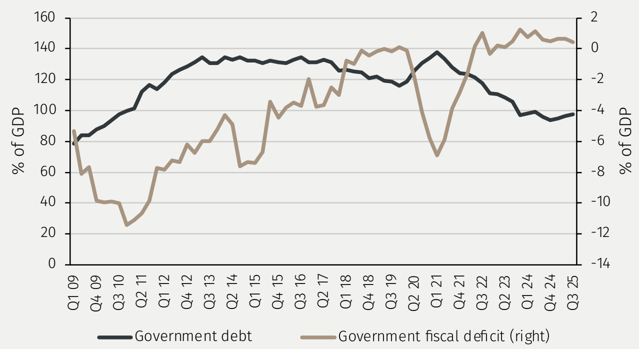


Source: ECB. Data as of 18 February 2026.

Inflation dynamics have improved significantly. Both headline and core Harmonized Index of Consumer Prices (HICP) inflation were around 2% in January 2026, close to the European Central Bank's target for the overall eurozone economy. This represents substantial disinflation from the peak in Q3 2022, when headline inflation exceeded 10% and core inflation rose above 6%. The OECD expects inflation to remain around 2% over the coming years, indicating a relatively benign price environment. Importantly, disinflation has occurred alongside continued growth and strong employment, pointing to an orderly normalisation rather than demand weakness.

Chart 4.

Fiscal balance and public debt



Source: ECB. Data as of 18 February 2026.

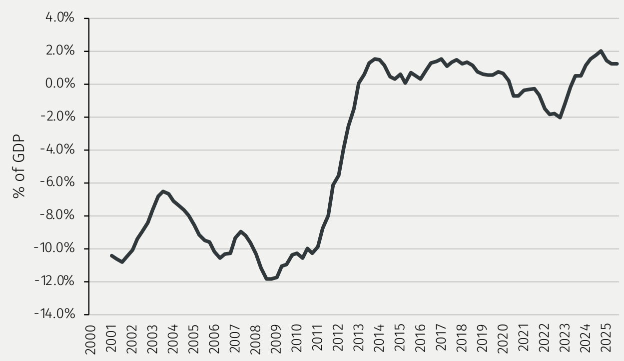
Public finances have strengthened markedly over the last 15 years. The fiscal deficit, which exceeded 10% of GDP during the crisis period, has been gradually reduced and has recently turned into a small surplus. As a result, the debt-to-GDP ratio, which peaked at close to 140% during the pandemic, has fallen to below 100%.

[1] https://www.oecd.org/en/publications/oecd-economic-surveys-portugal-2026_025b3445-en.html

The OECD emphasises that Portugal has rebuilt fiscal buffers and reduced public debt significantly over the past decade, although ageing related spending pressures will increase over time. Maintaining prudent fiscal policy and prioritising productivity enhancing public investment will therefore be crucial to sustain the declining debt trajectory.

Chart 5.

Current account balance has shifted to a small surplus

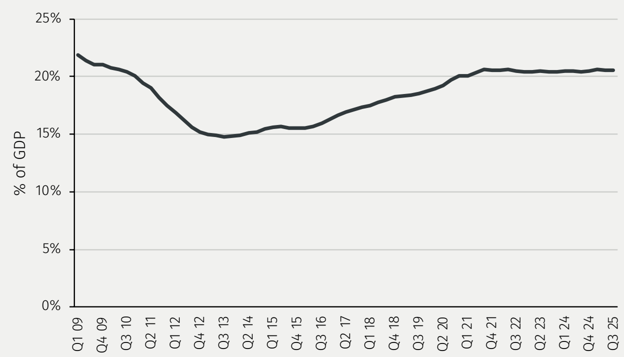


Source: ECB. Data as of 18 February 2026.

The external position has also improved dramatically compared to the crisis period, no doubt helped by fiscal consolidation. The current account, which showed deficits of over 10% of GDP during the sovereign debt crisis, has shifted into a small surplus of 1-2% of GDP in recent years. This external adjustment reduces macroeconomic vulnerabilities and contrasts sharply with the imbalances seen a decade ago.

Chart 6.

Gross fixed capital formation



Source: ECB. Data as of 18 February 2026.

Investment has recovered but remains somewhat uneven. Gross fixed capital formation fell to around 15% of GDP during the crisis but has since risen to just above 20%. This improvement is supported by EU funds and public investment, including under the Recovery and Resilience Plan. However, the OECD stresses that weak investment during the adjustment period and continued productivity gaps still weigh on potential growth.

Demographics and productivity may present challenges
Despite these strong cyclical fundamentals, the OECD highlights important medium-term challenges. Portugal's ageing population, labour shortages and relatively low productivity are likely to constrain long-term growth and living standards. Labour productivity remains below the OECD average and the business sector is dominated by small firms with limited innovation capacity. Housing affordability pressures, skill mismatches and administrative burdens may also weigh on investment and labour mobility.

While fiscal outcomes are currently favourable, long-term spending pressures related to pensions, healthcare and ageing will require continued fiscal prudence and structural reforms. Sustaining growth will therefore depend on higher investment, stronger skills policies and reforms that enhance productivity and labour supply.

Conclusion: strong performance, but structural reforms needed
Overall, Portugal stands out as a strong cyclical performer within the euro area. Growth is stable, unemployment is at multi-decade lows, inflation is close to target and both fiscal and external balances have improved substantially. However, structural constraints, together with only moderate investment, suggest that maintaining the current performance over the medium term will require higher productivity and sustained increases in productive investment rather than continued reliance on favourable cyclical conditions.

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