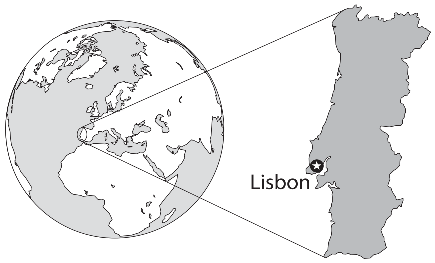
PORTUGAL



Rank: 53

Regional Rank: 26 of 41

Portugal's economy is 64.3 percent free, according to our 2008 assessment, which makes it the world's 53rd freest economy. Its overall score is 0.2 percentage point lower than last year, reflecting worsened scores in four of the 10 economic freedoms. Portugal is ranked 26th freest out of 41 countries in the European region, and its overall score is slightly lower than the regional average.

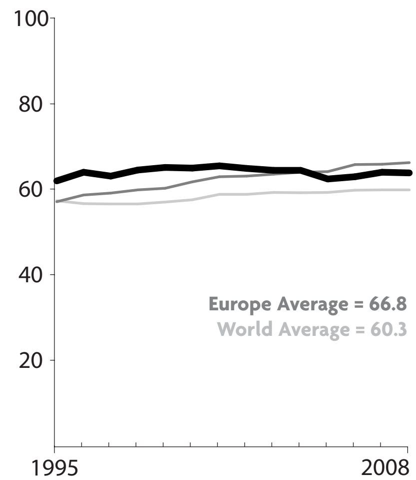
Portugal enjoys very high levels of business freedom, trade freedom, investment freedom, property rights, and freedom from corruption. The average tariff rate is low, but non-tariff barriers include distortionary EU subsidies on agriculture and other goods. Business formation is efficient, although other commercial operations are often slowed by bureaucracy. Inflation is low, and the government actively promotes foreign investment. Case resolution is slower than the EU average, but the judiciary is independent and free of corruption.

Portugal has very low scores in government size, fiscal freedom, and labor freedom. Total government spending equals almost 50 percent of GDP, and the labor sector is highly restrictive in all areas, from maximum workweek hours to employment severance procedures.

BACKGROUND: After the 1974 "Revolution of the Carnations" that overthrew its long-running dictatorship, Portugal embarked on a course of rapid democratization and adopted a strong Euro-Atlantic outlook. It joined the European Union in 1986, liberalizing many parts of the economy and improving its infrastructure with the help of EU funds. However, Portugal has suffered in recent years from low educational achievement, sluggish growth, and fiscal imbalances. It also faces challenges from the loss of its comparative advantage in cheap labor following the accession of Central and Eastern European countries to the European Union. Portugal's main exports include agricultural produce, wood products (especially cork), and canned foods.

How Do We Measure Economic Freedom? See Chapter 4 (page 39) for an explanation of the methodology or visit the *Index* Web site at *heritage.org/index.*

The economy is 64.3% free



QUICK FACTS

Population: 10.5 million

GDP (PPP): $215.3 billion
0.5% growth in 2005
0.5% 5-yr. comp. ann. growth
$20,410 per capita

Unemployment: 7.6%

Inflation (CPI): 2.1%

FDI (net flow): $2.0 billion

Official Development Assistance:
Multilateral: None
Bilateral: None

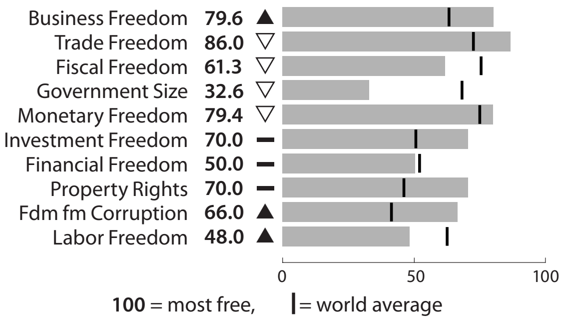
External Debt: $272.2 billion

Exports: $53.3 billion
Primarily clothing and footwear, machinery, chemicals, cork and paper products

Imports: $69.1 billion
Primarily machinery and transport equipment, chemicals, petroleum, textiles, agricultural products

2005 data unless otherwise noted.

PORTUGAL'S TEN ECONOMIC FREEDOMS



BUSINESS FREEDOM — *79.6%*

The overall freedom to start, operate, and close a business is relatively well protected by Portugal's regulatory environment. Starting a business takes an average of seven days, compared to the world average of 43 days. Obtaining a business license requires more than the world average of 19 procedures and 234 days. Bankruptcy proceedings are fairly easy and straightforward.

TRADE FREEDOM — *86%*

Portugal's trade policy is the same as those of other members of the European Union. The common EU weighted average tariff rate was 2 percent in 2005. Non-tariff barriers reflected in EU policy include agricultural and manufacturing subsidies, import restrictions for some goods and services, market access restrictions in some service sectors, nontransparent and restrictive regulations and standards, and inconsistent customs administration across EU members. Pharmaceutical regulations and non-transparent government procurement also add to the cost of trade. Consequently, an additional 10 percentage points is deducted from Portugal's trade freedom score.

FISCAL FREEDOM — *61.3%*

Portugal has a high income tax rate and a moderate corporate tax rate. The top income tax rate is 42 percent, and the top corporate tax rate is 27.5 percent. Other taxes include a value-added tax (VAT), a property tax, and a vehicle tax. In the most recent year, overall tax revenue as a percentage of GDP was 36.3 percent.

GOVERNMENT SIZE — *32.6%*

Total government expenditures, including consumption and transfer payments, are high. In the most recent year, government spending equaled 47.4 percent of GDP. The government has slowly pushed forward public administration reform as part of its effort to reduce the budget deficit.

MONETARY FREEDOM — *79.4%*

Portugal is a member of the euro zone. Inflation is relatively low, averaging 2.8 percent between 2004 and 2006. Relatively stable prices explain most of the monetary freedom score. As a participant in the EU's Common Agricultural Policy, the government subsidizes agricultural production, distorting the prices of agricultural products. The government also influences prices through state-owned enterprises and utilities. Consequently, an additional 10 percentage points is deducted from Portugal's monetary freedom score.

INVESTMENT FREEDOM — *70%*

Foreigners may invest in almost all sectors that are open to private enterprise. Non-EU investment in defense, water management, public-service telecommunications, railways, and maritime transportation requires approval; non-EU investment in regular air transport and television operations is also restricted. The government's "Simplex 2007" plan aims to simplify business investment and approval measures. Privatization of parts of the state airline, a utility, and a paper company are also scheduled. Residents and non-residents may hold foreign exchange accounts. There are no controls or restrictions on repatriation of profits, current transfers, payments for invisible transactions, or real estate transactions.

FINANCIAL FREEDOM — *50%*

Financial institutions may offer a variety of services, and regulation by the central bank is improving. The sole remaining state-owned financial services firm, Caixa Geral de Depósitos (CGD), is Portugal's largest financial group. CGD and four large private banks account for about 80 percent of assets. Consolidation continued in 2006 with the merger of the largest and fourth-largest private banks. The government influences the allocation of credit through a program to assist small and medium-size enterprises. CGD also owns two of the three firms that dominate insurance. Capital markets and the stock market remain relatively small. The stock exchange participates in Euronext, the common trading platform linking the bourses of Paris, Brussels, and Amsterdam.

PROPERTY RIGHTS — *70%*

The judiciary is independent. The court system is slow and deliberate, and the number of years it takes to resolve cases is well above the EU average. Portugal implements the WTO's Trade-Related Aspects of Intellectual Property Rights (TRIPS) and European intellectual property protection standards and has increased the penalties for violators.

FREEDOM FROM CORRUPTION — *66%*

Corruption is perceived as present. Portugal ranks 26th out of 163 countries in Transparency International's Corruption Perceptions Index for 2006. Foreign firms no longer identify corruption as an obstacle to investment. Portugal has ratified the OECD Anti-bribery Convention and recently passed legislation to bring its criminal code into compliance with it.

LABOR FREEDOM — *48%*

Inflexible employment regulations hinder overall productivity growth and employment opportunities. The non-salary cost of employing a worker is high, and the rigidity of hiring and firing a worker creates a risk aversion for companies that would otherwise employ more people. Regulations related to the number of work hours are not flexible.