INTERNATIONAL MONETARY FUND

IMF Country Report No. 18/65

REPUBLIC OF MOZAMBIQUE

March 2018

2017 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE REPUBLIC OF MOZAMBIQUE

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2017 Article IV consultation with the Republic of Mozambique, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Chair of the Executive Board and summarizing the views of the Executive Board as expressed during its March 5, 2018 consideration of the staff report on issues related to the Article IV Consultation and the IMF arrangement.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 5, 2018, following discussions that ended on December 13, 2017, with the officials of the Republic of Mozambique on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 15, 2018.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- A **Staff Supplement** updating information on recent developments.
- A **Statement by the Executive Director** for the Republic of Mozambique.

The documents listed below have been or will be separately released:

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
PO Box 92780 • Washington, D.C. 20090
Telephone: (202) 623-7430 • Fax: (202) 623-7201
E-mail: publications@imf.org Web: http://www.imf.org
Price: $18.00 per printed copy

International Monetary Fund
Washington, D.C.

© 2018 International Monetary Fund

Press Release No. 18/77
FOR IMMEDIATE RELEASE
March 07, 2018

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2017 Article IV Consultation with the Republic of Mozambique

On March 5, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with the Republic of Mozambique.

In recent years, Mozambique's economy has been adversely affected by the fall in commodity prices and adverse weather conditions, as well as by the issue of undisclosed loans in the spring of 2016 and the ensuing freeze in donor support. Growth decelerated in 2016 to 3.8 percent (from 6.6 percent in 2015) and the latest data show that the economy grew by 3.7 percent in 2017, driven by a recovery in agriculture and mining activity (due to a surge in coal production). A tight monetary stance, coupled with exchange rate appreciation, led to a steep fall in inflation to 6.3 percent (year on year) in January 2018, from a peak of 26 percent in November 2016. However, the 2017 fiscal deficit on a modified cash basis (i.e., including external and domestic arrears) is estimated to have increased to around 8.2 percent of GDP compared to 7.6 percent of GDP in 2016, mainly due to continued spending pressures, including from a higher wage bill and high debt service costs.[2] The external current account deficit continued to narrow in 2017. This was due to a boom in mining exports and to a contraction in megaproject imports of services. Another factor was the one-off inflow in income associated with the capital gain tax from the sale of ENI's stake in the Coral South natural gas field to Exxon Mobil. Debt remains in distress as the stock of public sector debt-to-GDP reached 128.3 percent at end-2016, with several debt payments missed, including on the Mozam Eurobond.

The outlook remains challenging. Absent further policy action, real GDP growth is expected to further decline over time while inflation would remain at current levels. The fiscal deficit would

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] This excludes the one-off capital gain tax revenue ($350 million or 2.8 percent of GDP) accrued due to the sale of 50 percent of ENI Africa share in the Coral South natural gas field to Exxon Mobil.

expand, leading to further accumulation of public debt and crowding out of the private sector. Banks' rising exposure to the government, combined with high interest rates, create potential macrofinancial vulnerabilities.

Executive Board Assessment[3]

Executive Directors noted that Mozambique's economy is facing difficult challenges. While inflation has declined rapidly, real GDP growth remains weak and macroeconomic imbalances are growing. Directors stressed the need for a rebalancing of the policy mix to ensure durable macroeconomic stability and for advancing structural reforms to support inclusive growth.

Directors noted that a steadfast fiscal consolidation effort aimed at closing the primary deficit is essential to ensure fiscal sustainability. They urged the need to broaden the tax base by eliminating VAT and other tax exemptions and to reduce current spending, while protecting outlays to social protection and infrastructure projects. Directors welcomed the authorities announced plans to resume discussions with private creditors and stressed that making progress in debt restructuring discussions would be an important step towards restoring debt sustainability.

Given the reduction in inflation and the high real interest rates, Directors welcomed the recent decision to reduce the monetary policy rate. Directors felt that fiscal consolidation could provide room for further cautious easing of monetary policy, thus rebalancing the policy mix. They encouraged the authorities to maintain exchange rate flexibility to help mitigate shocks.

Directors observed that implementing financial sector and monetary regime reforms is essential to strengthen resilience and mitigate risks. They welcomed the central bank's efforts to enhance its supervisory capacity, modernize the bank resolution framework, and to revise the central bank law to provide it with a clear mandate and operational autonomy.

Directors welcomed the authorities' action plan to improve governance, transparency, and accountability. They noted that while Mozambique has a sound anti-corruption legal framework in place, strengthening implementation and enforcement going forward is key to fighting corruption. Directors welcomed the approval of a decree establishing a framework for contracting public debt and issuing guarantees. They stressed that providing full clarity on the use of the proceeds of the previously undisclosed loans contracted by three public companies will be critical to restoring confidence and encouraging private investment.

---

[3] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Directors called for a renewed effort to strengthen the business climate and governance to boost private investment and job creation to support inclusive growth and further reduce poverty and inequality. They noted that restructuring ailing state-owned enterprises will be key to improving efficiency, and reducing financial losses.

Mozambique: Selected Economic Indicators

	2016	2017	2018
	(Annual percentage change, unless otherwise indicated)		
National income and prices			
Nominal GDP (MT billion)	689	802	875
Real GDP growth	3.8	3.0[1]	3.0
Consumer price index (end of period)	21.1	7.2	6.5
	(Percent of GDP)		
Government Operations			
Total revenue	24.0	25.1	22.1
Total expenditure and net lending	32.4	32.1	30.9
Overall balance, after grants	-7.6	-8.2	-7.5
Primary Balance after grants	-4.6	-4.5	-3.2
	(Annual percentage change, unless otherwise		
Money and Credit			
Reserve money	35.2	1.4	5.6
M3 (Broad Money)	10.1	4.5	7.9
Credit to the economy	12.6	-10.4	2.9
(Percent of GDP)	37.9	29.2	27.6
External sector			
Merchandise exports	-2.5	27.9	18.1
Merchandise exports, excluding megaprojects	-32.5	-7.9	7.5
Merchandise imports	-37.5	2.9	13.7
Merchandise imports, excluding megaprojects	-40.5	3.3	7.3
	(Millions of U.S. dollars)		
External Public Debt	10,065	11,395	13,413
External current account, after grants	-4,424	-2,039	-2,424
Net international reserves (end of period)	1,753	2,297	2,573
Gross international reserves (end of period)	1,988	2,532	2,808

Sources: Mozambican authorities; and IMF staff estimates and projections.

1/ The latest data from the Mozambican Statistical Agency show that the economy grew by 3.7 percent in 2017.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION

February 15, 2018

KEY ISSUES

Context. The fall in commodity prices and adverse weather conditions have adversely affected economic activity. The latter further declined following the disclosure of hidden loans in the spring of 2016 and the ensuing freeze in donor support. While tight monetary policy has helped stabilize the exchange rate and lower inflation since the fall of 2016, an overly loose fiscal policy is crowding out the private sector and resulting in an accumulation of domestic arrears. Public debt is in distress with several external borrowing payments missed. While the actual and projected fiscal deficits remain excessively high, the government has implemented measures to ease spending pressures, such as the elimination of fuel and wheat subsidies and the reduction of civil servants' allowances and benefits.

Outlook and Risks. The outlook remains challenging with some risks rising. Continuation of the current policy mix would result in increasing difficulties for the private sector and further accumulation of public debt. Banks rising exposure to the government, combined with high interest rates, create potential macrofinancial vulnerabilities. Mozambique's high poverty rate remains persistent. Risks are broadly balanced, with an upside potential from rising commodity prices, the resolution of the hidden debt issue, and reengaging with donors. Downside risks include a deterioration in security conditions; further loosening of expenditures; increased debt service, liabilities from loss making SOEs, unavailability of domestic financing, and delays in megaprojects.

Policy Recommendations. Mozambique's key challenge is to restore macroeconomic stability, rebuild confidence in the near term, and foster economic recovery over the medium term, while making inroads in reducing poverty and income inequality. For **fiscal policy** a determined effort at consolidating public finances to restore sustainability, bring the deficit in line with financing availability, and contain public debt is urgently needed. Restoring **debt sustainability** would involve lowering Mozambique's external debt risk rating to "moderate" over the medium term. In view of rapid disinflation, **monetary policy** can be somewhat eased to avoid worsening credit contraction while remaining cautious given the fiscal stance. The **banking system** has recovered from the instability observed in 2016 but vulnerabilities remain due to strong sovereign-financial linkages, including high exposure to state owned enterprises (SOEs). Providing the information still missing after **the audit of the public companies involved in the hidden loans**, and in particular full clarity on how the loan proceeds were effectively used, would help restore confidence and encourage private investment.

Approved By
David Owen and Zeine Zeidane

A staff team comprising Mr. Lazare (head), Messrs. El Said, Wezel, Zavarce (all AFR), Abdallah (FAD), and Mansilla (MCM), Mmes. Balta (SPR) and Esquivel Soto (LEG) visited Maputo during November 30-December 13, 2017. Mr. Aisen (resident representative). Ms. Palacio and Mr. Simione (Economists, resident representative office) assisted the mission. The mission held discussions with Economy and Finance Minister Maleiane, Bank of Mozambique Governor Zandamela, other sectoral ministers, parliamentarians, representatives of the Judiciary, senior government officials, private sector, trade unions, civil society representatives, and development partners. Ms. Carvalho provided research support and Ms. Aliu provided assistance for the preparation of this report.

CONTENTS

BACKGROUND 4

RECENT ECONOMIC DEVELOPMENTS 5

OUTLOOK, AND RISKS: CHALLENGES AHEAD 7

POLICY DISCUSSIONS: MAINTAINING MACROECONOMIC STABILITY 10

A. Fiscal Policy: Strengthening the Fiscal Position 10

B. Monetary Policy and Foreign Exchange Management: Measured Normalization and Stability 14

C. Strengthening Resilience and Containing Financial Sector Risks 15

D. Debt Policy: Achieving Sustainability 18

E. Structural Policies: Strengthening Governance and Promoting Inclusive Growth 19

F. Data and AML/CFT Issues 21

STAFF APPRAISAL 21

BOXES

1. Adjustment Scenario 8
2. Social Protection 12
3. Monetary and Financial Sector Regulatory Measures 15
4. Nonperforming Loan Sensitivity Analysis. 16

FIGURES

1. Impact of Global Developments ____ 24
2. Inflation, Monetary and Financial Developments ____ 25
3. Selected External Sector Developments ____ 26
4. Fiscal Developments ____ 27

TABLES

1. Selected Economic and Financial Indicators, 2016-23 ____ 28
2. Government Finances, 2016–23 (billions of Meticais) ____ 29
3. Government Finances, 2016–23 (Percent of GDP) ____ 30
4. Monetary Survey, 2016–19 ____ 31
5a. Balance of Payments, 2016–23 (Millions of U.S. dollars, unless otherwise indicated) ____ 32
5b. Balance of Payments, 2016–23 (Percent of GDP) ____ 33
6. Financial Soundness Indicators for Banking Sector, 2013–17 ____ 34
7. Risk Assessment Matrix ____ 35

ANNEXES

I. Implementation of Past IMF Recommendations ____ 38
II. External Sector Assessment ____ 39
III. IMF-WB Joint Recommendations on Authorities' Action Plan ____ 43

BACKGROUND

1. **Mozambique's economy faces serious macroeconomic challenges.** Despite a loose monetary/fiscal policy mix through mid-2016, the economy slowed from 2015 because of a series of shocks, including lower commodity prices and adverse weather conditions. The economic situation deteriorated further following the disclosure in April 2016 of undisclosed borrowing by the Proindicus and MAM public companies and the ensuing freeze in donor budget support.[1] Growth has continued to slow and fiscal policy has remained fairly loose in 2017. Public debt has been rising at an unsustainable pace and debt has remained in distress with several payments on external borrowing missed.

2. **Monetary policy has carried the burden of adjustment.** Tight monetary policy since October 2016 has helped rebalance the foreign exchange market, lower inflation, and strengthen net international reserves. The government eliminated fuel and wheat subsidies, reintroduced automatic adjustment of fuel prices, and raised electricity and public transportation prices. However, significant spending pressures are expected to result in an overall 2017 fiscal deficit exceeding 8 percent of GDP (on a modified cash basis.[2]) The large financing needs of the Treasury combined with a restrictive monetary stance to stabilize inflation continues to press market interest rates higher, depressing credit availability to the private sector—particularly to SMEs—and affecting economic activity, employment, and socio-economic conditions.

3. **Mozambique's financial sector has come a long way since the volatility observed in 2016.** The instability created by the resolution of Moza Banco and Nosso Banco has abated. The system is currently characterized by an increasing gap between credit growth and monetary aggregates and high government financing needs. The rapid disinflation and returned stability in the FX market have left real interest rates in domestic currency at elevated levels. Private credit demand has contracted, which resulted in high liquidity for the balance sheet of the system being allocated to government securities. Vulnerabilities remain related to rising NPLs, increasing government expenditures arrears and debt sustainability of SOEs.

4. **Serious governance issues remain to be addressed.** The disclosure of hidden debt in April 2016 resulted in misreporting under the Policy Support Instrument (PSI) and breach of obligations under Article VIII, Section 5. The PSI 6th review and the Standby Credit Facility (SCF) 1st review did not take place as scheduled and both the PSI and the SCF lapsed. The authorities agreed in September 2016 to allow an independent audit of the undisclosed loans by Kroll, a risk management company. The completion of the Kroll audit report and the publication of its summary in June 2017 are important steps towards greater transparency. However, critical information gaps remain unaddressed regarding the use of the loan proceeds. In response to staff request to receive clarity

[1] This hidden debt included borrowing by two state-owned enterprises, Proindicus and MAM, disclosed in April 2016, for about $1.1 billion, and of several smaller bilateral loans ($0.3 billion)—a total of $1.4 billion or around 11 percent of the 2015 GDP. Borrowing ($0.85 billion) from a third state-owned company, Ematum, was discovered at an early stage in 2014. The three companies Ematum, Proindicus and MAM, aim respectively at fishing tuna, providing maritime protection, and building shipyards. The three companies were created shortly before the borrowing took place and were all headed by the same CEO, who at that time was a senior officer of the security services.

[2] The concept of modified cash basis refers to a cash basis deficit plus new accumulation of expenditure arrears.

on the use of the money, the Government recommended waiting for the outcome of the ongoing investigation by the Prosecutor General Office. Meanwhile, the authorities have approved a decree establishing a framework to contract public debt and issue guarantees and sent to Parliament a draft SOE law. They have initiated work with IMF/World Bank staff assistance on an action plan to strengthen governance, transparency, and accountability.

5. A durable peace agreement seems within reach. On February 7, 2018, President Nyusi announced that an agreement had been reached with the opposition party, Renamo, on draft amendments to the Constitution that foster decentralization and allow the designation of provincial governors representing opposition parties. Discussions aimed at integrating Renamo fighters in the army are continuing. The September 2017 Congress of the ruling party (Frelimo) confirmed President Nyusi as the party's candidate for the 2019 presidential elections. On the downside, several shootouts involving armed Islamic fundamentalists and the police occurred in the North, in the area where natural gas megaprojects will be built.

6. Implementation of past IMF policy advice has been mixed (Annex I). Advice on fiscal policy was partially followed, (e.g. fuel subsidies), but the recommended fiscal consolidation was not achieved. In line with staff advice, Bank of Mozambique (BM) maintained a tight monetary stance to curb inflationary pressures and help stabilize the foreign exchange market.

RECENT ECONOMIC DEVELOPMENTS

7. GDP performance has remained weak and inflation plummeted. Growth decelerated in 2016 to 3.8 percent (from 6.6 percent in 2015).[3] It is projected to barely reach 3.0 percent in 2017, mainly due to a surge in coal production and a modest rebound in agriculture activity.[4] A tight monetary stance, coupled with an exchange rate appreciation, led to a steep fall in (y/y) inflation to 7.2 percent in December as measured by the Maputo inflation index and 5.7 percent using a broadly-based index (from a high of 26 percent in November 2016). Average inflation remained in double digits at 15.3 percent in 2017.

8. Fiscal policy remained loose in 2017. Following several years of large deficits, the 2017 fiscal deficit (on a modified cash basis) is estimated to have increased to around 8.2 percent of GDP (compared to 7.6 percent of GDP in 2016). This excludes the one-off capital gain tax revenue ($350 million or 2.8 percent of GDP) for the sale of 50 percent of ENI's stake in the Coral South natural gas field to Exxon Mobil. The implied primary deficit of around 4.5 percent remain broadly unchanged relative to 2016. Such a high fiscal deficit reflects both rigidity and persistence of spending pressures.

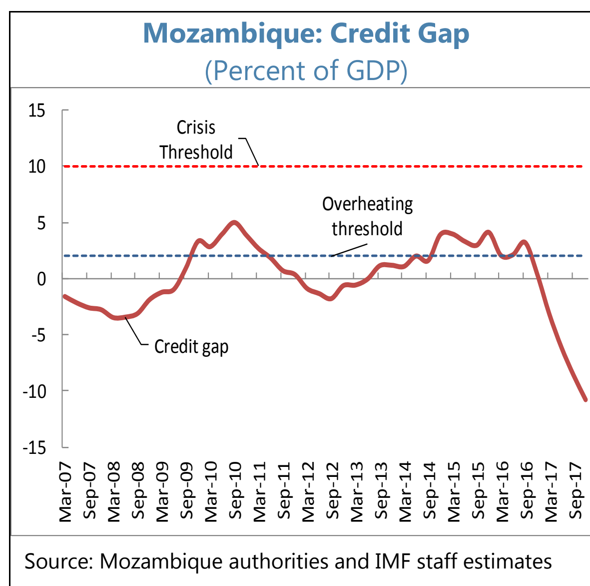
[3] This is relative to an average growth rate of 7.5 percent over the last decade.

[4] Non-mining non-agriculture growth is projected at around 1.0 percent in 2017.

9. In response to then high inflation and depreciating exchange rate, the Bank of Mozambique (BM) considerably tightened monetary policy from October 2016.[5] This tightening increased demand for domestic currency and helped stabilize the exchange rate and rebalance the foreign exchange market.[6] Since June 2017, broad stability has returned to the foreign exchange market. International reserves increased because of the accumulation of external arrears and of occasional interventions by the BM. At end 2017, reserves reached a level equivalent to 5.5 months of non-megaproject imports. In April 2017, the BM changed its operational monetary target to a short-term interest rate (MIMO)[7] and started a cautious easing cycle totaling three policy rate cuts by 225 basis points to 19.5 percent in December (SIP Chapter 1).[8] In the same period, reserve requirements were reduced by 150 basis points to 14 percent.

10. The current policy mix has resulted in a sharp decline in credit to the economy. The rapid reduction in inflation in the last year led to high real interest rates and higher demand for deposits and lower demand for credit in domestic currency. In December 2017, the policy rate reached 12 percent in real terms while y/y domestic credit to the economy contracted by 12 percent in nominal terms whereas deposits in domestic currency grew by 13 percent till November. The resulting gap between credit to the private sector and monetary aggregates in domestic currency has helped finance the governments' significant funding needs, albeit at a higher cost.

11. Following a period of instability that led to the resolution of two banks, in 2017 the system is showing lower volatility, but vulnerabilities persist. In 2016 the banking system concluded a cycle of fast credit growth (Figure 1),[9] which had increased the banks' vulnerability. In this context, the BM had to resolve two banks: Moza Banco, the fourth largest bank with 6 percent of assets, was put under official administration while another bank, Nosso Banco, holding less than 1 percent of assets, was liquidated after failing to comply with capitalization requirements. NPLs have more than doubled, reaching 11.4 percent in September 2017, but overall, banks seem well capitalized with reported regulatory capital-to-risk weighted assets ratio increasing to 20.2 percent in September 2017. Vulnerabilities remain due to exposure to the public sector, substantial government and SOEs' arrears with suppliers, sluggish economic growth and high real interest rates.



Source: Mozambique authorities and IMF staff estimates

[5] The BM increased its lending rate by 600 basis point to 23.25 percent.

[6] The metical nominally has appreciated by almost 24 percent against the USD since October 2016.

[7] The change is part of a longer-term transition to inflation targeting (SIP Chapter 1).

[8] The BM cut the policy rate by 150 points in December.

[9] The credit gap analysis reveals that credit-to-GPD compared to its trend was above the 2 percent overheating threshold between June 2014 and September 2016.

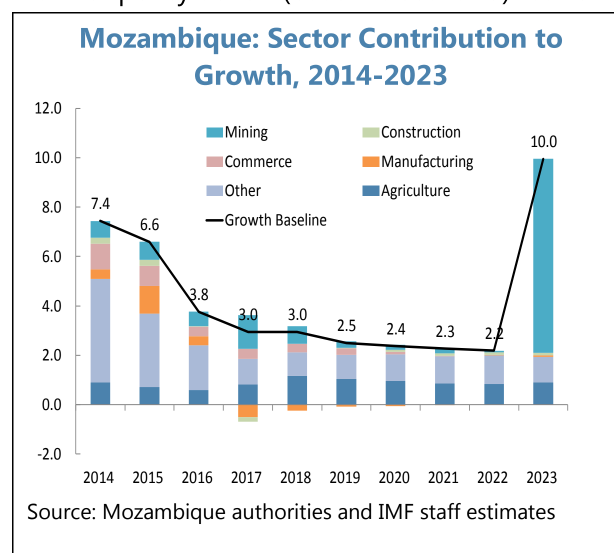
12. The current account deficit has continued to narrow in 2017. An essential factor in this narrowing was the one-off inflow in income associated with the capital gain tax (see above). It was also due to a 12.7 percent of GDP megaproject current account surplus. This surplus resulted from a boom in coal export volumes and prices, and to the 55 percent contraction in megaproject imports of services as many of the on-going projects were completed in 2016. The non-megaproject trade balance of goods deteriorated, with exports of goods falling by almost 8 percent, and imports growing by 3.3 percent, year-on-year in 2017. At the same time, net foreign direct investment in the non-megaproject economy continued to fall to about $1.3bn in 2017, half of the $2.6bn inflows registered in 2015.

13. Mozambique's public debt is in distress. The stock of public sector debt-to-GDP reached 128.3 percent at end-2016, including domestic debt (24.6 percent of GDP). Sovereign arrears have been incurred on the Mozam Eurobond coupon and on the debt service of Proindicus and MAM, as well as on two loans from Brazil to the state-owned airports company, *Aeroportos de Mozambique* (AdM), for which the state-guarantee has been called. The overall stock of external arrears on public and publicly guaranteed external debt service reached $709.7 million by end-2017, including arrears under bilateral discussions with five official creditors amounting to $94 million (Libya, Iraq, Angola, Bulgaria and Poland).[10] The authorities are currently servicing all other multilateral and bilateral external debt obligations. Discussions between the government and private creditors have not progressed since the government announced in October 2016 its intention to restructure the private external debt.

OUTLOOK, AND RISKS: CHALLENGES AHEAD

14. The outlook remains challenging. Absent further policy action (baseline scenario) real GDP is expected to further decelerate while inflation would remain at current levels (Figure 2). This would result from a policy mix marked by a loose fiscal stance and a restrictive monetary stance. Absent new fiscal measures, the fiscal deficit would expand leading to further accumulation of domestic arrears and crowding out of the private sector. The health of the banking sector would deteriorate, with NPLs rising further. However, investment in the large natural gas megaprojects would support growth.

Mozambique: Sector Contribution to Growth, 2014-2023



Source: Mozambique authorities and IMF staff estimates

15. The baseline scenario would result in widening current account deficits and mounting pressures on external reserves. The non-megaproject current account deficit is expected to widen from 2018 and remain at elevated levels over the medium term (to about 30

---

[10] The estimate for the stock of arrears does not include any contractual penalty fees or rates on the missed payments.

percent of GDP, and respectively, 17 to 18 percent of GDP, when adjusting further for imports of domestic firms that are used to supply mega-projects). As the non-megaproject current account deficit is the main driver of future pressures in the domestic foreign exchange market over the next 5 years or so (as LNG projects get implemented), the absence of a real depreciation of the exchange rate could result in a loss of reserves.[11] The external position is substantially weaker than the level consistent with medium-term fundamentals and desirable policies.

16. Mozambique's total public debt is on an unsustainable path. The updated debt sustainability analysis (see attached DSA) shows that Mozambique's external debt rating is "in distress", and total public debt is on an unsustainable path. All debt burden indicators, except the ratio of external debt service to exports, surpass prudent thresholds for several years. Under the baseline scenario, which does not assume any debt restructuring, the PV of external public and publicly guaranteed debt (PPG) to GDP ratio largely exceeds the 40 percent prudent threshold for about eight years, while external debt service to government revenues remains on average at about 30 percent over the medium-term. Moreover, significant vulnerabilities related to domestic debt, which reached about 25 percent of GDP in 2017, are rapidly escalating. The PV of total public debt to GDP ratio is expected to peak at 126 percent by 2022, well above the 56 percent benchmark.

17. Risks are broadly balanced (see Risk Assessment Matrix). Downside risks include a deterioration in security conditions; further loosening of expenditures; increased debt service, including from loss making SOEs, unavailability of domestic financing, and delays in megaprojects. Further policy inaction could lead to reduced confidence in the government ability to honor its commitments, posing additional risks to the banking sector. A recovery in commodity prices; new oil and gas discoveries; resolution of the hidden debt issue, and reengaging with donors in a more transparent and business friendly environment constitute upside risks. Furthermore, the start of natural gas production toward 2023 would boost growth performance and, over time, fiscal revenues. Overall, if downside risks materialize, the long-term viability of this baseline scenario would become questionable. Without strong policy adjustments, the outlook entails a rising risk of disorderly adjustment over the medium term. This calls for policy action, including through a tightening of the fiscal stance (see Box 1).

Box 1. Adjustment Scenario

In the baseline scenario, no further policy actions are taken by the authorities from 2018. This box presents an alternative scenario in which policy adjustment, in line with Fund advice, is implemented. The scenario is designed to illustrate the policy trade-offs and the importance of policy implementation to lower risks. Fiscal policy would be tightened, targeting a zero-primary balance by 2022 achieved through a combination of spending and tax policy deficit reducing measures (mostly through the elimination of tax exemptions); a gradual depreciation in the real effective exchange rate needed to stabilize the external sector (see Annex 2, External Sector Assessment); a cautious normalization of monetary policy with further cuts in the interest rate in line with the pace of fiscal consolidation and the inflation target of 5-6 percent range over the medium term.

[11] Capital flows associated with the LNG gas projects are expected to finance imports over the implementation period, and therefore, they should not exert pressures on the domestic foreign exchange market.

Box 1. Adjustment Scenario (concluded)

Overall, a consistent fiscal and monetary policy mix would improve fiscal and external balances, create fiscal space to meet social and development needs, reduce arrears accumulation, bring domestic debt onto a downward path, foster capital inflows to support investment and rebuild reserves. The banking sector, supported by a return of confidence and strengthened regulation, and lower financing needs of the government, would crowd-in credit to the private sector, reduce banks' exposure to sovereign risks and decrease government borrowing costs. In parallel, structural reforms, including adopting the action plan to strengthen governance and accountability (see below) will further support inclusive growth and poverty reduction. Fiscal retrenchment would limit the positive impact on growth in the near term, but other positive factors, including the normalization of monetary policy, the gradual correction of the overvaluation (with a positive impact on exports), and FDI inflows would offset the negative impact of fiscal consolidation and improve growth potential over the medium term.

Mozambique: SEI Baseline and Adjustment Scenario, 2016-22

	2016	2017	2018	2019	2020	2021	2022	2018	2019	2020	2021	2022
	Prel.	Baseline						Adjustment				
	(Annual percentage change, unless otherwise indicated)											
National income and prices												
Nominal GDP (MT billion)	689	802	875	949	1026	1108	1195	903	1010	1116	1231	1356
Real GDP growth	3.8	3.0	3.0	2.5	2.4	2.3	2.2	2.8	3.0	3.3	3.8	4.4
Consumer price index (end of period)	21.1	7.2	6.5	5.5	5.5	5.5	5.5	6.8	6.5	6.2	6.0	5.8
External sector												
Merchandise exports	-2.5	27.9	18.1	7.4	-1.2	2.9	2.8	18.4	7.9	-0.4	4.0	4.3
Merchandise exports, excluding megaprojects	-32.5	-7.9	7.5	6.7	6.6	7.3	7.4	8.8	9.4	10.2	11.6	12.6
Merchandise imports	-37.5	2.9	13.7	61.2	30.8	30.5	27.4	10.4	60.2	32.2	32.9	28.4
Merchandise imports, excluding megaprojects	-40.5	3.3	7.3	0.1	3.2	3.9	4.3	3.4	-3.5	4.0	8.5	6.8
Money and credit												
Reserve money	35.2	1.4	5.6	5.2	5.0	5.0	5.1	8.3	8.6	8.7	9.1	10.1
M3 (Broad Money)	10.1	4.5	7.9	7.8	7.6	7.5	7.4	10.5	10.9	11.1	11.5	11.7
Credit to the economy	12.6	-10.4	2.9	2.8	2.7	2.3	2.1	6.3	7.6	8.4	10.1	10.9
(Percent of GDP)	37.9	29.2	27.6	26.1	24.8	23.5	22.2	27.6	26.5	26.0	26.0	26.2
Investment and saving	(Percent of GDP)											
Gross domestic investment	42.7	36.5	54.7	86.3	106.8	138.4	134.5	54.1	85.2	104.7	135.0	147.0
Gross domestic savings (excluding grants)	2.7	20.4	37.6	41.5	40.0	47.3	18.0	38.2	40.6	35.0	36.5	20.8
External current account, before grants	-39.9	-16.1	-17.1	-44.7	-66.7	-91.1	-116.5	-15.9	-44.6	-69.7	-98.5	-126.2
External current account, after grants	-39.2	-16.1	-16.9	-44.6	-66.6	-91.0	-116.4	-15.7	-44.5	-69.6	-98.4	-126.1
Government budget												
Total revenue [1]	24.0	25.1	22.1	22.0	21.9	21.8	21.8	22.3	24.2	24.3	24.3	24.4
Total expenditure and net lending	32.4	32.1	30.9	33.9	32.5	32.1	33.0	30.7	32.5	30.1	28.6	28.2
Payments in arrears	1.3	...	...	...	...	...	...	...	...	...	...	...
Overall balance, before grants[2]	-9.7	-7.0	-8.8	-12.0	-10.6	-10.3	-11.2	-8.4	-8.3	-5.8	-4.2	-3.8
Total grants	2.1	1.6	1.3	1.2	0.7	0.6	0.6	1.3	1.2	0.8	0.7	0.6
Overall balance after grants[2 3]	-7.6	-8.2	-7.5	-10.8	-9.9	-9.6	-10.6	-7.1	-7.1	-5.1	-3.5	-3.2
Primary Balance after grants[2 3]	-4.6	-4.5	-3.2	-5.1	-5.5	-6.4	-7.6	-2.8	-1.8	-1.1	-0.3	0.0
External financing (incl. debt relief)	2.2	0.9	1.0	3.0	3.6	3.8	5.1	1.0	3.2	4.0	4.2	5.5
Net domestic financing	2.0	0.4	3.3	1.8	1.1	-0.1	-0.2	2.8	0.6	-1.0	-2.7	-3.4
Total nominal public debt[4]	128.3	112.0	121.6	130.0	136.5	142.1	145.9	125.4	127.2	129.3	131.8	130.1
Of which: external	103.7	85.2	95.1	101.2	105.8	109.6	111.0	101.9	111.8	118.2	122.5	121.8
Of which: domestic	24.6	26.7	26.5	28.8	30.7	32.5	34.9	23.6	15.4	11.1	9.3	8.3
	(Millions of U.S. dollars, unless otherwise indicated)											
External Public Debt[4]	10,065	11,395	13,388	14,952	16,326	17,647	18,589	13,388	14,952	16,326	17,647	18,589
External current account, after grants	-4,424	-2,039	-2,424	-6,700	-10,461	-14,910	-19,849	-2,207	-6,225	-9,942	-14,578	-19,627
Net international reserves (end of period)	1,753	2,297	2,573	2,588	2,384	2,212	3,212	2,640	2,848	2,843	2,857	4,068
Gross international reserves (end of period)	1,988	2,532	2,808	2,823	2,619	2,447	3,447	2,876	3,083	3,079	3,092	4,304

Sources: Mozambican authorities; and IMF staff estimates and projections.

[1] Net of verified VAT refund requests.

[2] Modified cash balances and includes payment arrears.

[3] Excludes a 2.7 percent of GDP one-off 2017 capital gains tax revenues

[4] Includes the participation of ENH (national hydrocarbon company) in the LNG gas projects.

POLICY DISCUSSIONS: MAINTAINING MACRO-ECONOMIC STABILITY

The current economic situation requires an urgent rebalancing of the policy mix to ensure durable macroeconomic stability, while enhancing growth prospects and making inroads in reducing poverty and income inequality. Discussions focused on the need for: (i) fiscal adjustment to restore fiscal sustainability and bring the fiscal deficit in line with financing availability while containing public debt; (ii) normalization of monetary policy and challenges in the financial sector, and (iii) strengthening governance and transparency, including by addressing the institutional weaknesses and corruption underlying the hidden loans, while advancing other structural reforms to generate growth and employment.

A. Fiscal Policy: Strengthening the Fiscal Position

18. The 2018 budget targets a reduction in the overall deficit after grants to 3.8 percent of GDP.[12] The budget assumes a non-resumption of direct budget support by donors, higher transfers (0.6 percent of GDP, mostly military pensions and social protection), and higher election spending (0.6 percent of GDP).[13] Those increases are offset by deficit-reducing measures on both the revenue and spending fronts. Proposed tax policy measures include the introduction of new excises (e.g., soft drinks, plastic bags) and new customs and tariffs (e.g., surcharges on imports of electrical conductors, new telephone call service rates). Spending measures mainly target the wage bill (reductions in specific allowances and bonuses). In addition, the 2018 budget does not incorporate the full debt service obligations on external and domestic debt.

Mozambique: Government Finances, 2018
(percent of GDP)

	2018	
	Budget	Proj.
Total revenue	22.5	22.1
Tax revenue	18.8	18.6
Nontax revenue	3.6	3.5
Total expenditure and net lending	27.9	30.9
Current expenditure	18.5	22.0
Compensation to employees	9.3	11.1
of which: Social Insurance	0.0	0.5
Goods and Services	3.1	4.1
Interest on public debt	3.3	4.3
Domestic	2.0	2.3
External	1.4	2.0
Subsidies and Transfers	2.8	2.5
Capital expenditure	8.0	5.6
Domestically financed	3.3	3.2
Externally financed	4.7	2.4
Net lending	1.4	3.2
Overall balance (modified cash basis), before grants	-5.4	-8.8
Grants received	1.7	1.3
of which: budget support	0.0	0.0
Overall balance (modified cash basis), after grants	-3.8	-7.5
Primary balance (modified cash basis), after grants	-0.4	-3.2
Memorandum items:		
Nominal GDP (Billions of Meticais)	992	875

Source: Mozambique authorities and IMF staff estimates.

19. However, in staff's view, the 2018 budget targets are unlikely to be achieved. On the back of slower growth (relative to the budget), based on conservative yields for the deficit reducing

[12] The 2018 budget assumes a GDP growth of 5.3 percent and a GDP deflator of 10.5 percent.

[13] Direct budget support refers to grants by donors that can finance any expenditure item. Donors have not resumed such form of budget support, but are still engaged in project financing (e.g., project grants).

measures, and considering full debt service obligations, staff estimates that the 2018 overall deficit would reach 7.6 percent of GDP down from an estimate of 8.2 percent of GDP in 2017.[14]

20. Beyond 2018, and absent new policy measures, the fiscal stance would be unsustainable over the medium term. While the policy measures undertaken in the 2018 budget proposal are encouraging, they are not sufficient to bend the trajectory of the primary deficit. Such a fiscal stance may result in further accumulation of arrears.

21. Fiscal consolidation is needed. Staff recommended targeting a zero-primary balance by 2022 (Text table 1). This anchor would be consistent with putting debt on a downward trajectory while being realistic given political economy considerations.[15] Financing of the underlying deficit does not assume recourse to central bank overdraft and accumulation of arrears. It would be achieved through a combination of spending and tax policy deficit reducing measures.[16,17] Meanwhile, the impact of these measures on the most vulnerable households would be mitigated through increases in social assistance spending (Box 2).

Mozambique: Adjustment Scenario Yield by Measure
(Percent of GDP)

	2019	2020	2021	2022
All measures	3.5	4.5	6.2	7.4
A. Tax revenue measures	1.9	1.9	1.9	1.9
Remove VAT exemptions on select food produts, public works, and products and	1.9	1.9	1.9	1.9
B. Wage bill rationalization measures	0.9	1.6	2.3	2.7
C. Other measures[1]	0.7	1.0	2.0	2.8
Primary balance after grants (proposed under adjustment scenario)	-1.8	-1.1	-0.3	0.0

Source: IMF staff estimates
[1] Other measures could include, for example, other tax policy and tax administration measures, streamlining of transfers to SOEs, rationalization of spending on goods and services.

[14] Staff estimates of the authorities proposed measures in the 2018 budget are as follows: (i) 0.4 percent of GDP in new excise tax measures; (ii) 0.1 percent of GDP in specific taxation on mining and petroleum activities; and (iii) 0.3 percent of GDP in wage bill savings measures.

[15] Staff assumes fiscal multipliers of 0,5, which are comparable to those observed in low income developing countries taxes and current spending.

[16] Based on IMF technical assistance, staff has identified spending and tax policy measures that would support the achievement of this objective. The unidentified measures in Text Table 2 reflect the remaining fiscal effort. This could come from wage bill, revenue administration, and other tax policy measures among others.

[17] While front loading of fiscal adjustment would have been desirable, only further spending cuts can take place in 2018, because changes in the tax base or tax rates approved during the course of the year can only take effect in the next year.

Box 2. Social Protection

Mozambique's non-contributory social protection system comprises mainly three programs. These include (a) the PSSB (*Programa Subsidio Social Basico*), the main program, which is a cash transfer mechanism aimed at elderly and disabled people; (b) the PASP (*Programa de Acção Social Produtiva*), a public works program for extremely poor households; and (c) the PASD (*Programa de Apoio Social Directo*), a temporary support program for poor households with adults who are temporarily unable to work.
Mozambique's social protection system has improved its coverage in recent years, benefiting from increased domestic financing. Following past assessments of the social protection system showing that the system was not responsive to emerging vulnerabilities, the government has invested significant resources to improve coverage. The numbers of households covered under the three main social protection programs has increased from 287,000 in 2011to 549,565 households in 2017. Nevertheless, the level of coverage is still deemed relatively low (around 19% of people living below the poverty line), especially compared to comparator countries. The National Strategy for Basic Social Security (ENSSB) 2016-2024 approved by the Council Ministers in 2016 suggests a shift from a targeted, charity focus to a rights-based universal benefit approach.

Improvements in the generosity of social protection benefits are also underway. Benefits under these social assistance programs tend to be very low. For instance, in the case of the PSSB, benefits range from 310 Meticais (around $5) per month for individuals to 620 Meticais (around $10) per month to elderly people with four dependents. Nevertheless, there have been efforts to increase the benefit amount over the years, especially in the case of the PSSB. More recently, the 2018 budget which was approved by parliament, envisages a significant increase in the allocation for social protection programs. For the PSSB, the budget allocation is set to increase from around 1.7 billion Meticais in 2017 to around 3.2 billion Meticais in 2018. Overall, spending on all three programs is set to increase by around 2 billion Meticais (or around 0.2 percent of GDP) in 2018. The increase in the budget allocation in 2018 mostly implies an increase in the amount of benefit rather than the number of households covered (which is set to increase by around 12 percent). Overall cost remains low, below 0.5% of GDP, far below the average in the region regarding cash transfer programs.

Overall, while the observed progress is encouraging, there are still a number of areas where social protection can be improved. Despite the positive steps, there are still major gaps in coverage and the generosity of benefits. For instance, the amount allocated to PSSB beneficiaries is still not enough to cover for basic needs of poor households. Similarly, the coverage of beneficiaries is still relatively low. The government should continue efforts to improve coverage and generosity further, and reduce program fragmentation. Furthermore, as suggested by the World Bank and UN agencies as ILO and UNICEF, deep reforms should also address key operational aspects including: (a) streamlining criteria and approaches to targeting the poorest households (e.g., proxy means tests); (b) instituting a single registry of all beneficiaries and integrating it into e-INAS, the management information system build with support from ILO, to improve monitoring and efficiency; and (c) adopting a formal electronic payment system, through outsourcing, for all cash-based benefit programs.

22. Achieving the proposed fiscal targets would require resolute fiscal efforts.

- Revenue measures should aim at broadening the tax base and improving revenue administration.

  2018 Budget measures

  - Reviewing the Excise Tax Code (ICE) as proposed in the 2018 budget proposal that was submitted to Parliament.
  - Specific taxation on mining and petroleum activities.

Staff proposed measures

- Removing VAT exemptions in line with the recommendations stipulated in the FAD technical assistance.
- Revising the VAT refund mechanism, by clearing the backlog of VAT refund claims through securitization and enforcing the funding of a sub-account with a fixed percentage of VAT receipts to repay exclusively new VAT refunds claims.

23. Addressing existing domestic arrears should be a key priority. The stock of domestic arrears reached around 3.7 percent of GDP at end 2016.[18] Validating these arrears and gradually clearing them should be a priority. This should proceed after discussions with creditors and after reaching agreement on clearance modalities.

2018 Budget measures

- Reducing some bonuses and allowances as proposed in the 2018 budget proposal.

Staff proposed measures

- In the short-term, the growth of wage spending can be contained using short-term measures that address wage levels or employment: containing wage growth, streamlining allowances and bonuses, curtailing overtime pay, and attrition.
- Over the medium-term, structural reforms need to be implemented in order to induce sustainable and permanent savings in the wage bill, and improve the efficiency and efficacy of wage spending: structural pay reforms to align job specific requirements with compensation, systematic review of compensation aiming at simplifying it, functional reviews and restructuring of government entities, and strengthening wage bill budgeting, execution and control.

24. Preventing the accumulation of new domestic arrears requires addressing cash management flaws, lack of expenditure control, and transparency. Staff urged the authorities to timely record spending in the information management system at each stage of the spending process. Other recommendations to regain control over expenditures and reduce the stock of arrears are as follows: (i) streamlining the network of spending units (ii) enforcing budget ceilings; and (iii) optimizing government liquidity management.

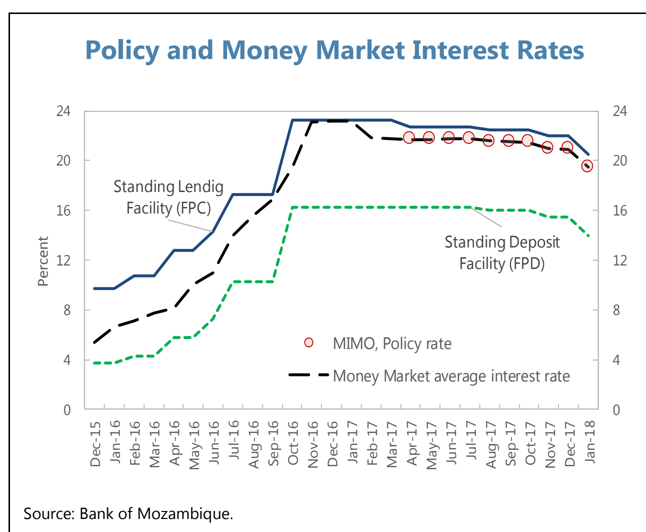
25. Authorities' Views. While the ministry recognized that reducing the fiscal deficit over the medium term was desirable, it was concerned about staff's views on the pace of the adjustment and intends to follow a more gradual deficit reduction path. The ministry expressed doubts about crowding out of the private sector as a result of the fiscal stance. They noted that a loosening of the monetary stance would help reduce public debt service costs and encourage private sector investment.

[18] Data for 2017 are not yet available.

B. Monetary Policy and Foreign Exchange Management: Measured Normalization and Stability

26. From April 2017, the central bank changed its operational target from monetary aggregates to a short-term interest rate (SIP Chapter 1)**.** Thus far, the interbank money market appears to follow the signals of the MIMO rate despite excess liquidity of the banking system (Figure 3). Given the rapid disinflation the Monetary Policy Committee (MPC) faces the challenge of pacing MIMO's rate cuts while accounting for fiscal risks. At the same time, sustaining a prolonged period of high real interest rates risks further weakening non-mining non-agriculture economic activity, possibly worsening NPLs, and increasing pressure on borrowing costs. Staff recommended cautious but decisive cuts in the policy rate.

27. The absence of a BM-issued security for monetary policy purposes, brings additional challenges to liquidity management by the central bank. As reserve requirements have been reduced and banks are near their exposure limits to sovereign risk, sterilization operations have become less successful. Interventions of the BM in the FX market have created additional needs to sterilize liquidity. Looking ahead, staff recommended cautiousness in further lowering reserve requirements level. The BM should remove the restriction on banks access to the standing lending facility (only twice a week) and explore issuing certificates (CDs) for monetary policy.



Source: Bank of Mozambique.

28. The exchange rate has appreciated in nominal terms by 24 percent since October-2016 and has been broadly stable since June 2017. BM's net selling operations have become rare since late 2016 and BM has become a net buyer. Inflows from primary exports activities—notably coal—are bringing increasing FX availability to the market, while demand is low. Staff encouraged the authorities to rely on exchange rate flexibility as an absorber of external shocks and to develop a robust FX strategy that further deepens the market and strengthens financial stability while limiting central bank interventions to addressing excessive volatility. The External Balance Assessment (EBA) concludes that the metical is overvalued given current and projected fundamentals over the medium term under current policies (Annex 2).

29. A new FX market law was introduced in December 2017 allowing more flexibility in the management of exports proceeds. Staff supports the authorities' intentions to partially liberalize the capital account. The BM's reform allows exporters and investors to keep 100 percent of proceeds in foreign currency.[19] These reforms are expected to minimize forex risks to exporters,

[19] The previous regulation obliged conversion of 50 percent of the proceeds to domestic currency creating foreign exchange risk to companies.

mitigate capital flight, and reduce transaction costs. They, however, include a risk of higher dollarization and will result in lower FX flows going directly to the BM. The authorities must remain vigilant and consider whether higher reserve requirements on deposits in foreign currency, and minimum liquidity requirements in FX, may be warranted.

30. Authorities' Views. The BM concurred with the mission on the need to reevaluate the pace of interest rates normalization and on relying on the exchange rate as shock absorber. The BM stressed that high interest rates were instrumental to rapid disinflation in 2017 and that fiscal consolidation is needed to complete the monetary policy normalization and achieve a balanced policy mix that can sustain growth with price and financial stability. Furthermore, the BM stated that it would let the exchange rate clear the market in case of excess demand for FX. It also noted that macroprudential measures against dollarization are in place, such as ex-ante provisioning for non-exporters borrowing in dollars.

C. Strengthening Resilience and Containing Financial Sector Risks

31. The central bank is committed to implementing further monetary and financial sector reforms to gain structural resilience (Box 3). The central bank continues to strengthen its governance, organization, analytical tools and monetary and FX operation framework with cooperation of Norges Bank and IMF technical assistance. The plan intends to enhance financial stability analysis, reporting, communication; modernize the national payment system and oversight; and improve currency cash management. The financial regulatory framework is being strengthened to mitigate vulnerabilities and enhance bank resolution capacity.

Box 3. Monetary and Financial Sector Regulatory Measures

Monetary

- Adopted an indirect monetary policy instrument: the MIMO rate in April 2017.
- Revoked the limit of 700 thousand Mts. per person for the use of credit cards abroad in April 2017 introduced in December 2015.
- Changed the reserve requirement base of calculation from daily to monthly average, starting in June 2017.
- Broadened the investor base for primary issuance of T-bills to include non-bank financial institutions effective in June 2017.
- Implemented new foreign exchange market regulation in December 2017.

Financial

- Approved the national strategy for financial inclusion 2016-2022 in March 2016 and operationalized the National Committee on Financial Inclusion with two working groups in mid-November 2017.
- Increased the minimum capital adequacy ratio (to 12 percent) and the minimum social capital value (to Mt. 1.7 billion) to be phased in until 2020 in April 2017.
- Introduced a minimum liquidity ratio fixed at 25 percent of short-term liquid assets in June 2017.

Transparency and competition

- Required banks to publish quarterly selected FSIs on solvency and liquidity effective March 2017.
- Revised methodology for calculating the foreign exchange reference rate and related regulation in April 2017.

Introduced a Standardized Prime Interest Rate for bank lending ('Indexante Unico') jointly with the Mozambique Bank Association effective June 2017.

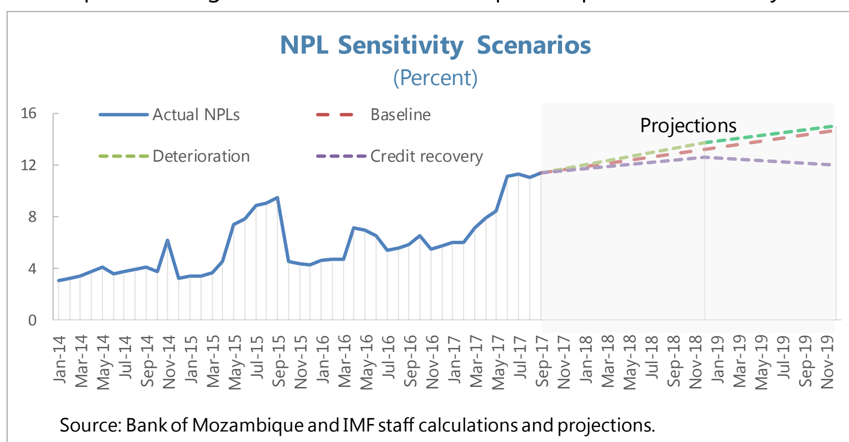
32. The current environment constrains credit growth. Banks are placing their extra-balances in domestic currency at the central bank in the form of excess reserves, or via reverse repos in the overnight market. The currently high real returns and low risks of those liquidity placement options constrain credit growth.[20] Moreover, the increase in minimum capital requirements, to be phased in over three years, while welcome for the overall strengthening of the system, reduces at the margin the profitability of intermediation in the current circumstances.

33. The banking system continues to hold significant capital and liquidity buffers. New regulations to increase the CAR and establish minimum liquidity requirements were put in place in 2017. While reports indicate that banks remain liquid, well capitalized, and profitable on average (Table 6), there is heterogeneity across institutions. In addition, nonperforming loans (NPLs) have increased substantially, from 5.5 percent of total loans at end-2016 to 11.4 percent in September 2017. Several factors underlie this deterioration (Box 4). Staff encouraged the authorities to remain watchful of loan classification, collateral valuation, and provisioning.

Box 4. Nonperforming Loan Sensitivity Analysis.

The level of nonperforming loans in the Mozambican banking system doubled to 11.4 percent in September 2017 since end-2016, on average. Several factors underlie this deterioration: (i) enhanced credit risk supervision, (ii) the slow economy, (iii) the rise in real interest rates, and (iv) the arrears of the public sector. The main mitigating factor is the level of provisioning, which remains considerable at 79 percent of NPLs (58 percent in specific provisions, down from 78 percent at end-2016, 11 percent in general provisions, and 10 percent prudential provisions beyond those required by IFRS). Looking forward**,** NPLs will likely remain a vulnerability factor on the system's balance sheets. To gauge possible impacts of NPL growth on provisioning and capital requirements, the mission worked on a sensitivity analysis under three scenarios of portfolio deterioration for 2018-19**.** The scenarios include a baseline one under current trends, a second scenario of low credit growth with fast NPL increase, and a third one with credit recovery.

All three scenarios result in material provisioning needs and additional capital requirements. The system would remain solvent, though capital adequacy buffers would be eroded and some banks would require additional capital. These results suggest that the BM must remain watchful of the banks' portfolio performance, through the enforcement of loan classification rules, collateral valuation, and the opportune provision building.



Source: Bank of Mozambique and IMF staff calculations and projections.

34. Meanwhile, exposure of banks to sovereign risk is at a high point. Given the high and rising level of such exposures (estimated at 25 percent of total assets by end September 2017), some

[20] In December 2017, the deposit facility of the BM earned 7 percent in real terms.

institutions cannot further accumulate claims on the government and, at times, the weekly T-bill market auctions have been deserted.

35. Bank exposure to loss-making state-owned enterprises presents risks. In 2016, the ten largest non-financial SOEs experienced rising losses as bank debt and loan rates increased. A debt sustainability test performed by staff based on SOEs' debt stock at end-2016 in relation to a cash flow proxy (earnings before interest, taxes, depreciation and amortization) suggests that about half of those SOEs have a substantial debt overhang (SIP Chapter 3). In the absence of corporate restructuring, restoring a sustainable debt level would require partial debt forgiveness or adjusting debt service terms. If banks should fully provision for debt at risk,[21] the banking system's capital adequacy ratio would drop by about 5 percentage points to 16 percent, with a few banks close to or below the minimum required ratio. Banks have started to reflect the higher risk of SOE loans in their loan classification and provisioning practices, but supervisory authorities should ensure such prudent practices are entrenched while making sure banks build capital buffers for instance through earnings retention.

36. The bank resolution framework needs strengthening to deal with systemic failures and the safety net is still incipient. Weaknesses in the legal framework complicated the resolutions of Moza and Nosso Banco. In the absence of other reputable buyer, Moza was sold to the BM's pension fund; Moza is currently run by professional bankers and is gradually recovering. Staff encouraged the authorities to establish a policy to ensure independent governance and adequate surveillance, and prepare a divestment strategy for the medium term. It supports ongoing work to prepare a new bank resolution framework aimed at enhancing the resolution powers of the BM. Strengthening the deposit insurance scheme is also warranted. The Fund stands ready to continue providing technical assistance in these areas.

37. Modernizing the 1992 central bank law would strengthen the BM's credibility and monetary policy effectiveness. In particular, the law allows lending to the government interest-free yearly-loans up to 10 percent of revenue collected in the penultimate year. Staff recommended that, as a first best, the new law ban credit to the government or strictly limit it as a second best.

38. Staff commended the authorities for their efforts at promoting financial inclusion within the 2016-2022 National Strategy (SIP Chapter 3). Mobile banking and electronic currency could play a key role in extending the network of transactions and creating opportunities for people in rural areas with low income levels. Staff encourages the authorities to continue efforts to implement the Financial Inclusion Strategy and periodically assess if further measures are needed.

39. Mozambique adopted IFRS in 2007 and will transition to IFRS9 in 2018. The change includes a move toward impairment modelling, among other factors, and the process should be carefully phased-in to avoid unintended consequences.

[21] This is an acid test, since some loans may have collateral or guarantees that warrant partial provisioning.

Authorities' Views

40. The BM concurred with staff's views and expressed its commitment to modernize central banking, and strengthen regulation and prudential supervision. The BM appreciated Fund multiyear TA support in partnership with Norges Bank to strengthen governance and capacities to face modernization challenges in core functions. It envisions requesting TA support for key legal reforms. The authorities stressed their intention to improve bank resolution tools, strengthen the safety net and continue revamping risk based bank supervision.

41. The BM concurred on the need to remain vigilant to macrofinancial risks in an environment of low growth, high real interest rates, and tight financial conditions. It emphasized that current conditions require close monitoring of the financial system's exposure to SOEs and government securities, and exposure of firms to SOEs and government arrears. In this context, it agreed to further develop capacities in macroprudential surveillance and communications on financial stability issues by focusing resources to produce a biannual stability report and regularly publish Financial Soundness Indicators (FSIs).

D. Debt Policy: Achieving Sustainability

42. Debt sustainability. Staff argued that the authorities need to adopt a comprehensive debt strategy aiming at bringing down the debt risk rating of Mozambique to "moderate" over the medium term and reducing financing needs to prudent levels. This could be achieved by aiming at a reduction in the solvency indicators (the present value of the external public and publicly guaranteed debt relative to GDP, to exports and to revenue) to below the prudent thresholds over the medium term (which should be greatly helped by the completion of big LNG projects by 2023), coupled with a trajectory for the liquidity indicators (the external debt service relative to revenue and to exports) well contained beneath their respective thresholds to mitigate risks associated with high debt levels. In staff's view, given current financing prospects, this will be difficult to achieve even under the scenario implementing a fiscal effort that achieves a primary fiscal balance by 2022, and more measures will be needed.

43. Debt management. Staff urged the authorities to improve debt management. In particular, the debt unit's capacity needs to be strengthened to exercise effective oversight over the entire public debt portfolio, including SOEs and loans that are part of cooperation agreements signed by other line ministries. Moreover, implementing the joint Fund and World Bank recommendations to strengthen governance, improve transparency, and ensure accountability in the area of debt management is crucial.

Authorities' Views

44. While the authorities recognized the need for reducing financing needs over the medium term and improving debt management, they had reservations on the pace of adjustment of the primary balance recommended by staff (see fiscal section above). The authorities intend to actively resume discussions for the restructuring of public debt owed to private creditors, initiated in October 2016, as well as bilaterally, the discussions with the six official creditors (Libya, Iraq, Angola, Bulgaria and Poland, as well as Brazil).

E. Structural Policies: Strengthening Governance and Promoting Inclusive Growth

Governance

45. While Mozambique's anti-corruption legal framework is sound, it is lacking in implementation and enforcement (SIP Chapter 2)**.** In 2012, a comprehensive legislative anti-corruption package was approved and aligned the legal framework with international standards. Notwithstanding these efforts, lack of resources and poor prioritization have resulted in an ineffective implementation of the legal framework. A Central Public Ethics Commission (GCCC) was created to prevent and investigate conflict of interest. Yet it was only recently given an office; the commissioners cumulate their GCCC responsibilities with other full-time jobs. While the asset disclosure system is comprehensive, its implementation falls behind international best practices: asset disclosures are not published, sanctions for non-compliance or false declarations are not sufficiently dissuasive, and verifications are not strategic. During 2017, only 55 percent of officials complied with their obligation to declare assets with no consequences for the 45 percent who did not declare.

46. In the wake of disclosure of hidden debt in 2016, the authorities are working on an action plan to strengthen governance, improve transparency, and ensure accountability. Fund and World Bank staff discussed with the authorities' joint recommendations for the action plan (Annex III). The key recommendations include:

- **Governance:**
    - Introduce a framework for fiscal responsibility and efficient management of natural resources wealth.
    - Strengthen the issuance and management of public debt and guarantees, and prepare recovery or restructuring plans for SOEs in financial distress; the latter includes liquidating Ematum, MAM, and Proindicus after transfer of security assets to the State.
    - Improve public investment and assets management, and put in place a framework for government autonomous entities, and address arrears.
- **Transparency:**
    - Support public and parliamentary oversight through reporting, disclosure, and amendments to laws governing public finance, SOEs and the extractive industry sector. Improving fiscal reporting through: (i) enhancing reporting on commitments, arrears, debts and other obligations under guarantees, and major public investment decisions; (ii) requiring annual reporting on SOEs and government autonomous entities, including quarterly reporting on the financial operations of a subset of SOEs presenting large fiscal risks; (iii) publishing annual fiscal risks assessment and consolidated financial statements of SOEs in line with IFRS standards; and (iv) disclosing beneficial ownership in the

extractives sector, including State's participation and the rules governing its financial relations with SOEs.

- **Accountability:**

  - Resolve the issue of unreported loans of EMATUM, MAM and Proindicus, and strengthen compliance, enforcement and key laws supporting the fight against corruption, including stepping-up anti-corruption efforts to prevent abuses in the administration of SOEs, and back accountability process and case resolution.

Staff commends the authorities for submitting to Parliament the SOE law and for approving a decree providing a regulatory framework for the issuance of public debt and guarantees.

47. Information gaps in the audit of hidden loans need to be addressed. The completion of the Kroll audit report and the publication of its summary in June 2017 are important steps towards greater transparency. However, critical information gaps remain unaddressed regarding the use of the loan proceeds. Staff urged the authorities to provide full clarity on this use.

48. Strengthening the fiscal framework for managing natural resource wealth is essential. Staff recommended to consider fiscal rules and a sovereign wealth fund to underpin a fiscal responsibility law, while noting that reducing costly debt must take precedence in the short term. To raise awareness on these issues, staff suggested organizing a high-level workshop to discuss international experiences and best practices ensuring an efficient management of natural resources over time.

49. Structural reforms to support inclusive growth, reduce poverty, and promote economic diversification. Structural reforms to remove impediments to investment and employment creation are necessary for diversified and sustained inclusive growth, and to support poverty reduction. Underdeveloped infrastructure, difficulties with corruption, and ambiguous regulations are key challenges according to Doing Business (Mozambique ranks 138th out of 190 countries in 2018).[22] The private sector also struggles with unresolved public-sector arrears and tight and expensive access to credit. Staff urged the authorities to adopt, in consultation with the World Bank, a set of reforms aimed at improving the weak business climate.

50. Mozambique is one of the most vulnerable countries to natural disasters and climate risks (SIP Chapter 5)**.** The country's geographic location and topography (particularly low-lying elevation) add to the risk. Additionally, weak socio-economic infrastructure, high poverty, and heavy dependence on rain-fed agriculture magnify these risks, in a context of limited access to insurance. Limited preparedness and lack of adequate resources further inhibit the country's crisis adaptation and response capacity. Staff recommends the authorities integrate climate change mitigation within their developmental agenda and preparedness going forward.

[22] The World Bank *Doing Business Indicators* and other rankings used in this Staff Report, such as the *Corruption Perception Index*, are subject to uncertainty around the point estimate. Rankings reflect the relative, not the absolute, performance of the country.

Authorities' Views

51. The authorities welcomed IMF-WB recommendations on their action plan. The MoF noted that the government passed a decree establishing a framework to contract public debt and issue guarantees, and transmitted to Parliament a draft SOE law. In addition, it recognized that substantial technical assistance would be required to implement the action plan. On the follow up to the Kroll audit, the authorities noted that the issue is under investigation by the Prosecutor general and urged the staff to wait for the outcome of this investigation, which hopefully would answer the staff's queries on the use of the money borrowed by Ematum, Proindicus, and MAM.

F. Data and AML/CFT Issues

52. Data provision has some shortcomings but is broadly adequate for surveillance. The authorities are encouraged to address long-standing data gaps in fiscal reporting and national accounts. At the same time, they should continue their efforts to improve BOP and banking sector data, including by updating data more regularly and increasing the categories of data disseminated through the National Institute of Statistics (INE).

53. An effective implementation of the AML/CFT framework could support Mozambique's anti-corruption efforts. While Mozambique has a generally adequate AML/CFT legal framework, it must take important strides to achieve an acceptable level of effectiveness. This would imply improving the AML/CFT supervision of financial institutions as well as implementing enforceable requirements to identify politically exposed persons; and increased transparency of the beneficial ownership of corporate vehicles. Additional laws and regulations are required, namely an asset recovery law and a mutual legal assistance law. There are challenges in the implementation of certain provisions in the AML/CFT law, such as with the supervision of Designated Non-Financial Businesses and Professions (DNFBPs).

54. An update of the safeguards assessment of the BoM was completed in June 2016. The assessment found that the governance structure at the bank continues to lack independent oversight of management and operations. Legal reforms are needed to address weaknesses in the governance arrangements and to strengthen provisions on autonomy and accountability. The BoM publishes its financial statements that are prepared and audited in accordance with international standards.

STAFF APPRAISAL

55. Mozambique's economy is facing difficult challenges. While inflation has declined rapidly, real GDP growth continues to weaken. An excessively loose fiscal policy and a tight monetary policy stance in 2017 resulted in a crowding out of the private sector. The treasury is absorbing available credit through the issuance of T-bonds, while credit to the economy is declining. Public debt remains in distress. Domestic public debt is in distress and several repayments on external borrowing were missed.

56. An urgent rebalancing of the policy mix is needed to ensure durable macroeconomic stability. A sustained fiscal consolidation effort aimed at closing the primary balance deficit over the

medium term is critical. Staff urges the authorities to further consolidate its fiscal position by eliminating VAT and other tax exemptions that could help mobilize additional revenues and by reducing current spending, while protecting outlays to social and infrastructure spending. While the monetary authorities managed to restore fluidity in the FX market and inflation declined rapidly, monetary policy has become too tight. Staff encouraged the authorities to rely on exchange rate flexibility as a shock absorber and welcomes the December 2017 decision of the MPC to lower the policy rate by 150 basis points. Looking ahead, monetary policy can be further eased while remaining cautious given the fiscal stance. To this end, the MPC faces the challenge of pacing policy rate cuts in an environment of rapid disinflation, weak domestic demand, and fiscal pressures.

57. Restoring debt sustainability and reducing financing needs to prudent levels over the medium term is crucial. As the magnitude of the government's planned fiscal effort over the medium term remains unclear, uncertainties on the size of the financing needs over the next few years remain high. Moreover, progress in discussions with creditors on a debt restructuring would be an essential contribution to restoring debt sustainability. To that effect, staff urges the government to clarify its medium-term fiscal objectives.

58. Steadfast implementation of financial sector and monetary regime reforms is essential to strengthen resilience and mitigate macrofinancial risks. The authorities must remain vigilant vis-à-vis the risks stemming from a prolonged period of high real interest rates, low growth, rapid increase in public domestic debt, and accumulation of public sector arrears. These risks could weaken non-mining activity, cause higher NPLs and SOEs financial distress, increase banks sovereign risk exposure, and pressure public finances through high borrowing costs and contingent liabilities. Staff supports the BM's efforts to enhance supervisory capacities and the bank resolution framework. The evolving monetary regime should build on enhanced communications, increased technical capacities and a reformed central bank law with a clear mandate, granting operational autonomy, precluding or strictly limiting lending to the government and strengthening accountability. The authorities should also consider a strategy to deal with SOEs over indebtedness to mitigate spillovers to the financial system.

59. Staff welcomes the authorities' commitment in principle to improve governance, transparency, and accountability, but stresses the need to strengthen implementation and enforcement going forward. While Mozambique has a sound anti-corruption legal framework in place, staff recommends that the authorities strengthen its enforcement. Looking ahead, staff urges the authorities to redouble their efforts aimed at fighting corruption. Reforming the SOE sector and to implementing a robust action plan to strengthen governance, transparency, and accountability, is also crucial.

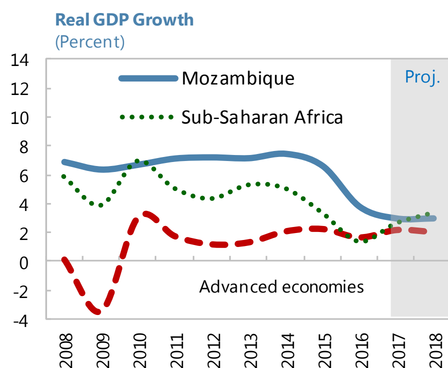
60. Addressing the missing information in the audit report requires decisive action by the government. Bridging the information gaps that remain after the completion of the audit of three public companies involved in the hidden loans would help restore confidence and encourage private investment. Staff urges the government to provide full clarity on the use of the proceeds of the Ematum, Proindicus, and MAM loans. Staff welcomes the authorities' approval of a decree establishing a framework to contract public debt and issue guarantees, and the submission to Parliament of a new SOE law.

61. Further progress on the structural reform agenda will be important to support higher and more inclusive growth, job creation, and further reduction of poverty and inequality. Restructuring and attracting private sector participation in ailing SOEs will be key to improve efficiency, reduce financial losses and related fiscal costs and vulnerabilities. Implementation of further steps in strengthening the business climate and governance will be important to support private investment and job creation, as well as continued efforts to foster financial deepening and inclusion through the national strategy already laid out.

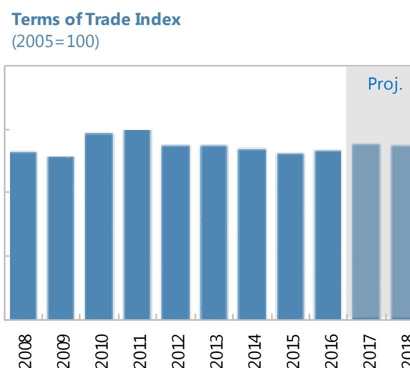
62. It is recommended that the next Article IV consultation take place on the standard 12-month cycle.

Figure 1. Mozambique: Impact of Global Developments

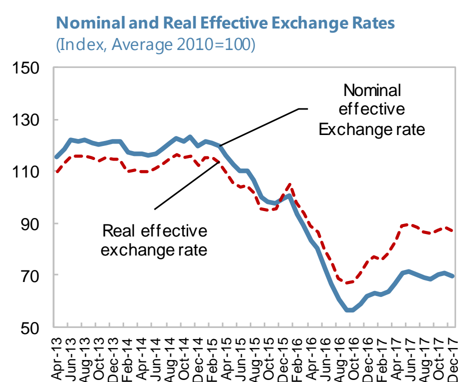
Mozambique's growth outlook weakened relative to SSA countries



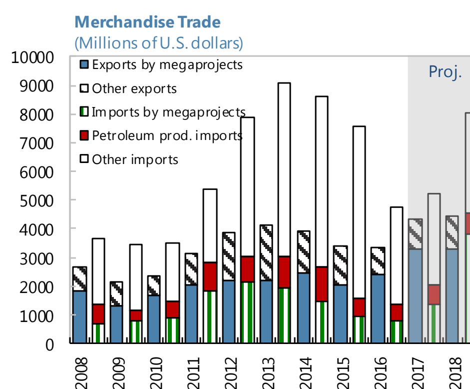
...despite recent gains in terms of trade due to higher international coal prices.



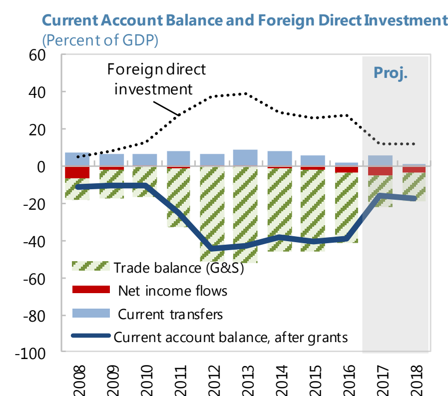
The metical recovered after a sharp depreciation starting in 2015.



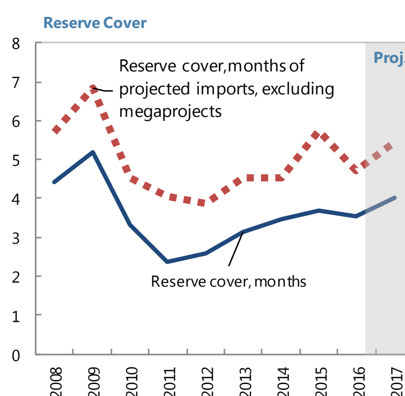
And the overall trade deficit narrowed, due to lower imports and higher export prices for coal.



As a result, the current account deficit narrowed...



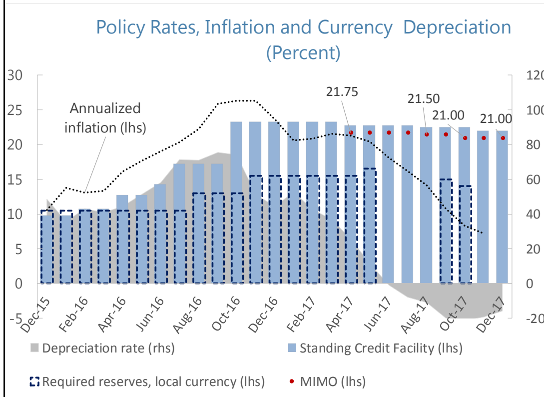
...and reserve coverage excluding mega projects has recovered



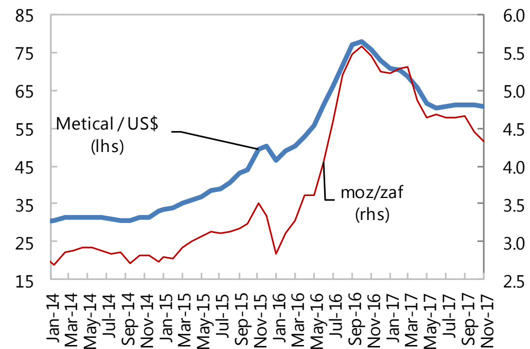
Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 2. Mozambique: Inflation, Monetary and Financial Developments

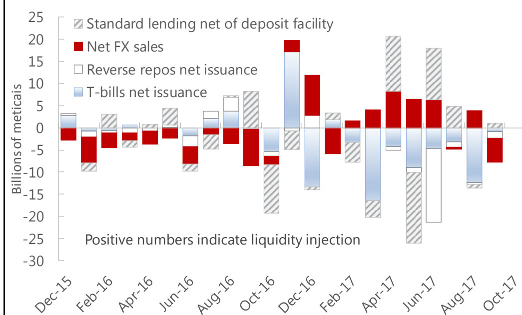
The monetary policy was tightened from Oct '16 in response to high inflation…



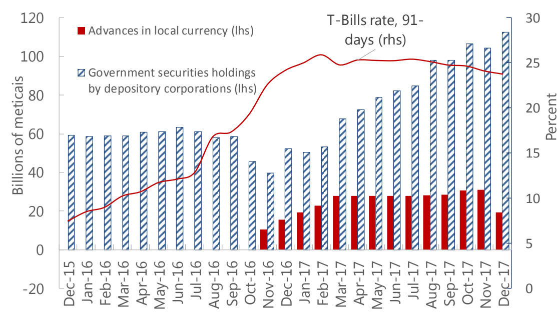
…that helped stabilize the exchange rate market.



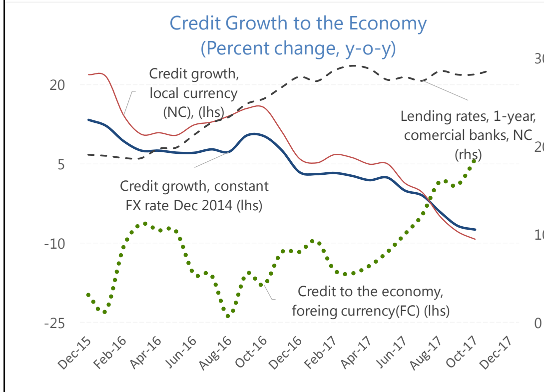
Open market operations issuing T-bill mopped out liquidity, and…



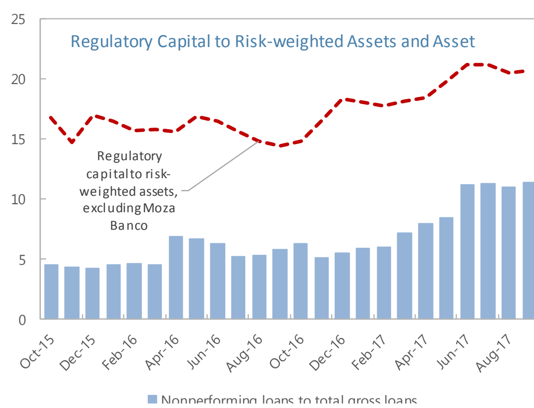
…increased government borrowing cost despite recurrence to short-term credit from the central bank.



Credit and monetary aggregates growth slowed down and has started to fall in real terms since May 2017…



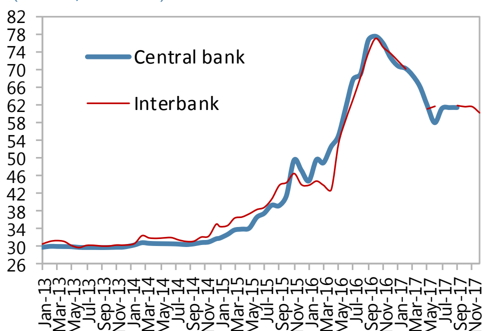
The financial sector signaled vulnerabilities halted with the resolution of two banks.



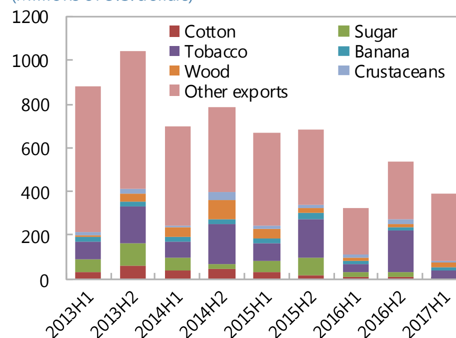
Sources: Central Bank of Mozambique

Figure 3. Mozambique: Selected External Sector Developments

Exchange rate pressures eased in line with the tight monetary policy

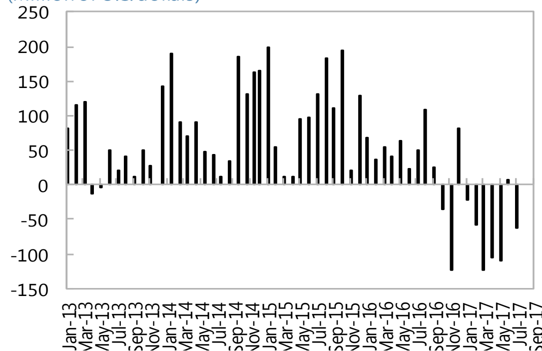


Backed with a recovery in coal export volumes and prices …

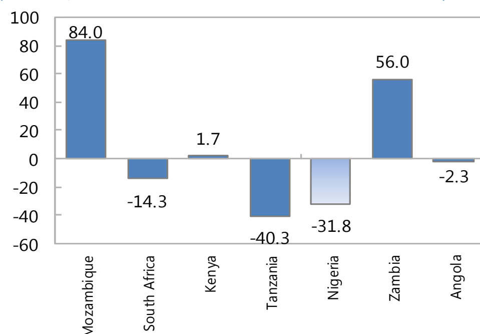


…and deposits are recovering

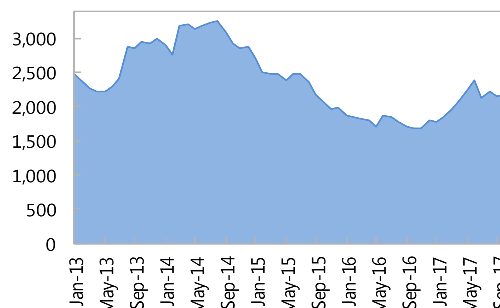
With BM reducing its FX interventions.



Despite a strengthening of the US dollar.



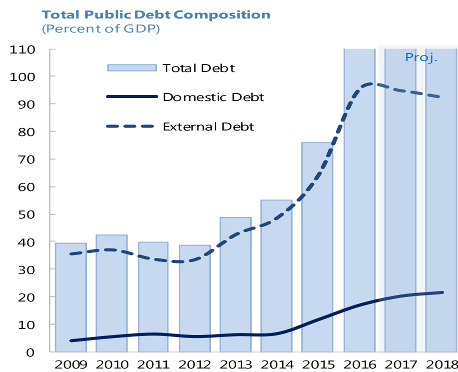
And overall reserves stabilized.



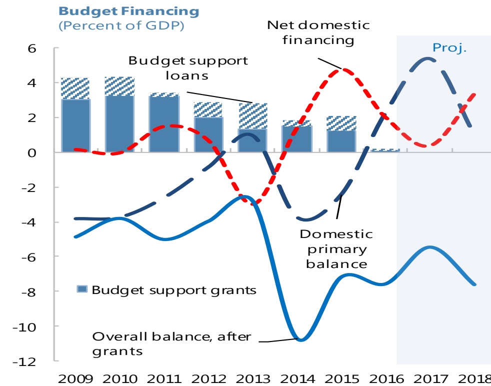
Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 4. Mozambique: Fiscal Developments

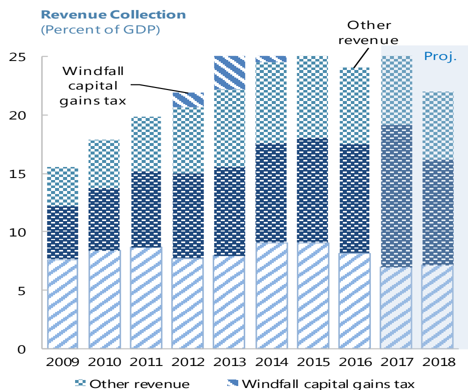
Public Debt has been rising fast because of the disclosure of hidden loans, and stabilized following the metical appreciation.



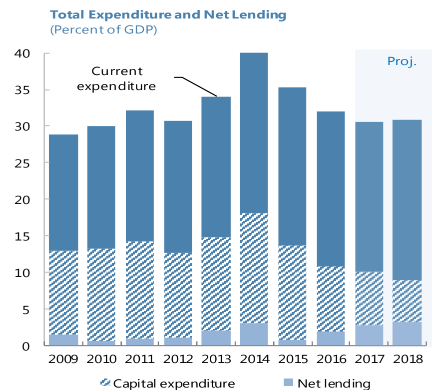
...but fiscal policy remains loose with the overall deficit remaining large



...as revenue collection continue to weaken



...coupled with an increase in expenditures.



Sources: Mozambican authorities and IMF staff estimates and projections.

Table 1. Mozambique: Selected Economic and Financial Indicators, 2016–23

	2016	2017	2018	2019	2020	2021	2022	2023
	Prel.				Proj.			
	(Annual percentage change, unless otherwise indicated)							
National income and prices								
Nominal GDP (MT billion)	689	802	875	949	1026	1108	1195	1386
Nominal GDP growth	16.5	16.4	9.0	8.4	8.1	8.0	7.9	16.0
Real GDP growth	3.8	3.0	3.0	2.5	2.4	2.3	2.2	9.9
GDP per capita (US$)	392	429	472	482	491	499	506	551
GDP deflator	12.3	13.1	5.9	5.8	5.6	5.6	5.6	5.5
Consumer price index (annual average)	19.2	15.3	6.7	5.7	5.5	5.5	5.5	5.5
Consumer price index (end of period)	21.1	7.2	6.5	5.5	5.5	5.5	5.5	5.5
Exchange rate, MT per US dollar, eop	71.0	...	...	...	...	...	...	...
Exchange rate, MT per US dollar, per.avg.	61.1	...	...	...	...	...	...	...
External sector								
Merchandise exports	-2.5	27.9	18.1	7.4	-1.2	2.9	2.8	29.7
Merchandise exports, excluding megaprojects	-32.5	-7.9	7.5	6.7	6.6	7.3	7.4	7.8
Merchandise imports	-37.5	2.9	13.7	61.2	30.8	30.5	27.4	8.6
Merchandise imports, excluding megaprojects	-40.5	3.3	7.3	0.1	3.2	3.9	4.3	3.8
Terms of trade	1.9	3.2	0.0	-0.4	-0.4	-0.7	0.0	0.0
Nominal effective exchange rate (annual average)	-33.0	...	...	...	...	...	...	...
Real effective exchange rate (annual average)	-22.3	...	...	...	...	...	...	...
	(Annual percentage change, unless otherwise indicated)							
Money and credit								
Reserve money	35.2	1.4	5.6	5.2	5.0	5.0	5.1	9.2
M3 (Broad Money)	10.1	4.5	7.9	7.8	7.6	7.5	7.4	11.6
Credit to the economy	12.6	-10.4	2.9	2.8	2.7	2.3	2.1	5.2
(Percent of GDP)	37.9	29.2	27.5	26.1	24.8	23.5	22.2	20.2
	(Percent of GDP)							
Investment and saving								
Gross domestic investment	42.7	36.5	54.7	86.3	106.7	138.4	162.8	136.6
Government	10.8	10.1	8.9	10.9	10.4	10.9	11.7	11.5
Other sectors	31.9	26.4	45.8	75.4	96.3	127.5	151.1	125.1
Of which: Megaprojects	11.1	1.5	5.9	31.8	53.7	79.7	112.5	116.3
Of which: non-Megaprojects	20.8	24.9	39.9	43.6	42.6	47.8	38.6	8.8
Gross domestic savings (excluding grants)	2.7	20.4	37.6	41.5	40.0	47.3	46.4	18.8
Government	2.8	4.6	0.0	-1.1	-0.2	0.6	0.5	1.1
Other sectors	-0.1	15.9	37.6	42.7	40.2	46.6	45.9	17.7
External current account, before grants	-39.9	-16.1	-17.1	-44.7	-66.7	-91.1	-116.5	-117.8
External current account, after grants	-39.2	-16.1	-16.9	-44.6	-66.6	-91.0	-116.4	-117.7
Government budget								
Total revenue [1]	24.0	25.1	22.1	22.0	21.9	21.8	21.8	21.6
Total expenditure and net lending	32.4	32.1	30.9	33.9	32.5	32.1	33.0	32.1
Deficit reducing measures	0.0	-1.5	0.0	0.0	0.0	0.0	0.0	0.0
Payments in arrears	1.3	...	...	...	...	...	...	...
Overall balance, before grants[2]	-9.7	-7.0	-8.8	-12.0	-10.6	-10.3	-11.2	-10.4
Total grants	2.1	1.6	1.3	1.2	0.7	0.6	0.6	0.5
Overall balance, after grants[2]	-7.6	-5.5	-7.5	-10.8	-9.9	-9.6	-10.6	-9.9
Primary Balance, after grants[2]	-4.6	-1.8	-3.2	-5.1	-5.5	-6.4	-7.6	-7.6
Overall balance (excl. the one-off 2017 capital gains tax revenues), after grants[2]	-7.6	-8.2	-7.5	-10.8	-9.9	-9.6	-10.6	-9.9
Primary Balance (excl. the one-off 2017 capital gains tax revenues), after grants[2]	-4.6	-4.5	-3.2	-5.1	-5.5	-6.4	-7.6	-7.6
External financing (incl. debt relief)	2.2	0.9	1.0	3.0	3.6	3.8	5.1	0.8
Net domestic financing	2.0	0.4	3.3	1.8	1.1	-0.1	-0.2	-0.1
Total nominal public debt [3]	128.3	112.0	121.8	130.1	136.7	143.1	149.3	137.5
Of which: external	103.7	85.2	95.3	101.3	106.0	110.6	114.3	107.4
Of which: domestic	24.6	26.7	26.5	28.8	30.7	32.5	34.9	30.1
	(Millions of U.S. dollars, unless otherwise indicated)							
External Public Debt [3]	10,065	11,395	13,413	14,973	16,354	17,812	19,152	20,137
of which: Exceptional financing	184	710	1,178	1,628	1,923	2,210	2,369	3,215
External current account, before grants	-4,502	-2,039	-2,444	-6,718	-10,478	-14,926	-19,864	-22,476
External current account, after grants	-4,424	-2,039	-2,424	-6,700	-10,461	-14,910	-19,849	-22,462
Overall balance of payments	-685	17	-192	-433	-498	-456	844	43
(incl. exceptional financing)	184	526	469	449	296	287	159	845
Net international reserves (end of period)	1,753	2,297	2,573	2,588	2,385	2,214	3,214	4,100
Gross international reserves (end of period)	1,988	2,532	2,808	2,824	2,620	2,449	3,450	4,335
Months of projected imports of goods and nonfactor services	3.5	3.9	2.8	2.2	1.6	1.2	1.5	2.0
Months of projected imports of goods and nonfactor services, excl. megaprojects	4.6	5.3	5.7	5.4	4.8	4.2	5.7	6.7

Sources: Mozambican authorities; and IMF staff estimates and projections.

[1] Net of verified VAT refund requests.

[2] Modified cash balances and includes payment arrears.

[3] It includes accummulation of the stock of arrears on debt service the authorities stopped payments, and announced restructuring. Also Includes the participation of ENH (national hydrocarbon company) in the LNG gas projects.

Table 2. Mozambique: Government Finances, 2016–23

(Billions of Meticais)

	2016	2017	2018	2019	2020	2021	2022	2023
	Est.				Current Proj.			
Total revenue [1]	165.6	201.1	193.1	209.0	224.8	242.0	260.1	299.9
Tax revenue	138.5	171.7	162.4	175.7	188.8	203.2	217.8	237.4
Income and profits	64.3	97.7	79.6	86.3	93.4	101.7	109.6	120.3
Of which:								
Capital gain tax	0.0	22.1	0.0	0.0	0.0	0.0	0.0	0.0
Goods and Services [1]	56.4	55.8	62.8	66.7	70.5	75.2	79.7	84.9
International trade	12.3	11.8	12.1	13.9	15.3	16.6	18.0	20.0
Other	5.5	6.4	8.0	8.8	9.7	9.7	10.5	12.2
Nontax revenue	27.1	29.4	30.7	33.3	36.0	38.9	42.3	62.5
Total expenditure and net lending	223.1	257.6	270.3	322.9	333.5	355.6	393.9	444.4
Current expenditure	146.2	164.6	192.7	219.6	226.4	235.0	254.1	285.3
Compensation to employees	78.1	88.6	96.7	107.6	119.4	132.8	146.0	168.9
oh which: Social Insurance	3.7	4.2	4.7	5.2	5.8	6.4	7.0	8.2
Goods and services	24.4	28.8	35.9	33.5	36.2	39.1	42.2	48.9
Interest on public debt	20.2	29.8	37.7	54.4	44.8	35.5	36.2	33.0
Domestic	7.7	10.2	20.3	36.4	26.2	14.8	12.4	8.1
External	12.5	19.6	17.5	18.0	18.6	20.7	23.8	24.9
Subsidies and Transfers	23.5	17.5	22.3	24.1	26.1	27.6	29.8	34.5
Capital expenditure	60.6	58.7	49.4	68.5	71.8	81.0	96.0	125.5
Domestically financed	23.8	23.1	28.2	30.0	33.2	36.2	39.1	48.3
Externally financed	36.9	35.6	21.2	38.4	38.6	44.8	56.9	77.2
Net lending	13.5	22.0	28.3	34.9	35.3	39.7	43.8	33.6
Domestically financed	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.4
Externally financed loans to public enterprises	13.3	21.8	28.0	34.6	35.0	39.3	43.5	33.2
Unallocated expenditures	2.7	12.3	0.0	0.0	0.0	0.0	0.0	1.0
Payments in arrears	9.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance (modified cash basis), before grants [2]	-66.7	-56.5	-77.2	-113.9	-108.7	-113.6	-133.9	-144.4
Grants received	14.5	12.6	11.4	11.0	7.3	7.0	6.8	6.5
Project support	13.8	12.6	11.4	11.0	7.3	7.0	6.8	6.5
Special programs	6.7	5.2	1.2	1.2	1.1	1.1	1.0	1.0
Direct financing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Budget support	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Primary balance (modified cash basis), after grants [2]	-32.0	-14.1	-28.1	-48.6	-56.7	-71.1	-90.9	-104.9
Overall balance (modified cash basis), after grants [2]	-52.2	-43.9	-65.8	-102.9	-101.4	-106.6	-127.1	-137.9
Primary Balance (excl. the one-off 2017 capital gains tax revenues), after grants[2]	-32.0	-36.3	-28.1	-48.6	-56.7	-71.1	-90.9	-104.9
Overall balance (excl. the one-off 2017 capital gains tax revenues), after grants[2]	-52.2	-66.0	-65.8	-102.9	-101.4	-106.6	-127.1	-137.9
Net external financing	15.3	7.5	8.6	28.6	37.2	42.6	60.5	10.6
Disbursments	36.9	38.0	37.8	62.0	66.3	77.1	93.6	103.9
Project	23.0	23.0	9.8	27.5	31.3	37.8	50.1	70.7
Nonproject support	13.9	15.0	28.0	34.6	35.0	39.3	43.5	33.2
Amortization	-21.6	-30.6	-29.2	-33.4	-29.2	-34.5	-33.1	-93.2
Exceptional financing (external debt service) [3]	13.8	33.3	28.6	28.3	19.2	19.3	11.0	61.2
of which: interest payments	3.8	12.1	9.1	8.1	7.1	6.7	6.3	3.6
Exceptional financing (domestic arrears)	0.0	0.0	0.0	28.8	33.5	46.4	58.2	68.0
Net domestic financing	13.9	3.1	28.6	17.3	11.6	-1.6	-2.6	-1.9

Sources: Mozambican authorities; and IMF staff estimates and projections.

[1] VAT presented on a net basis (collection minus requested VAT refunds).

[2] Modified cash balances include an adjustment for payment arrears

[3] Exceptional financing for the debt service subject to restructuring (EMATUM, Proindicus, MAM, and six official creditors)

Table 3. Mozambique: Government Finances, 2016–23

(Percent of GDP)

	2016	2017	2018	2019	2020	2021	2022	2023
	Est.			Current Proj.				
Total revenue [1]	24.0	25.1	22.1	22.0	21.9	21.8	21.8	21.6
Tax revenue	20.1	21.4	18.6	18.5	18.4	18.3	18.2	17.1
Taxes on income and profits	9.3	12.2	9.1	9.1	9.1	9.2	9.2	8.7
Capital gain tax	0.0	2.8	0.0	0.0	0.0	0.0	0.0	0.0
Taxes on goods and services [1]	8.2	7.0	7.2	7.0	6.9	6.8	6.7	6.1
Taxes on international trade	1.8	1.5	1.4	1.5	1.5	1.5	1.5	1.4
Other taxes	0.8	0.8	0.9	0.9	0.9	0.9	0.9	0.9
Nontax revenue	3.9	3.7	3.5	3.5	3.5	3.5	3.5	4.5
Total expenditure and net lending	32.4	32.1	30.9	33.9	32.5	32.1	33.0	32.1
Current expenditure	21.2	20.5	22.0	23.1	22.1	21.2	21.3	20.6
Compensation to employees	11.3	11.0	11.1	11.3	11.6	12.0	12.2	12.2
oh which: Social Insurance	0.5	0.5	0.5	0.5	0.6	0.6	0.6	0.6
Goods and Services	3.5	3.6	4.1	3.5	3.5	3.5	3.5	3.5
Interest on public debt	2.9	3.7	4.3	5.7	4.4	3.2	3.0	2.4
Domestic	1.1	1.3	2.3	3.8	2.6	1.3	1.0	0.6
External	1.8	2.4	2.0	1.9	1.8	1.9	2.0	1.8
Subsidies and Transfers	3.4	2.2	2.5	2.5	2.5	2.5	2.5	2.5
Capital expenditure	8.8	7.3	5.6	7.2	7.0	7.3	8.0	9.0
Domestically financed	3.5	2.9	3.2	3.2	3.2	3.3	3.3	3.5
Externally financed	5.3	4.4	2.4	4.0	3.8	4.0	4.8	5.6
Net lending	2.0	2.7	3.2	3.7	3.4	3.6	3.7	2.4
Domestically financed	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Externally financed loans to public enterprises	1.9	2.7	3.2	3.6	3.4	3.6	3.6	2.4
Unallocated expenditures	0.4	1.5	0.0	0.0	0.0	0.0	0.0	0.0
Payments in arrears	1.3	…	…	…	…	…	…	…
Overall balance (modified cash basis), before grants [2]	-9.7	-7.0	-8.8	-12.0	-10.6	-10.3	-11.2	-10.4
Grants received	2.1	1.6	1.3	1.2	0.7	0.6	0.6	0.5
Project Support	2.0	1.6	1.3	1.2	0.7	0.6	0.6	0.5
Budget support	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Primary balance (modified cash basis), after grants [2]	-4.6	-1.8	-3.2	-5.1	-5.5	-6.4	-7.6	-7.6
Overall balance (modified cash basis), after grants [2]	-7.6	-5.5	-7.5	-10.8	-9.9	-9.6	-10.6	-9.9
Primary Balance (excl. the one-off 2017 capital gains tax revenues), after grants[2]	-4.6	-4.5	-3.2	-5.1	-5.5	-6.4	-7.6	-7.6
Overall balance (excl. the one-off 2017 capital gains tax revenues), after grants[2]	-7.6	-8.2	-7.5	-10.8	-9.9	-9.6	-10.6	-9.9
Net external financing	2.2	0.9	1.0	3.0	3.6	3.8	5.1	0.8
Disbursements	5.4	4.7	4.3	6.5	6.5	7.0	7.8	7.5
Project	3.3	2.9	1.1	2.9	3.1	3.4	4.2	5.1
Nonproject support	2.0	1.9	3.2	3.6	3.4	3.6	3.6	2.4
Amortization	-3.1	-3.8	-3.3	-3.5	-2.8	-3.1	-2.8	-6.7
Exceptional financing (external debt service) [3]	2.0	4.1	3.3	3.0	1.9	1.7	0.9	4.4
of which: interest payments	0.5	1.5	1.0	0.9	0.7	0.6	0.5	0.3
Exceptional financing (domestic arrears)	0.0	0.0	0.0	3.0	3.3	4.2	4.9	4.9
Net domestic financing	2.0	0.4	3.3	1.8	1.1	-0.1	-0.2	-0.1
Memorandum items:								
Nominal GDP (Billions of Meticais)	689	802	875	949	1026	1108	1195	1386

Sources: Mozambican authorities; and IMF staff estimates and projections.

[1] VAT presented on a net basis (collection minus requested VAT refunds).

[2] Modified cash balances include an adjustment for payment arrears

[3] Exceptional financing for the debt service subject to restructuring (EMATUM, Proindicus, MAM, and six official creditors)

Table 4. Mozambique: Monetary Survey, 2016–19
(Billions of Meticais, unless otherwise indicated)

	2016	2017	2018	2019
	Act.	Proj.	Proj.	Proj.
Bank of Mozambique				
Net foreign assets	119.5	130.6	152.4	158.5
(US$ billions)	1.7	2.2	2.5	2.5
Net international reserves	128.1	137.9	160.0	166.2
(US$ billions)	1.8	2.3	2.6	2.6
Net domestic assets	-19.6	-29.3	-45.4	-45.9
Credit to government (net)	-13.0	-39.7	-61.4	-43.7
Credit to banks (net)	3.3	-8.5	-19.1	-38.9
Credit to the economy	2.4	2.4	2.4	2.4
Other items (net; assets +)	-12.3	16.5	32.7	34.4
Reserve money	99.9	101.3	107.0	112.6
Currency in circulation	47.6	46.9	50.8	55.0
Bank deposits in BM	52.3	54.5	56.2	57.5
Deposits in MT	32.7	40.2	42.5	45.8
Deposits in foreign currency	19.6	14.2	13.7	11.7
Commercial Banks				
Net foreign assets	34.7	31.8	36.1	41.1
(US$ billions)	0.5	0.5	0.6	0.6
Net domestic assets	294.1	318.7	337.6	364.2
Banks' reserves	67.3	68.3	66.9	71.6
Credit to BM (net)	-13.8	8.5	19.1	38.9
Credit to government (net)	54.5	94.2	137.5	137.0
Credit to the economy	259.0	231.9	238.7	245.4
Other items (net; assets +)	-72.9	-84.2	-124.5	-128.8
Deposits	328.8	350.4	373.7	405.3
Demand and savings deposits	205.2	222.1	234.3	254.0
Time deposits	123.7	128.4	139.4	151.3
Monetary Survey				
Net foreign assets	154.2	162.4	188.6	199.6
(US$ billions)	2.2	2.7	3.0	3.1
Net domestic assets	212.9	221.1	225.2	246.7
Domestic credit	302.8	288.8	317.1	341.1
Credit to government (net)	41.5	54.6	76.0	93.3
Credit to the economy	261.4	234.2	241.0	247.8
Cred. economy in foreign currency	60.5	52.5	55.0	57.5
Other items (net; assets +)	-89.9	-67.7	-91.8	-94.4
Money and quasi money (M3)	367.2	383.5	413.8	446.2
Foreign currency deposits	112.0	108.1	115.2	122.8
(US$ billions)	1.6	1.8	1.9	1.9
M2	255.2	275.4	298.6	323.4
Currency outside banks	36.3	33.1	40.1	41.0
Domestic currency deposits	218.9	242.3	258.5	282.5
Memorandum Items				
12-month percent change				
Reserve money	35.2	1.4	5.6	5.2
Currency in circulation	21.0	-1.6	8.4	8.3
Bank reserves	51.3	4.2	3.2	2.4
M2	2.4	7.9	8.4	8.3
Domestic deposits	-0.2	10.7	6.7	9.3
M3	10.1	4.5	7.9	7.8
Credit to the economy	12.6	-10.4	2.9	2.8
Credit to the economy in domestic currency	6.1	-9.4	2.4	2.3
Money multiplier (M2/reserve money)	2.6	2.7	2.8	2.9
Velocity (GDP/M2)	2.7	2.9	2.9	2.9
Nominal GDP	689	802	875	949
Nominal GDP growth	16.5	16.4	9.0	8.4
Policy lending rate (end-of-period)	23.25	…	…	…
T-bill 91 days rate	24.15	…	…	…

Sources: Bank of Mozambique; and IMF staff estimates and projections.

Table 5a. Mozambique: Balance of Payments, 2016–23

(Millions of U.S. dollars, unless otherwise indicated)

	2016	2017	2018	2019	2020	2021	2022	2023
	Proj.	Proj.			Projections			
Current account balance	-4,424	-2,039	-2,424	-6,700	-10,461	-14,910	-19,849	-22,462
Trade balance for goods	-1,404	-614	-509	-3,529	-6,347	-9,753	-13,780	-13,776
Of which: Megaprojects	1,643	2,637	2,978	-98	-2,840	-6,143	-10,051	-9,953
Exports, f.o.b.	3,329	4,258	5,031	5,401	5,334	5,487	5,640	7,314
Megaprojects	2,414	3,415	4,125	4,435	4,304	4,382	4,453	6,035
Other	915	843	906	967	1,030	1,105	1,187	1,279
Imports, f.o.b.	4,733	4,872	5,540	8,931	11,682	15,241	19,420	21,090
Megaprojects	771	778	1,147	4,533	7,144	10,525	14,504	15,988
Other	3,962	4,094	4,393	4,398	4,537	4,716	4,916	5,102
Services (net)	-2,844	-1,458	-1,544	-2,543	-3,329	-4,152	-5,056	-5,379
Megaprojects	-2,086	-950	-933	-1,754	-2,305	-2,984	-3,730	-3,935
Other	-757	-508	-610	-789	-1,024	-1,168	-1,326	-1,444
Primary income (net)	-405	-682	-560	-814	-969	-1,188	-1,197	-3,492
Of which: Interest on public debt (net) [1]	-235	-338	-307	-303	-302	-323	-354	-319
Of which: Megaprojects (Net Interest and Dividends)	-18	-59	-124	-344	-472	-677	-708	-3,054
Secondary income (net)	229	714	188	186	184	184	184	185
Of which: External grants	78	0	20	19	17	16	15	14
Capital account balance	143	241	283	271	210	204	198	194
Financial account balance	3,631	1,816	1,949	5,996	9,753	14,250	20,494	22,312
Net foreign direct investment	3,093	1,538	1,771	5,185	8,387	12,284	3,379	724
Megaprojects	1,288	229	697	4,268	7,522	11,455	2,579	83
Other	1,806	1,309	1,074	917	865	830	800	641
Borrowing (net) by the general government	200	117	87	398	495	556	858	137
Disbursements	554	612	619	982	1,015	1,140	1,335	1,429
Repayments [2]	354	495	532	584	519	584	477	1,293
Loans (net) by the nonfin private sector	-23	48	247	607	1,007	1,703	16,712	22,224
Megaprojects	-36	-40	147	508	909	1,604	16,613	22,109
Other	13	89	100	99	99	99	100	114
Other financial flows (net) [3]	360	112	-155	-194	-137	-294	-456	-773
Net errors and omissions	-34.2	0	0	0	0	0	0	0
Overall balance	-685	17	-192	-433	-498	-456	844	43
Financing	685	-17	192	433	498	456	-844	-43
Reserve assets (- = increase)	534	-512	-244	31	233	198	-974	-859
Net use of credit	-33	-32	-33	-46	-29	-27	-27	-27
Of which: IMF disbursements (+)	0	0	0	0	0	0	0	0
Of which: Repayments to the IMF (-)	-33	-32	-33	-46	-29	-27	-27	-27
Exceptional financing	184	526	468	448	294	285	157	842
Financing Gap	-292.0	-651.6	-655.0	-621.7	-405.6	-388.8	-253.0	-932.1
Donor support	108.5	125.5	186.7	173.6	111.5	103.7	96.4	89.7
Exceptional financing (external arrears on PPG external debt)	183.5	526.1	468.3	448.1	294.1	285.1	156.6	842.5
Memorandum items:								
Current account balance (percent of GDP)	-39.2	-16.1	-16.9	-44.6	-66.6	-91.0	-116.4	-117.7
Current account excl. Megaprojects (Percent of GDP)	-34.8	-28.8	-30.1	-29.7	-30.5	-30.8	-31.3	-29.1
Excluding Megaprojects and indirect MP imports [4]	-22.0	-17.9	-20.8	-19.3	-18.4	-17.2	-16.0	-14.2
Net foreign assets (USD millions)	1,675	2,176	2,453	2,468	2,264	2,093	3,094	3,980
Net international reserves (USD millions) [5]	1,753	2,297	2,573	2,588	2,385	2,214	3,214	4,100
Net international reserves (USD millions), under full debt service	1,570	1,771	2,105	2,140	2,091	1,929	3,058	3,258
Gross international reserves (USD millions) [6]	1,988	2,532	2,808	2,824	2,620	2,449	3,450	4,308
Gross international reserves (USD millions), under full debt service	1,805	2,006	2,340	2,375	2,326	2,164	3,293	3,466
Months of projected imports of goods and services	3.5	3.9	2.8	2.2	1.6	1.2	1.5	2.0
Months of projected imports of G&S (under full debt service)	3.1	3.1	2.3	1.8	1.4	1.0	1.5	1.6
Months of projected G&S imports (excl. megaproj.)	4.6	5.3	5.7	5.4	4.8	4.2	5.7	6.7
Months of projected G&S imports (excl. megaproj.), full debt service	4.2	4.2	4.8	4.6	4.2	3.7	5.4	5.4
Percent of broad money (M2)	55.3	55.2	58.5	56.1	49.8	44.6	60.4	69.8

Sources: Data from Government of Mozambique and projections by IMF staff.

[1] Includes interest payments for Ematum and previously undisclosed loans.

[2] Includes previously undisclosed loans.

[3] Other financial account flows include net portfolio investment; net financial derivatives; net currency and deposits; insurance, pension and standardized guarantee schemes (net); net trade credits and advances; net other accounts receivable/payable; net other equity and net special drawing rights.

[4] Also excludes imports by domestic firms that are used to supply megaprojects (estimated).

[5] NIR include USD reserve deposits of commercial banks at the Bank of Mozambique. NIR do not include any disbursements by the IMF, foreign currency swaps, foreign currency deposits by resident banks, or reserve requirement deposits in foreign currency by resident banks.

[6] The ratio to short term debt is not presented due to availability of the data.

Table 5b. Mozambique: Balance of Payments, 2016–23
(Percent of GDP)

	2016	2017	2018	2019	2020	2021	2022	2023
	Prel.	Proj.			Projections			
				(Percent of GDP)				
Current account balance	-39.2	-16.1	-16.9	-44.6	-66.6	-91.0	-116.4	-117.7
Trade balance for goods	-12.5	-4.8	-3.6	-23.5	-40.4	-59.6	-80.8	-72.2
Of which: Megaprojects	14.6	20.8	20.8	-0.7	-18.1	-37.5	-58.9	-52.2
Exports, f.o.b.	29.5	33.6	35.1	36.0	34.0	33.5	33.1	38.3
Megaprojects	21.4	26.9	28.8	29.5	27.4	26.8	26.1	31.6
Other	8.1	6.6	6.3	6.4	6.6	6.7	7.0	6.7
Imports, f.o.b.	42.0	38.4	38.7	59.5	74.4	93.1	113.9	110.5
Megaprojects	6.8	6.1	8.0	30.2	45.5	64.3	85.0	83.8
Other	35.1	32.3	30.7	29.3	28.9	28.8	28.8	26.7
Services (net)	-25.2	-11.5	-10.8	-16.9	-21.2	-25.4	-29.6	-28.2
Megaprojects	-18.5	-7.5	-6.5	-11.7	-14.7	-18.2	-21.9	-20.6
Other	-6.7	-4.0	-4.3	-5.3	-6.5	-7.1	-7.8	-7.6
Primary income (net)	-3.6	-5.4	-3.9	-5.4	-6.2	-7.3	-7.0	-18.3
Of which: Interest on public debt (net) [1]	-2.1	-2.7	-2.1	-2.0	-1.9	-2.0	-2.1	-1.7
Of which: Megaprojects (net Interest and dividends)	-0.2	-0.5	-0.9	-2.3	-3.0	-4.1	-4.2	-16.0
Secondary income (net)	2.0	5.6	1.3	1.2	1.2	1.1	1.1	1.0
Of which: External grants	0.7	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Capital account balance	1.3	1.9	2.0	1.8	1.3	1.2	1.2	1.0
Financial account balance	32.2	14.3	13.6	39.9	62.1	87.0	120.2	116.9
Net foreign direct investment	27.4	12.1	12.4	34.5	53.4	75.0	19.8	3.8
Megaprojects	11.4	1.8	4.9	28.4	47.9	69.9	15.1	0.4
Other	16.0	10.3	7.5	6.1	5.5	5.1	4.7	3.4
Borrowing (net) by the general government	1.8	0.9	0.6	2.7	3.2	3.4	5.0	0.7
Disbursements	4.9	4.8	4.3	6.5	6.5	7.0	7.8	7.5
Repayments [2]	3.1	3.9	3.7	3.9	3.3	3.6	2.8	6.8
Loans (net) by the nonfin private sector	-0.2	0.4	1.7	4.0	6.4	10.4	98.0	116.5
Megaprojects	-0.3	-0.3	1.0	3.4	5.8	9.8	97.4	115.9
Other	0.1	0.7	0.7	0.7	0.6	0.6	0.6	0.6
Other financial flows (net) [3]	3.2	0.9	-1.1	-1.3	-0.9	-1.8	-2.7	-4.1
Net errors and omissions	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-6.1	0.1	-1.3	-2.9	-3.2	-2.8	4.9	0.2
Financing	6.1	-0.1	1.3	2.9	3.2	2.8	-4.9	-0.2
Reserve assets (- = increase)	4.7	-4.0	-1.7	0.2	1.5	1.2	-5.7	-4.5
Net use of credit	-0.3	-0.3	-0.2	-0.3	-0.2	-0.2	-0.2	-0.1
Of which: IMF disbursements (+)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which: Repayments to the IMF (-)	-0.3	-0.3	-0.2	-0.3	-0.2	-0.2	-0.2	-0.1
Exceptional financing	1.6	4.1	3.3	3.0	1.9	1.7	0.9	4.4
Financing Gap	-2.6	-5.1	-4.6	-4.1	-2.6	-2.4	-1.5	-4.9
Donor support	1.0	1.0	1.3	1.2	0.7	0.6	0.6	0.5
Exceptional financing (external arrears on PPG external debt)	1.6	4.1	3.3	3.0	1.9	1.7	0.9	4.4

Sources: Data from Government of Mozambique and projections by IMF staff.

[1] Includes interest payments for Ematum and previously undisclosed loans.

[2] Includes previously undisclosed loans.

[3] Other financial account flows include net portfolio investment; net financial derivatives; net currency and deposits; insurance, pension and standardized guarantee schemes (net); net trade credits and advances; net other accounts receivable/payable; net other equity and net special drawing rights.

Table 6. Mozambique: Financial Soundness Indicators for Banking Sector, 2013–17[1]

(In percent, unless otherwise indicated)

	2013	2014	2015	2016				2017		
				Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.
Capital Adequacy										
Regulatory capital to risk-weighted assets (CAR)	16.9	15.1	17.0	15.8	16.5	5.3	8.8	8.5	20.5	20.2
Regulatory Tier I capital to risk-weighted assets	16.0	13.6	15.5	14.5	15.7	13.1	14.2	13.5	20.1	19.5
Total Capital to total Assets	9.5	9.6	9.3	9.1	9.5	3.2	5.3	4.8	11.0	10.9
Tier I Capital to total Assets	9.0	8.7	8.5	8.3	9.1	7.7	8.5	7.7	10.8	10.6
Asset Quality										
NPLs to total gross loans	2.9	3.2	4.3	4.6	6.3	5.8	5.5	7.1	11.2	11.4
Total provisions to NPLs	135.2	99.3	107.9	104.3	76.3	96.7	99.3	108.3	71.1	68.9
NPLs net of provisions to total capital	6.8	3.8	5.4	5.7	16.7	24.2	13.3	19.3	20.6	23.2
NPLs net of provisions to capital and reserves	4.5	2.4	3.4	3.6	11.6	5.9	5.2	6.9	14.3	16.0
Specific provisions to NPLs	58.7	81.6	79.3	81.0	56.4	76.6	78.3	75.7	61.8	58.6
Earnings and Profitability										
Return on Equity (ROE)	21.0	21.6	20.4	14.2	14.0	12.8	10.1	31.1	40.6	35.7
Return on Assets (ROA)	2.0	2.1	2.0	1.3	1.3	1.1	0.7	2.0	2.4	2.5
Interest margin to total income	55.6	55.4	52.7	58.0	58.7	62.2	65.5	77.9	73.9	71.8
Noninterest expenses to total income (cost-to Income Ratio)	65.3	62.4	62.8	64.8	66.3	66.4	67.0	67.0	59.9	58.2
Personnel expenses to noninterest expenses	47.6	47.1	46.9	46.1	44.8	45.2	44.1	44.0	45.0	46.1
Trading income to total income	17.0	20.8	26.0	24.0	20.8	18.7	16.6	6.7	9.5	11.3
Fee and comission to total income	21.5	20.0	17.5	17.0	20.0	19.2	19.3	16.4	15.6	16.0
Liquidity										
Liquid assets (core) to total assets	17.3	13.5	18.6	17.3	19.0	18.7	20.6	20.8	21.4	19.4
Liquid assets (broad measure) to total assets	30.7	28.2	32.2	30.9	32.5	30.1	31.4	34.6	38.3	38.8
Liquid assets (core) to total deposits	24.3	18.7	26.3	24.5	26.6	26.9	29.4	29.1	30.3	27.8
Liquid assets (core) to demand deposits	38.5	28.8	42.0	39.3	41.2	41.8	46.2	46.8	50.0	47.1
Liquid assets (core) to short term liabilities	23.1	17.6	24.9	23.5	25.6	26.0	28.8	28.5	29.7	27.0
Liquid assets (broad measure)to short term liabilities	40.8	36.8	43.1	41.8	44.0	41.7	43.9	47.4	53.2	54.0
Customer Deposits to total (noninterbank) loans	132.5	127.0	130.0	128.1	129.2	127.4	124.2	135.8	138.5	142.9
Sentivity to market risk										
FX loans to FX deposits	74.4	77.7	64.8	81.3	69.9	66.4	71.3	70.0	73.7	70.5
FX loans to total loans	21.9	22.2	22.1	26.6	28.2	31.4	28.7	29.4	27.1	26.5
FX liabilities to total liabilities	25.4	22.8	24.8	24.6	29.5	32.9	28.9	27.4	24.6	25.5

Source: Bank of Mozambique (BM).

[1] Banking sector refers to deposit coorporations

Table 7. Table Mozambique: Risk Assessment Matrix[1]				
Source of Risks	**Relative Likelihood**	**Time Horizon**	**Impact on Mozambique**	**Policy Response**
Retreat from cross-border integration. Fraying consensus about the benefits of globalization leads to protectionism and economic isolationism, resulting in reduced global and regional policy and regulatory collaboration with negative consequences for trade, capital and labor flows, sentiment, and growth.	Medium	ST, MT	Medium	• Anchor **macroeconomic stability** to mobilize foreign investors' interest in Mozambique, including through appropriate fiscal and monetary policy mix and structural policies. • ***Diversify exports,*** both in terms of export products and trading partners. • Continue improving the **business environment** to boost productivity and competitiveness.
Policy and geopolitical uncertainties:				
• **Policy uncertainty.** Two-sided risks to U.S. growth with uncertainties about the positive short-term impact of the tax bill on growth and the extent of potential medium-term adjustment to offset its fiscal costs; uncertainty associated with negotiating post-Brexit arrangements and NAFTA and associated market fragmentation risks; and evolving political processes, including elections in several large economies, weigh on the whole on global growth..	Medium	ST, MT	High	• Maintain ***exchange rate flexibility*** to cushion the impact of related shocks and • ***Structural reforms*** should be advanced to improve economic efficiency and enhance diversification. • Aim to rebuild fiscal buffers and reserves.
• **Intensification of the risks of fragmentation/security dislocation** in part of the Middle East, Africa, Asia, and Europe, leading to socio-economic disruptions.	High	ST, MT	Medium	
Financial conditions:				
• **Tighter global financial conditions.** Against the backdrop of continued monetary policy normalization and increasingly stretched valuations across asset classes, an abrupt change in global risk appetite (e.g., due to higher-than-expected inflation in the U.S) could lead to sudden, sharp increases in interest rates and associated tightening of financial conditions. Higher debt service and refinancing risks could stress leveraged firms, households, and vulnerable sovereigns, including through capital account pressures in some cases.	High	ST, MT	High	• Up-front measures for ***fiscal consolidation*** to ensure continued access to international capital markets. • Strengthen the ***supervisory and regulatory framework***, especially as it pertains to cross-border banking activity and oversight of holding companies; improve corporate governance; and address weaknesses in the bank resolution framework.
• **Further pressure on traditional bank business models:** Legacy problems, and potential competition from non-banks curtail banks' profitability globally. Loss of confidence if such profitability challenges are not addressed could increase the risk of distress at one or more major banks with possible knock-on effects on the broader financial sector and for sovereign yields in vulnerable economies. Migration of activities outside of the traditional banking sector, including provision of financial services by fintech intermediaries, raises competitive pressures on traditional banks, making risk monitoring and mitigation more difficult.	Medium	MT	High	

Table 7. Mozambique: Risk Assessment Matrix (continued)

Source of Risks	Relative Likelihood	Time Horizon	Impact on Mozambique	Policy Response
Weaker-than-expected global growth:				Mozambique needs to: • ***Diversify its exports*** both in terms of export products and trading partners. • focus on ***revenue mobilization*** • Continue improving the **business environment** to boost productivity and competitiveness. • Develop the country's ***infrastructure***.
• **Structurally weak growth in key advanced economies:** Low productivity growth (U.S., euro area and Japan), high debt, and failure to fully address crisis legacies by undertaking structural reforms amidst persistently low inflation (euro area and Japan) undermine medium-term growth.	High	MT	High	
• **Significant U.S. slowdown and its spillovers:** As the current recovery ages and vulnerabilities build up, the risks of a sharper-than-expected slowdown increase. The proximate causes could be a fiscal contraction associated with the eventual planned withdrawal of the tax stimulus or market fears of overheating. A sharp adjustment necessitated by relatively limited fiscal policy space would create global spillovers.	Medium	MT	Medium	
• **Significant China slowdown and its spillovers:** While ongoing efforts by the Chinese authorities to "de-risk" the financial system are welcome, too fast an adjustment and improper sequencing of actions may adversely affect near-term growth (low likelihood). Over the medium term, overly ambitious growth targets, including by over reliance on credit stimulus and investment, lead to unsustainable policies, reducing fiscal space, further increasing financial imbalances. A sharp adjustment would weaken domestic demand, with adverse international spillovers, including a pullback in capital flows to EMs (medium likelihood).	Low/ Medium	ST	Low	
Lower energy prices, driven by weakening OPEC/Russia cartel cohesion and/or recovery of oil production in the African continent.	Low	ST, MT	Low	• ***Contain recurrent expenditure*** by maintaining fuel price automatic adjustment mechanism. • Allow greater ***exchange rate flexibility*** to support adjustment to external shocks and reflect economic fundamentals, supported by a tighter monetary stance to prevent capital outflows and bolster reserves. • **Structural reforms** should be advanced to improve economic efficiency and enhance diversification.
Cyber-attacks on interconnected financial systems and broader private and public institutions that trigger systemic financial instability or widely disrupt socio-economic activities.	Medium	ST, MT	Medium	• Maintain awareness that **cybersecurity is a priority** • Ensure that **financial networks and data** are secure and protected. • Strengthen **operational risk mitigation strategies** in the financial sector.

Mozambique: Risk Assessment Matrix (concluded)

Source of Risks	Relative Likelihood	Time Horizon	Impact on Mozambique	Policy Response
Mozambique specific risks:				• Continue drive for signing the peace agreement by end-2017 to support security and peace. • Urgent need for a balanced package of policies and reforms to address fiscal risks. • Adopt the action plan to strengthen governance, transparency, and accountability • Implement effectively targeted anti-money laundering measures to help detect and investigate illicit financial flows related to fraud and corruption. • Implement financial reforms including banking resolution, strengthening the deposit guarantee scheme and banking regulation and supervision. • Enhance operational independence of the monetary authorities. • Conduct asset quality reviews and adjust provisioning accordingly. Step up risk-based supervisions. • Structural reform to support economic diversification and inclusive growth. • Address infrastructure gaps and income/developmental disparities among regions, while instituting appropriate social safety nets.
• Deterioration in security	High	ST, MT	High	
• Failure of the peace negotiations	Medium	ST, MT	High	
• Prolonged uncertainty and further deterioration related to the hidden debt issue could take a toll on confidence, donor and multilateral budget support and investment	High	ST, MT	High	
• Increasing fiscal risks including non-performing SOEs and government expenditure arrears	High	ST, MT	High	
• Recurrence of banking sector stress, including deterioration in asset quality and liquidity shortfalls due to protracted low growth and high real interest rates	High	MT	High High	
• Delay in implementation of megaprojects	Medium	ST, MT	High	
• Volatility in commodity prices	Medium	ST	High	
• Extreme climate events	Medium	ST	High	
• Deterioration in the political environment in neighboring countries	Low	ST	High	

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term (ST)" and "medium term (MT)" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Annex I. Implementation of Past IMF Recommendations

Recommendation	Status
Fiscal - Attain a pace of fiscal consolidation to ensure debt sustainability and contribute to required external adjustment. - Contain wage bill increase through a deceleration in the pace of new hiring and stronger administrative controls on salary payments and bonuses. - Reform fuel and wheat subsidies, and reinstate automatic fuel price adjustment mechanism to address future subsidies while strengthening the social safety net. - Monitor fiscal risks and public enterprises and continue to strengthen debt management.	- While the government eliminated subsidies on fuel and wheat, and reintroduced an automatic price adjustment mechanism for fuel, significant spending pressures from debt service and wages resulted in an overall increase in the fiscal deficit. - The 2018 budget proposal includes measures to contain the wage bill and safeguard revenues. - Authorities approved a decree establishing a framework to contract public debt and issue guarantees in November 2017 and approved a new SOEs Law.
Monetary and Exchange Rate - Decisive actions to curb inflation through a cycle of monetary tightening and stabilize the foreign exchange market by addressing FX market distortions. - Continue to strengthen the Bank of Mozambique (BM) analytical tools and monetary policy operations framework.	- Tight monetary policy successfully reduced annual inflation to about 7.2 percent in December 2017, and helped stabilize the FX market over the last 3 quarters. More recently, a new FX market law was introduced in December 2017 allowing exporters and investors to keep 100 percent (as opposed to 50 percent) of proceeds in foreign currency. The BM continued to strengthen its monetary policy framework. In April 2017, it changed its operational target from monetary aggregates to short-term interest rates.
Financial - Implement reforms to strengthen bank supervision and crisis management tools.	- The BM is preparing a new bank resolution framework that enhances its resolution powers with tools designed to deal with systemic failures.
Structural - Start to develop a strong medium-term fiscal framework and a formal fiscal rule - Enhance transparency in natural resource wealth management. - Improve the business environment to promote enterprises, job creation and deepening financial inclusion.	- Authorities are evaluating the merits of a fiscal responsibility law and actions to enhance transparent and efficient use of natural resource as part of an action plan to strengthen governance, transparency and accountability. - A national strategy for financial inclusion was launched in 2016 and a National Committee operationalized to steer initiatives with stakeholders in 2017. E-money and banking infrastructure is being promoted under BM oversight.

Annex II. External Sector Assessment

The external position of Mozambique has improved, reflecting the stabilization of the exchange rate, lower inflation, and higher net international reserves. However, it remains substantially weaker than the level consistent with medium term fundamentals. The current account adjustment has been achieved in part through a crowding out of the non-megaproject traditional economy, which is not expected to recover over the medium term under current policies. The external position and the stabilization of the metical, if not accompanied by policy adjustment measures in 2018, are not sustainable under current policies over the medium term (2018-2023). The EBA-lite methodology indicates an overvaluation in the range of 15 to 20 percent over the medium term in the absence of new policy action. This misalignment would, however, gradually decline over time as the LNG gas production begins around 2023.

1. External assessments for Mozambique are still subject to considerable uncertainty due to data limitation surrounding megaproject-related activities. While the Mozambican authorities produce accurate external sector data for megaprojects, only exploratory data is available on domestic firms exclusively related to megaprojects activity.[1] To describe accurately the country's core economy, staff has estimated a current account and a net international investment position unrelated to megaprojects following the same approached used in the 2015 Article IV External Sector Assessment.[2]

2. Staff estimates show that the non-megaproject-related current account has narrowed to 17.9 percent of GDP in 2017. However, this has been achieved mainly on the back of the one-off inflow in income associated with the capital gain tax received by the government for the sale of 50 percent of ENI's stake in the Coral South natural gas field to Exxon Mobil (about $352.6 million, x percent of GDP). The non-megaproject-related external position shows that the current account has been considerably worsening from about 10% on average in 2011 and 2012 to 18 percent and 22 percent in 2015 and 2016, respectively. The latter has been broadly consistent with a deteriorating net international investment position (IIP) from 2013 to 2016.

3. The extended drop in megaproject investment activity is likely to have also contributed to the narrowing of the non-megaproject-related current account deficit in 2017. Megaproject direct investment inflows collapsed to an average of about $1.3 billion in 2015-2017 from an average of $4 billion in 2012-14. Although a clear majority of these FDI inflows go into imports, their sheer size (of $4 billion on average during 2012-14) implied that even small leakages into domestic goods and services constituted significant financing. The megaproject trade balance improved significantly leading to a 12.7 percent of GDP current account surplus for the megaproject economy. Megaproject imports of services have contracted by about 55 percent, as many of the on-

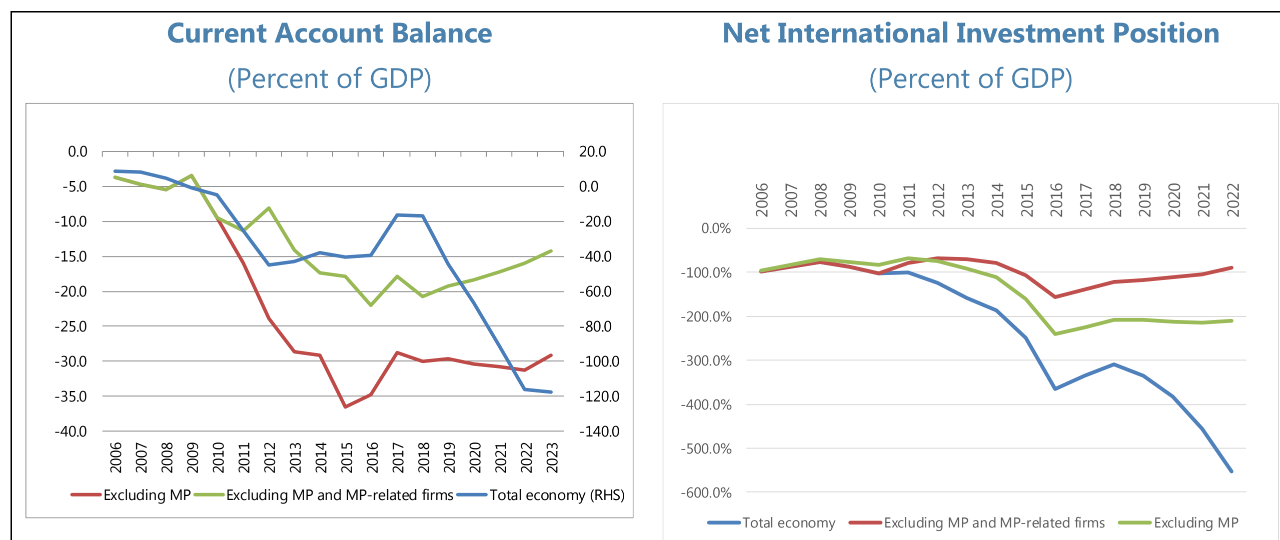
---

[1] For instance, there are domestic firms engaged in extraction and processing steps for coal and exclusively sell their services to megaprojects. Data is available only for coal sector for 2013, and suggests that the imports of MP-related domestic firms was larger than that of the coal MPs themselves.

[2] Other considerations taken into account include a doubling of "unclassified" non-MP imports between 2011 and 2012, as megaprojects were strongly expanding at the time, which can hardly be explained by the traditional economy alone.

going projects were completed in 2016, while the surge in coal prices and export volumes significantly boosted megaproject exports. In absence of high megaproject investment activity, high non-megaproject-related current account deficits (i.e. above 10 percent of GDP) are not likely to be sustainable.

4. The current account deficit is projected to gradually stabilize over the medium term and narrow in percent of GDP by 2025, and thereby improve the Mozambique's non-megaproject-related IIP. The current account deterioration has put the non-MP-related IIP on a declining path starting from its peak of 67 percent of GDP in 2012**.** The deterioration resulted from overly expansive fiscal policies in the run up to the 2014 elections, an overvalued exchange rate and relatively loose monetary policy until the recent past. In 2017, monetary policy tightening has helped lower inflation and stabilize the foreign exchange market and net international reserves, but growth remains subdued over the medium-term in the non-megaproject economy, with too loose fiscal policy crowding-out investment by the private sector. The current account deficit is expected to remain at elevated levels of 15 to 18 percent of GDP from 2018 to 2024, and stabilize around 10 percent of GDP only in 2025 with gas projects coming into full production (see Figure 1a). As a consequence, the non-MP-related IIP is expected to gradually recover starting with 2017 and continue to improve over the medium-term as activity in the traditional economy shrinks in percent of GDP (see Figure 1b).



5. The non-megaproject financial account has also deteriorated in 2017. Private sector FDI and loan inflows have collapsed in 2017, and are projected to remain low, after a slightly better performance than megaprojects inflows in 2015 and 2016. The non-megaproject financial account in 2017 is therefore expected to net below $1 billion in inflows after a much better performance in 2015 and 2016 ($4.5 billion, and $2.7 billion, respectively).

6. There is no evidence so far of capital flight. While megaprojects' transactions (currency and deposits outflows) have been offset by non-megaproject trade credit inflows, currency and deposits and trade credits of the traditional economy still recorded a net inflow in 2017. These flows

are registered under "other" financial account flows (in Table 5), and in general continue to be driven by megaprojects' transactions.

7. The External Balance Assessment (EBA) concludes that the metical is overvalued in a range of 15 to 20 percent over the medium term (2018-2023). After having been mostly stable during 2012-14, the real effective exchange rate (REER) depreciated sharply by about 32 percent between end-December 2014 and end-December 2016. In 2017, with the stabilization of the foreign exchange rate market, the REER has appreciated by about 8 percent, a trend which is expected to continue in 2018 given less pressures on the foreign exchange market, as the mega-project current account is expected to remain in surplus in 2018 at about 12 percent of GDP. The current account deficit (excluding megaproject-related flows) is projected to contract from the 2016 level of 22 percent of GDP to about 18 percent of GDP in 2017, and 20 percent of GDP in 2018. This is much higher than the current account norms derived under EBA-lite Current Account and External Sustainability Approaches of 9.8 percent and 8.7 percent of GDP, respectively.[3]

8. However, this misalignment is expected to gradually decline in 2025, as the current account in percent of GDP is projected to narrow in the long run due to the impact on GDP of the LNG gas projects production. With the LNG gas projects coming into full production, the current account deficit (excluding megaproject-related flows) is expected to narrow in percent in GDP to 10 percent by 2025 (see Table 1. EBA-lite results).

Estimates of the Valuation of the Metical Using EBA-Lite Approaches

Approach	Current Account Gap (percent of GDP) 1/	Overvaluation (+) / Undervaluation (-) (percent) 2/
Current Account Approach		
2017	-8.4	23.9
2019 (after exchange rate pass-through to trade)	-8.9	25.4
2025	0	0.0
Index REER Approach (2017)	...	-11.5
External Sustainability Approach 3/		
2017	-9.2	26.3
2019 (after exchange rate pass-through to trade)	-10.0	28.6
2025	-0.3	0.9

Source: IMF staff estimates.

1/ The EBA considers a non-megaproject current account, which is further adjusted by indirect megaproject imports related to services supplied to megaprojects by other domestic firms. This amount is estimated, while BM continues to work on official statistics quantifying these imports.

2/ As in past analyses, the Tokarick (2010) elasticity is used to translate the current account gap into the implied valuation, because it is derived on a small country assumption (see EBS/13/76, p. 81).

3/ Based on stabilizing the non-MP related IIP position at its estimated end-2017 level of 138.4 percent of GDP.

[3] The Index REER Approach gives somewhat different results as it was not possible to run the model only for the non-MP related economy given data limitations.

9. Although data limitations impose some uncertainty, the stabilization of the metical and the net international reserves, if not accompanied by policy adjustment measures in 2018, are likely not to be safeguarded over the medium term (2018-2023). Therefore, the adjustment scenario assumes that the real exchange rate would depreciate over the medium term, to ensure the exchange rate channel can play the role of a shock absorber for external shocks.

10. This assessment of international reserves adequacy judged 5.0 months of non-megaproject imports to be a prudent reserve cover. End-2017 reserves are projected to cover 5¼ months of non-MP imports, up from 4.6 months at end-2016, albeit on the back of accumulation of external arrears. As exports continue to shift toward natural resources, a path of reserves of 5.0 months of non-MP imports will be needed to withstand increasing possibility of export shocks.

Action	Date of Implementation	Description	Macroeconomic Relevance
Governance			
Submit to the National Assembly a draft law on Fiscal Responsability Law	End-2018	The draft law should have the main purpose of (a) maintaining fiscal stability and ensuring debt sustainability ; (b) warranting fiscal transparency; (c) establishing forward-looking and performance oriented financial management ; and (d) ensuring accountability of the government to parliament . The draft law should be anchored on a sustainable medium-term debt strategy, and encompass the creation of a Sovereign Wealth Fund (SWF) and fiscal rule(s) aimed at ensuring an efficient management of natural resources over time. Regulations should be adopted in the following six months, for the effective implementation of the SWF.	Strenghtening fiscal sustainability, transparency and accountability (PFM)
Issue a decree to regulate the issuance and management of public sector debt and government guarantees	End-November 2017	The decree should require (a) all central government borrowing and contingent liabilities (including guarantees) to be contracted by the Minister of Finance on behalf of the central government, with the approval of the Council of Ministers, and, in the case of borrowing above a certain threshold undertaken by local authorities and SOEs, with the approval of the Minister of Finance and relevant sector minister ; (b) ex-ante consultation of Banco de Moçambique; (c) disclosure of loans and guarantees approved including feasibility study and assessment of fiscal risks; and (d) regular update of public sector debt records reconciled with creditors after the end of the quarter. The decree should explicitly indicate that the loans and guarantees not meeting the decree requirements will be deemed legally invalid.	Strenghtening public debt management (PFM)
Approve regulations aimed at implementing the new SOEs Law	End-June 2018	The draft law submitted to parliament in September 2017 for approval by end-2017 defines state-ownership of companies broadly in consistency with GFS international standards and state clearly that an entity will be designated to manage and coordinate the SOEs sector and to exercise an oversight role on SOEs. Specific regulations should include limits for borrowing, reporting obligations, clear compensation for activities carried out at a cost below the recovery cost and policy for payment of dividends.	Strenghtening SOE's management and mitigating fiscal and financial risks (PFM)
Strengthen SOEs oversight	End-2018	Actions include (a) mapping and publishing a list of all SOEs controlled by the State directly or indirectly ; (b) clarifying the institutional arrangements for the unified SOE management and oversight; and (c) adopting regulations or guidelines to regulate SOE borrowing.	Strenghtening SOE's management and mitigating fiscal and financial risks (PFM)
Prepare a recovery and/or restructuring plan for SOEs in financial distress.	End-2018	Identify the SOEs in financial distress and prepare (a) financial and fiscal risk assessments; and (b) recovery and/ or restructuring plans by end-2018.	Strenghtening SOE's management and mitigating fiscal and financial risks (PFM)
Submit to the National Assembly a draft law for Government Autonomous Entities	End-2018	The law should provide borrowing limits, harmonize financial reporting requirements, limits capacity of these entities to create or hold shares in other public bodies, and require registration.	Strenghtening fiscal risks and public debt management (PFM)
Adopt a strategy to monitor and resolve arrears with suppliers and VAT refunds	End-2017	The strategy should include mandatory recording of commitments and verification steps in real time in the e-SISTAFE system from January 1, 2018, and ensure the system captures data on the stock, age, and composition of arrears. It should also involve an audit of these arrears including the non-budgetary arrears.	Clarifying fiscal position and strengthening fiscal risk management (PFM)
Maintain an updated register of government assets and adopt procedures and rules to transfer and dispose of government's real assets	End-2018	Assets include financial assets, fixed assets, land and subsoil assets.	Strenghtening asset liability management and transparency (PFM)

Action	Date of Implementation	Description	Macroeconomic Relevance
Transparency			
Adopt the IMF's Government Finance Statistics standard	End-January 2019	Includes economic, administrative and functional classification and its use for budget formulation, execution and reporting.	Strenghtening fiscal transparency (PFM)
Strengthen parliamentary oversee on public finance	End-September 2018	Strengthen parliamentary oversight on public finance. Annex to each initial draft budget law submitted to parliament in year n: (a) a summary statement for each SOE ; (b) a similar report for each government autonomous entity; and (c) an assessment of fiscal risks that quantify and consolidate information on all significant contingent liabilities and other risks of the central government and include mitigation strategy	Strenghtening fiscal risk management and oversight (PFM)
Strengthen public oversight on public finance	Continuous and end-2019	Publish: (a) reconciliation of sources of changes to the fiscal forecast and of deviations between forecasts and outturns, (b) quarterly information on arrears in the budget execution reports, (c) quarterly and annual debt report on domestic and external public debt including guarantees, (d) economic feasibility studies of major public investments above a threshold, and (e) State's participation in the extractive industries sector with full discourse by end-2019.	Strenghtening fiscal transparency (PFM)
Strengthen public oversight on SOE performance.	Continuous	Publish annual external Audit Reports of majority controlled SOEs on their respective websites and comprehensive annual report on SOE portfolio performance including compliance with corporate governance standards and information on all financial relations with government published by end September of each year.	Strenghtening fiscal risk management and oversight (PFM)
Enhance transparent and efficient management of natural resources	End-2018,2019 and 2020	Actions include: (a) clarify and disclosing the rules regarding the financial relationship between the government and the sector SOEs , by end-2018, (b) disclose direct and indirect State's participation in the extractive industries sector , by end 2019, and (c) implement the roadmap to disclose beneficial ownership in the extractives sector, by end-2020.	Strenghtening fiscal transparency (PFM)
Submit to the National Assembly all legislative amendments which are necessary to support the transparency reforms mentioned	End-2018	This might include changes in the SISAFE Law governing public financial management.	Strenghtening fiscal transparency (PFM)
Accountability			
Support the accountability process and resolve the issue of unreported loans of EMATUM, Proindicus, and MAM companies	End-2017	Support the accountability process and resolve the issue of unreported loans of EMATUM, Proindicus, and MAM companies. The actions encompass: (a) report to the Administrative Tribunal and the Attorney General, the part of the guaranteed loans to be included in the budget and the part to be kept within the companies; (b) provide clear, comprehensive, and credible information on the effective use of the loan proceeds and overpricing practices; (c) continue to provide full support to the Attorney General in the investigation process to ensure accountability by committing logistical resources, financial support, and information access; (d) ensure transfer to the State of the security related assets of the three companies; and (e) consider the viability of the three companies and envisage their possible liquidation once the restructuring of the government's private debt is completed.	Strenthening fiscal accountability (PFM)
Support anti-corruption and governance efforts by strengthening the legal and institutional framework, and by improving effective enforcement	End- 2019	Authorities are encouraged to enhance good governance policies by taking priority measures to bring anti-corruption laws in line with international standards, and ensure their implementation. These measures include: (a) support the criminalization of corrupt practices and asset recovery, in line with international treaties, by criminalizing all UNCAC offences with sufficiently dissuasive sanctions; implementing and enforcing a comprehensive system of asset disclosure of public officials, subject to dissuasive sanctions, verifiable and publicly available online; enforcing accountability mechanisms for public managers; and ensuring the independence and operational capacity of anti-corruption agencies, courts and judiciary inspections; (b) promote the simplification of administrative procedures to reduce time-lags and cost to the public in line with international guidelines, such as the APEC-OECD Initiative on Regulatory Reform; and (c) upgrade the system for the recruitment, hiring, retention and promotion of civil servants and, where appropriate, other non-elected officials, including judges.	Strenthening fiscal accountability (PFM)

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

February 27, 2018

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—SUPPLEMENTARY INFORMATION

Prepared by The African Department

The purpose of this supplement is to inform the Board about the latest economic and policy developments in Mozambique since the staff report was issued to the Board. These developments do not alter the thrust of the staff appraisal.

RECENT ECONOMIC DEVELOPMENTS

1. **Growth and inflation.** GDP data recently published by Mozambique's National Institute of Statistics (INE) shows that the economy grew by 3.7 percent in 2017, driven by a recovery in agriculture and mining activity (notably coal).[1] Meanwhile, non-mining non-agricultural growth decelerated in 2017 to 1.8 percent (from 3.5 percent in 2016). Differences from the staff projections (3.0 percent real growth in 2017) result mainly from an upward revision of growth performance in the first three quarters of the year in a limited number of sectors. Inflation has continued to fall rapidly—the Maputo inflation index fell to 6.3 percent while for the national index it declined to 3.8 per-cent by end-January (y/y).

Mozambique: Real GDP Growth, 2016-2017

	2016	2017	
		Staff Report	INE
	Year-on-Year Growth Rate		
GDP at factor cost	3.3	3.4	3.8
of which: Nonmining-non agriculture	3.5	1.0	1.8
GDP at market prices	3.8	3.0	3.7

Source: Mozambique National Institute of Statistics (INE).

2. **Monetary and banking sector.** Data for January 2018 shows that credit to the economy declined y/y by 12.8 percent in nominal terms. Real interest rates remain elevated with bank's nominal average rates for 1-year loans and deposits around 28 percent and 18 percent respectively while average inflation is expected to remain in single digits in 2018.

[1] The latest national accounts data include an upward revision of past Q1-Q3 data and newly published Q4 data.

3. Government revenues. Recently published fiscal accounts show that revenue collection in 2017 reached 213.9 billion Meticals, exceeding staff projections (201.1 billion Meticals) by 12.8 billion Meticals (about 1.6 percent of GDP). The difference is mostly accounted for by a large overperformance (about 1.4 percent of GDP) in non-tax revenues. This reflects large unexpected dividends from both the Bank of Mozambique and the railway authority CFM (Caminhos de Ferro de Moçambique).

4. Government expenditures and fiscal deficit. The expenditures in the fiscal accounts data are not directly comparable to the staff report data, as the former are on a cash basis (i.e., they do not reflect the partial non-payment of debt service due or any domestic arrears). Nevertheless, they show that total primary expenditure (i.e., excluding interest) in 2017 amounts to around 230.5 billion Meticals, which is slightly higher than the staff's projection by 2.5 billion Meticals (or 0.3 percent of GDP). Reflecting mostly the over performance of revenues, and low debt servicing on a cash basis, the overall deficit shown by the fiscal accounts is about 5.4 percent of GDP.

5. Anadarko natural gas project. On February 20, Anadarko announced that it had sold about 10 percent of the future production of its natural gas field to the French power company EDF.[2] Including previously signed sales contracts, Anadarko has now sold about one half of the volume of production it needs to sell before a final investment decision can be considered. This, together with the approval of the project's development plan by the council of ministers a few weeks ago, shows that Anadarko is making steady progress toward a final investment decision, which staff projects to be in mid-2019.

POLICY DEVELOPMENTS

6. Monetary Policy Committee (MPC) decision. On 26 February, the MPC lowered the policy rate by 150 basis points to 18.0 percent. In addition, the MPC increased reserve requirements in foreign currency by 800 basis points to 22.0 percent effective on March 7 while keeping constant (14.0 percent) the reserve requirements in domestic currency.

7. Debt restructuring. The Ministry of Finance announced last week that it will resume discussions with private creditors in London on March 20. The government intends to present a proposal for debt restructuring aimed at bringing Mozambique's debt back to sustainable levels.

IMPLICATIONS

8. The above-mentioned recent economic developments and policy decisions do not alter the thrust of the staff appraisal. The released data include several one-off factors (e.g., non-tax revenues) and, therefore, the macro-projections for 2018 and the medium term remain largely valid. Similarly, the fiscal accounts for 2017 confirm that the deficit remains high and that there is a need for sustained fiscal consolidation efforts. On the monetary side, the MPC decisions are in line with staff advice.

[2] In addition, press reports indicate that Anadarko is actively discussing further sales with several South Asian companies.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

February 15, 2018

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By African Department

CONTENTS

FUND RELATIONS 2

JOINT WORLD BANK-IMF WORK PROGRAM, 2016–17 8

STATISTICAL ISSUES 12

FUND RELATIONS

(As of December 31, 2018)

Membership Status: Joined: September 24, 1984;		Article VIII
General Resources Account:	**SDR Million**	**%Quota**
Quota	227.20	100.00
IMF's Holdings of Currency (Holding Rate)	198.78	87.49
Reserve Tranche Position	28.43	12.51

SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	108.84	100.00
Holdings	15.39	14.14
Outstanding Purchases and Loans:	**SDR Million**	**%Quota**
ESF Arrangements	46.86	20.63
SCF Arrangements	85.20	37.50

Latest Financial Arrangements:

Past Engagement Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
SCF	Dec 18, 2015	Jun 17, 2017	204.48	85.20
ESF	Jun 30, 2009	Jun 28, 2010	113.60	113.60
ECF[1/]	Jul 06, 2004	Jul 05, 2007	11.36	11.36

[1/] Formerly PRGF

Overdue Obligations and Projected Payments to Fund[2]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2018	2019	2020	2021	2022
Principal	22.72	32.19	20.35	18.93	18.93
Charges/Interest	0.70	0.72	0.70	0.82	0.78
Total	**23.42**	**32.91**	**21.05**	**19.76**	**19.71**

[1]When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Implementation of HIPC Initiative:

I. Commitment of HIPC assistance	Original Framework	Enhanced Framework	Total
Decision point date	Apr 1998	Apr 2000	

Assistance committed by all creditors (US$ Million)[1/]	1716.00	306.00	
Of which IMF assistance (US$ Million)	124.60	18.46	
(SDR Equivalent in millions)	93.17	13.73	
Completion point date	Jun 1999	Sep 2001	

II. Disbursement of IMF assistance (SDR Million)

Assistance disbursed to the member	93.17	13.73	106.90
Interim assistance	--	2.31	2.31
Completion point balance	93.17	11.42	104.58
Additional disbursement of interest income [2/]	--	1.10	1.10
Total disbursements	93.17	14.83	108.00

[1/] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.
[2/] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

Implementation of Multilateral Debt Relief Initiative (MDRI):

MDRI-eligible debt (SDR Million)[1/]	106.56
Financed by: MDRI Trust	83.05
Remaining HIPC resources	23.51

Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGT**	**Total**
January 2006	N/A	106.56	106.56

[1/] The MDRI provides 100 percent debt relief to eligible member countries that qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable

Exchange Rate Arrangement

Mozambique has a de jure and de facto floating exchange rate arrangement. The exchange rate is largely determined in the interbank foreign exchange market (MCI). The BM regularly intervenes in the market to smooth seasonal fluctuations, provide foreign exchange liquidity received by the government in the form of aid, and sterilize domestic liquidity as part of its monetary policy operations. Mozambique is an Article VIII member and does not maintain exchange restrictions or multiple currency practices subject to Fund approval under Article VIII, Sections 2(a) and 3.

Safeguards Assessment

The previous assessment, completed in 2016. The assessment concluded that reforms are needed in the Bank of Mozambique (BM) governance and legal frameworks. The BM continues to lack independent oversight of management and operations. The BM's Board of Directors consists solely of executives responsible for specific operational areas, while other statutory bodies (primarily, the Audit Board) do not have an adequate mandate and capacity to oversee internal controls and audit mechanisms. The report noted that reforms to the central bank's legal framework is needed. While internal audit capacity has improved, its independence and authority need to be strengthened. Financial statements are audited by international firms, but transparency should be improved by making clear references to compliance with International Financial Reporting Standards. the Central Bank.

AML/CFT framework

Mozambique has taken several steps to address the deficiencies identified in its 2011 mutual evaluation report. With assistance from the Fund, it enacted a new AML/CFT law and regulations in 2013 and 2014 respectively. A new Penal code which increases the number of predicate offences for money laundering was enacted in December 2014. The Bank of Mozambique further strengthened the regulatory framework by issuing enforceable guidelines for financial institutions in May 2015. Draft amendments to the FIU law which are designed, in part, to strengthen its operational independence have been approved by Cabinet. The Financial Intelligence Unit (GIFiM) continues to work towards membership of the Egmont Group of Financial Intelligence Units and with assistance from the Fund, has developed Guidance on Reporting Suspicious Transactions, which will be issued to reporting entities. Going forward, the authorities should build on progress achieved and take important strides to achieve an acceptable level of effectiveness, including by improving the AML/CFT supervision of financial institutions as well as implementing enforceable requirements to identify politically exposed persons; and increased transparency of the beneficial ownership of corporate vehicles. Additional laws and regulations are required, namely to implement the supervision of Designated Non-Financial Businesses and Professions (DNFBPs), an asset recovery law and a mutual legal assistance law. Under a LEG TA project, GIFiM developed tools to be used in the AML/CFT supervision of real estate agents.

Article IV Consultation

The 2015 Article IV consultation was completed by the Executive Board on December 18, 2015 (Country Report No. 15/141). It is recommended that the next Article IV consultation take place on the standard 12-month cycle.

Ex post assessment of performance under Fund-supported programs

An ex post assessment (EPA) of Mozambique's performance under Fund-Supported Programs since 1987 was undertaken in December 2003 under the guidelines on assessments of countries with a longer-term program engagement. The EPA was circulated to the Executive Board on November 21, 2003 (Country Report No. 04/53).

Directors commended the authorities for their pursuit of sound macroeconomic policies and wide ranging structural reforms over the past fifteen years which contributed to strong growth of the economy, and a steady decline in poverty rates. Noting that despite considerable progress Mozambique remains a very poor and vulnerable country, Directors urged the authorities to persevere in their efforts to consolidate macroeconomic stability and accelerate and deepen structural reforms with a view to sustaining economic growth, encouraging employment creation, and further reducing poverty.

Management's visit

At the invitation of the authorities, Mr. Kato, Deputy Managing Director, visited Maputo, Mozambique in July 2005. Mr. de Rato, Managing Director, visited Mozambique on August 2007 for a meeting with the African Consultative Group on Quotas, Voice, and Representation. Mr. Lipton, Deputy Managing Director, visited Maputo, in May 2013. Ms. Lagarde, Managing Director, visited Mozambique on May 2014 for the Africa Rising conference.

Resident representative

Mr. Ari Aisen has been the IMF's resident representative to Mozambique since September 9, 2016.

Technical Assistance (2015–2017)

IMF Technical Assistance Provided to Mozambique (2015–17) (As of December, 2017)				
Departments	**Timing**	**Form**	**Purpose**	**Counterparts**
Fiscal Affairs	December 2017	Mission (Jointly with AFS)	PFMI training and capacity building	Ministry of Economy and Finance (MEF)
	October 2017	Mission	Capacity building to administer revenue from extractive industries	Revenue Authority (AT)/MEF
	September 2017	Mission	Extractive Industry–Developing a medium to long term revenue management strategy	AT/MEF
	September 2017	Mission	FARI Capacity Building Workshop	AT/MEF, Ministry of Natural Resources and Energy (MIREME), National Mining Agency (INAM) and the Bank of Mozambique (BM),
	July 2017	Mission	Revenue Administration	AT
	December 2015		MNRW-TTF – Follow-up on natural resources tax administration	AT/ MEF
	November 2015	Mission	Annual follow-up on PFM reforms (including fiscal risks and public investment, PIMA)	MEF
	November 2015	Mission	Follow-up on Revenue Administration	AT/MEF
	October 2015	Mission	Fuel imports and subsidies	MEF, MIREME
	April 2015	Mission	Follow-up on PFM reforms	MEF
	March 2015	Mission	Tax administration performance assessment (TADAT)	AT/MEF
	March 2015	Mission (jointly with AFR)	MNRW-TTF – Update on natural resources tax projections	AT/MEF
Institute	October 2017	Mission (Jointly with MCM and AFS)	Developing a Forecasting and Policy Analysis System (FPAS)	BM

Legal	September 2015	Mission	AML/CFT diagnostic project (Phase II, follow up)	GIFIM/BM
	April 2015	Mission	AML/CFT diagnostic project (Phase II, follow up)	GIFIM/BM
Monetary and Financial Sectors	December 2017	Mission (Jointly with AFS)	Training and Capacity Building- Payments & Settlement Systems	BM
	November 2017	Mission	Financial stability analysis and communication	BM
	September 2017	Mission	Central Bank Modernization Technical Assistance Project: discussion with Norges Bank experts	BM
	June 2017	Mission	Monetary policy, foreign exchange operations and central bank modernization and communication	BM
	November 2015	Peripatetic expert	Liquidity forecasting framework (Follow up)	BM
Statistics	August 2017	Mission (Jointly with AFS)	National Accounts S tatisics	INE
	March 2015	Peripatetic expert	Follow-up on balance of payments statistics reform	BM
	February 2015	Mission	MNRW-TTF - Statistics for managing natural resources	INE/MEF
AFRITAC South (AFS)	August 2017	Mission	Develop the customs post clearance audit (PCA) Function	Customs Authority
	October 2015	Peripatetic expert	Procedures for Central Bank communication	BM
	August 2015	Peripatetic expert	Strengthening macro-fiscal forecasts and fiscal risks management	MEF
	April – May 2015	Peripatetic expert	Follow-up on compliance with Basel core principles	BM
	April 2015	Mission	Technical assistance and training priorities going forward	MEF/BM
	April 2015	Peripatetic expert	Follow-up on national accounts statistics	INE/MEF

JOINT WORLD BANK-IMF WORK PROGRAM, 2016–17

(As of December 31, 2018)

The IMF and World Bank staff collaborate closely in their work on Mozambique. Bank staff participates in IMF missions, while the Bank's analysis and advice to the government in key structural reform areas informs Fund surveillance. The Fund Mozambique team met with the World Bank Mozambique team in Maputo during the mission in December 2017.

The Fund and the World Bank teams share a common assessment and have identified seven structural reform areas as macro-critical, in view of their central role in achieving higher and more inclusive growth:

Debt management and investment planning. The authorities' ambitious investment program will need to be backed by a strong reform agenda to enhance capacity to manage fiscal risks and ensure value for money. In the field of investment selection, several measures are being implemented to improve the investment pipeline and the project selection process. Debt management will be strengthened to ensure that borrowing and investment decisions entail value for money. This is underpinned by a new medium-term debt strategy.

Public financial management. The focus will be on consolidating PFM achievements, while enhancing the capacity to manage risks outside the central government, including in the area of state-owned enterprises (SOEs) and decentralized administrative units. To achieve this objective, the authorities will step up a framework to identify, monitor and mitigate fiscal risks, continue rolling out their new PFM system, and enhance budget execution and monitoring reports. Other critical measures aim at enhancing control of public spending to ensure budget appropriations remain within the limits, arrears are properly tracked and reduced. These reforms are macro-critical since they will protect fiscal space needed to reduce poverty and increase priority spending, while managing risks related to SOE's large-scale investment plans and enhancing the government's oversight.

Tax administration. Despite the strong increase in revenue collections, the tax system is still complex to administer and comply with. It is marked by numerous tax benefits and an overall low contribution from the mega-project sectors. Going forward, the government plans to facilitate tax compliance through electronic tax payment and continue to expand the tax base to cover the large informal sector. The revenue management system will be enhanced, in line with a set of agreed performance indicators.

Social safety nets. Two decades of high GDP growth have not yet resulted in significant poverty reduction. This, in turn, undermines the country's long-term growth potential. To address this, the authorities have started to strengthen their safety nets. Measures include: (i) rationalizing and expanding health insurance coverage; (ii) strengthening higher education and vocational training;

(iii) strengthening the financial sustainability and administration of the National Social Security Fund, and creating a new pension system for private sector workers; and (iv) improving the targeting of social protection systems to the most needy. These measures are macro-critical, as better health and education services, stronger pensions systems, and a more effective social safety net can enhance the productivity of the workforce and support social cohesion.

Natural resource wealth. Mozambique is endowed with rich natural resource reserves which are largely not exploited so far. With the recently started coal and gas projects, the extractive sector is slated for a boom which could make significant contributions to the country's economic growth and government revenues. This poses challenges for economic management, the sector's legal and regulatory frameworks and the government's capacity in managing contracts and revenues. Mozambique remains full membership of the Extractive Industries Transparency Initiative (EITI).

Investment climate. Mozambique's private sector is held back by the high costs of doing business. These arise mainly from weaknesses in governance, access to finance, power supply, tax and regulatory systems, and contract enforcement. Wide-ranging reforms are needed to address these issues. They are macro-critical because a better investment climate is conducive to supporting private sector activities, thereby broadening the country's productive and export base, creating jobs, and thus helping reduce poverty.

Financial sector stability and development. Strong past growth of credit to the private sector, the expansion of the banking system and its potential exposure to cross-border risks call for strengthening the continuous supervision of the financial sector, as well as the capacity to identity and address potential sources of vulnerabilities. In this context, a financial distress simulation exercise was carried out in April 2015 by the WB and the BOM, and the results will inform an action plan to address potential vulnerabilities. Meanwhile, improving financial intermediation and access to credit remains a top priority. To this end, the authorities have prepared the 2013-22 Financial Sector Development Strategy which includes a wide-ranging and clearly sequenced action plan, covering ways to, among other things, enhance financial inclusion, competition, consumer protection, and financial literacy.

4. **The teams agreed on the following division of labor:**

Debt management and investment planning reforms. The Fund will continue to play a key role in building government capacity to assess debt sustainability and define a coherent debt strategy through TA and continued support from HQ. Both institutions will assist the authorities in strengthening their debt management capacity, with TA support from the Fund and on-site assistance from the Bank. The Fund will continue to play a key role in helping the authorities improving debt management and public investment selection process. The Bank will continue providing technical assistance for enhancing project investment management and medium-term debt strategy.

Public financial management reform. The Bank and the Fund will cooperate in the field of rolling out the PFM system and improve financial management practices. The Fund will continue its support through regular TA missions from FAD and its AFRITAC South regional office in Mauritius. The Bank will provide ongoing consultation from its local office and supervision missions of projects under

implementation in this area. The Fund missions will provide opportunities to assess progress in this field.

Tax administration reforms. The Fund will take the lead in this area and provide support through ongoing advice based on regular TA missions from FAD and AFRITAC South. The Bank will advance reforms in this area in the context of its business environment policies and portfolio, and its program on natural resources (MAGTAP).

Social safety net reform. The Bank will take the lead in this field through continued TA in the design of more comprehensive and performing safety nets, in cooperation with other development partners and international organizations (including UNICEF and ILO). The Fund will play its role in identifying the fiscal space for the safety nets. The results will be discussed among the collaborators on a regular basis to inform policy discussions with the authorities. The Bank is also taking the lead in public pension reforms.

Natural resource wealth. The Fund will provide TA under the Topical Trust Fund for Managing Natural Resource Wealth (TTF-MNRW), relating to the fiscal regime of the extractive sector, revenue forecasting, and natural resource statistics, all being crucial to increase the sector's contribution to the budget and support the country's development agenda. The Bank is supporting Mozambique's implementation of EITI through its Multi-donor Trust Fund (MDTF). The Bank also funds it through the MAGTAP project.

Investment climate reform. The Bank will take the lead in working with government to enhance the investment climate, by deepening its agenda to help the authorities cut red tape and simplify the legal and regulatory framework. The results will be shared on an ongoing basis and discussed during the Fund program review missions.

Financial sector stability and development. The Fund will continue to help the Bank of Mozambique to build its capacity to assess risks to financial stability of the banking sector, while the Bank will take the lead in supporting financial sector development and reforms, including through enhanced financial inclusion, competition, consumer protection, and financial literacy. The results of their respective work will be shared and discussed regularly.

The teams have the following requests for information from their counterparts:

- The Fund team requests to be kept informed of progress in the above macro-critical structural reform areas. Timing: when milestones are reached; and during Fund program missions.
- The Bank team requests to be kept informed of the Fund's assessments of macroeconomic policies and prospects, and analytical work on areas under the Fund's lead, as well as on recommendations of Fund TA missions. Timing: in the context of Fund missions, and at least semi-annually.

The table below lists the teams' separate and joint work programs from May 2017 to April 2018.

Mozambique: Bank and Fund Planned Activities in Macro-Critical Structural Reform Areas, May 2017-April 2018

Title	Products	Timing of Missions	Expected delivery date
1. Bank Work Program	FSTAP project support to financial sector reforms	Ongoing	Ongoing
	Structural reforms: procurement, decentralization, business environment, financial sector	Ongoing	Ongoing
	Support on targeted, sustainable safety net measures (including public works system)	Ongoing	Ongoing
	Mozambique Economic Update	Ongoing	March 2016
	TA on public investment management	Ongoing	Ongoing
2. Fund Work Program			
	TA up mission on PFM	Dec. 2017	Dec. 2017
	Capacity building to administer revenue from extractive industries	Oct. 2017	Nov. 2017
	MNRW-TTF: FARI, macro fiscal issues	Sept. 2017	Nov. 2017
	Developing a Forecasting and Policy Analysis System (FPAS)	Oct 2017	Oct. 2017
	TA on national accounts statistics	Aug. 2017	Aug. 2017
	TA on financial stability and Communication	Nov. 2017	Nov. 2017
3. Joint Work Program	PFM: continue to monitor consolidation and expansion of e-SISTAFE	Ongoing	Ongoing
	Policy advice on public sector salary reforms (incl. pensions)	Ongoing	Ongoing
	Review of tax policy	TBD	TBD
	TA on Fiscal Risks Management	TBD	TBD
	Policy advice on natural resource wealth management	Ongoing	Ongoing
	Social Protection: Design of programs and assessment of fiscal space	Ongoing	Ongoing

STATISTICAL ISSUES

(As of February 6, 2017)

I. Assessment of Data Adequacy for Surveillance
General: Data provision has some shortcomings, but is broadly adequate for surveillance. The authorities are making efforts to improve the quality and timeliness of economic and financial data through participation in the Enhanced Data Dissemination Initiative (EDDI) funded by the U.K. Department for International Development (DFID). Weaknesses exist, particularly in the areas of national accounts, government finance, balance of payments, and external debt statistics.
Real sector statistics: The national accounts are prepared by the INE in accordance with the *1993 System of National Accounts* (*1993 SNA*). In July 2014, the INE released a revised annual GDP series for the period 1991-2013 with a switch from 2003 to 2009 as the base year. A partly revised GDP series was released in July 2015, in which the measurement of investments and imports for natural resource projects improved. The authorities are working to strengthen quarterly national accounts compilation at current prices. The INE's recent household income and expenditure survey conducted in 2015-2016 needs to be incorporated to strengthen the national accounts. A revamped consumer price index for Maputo based on weights derived from the 2008–09 household survey was released in February 2011. A national index obtained by integrating the indices for Maputo, Beira, and Nampula was released in April 2006. Several issues remain outstanding, however, including how to improve the housing market rent sample and expand coverage to include the Quelimane and Greater Maputo areas. There are also insufficient sectoral labor market and employment data, and where available, they have limited coverage. A one-year labor market survey of the entire country, undertaken by INE in collaboration with the Labor Ministry, was launched in October 2004.
Monetary and financial statistics: There have been significant improvements in the compilation of monetary statistics. There is need for more granular measures of commercial banks' foreign assets and liabilities. A 2004 work plan was developed to implement the Monetary and Financial Statistics Manual (MFSM) and develop an integrated monetary database (IMD) to meet the needs of the Bank of Mozambique (BM), AFR, and STA. In November 2007 the IMD was completed which allows the derivation of accurate and timely monthly monetary statistics, while reducing BM's reporting burden.
Balance of payments: With assistance from STA, provided in the context of the Enhanced Data Dissemination Initiative project financed by the United Kingdom's Department for International Development (DFID), the BM has made significant progress toward compiling and disseminating balance of payments (BOP) and international investment position (IIP) statistics. The migration process to the *Balance of Payments and International Investment Position Manual, sixth edition*

(*BPM6*) has been finalized; BOP and IIP statistics are now disseminated based on BPM6. Also, the IIP is compiled and disseminated on quarterly basis. The BM has an adequate institutional framework for the compilation of BOP and IIP statistics. However, further strengthening of external sector statistics needs to focus on: strengthening information technology (especially to apply data warehouse and on-line analytical processing tools); improving accuracy, consistency with BPM6 methodology, and coverage for several specific areas (especially in trade credit and advances and public and publicly-guaranteed private sector external debt). Also, there is need for improving data quality especially for foreign liability positions of non-megaprojects; and improving the compilation of imports of domestic enterprises supplying megaprojects. Joint work with other institutions to improve the quality of external trade data, especially about price and volume indices, also merits attention. Work is progressing to identify imports of domestic firms that are directly related to providing services to megaprojects. This will allow enhanced analysis of the impact of megaprojects and allow improved estimation of the economy's underlying (non-megaproject) current account position.

External debt statistics: While the authorities achieved a notable improvement in debt management under the 2010-13 PSI-supported program, improvements in this area are still needed. The debt unit needs to be strengthened (with respect to capacity) to exercise effective oversight over the entire public debt portfolio, including state-owned enterprises and loans that are part of cooperation agreements, and implement strong safeguards. As the information on disbursements received by entities outside the central government or by other line ministries as part of international cooperation agreements, comes with a delay to the debt office, when the confirmation from creditors or line ministries is missing, the stock figures can be subject to significant revisions. The strengthening of the debt office capacity is still needed to ensure a timely recording of disbursements in the external debt database.

II. Data Standards and Quality

Mozambique participates in the enhanced General Data Dissemination System but the country is yet to launch its NSDP for effective monitoring of progress in data transparency. Metadata are updated infrequently.	In May 2005, an update of the June 2002 data module of the Report on the Observance of Standards and Codes (Data ROSC) was prepared. Improvements in the institutional environment and increased allocation of resources for the compilation of national accounts and balance of payments statistics aimed to address weaknesses in the prerequisites for the quality of the statistics. Methodological soundness, accuracy, and reliability of macroeconomic statistics began to show improvements because of these efforts.

III. Reporting to STA
Mozambique does not report fiscal data for publication in the *International Financial Statistics* (*IFS)* but reports some revenue data for the *Government Finance Statistic Yearbook (GFSY)*. Mozambique now reports monthly monetary data to STA using the standardized reporting forms (SRFs). As a result, these enhanced data are being published in the *IFS Supplement*. In 2007, the BM started to compile and report comprehensive IIP data in the *Balance of Payments Statistics Yearbook*.

Mozambique: Table of Common Indicators Required for Surveillance

(As of February 6, 2018)

	Date of latest observation	Date received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]
Exchange Rates	Jan. 2018	Jan. 2018	D	W	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	Jan. 2017	Jan. 2018	W	W	W
Reserve/Base Money	Jan. 2017	Jan. 2017	D	W	D
Broad Money	Dec. 2017	Jan. 2018	M	M	M
Central Bank Balance Sheet	Dec. 2017	Jan. 2017	M	M	M
Consolidated Balance Sheet of the Banking System	Dec. 2017	Jan. 2018	M	M	M
Interest Rates[3]	Dec. 2017	Jan. 2018	M	M	M
Consumer Price Index	Dec. 2017	Jan. 2018	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[4] – General Government[5] and Central Government	2017 Q3	Jan 2018	M, Q	Q	Q
Stocks of Central Government and Central Government-Guaranteed Debt[6]	2017 Q3	Jan 2018	Q	Q	Q
External Current Account Balance	2017 Q3	Dec. 2017	Q	I	I
Exports and Imports of Goods and Services	2017 Q3	Dec. 2017	Q	I	I
GDP/GNP	2017 Q3	Feb. 2017	Q	Q	I
Gross External Debt	2015	Dec. 2016	A	I	I
International Investment Position[7]	2016	Sept. 2017	A	A	A

[1]Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

[2]Any reserve assets that are pledged of otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[3] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.

[4]Foreign, domestic bank, and domestic nonbank financing.

[5]Data is available for the central government. [The authorities are working on data compilation for the general government]. The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[6]Including currency and maturity composition.

[7] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

February 22, 2018

Approved By
David Owen and Zeine Zeidane (IMF) and Paloma Anos-Casero (IDA)

Prepared by the staffs of the International Monetary Fund (IMF) and the International Development Association (IDA)

Mozambique's debt is currently in distress, and total public debt is on an unsustainable path. The stark deterioration relative to the previous moderate debt distress rating has been driven by the delayed fiscal policy response to weaker commodity prices, limited control on State-owned enterprises (SOE) borrowing that resulted in large undisclosed external debt (of about $1.4 billion), and real exchange rate depreciation (48 percent since end-2014, even after accounting for the appreciation in 2017).

The DSA update[1] shows that the PV of external public and publicly guaranteed (PPG) debt relative to GDP (as well as relative to exports and revenues), and the ratio of external debt service relative to revenues, surpass by more than 50 percent the prudent thresholds for several years. The sovereign has been accumulating substantial external and domestic arrears (i.e. about 5 percent of GDP in external arrears, while the total amount of domestic arrears could be ranging from 2.5 to 4.5 percent of GDP) which adversely affect growth and financing prospects. Restoring debt sustainability would involve bringing Mozambique's external debt risk rating to "moderate" over the medium term (3-4 years), and reducing the overall public debt and financing needs to prudent levels. In 2016, the authorities announced plans to restructure their commercial debt but progress has been slow. Any restructuring agreed between the authorities and the creditors would need to consider the risk of prolonged delays in LNG project implementation in coming years, which is the major driver of growth and debt reduction over the longer term. Moreover, in staff's view there are substantial downside risks to the authorities' financing plans, notably in relation to the official concessional financing for the authorities' investment plan, which still needs to be contracted.

[1] The DSA presented in this document is based on the standard low-income countries (LIC) DSA framework. See "Staff Guidance Note on Application of the Joint Bank-Fund Debt Sustainability Framework for Low-Income Countries" and World Bank Report No. ACS6956, 10/23/13. Under the World Bank Country Policy and Institutional Assessment (CPIA); updated on July 18, 2017 with the 2016 CPIA rating, Mozambique maintains medium policy performer rating, albeit a second consecutive deterioration in the rating since 2014, with an average rating of 3.43 during 2014-16; the DSA uses the indicative thresholds for medium performers.

UNDERLYING DSA ASSUMPTIONS

1. Five important developments are affecting current assumptions compared to the previous DSA update prepared at the time of the fifth PSI review and Article IV Consultation in December 2015.[2] First, accounting for previously undisclosed external loans (totaling about $1.4 billion) significantly increases the outstanding debt stock, but even more so the debt service, as illustrated in Text Table 1 and Text Figure 1. Second, the refinancing of the EMATUM bond in April 2016, while reducing the debt service over the medium term, has created a spike in debt service due to its redemption profile taking the form of a large bullet repayment of the outstanding principle in 2023. Third, the rapid depreciation of the metical in 2014-16 has led to a drastic upward shift in debt and debt service ratios. Fourth, the short- and medium-term growth projections have been revised downward. And, fifth, there has been further delay in the investment and production schedule of natural gas projects, with investment beginning only in late 2017 for the Area 4 Coral project and production assumed to begin in 2023. The Area 1 project is assumed to start only in the second half of 2019, and production in 2024, respectively.

Text Table 1. Mozambique: Debt, Public and Publicly Guaranteed (Percent of GDP)

	2013	2014	2015	2016	2017p
Public sector debt [1]	**53.1**	**62.4**	**88.1**	**128.3**	**112.0**
Public sector external debt (incl. guarantees) (A+B+C)	**47.0**	**55.8**	**76.4**	**103.7**	**85.2**
A. Bank of Mozambique-IMF	1.1	1.1	1.9	2.2	1.3
B. General Government	36.3	44.8	62.4	88.9	72.7
Multilateral creditors, excl IMF	21.1	20.8	28.2	39.1	29.9
Bilateral creditors [1]	15.2	20.8	30.9	42.3	32.2
Paris Club	2.6	3.3	5.1	7.8	6.7
Banks	0.0	3.2	3.3	7.5	5.4
EMATUM/Mozam Eurobond	0.0	3.2	3.3	7.5	5.4
Other public sector : *ENH (Coral LNG project)*	0.0	0.0	0.0	0.0	5.2
C. Government guaranteed external debt	9.5	9.9	12.1	10.8	5.9
EMATUM	5.3	2.2	2.7	0.0	0.0
Proindicus	3.9	3.9	4.8	6.2	3.6
MAM	0.0	3.4	4.2	4.1	2.0
Other guarantees	0.3	0.4	0.4	0.5	0.3
Public sector domestic debt (incl. guarantees)	**6.2**	**6.5**	**11.7**	**24.6**	**26.7**

Sources: Mozambique authorities; and IMF Staff calculations and projections.

[1] This reflects the latest end-2016 debt stock data shared with IMF Staff in December 2017, and disbursements data from January to November for 2017. It includes the external arrears. Domestic debt includes domestic debt of a selected number of SOEs for 2016 and 2017, for which data was available. The selection criteria are set in the Joint IMF-Bank Guidance Note on Low-Income Countries Debt Sustainability Framework. The 2017 estimate includes ENH borrowing from external partners for its participation in Area 4 Coral LNG project.

[2] See IMF Country Report No. 16/9.

2. The macroeconomic outlook is expected to deteriorate compared to the previous Article IV DSA update (see Text Table 3)**.** Under the baseline scenario described in the staff report, the economic outlook is considerably less buoyant than previously projected, with economic growth projected at 3 percent in 2017 (compared to 7.2 percent in the previous Article IV DSA; the 2016 outcome was also lower than projected in 2015). This reflects the ongoing slowdown amid a loss of confidence after the previously undisclosed loans were revealed to the public and consequently triggered a freeze of budget support disbursement by donors. It also reflects, in 2016, adverse weather conditions. While substantial tightening of monetary policy has stabilized the exchange rate market in late 2016 and in 2017, and supported the correction of external imbalances, output growth is not expected to recover over the medium term as fiscal policy is assessed to remain loose, and domestic arrears to suppliers are expected to accumulate (to about 20 percent of GDP by 2023) as domestic financing is expected to reach its limits by end-2018. Growth is expected to recover only in 2023 on the back of the start of production of natural gas projects. The overall fiscal deficit (on a modified cash basis, excluding the 2017 one-off capital gain tax revenue) is expected to reach 8.2 percent of GDP in 2017, up from 7.6 percent in 2016, and to deteriorate further by 2023. The current account deficit is projected to increase to over 118 percent of GDP by 2023 reflecting a surge in imports of goods and services mainly related to construction of processing facilities for liquefied natural gas (LNG). Approximately one third of all imports related to such investments are financed by (frontloaded) FDI with the remainder financed by private debt.

3. The risks to the macroeconomic outlook are assessed to be numerous and the likelihood of downside risks higher. In the near term, the main risk relates to a disorderly adjustment due to a drying up of financing the fiscal deficits. Even if the authorities adhered to a lesser than projected spending envelope, the projected fiscal gap over the medium term is too large to be financed through a continuous accumulation of arrears. The accumulation of domestic and external arrears exerts several other negative effects such as increased crowding out of the private sector in credit markets and decreasing confidence, with potentially even more adverse effects on growth and the external sector than currently assumed in the baseline. Another near-term risk relates to whether the external sector's recent stabilization can be sustained only through monetary policy action over a prolonged period. Over the medium term, a substantial delay in the implementation of the Anadarko LNG project constitutes the main risk. In staff's view, given current financing prospects, there are also substantial downside risks to the authorities' external financing plans in relation to still-to-be-contracted concessional financing for the authorities' development investment plan. There are also several mitigating factors related to expansion in the coal and LNG sectors.[3] A further recovery of commodity prices, new oil and gas discoveries resulting from recently extended exploration rights, other FDI projects, or, over time. initiation of phase 2 of the natural gas projects would constitute upside risks.

4. The authorities have scaled back considerably contracting of government external debt. Projections assume that a prudent stance on new borrowing would be retained in the medium term. The authorities have currently put on hold, since the second half of 2017, the negotiations of large projects in

[3] The drag on growth of fiscal consolidation is projected to be offset by an ongoing expansion of coal production in light of the now completed Nacala rail corridor. During 2019-22, LNG investment should boost growth mainly due to higher activity in the construction sector.

pipeline financed on non-concessional terms. New disbursements from multilateral and bilateral creditors are assumed to be in line with the projects that are on-going or loans previously signed but not yet disbursed. New borrowing for projects in pipeline is assumed to gradually resume being contracted with multilateral and bilateral creditors largely from 2020 onwards as approaching the date when the LNG exports come on stream. The financing assumptions are in line with the long-term output growth projections for Mozambique, which are largely driven by the LNG exports coming on stream from 2023 onwards. There are, however, significant risks related to the availability of financing, in particular for large concessional official financing over the medium term. If the negative risks around the baseline materialize in 2018, external financing would need to be significantly revised down. A further delay in the LNG projects implementation constitutes another high risk. Text Figure 3 shows the assumed external disbursements and the financing assumptions up to 2023.

5. **Mozambique is currently in default, as the sovereign started to accumulate external arrears in 2016.** Projections assume that the arrears on the defaulted loans will continue to accumulate over the projection horizon. Sovereign arrears have been incurred on the Mozam Eurobond coupon and on the debt service of Proindicus and MAM. The March 2016 debt service payments on the Ematum and Proindicus loans were met, but required a $200 million loan from the Bank of Mozambique directly to the government. The overall stock of external arrears on public and publicly guaranteed external debt service has reached $710 million at end-2017 (see Text Table 2), including arrears under bilateral discussion with five official creditors amounting to $94 million (Libya, Iraq, Angola, Bulgaria and Poland)[4] and arrears amounting to about $23 million to Brazil on a $125 million state-guaranteed borrowing undertaken by the state-owned airport company for which the guarantee has been called.[5, 6] The government is

Text Table 2. Mozambique: Stock of External Arrears
(Millions of U.S. dollars)[1]

	End-2017
Commercial debt	592.86
Mozam	97.90
MAM	343.06
Proindicus	151.90
Bilateral debt	116.80
Paris Club: Brazil	22.93
Non-Paris Club [2]	93.87
Total	**709.66**

[1] Staff estimates based on information provided by the authorities. Contractual penalty fees or rates have not been included.

[2] Data reported by the authorities for Libya, Iraq, Angola, Poland and Bulgaria on the reconciled debt.

[4] The arrears with Libya, Iraq, Angola, Bulgaria and Poland are not new arrears. The authorities have reconciled the debt with these non-Paris Club creditors dating from the HIPC Initiative in 2006, 2011, and 2015, respectively, and are negotiating several solutions with these creditors for the restructuring of this debt. While the negotiations are on-going, the debt payment obligations incurred from the date of reconciliation until end-2017 have been included in the stock of arrears in line with the terms of the reconciliation registered in authorities' external debt database.

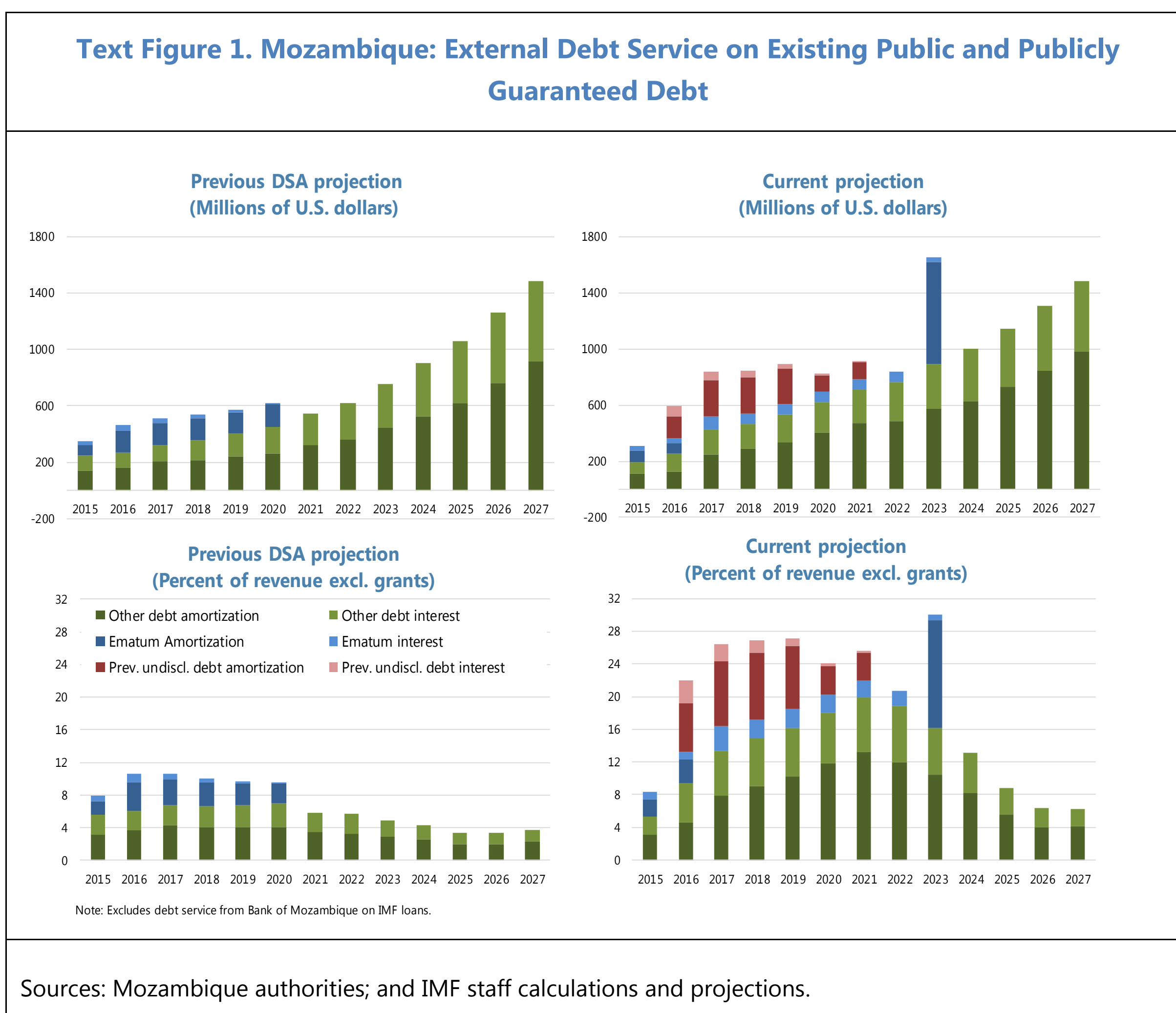
[5] Contractual penalty fees or rates on missed payments have not yet been included in the estimate for the stock of arrears reflected in the baseline.

[6] The two loans from the Brazilian Development Bank (BNDES) to the state-owned airports company, *Aeroportos de Mozambique* (AdM) were also guaranteed to BNDES by the Brazilian Export Guarantee Fund (this guarantee has also been called).

servicing all the remaining multilateral and bilateral external debt obligations.[7] While negotiations remain ongoing on solutions to regularize these arrears, it is staff's understanding that the authorities plan to hold off on making payments on the defaulted loans.

6. The government announced a debt restructuring in October 2016 and has initiated discussions with selected creditors. However, no significant progress has been made so far, and, therefore, the projections do not include any assumptions on the debt restructuring. A major step to initiate these discussions was the hiring in spring of 2016 of reputable financial and legal advisors. The authorities are focusing their restructuring efforts on the MAM and Proindicus loans, and the Mozam (ex-Ematum) Eurobond, but also on potential re-profiling of highly non-concessional bilateral loans.[8]

Text Figure 1. Mozambique: External Debt Service on Existing Public and Publicly Guaranteed Debt

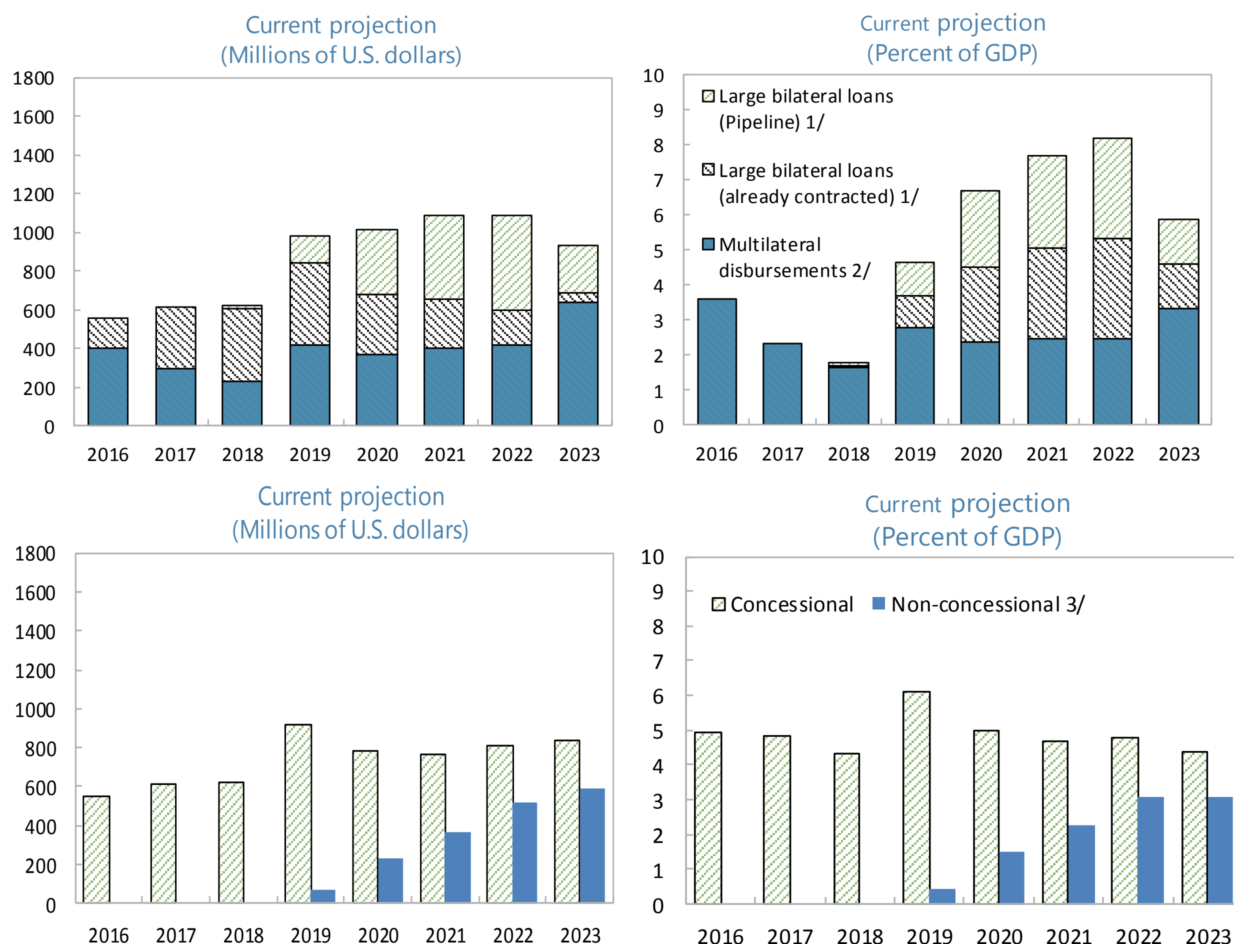


Sources: Mozambique authorities; and IMF staff calculations and projections.

[7] Based on the authorities' data reporting during the 2017 Article IV consultations.

[8] Based on the authorities reporting during the Article IV mission, an agreement has been reached with China and India on the re-scheduling of debt service payments on several bilateral loans. The new schedule of re-payments has been included in the baseline assumptions.

Text Figure 2. Mozambique: Public Sector External Disbursement Path



[1] Large bilateral loans are those with amounts exceeding US$60 million.

[2] Also includes disbursements on small bilateral loans.

[3] Negotiations put on hold in the second half of 2017; gradually resume in the second half of 2019 for large projects.

7. **Finally, a large government guarantee may need to be issued in the short term in favor of the hydrocarbon SOE, ENH, to ensure that Anadarko LNG investment can move forward.** ENH holds a 15 percent share in the Area 1 natural gas project, which is being developed by an Anadarko-led consortium. The planned development cost for the LNG processing facilities and associated investments is around $25 billion, of which about $15 billion will be debt financed. As ENH would be liable for 15 percent of this debt, the guarantee required by the consortium of export credit agencies and commercial banks assembled to provide this financing could amount to about $2¼ billion, which together with the equity borrowing from the partners of about $1.5 billion, would increase the PPG debt stock in line with the

disbursement plans.[9] The guarantee could only be called if the project was not completed or if there were extraordinarily lengthy delays in project completion.[10] In addition to the Area 1 project, ENH also holds a 10 percent share in the Area 4 natural gas projects, which is being developed by the ENI-led consortium. The planned development cost for the LNG processing facilities and associated investments is around $7 billion, of which about $4.5 billion is debt financed. While no government guarantee has been required for the debt financing of the project, the 10 percent share of ENH, amounting to about $700 million, would increase the PPG debt as it represents borrowing from external partners. The ENH shares both in Area 1 and Area 4 have been included in the DSA without increasing gross financing needs, as the debt service will be serviced out of projects' revenues, from ENH share in profits.

Text Table 3. Evolution of Selected Macroeconomic Indicators Between DSA Updates

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
				Projections						
Real GDP growth (%) [1]										
Previous DSA (PSI, 5th review)	7.2	6.3	6.5	7.2	8.3	7.6	7.5	33.9	14.0	...
Current DSA	7.4	6.6	3.8	3.0	3.0	2.5	2.4	2.3	2.2	9.9
Nominal GDP (US$ billion)										
Previous DSA (PSI, 5th review)	17.0	15.2	14.8	16.4	18.4	20.5	22.8	31.4	36.7	...
Current DSA	16.9	14.8	11.3	12.7	14.3	15.0	15.7	16.4	17.1	19.1
Overall fiscal deficit (%GDP)										
Previous DSA (PSI, 5th review)	10.6	6.0	4.0	4.3	4.4	4.2	4.3	1.3	2.0	...
Current DSA	10.7	7.2	7.6	5.5	7.5	10.8	9.9	9.6	10.6	9.9
Current account deficit (% GDP)										
Previous DSA (PSI, 5th review)	34.1	30.2	33.1	55.4	73.2	80.8	90.4	73.2	65.5	...
Current DSA	38.2	40.3	39.2	16.1	16.9	44.6	66.6	91.0	116.4	117.7
FDI (% of GDP) [2]										
Previous DSA (PSI, 5th review)	28.9	25.2	30.6	28.3	27.3	27.4	27.1	18.9	16.6	...
Current DSA	29.6	26.1	27.8	12.4	12.6	34.8	53.7	75.2	20.0	4.0

Source: IMF staff calculations and projections.

[1] Real GDP growth in the previous DSA jumped in 2021 due to the coming onstream of the first LNG production. In the current DSA, this is now projected for 2023.

[2] High FDI over the medium term is driven by LNG investment. The current DSA now assumes that the FDI share of such investment would enter first before switching to debt financing in 2021.

[9] No guarantee would be needed for ENH's equity share which will be financed by the Anadarko-led consortium with repayments coming out of LNG revenues during the first years of the project's operation.

[10] In the agreements, a two-year buffer is planned to be included between the expected completion data for the facilities and the deadline at which the guarantee could be called. If force majeure is involved, this buffer would increase to three years. Meanwhile, risks emanating from adverse gas price movements do not constitute a major concern, because the projects would be supported by long-term sales contracts with gas off-takers.

Box 1. Macroeconomic Assumptions 2017–2037

The medium-term assumptions in the Baseline Scenario for 2017-2037 are consistent with the medium-term macroeconomic framework in Annex 1.

Real GDP growth is not expected to recover and remain around a 2.2-2.5 percent range over the medium term, supported mainly by the expansion in coal mining and infrastructure investments, including LNG manufacturing. A sharp increase in growth in 2023 reflects the assumed coming on line of the first natural gas production plant ("train") and related exports in that year. Overall GDP growth will moderate once LNG production reaches its full capacity in 2028. Risks to long-term growth include public and private investment not achieving expected payoffs and thus limiting productivity gains, and the possibility of Dutch disease.

LNG sector. LNG plants totaling 13 onshore LNG manufacturing units ("trains") and 4 floating trains (FLNG), are assumed to be under construction from late 2017 through 2027. The first onshore train and the first floating train are assumed to start production in 2023, followed by remaining trains sequentially starting production. The final train will start production in 2029, by which time the value of production could approach $40 billion. Total investment from 2017 is projected at $110 billion. The schedule and size of the projects is highly ambitious and depend on the timing and content of final investment decisions, the first one has been made by the investors at end-2017. The assumption is subject to significant implementation risks and changes in gas market conditions.

Consumer price inflation is projected to gradually slow down to the authorities' target range of 5–6 percent over the medium term.

Export value growth is projected to be positive (27.6 percent) in 2017, as coal exports expanded much faster than expected in light of completion of the Nacala rail corridor, and despite the decrease in traditional exports by 8.7 percent. Over the medium-term exports are expected to fall back to around 3 percent, as economic activity slows down and coal exports reach potential. The coming on stream of LNG exports causes large increases in exports starting in 2023 (over 50 percent export value growth on average during 2023-26. The start of LNG production and exports was delayed by two years compared to the previous Art IV DSA. From the late 2020s onwards, export growth to fall back to the 2-3 percent range, as LNG exports are not projected to expand further.

Imports in the non-megaproject economy are projected to contract only slightly in 2017 supported by the metical appreciation. In the medium term, total imports would grow by more than 35 percent on average during 2019-22 as a result of LNG investment. Meanwhile, non-megaproject imports would remain relatively subdued growing by about 5 percent on average until 2023 as economic activity slows down. Annual non-megaproject import growth is expected to increase during 2024-28 (to about 8 percent on average), as LNG production increases available resources. Subsequently, import value growth is projected to remain subdued to around 3 percent under the baseline of current policies.

The external current account balance is projected to peak at a deficit of over 118.5 percent of GDP by 2023 driven by imports for LNG investment. The doubling of this peak compared to the previous DSA results from lower GDP, and the Metical depreciation. The current account deficit will be primarily financed through FDI and private external borrowing. The large size of LNG exports under the revised baseline implies it would subsequently turn into surplus during the mid-2020s and early 2030s. The current account deficit excluding all megaproject-related activity is projected to narrow but remain at elevated levels of about 15 to 18 percent of GDP over the medium term (from 22 percent of GDP in 2016) on the back of slowdown in economic activity, but also helped by the LNG investment inflows a fraction of which would go to procurement of domestic goods and services and thus support the external position.[1] Subsequently, the non-mega project current account deficit (excluding all megaproject-related activity) is projected in terms of GDP to mechanically decline to 9.7 percent by 2025 and in the long run, given the impact on GDP of the LNG gas projects.

Box 1. Macroeconomic Assumptions 2017–37 (concluded)

The primary fiscal deficit (on a modified cash basis) stood at 6.4 percent of GDP in 2015, and decreased to 4.6 percent of GDP in 2016. It is projected to remain at 4.5 percent of GDP in 2017 (when excluding the one-off 2017 capital gains tax revenues), narrow to 3.2 percent of GDP with the 2018 Budget, and then reverse to deficits of 5-7.5 percent of GDP during 2019-2022. The primary fiscal balance is expected to stay in deficit beyond 2023, and revert to balance by late 2020s. Even though the gas production would rapidly scale up during the early 2020s, fiscal revenues during the first few years are limited, because of the large cost recovery for continuous investments in building liquefaction plants. By the late 2020s, the fiscal revenues from the gas projects would account for more than half of total fiscal revenues.[2]

---

[1] While this fraction can be expected to be small, the large size of the LNG investment would nonetheless make it important for the balance of payments.

[2] We assume that fiscal revenues remain broadly constant as a percentage of GDP after the sizeable boost to real GDP from LNG production. This implicitly reflects the fiscal impact of LNG production. We consider this to be a rather conservative assumption, as the tax take out of LNG revenues, as suggested by the FARI model, can be substantially higher. Fully incorporating such revenues would constitute a significant upside risk to the fiscal framework going forward.

EXTERNAL DEBT SUSTAINABILITY ANALYSIS

8. **The risk rating of Mozambique's external PPG is re-classified to "in distress", while total public debt is assessed to be on an unsustainable path.** All five public external debt indicators breach their respective thresholds in the near and/or medium-term under the baseline (Baseline Scenario Figure 1)[11], four of which by more than 50 percent of their respective threshold for several years:

- **The PV of external public debt in terms of GDP** is projected at about 67 percent in 2017 (Baseline Scenario, Table 1), compared to 38.4 percent in the previous Article IV DSA and a threshold of 40 percent. It would remain above the threshold until 2026, when under baseline assumptions real GDP would jump by more than 75 percent from 2023 to 2025 taken together due to the LNG projects production. If the LNG projects were to be delayed, this indicator could be expected to remain above the prudent threshold until LNG investment commences.

- **The PV of debt in terms of exports** in 2016 has also increased considerably relative to the previous Article IV DSA (238 percent versus 129 percent), with declines in exports driving part of the increase. With exports recovering in 2017, as the completion of the Nacala rail corridor underpins coal exports, this indicator is projected to fall to about 176.7 percent in 2017, and deteriorate over the medium term with a peak at about 248.4 percent in 2022, as coal exports stabilize and non-megaproject exports are expected to remain subdued over the medium term. With the LNG projects

---

[11] As in the previous DSAs, the historical scenario has been excluded from DSA Figure 1 for both the baseline and alternative scenarios. The reason for the exclusion is that such a scenario shows unrealistically fast declines of public debt ratios over the medium term, because it fixes the non-interest current account deficit at a historical average which is much lower than projected deficits driven by the LNG investments. With private debt accumulation assumed to remain unchanged compared to the baseline, this assumption then results in unrealistically fast declines of public debt ratios.

coming into production, the indicator is expected to fall below its 150 percent threshold by 2024. Risks from possible renewed commodity price shocks, particularly with regards to coal, would weaken further the indicator over the medium term.

- **The PV of debt in terms of revenues** in 2016 increased to about 330 percent (versus 147 percent in the previous Article IV DSA), and is expected to fall to 265 percent in 2017. However, it is projected to deteriorate and stay at elevated levels above the prudent threshold for almost eight years. Apart from the shocks to nominal debt levels and the exchange rate, also declines in fiscal revenue are taking a toll. It is projected to decline below its 250 percent prudent threshold by 2024.

- **External public debt service in terms of revenues** deteriorated dramatically to about 27 percent of revenues in 2017 from 12½ percent in the previous Article IV DSA. Here the steep payments on the MAM, and Proindicus loans play a significant role, as well as the Ematum refinancing. This indicator would peak at the time of the Mozam Eurobond redemption at 44 percent, and only consistently fall below its 20 percent threshold in 2026, when the Mozam bond should be amortized and LNG production is largely on stream. After 2026, it would be in the 8-9 percent of revenue range.

- **External public debt service in terms of exports** is projected to stay slightly below threshold in the near-term and have a 1-single breach of the threshold in the medium term, at the time of the Mozam Eurobond redemption reaching 26.4 percent (or 6.4 percentage points above the 20 percent threshold).

9. In the long term, external debt remains mainly driven by assumptions on the LNG projects. External debt is now expected to peak in 2023 at 370.8 percent of GDP (compared to 232 percent of GDP in the previous November Article IV DSA update). The heightening of the peak is driven by the metical depreciation lowering the dollar value of Mozambique's GDP, while the nominal amount of LNG investment stays the same. The changes in public debt are also driven by the external arrears on PPG debt, which are assumed to still accumulate until that time. The ENH borrowing from external partners increases public debt by about 20 percentage points at the peak in 2023 (see Text Table 4).

Text Table 4. Mozambique: External PPG

(Millions of U.S. dollars)

	2016	2017	2018	2019	2020	2021	2022	2023
External PPG	103.7	85.2	95.3	101.3	106.0	110.6	114.3	107.4
External PPG, without ENH	103.7	80.0	79.7	81.4	83.0	84.8	88.5	86.2

Sources: Mozambique authorities; and IMF staff estimates and projections.

10. Compared to public debt, the risks emanating from private external debt seem much more benign. Although private external debt is expected to stand at 57.5 percent of GDP at end 2017 (versus the 43 percent in the previous Article IV DSA update), resulting vulnerabilities are

relatively low as much of such debt is owed by megaprojects, which receive their revenues in foreign currency and are, therefore, much less affected by metical depreciation than by commodity prices. In addition, many debts are owed to parent companies, attenuating risks further. Direct depreciation impacts on bank profits should be contained given the regulation on banks' net open positions (limited to less than 20 percent), although significant impact could result through higher NPLs. By 2022, private external debt is expected to quadruple relative to GDP driven by the large LNG investments. However, it would be expected to be reduced again equally rapidly until the late 2020s as initial LNG revenues are devoted to amortizations.

11. External debt and debt service ratios seem most sensitive to exchange rate shocks. The stress tests illustrate that a 30 percent further nominal depreciation of the metical in 2018 relative to projections would increase the PV of external public debt to GDP ratio by another 40 percentage points (to 105 percent) in that year relative to 2017. As a response to such a 30 percent FX shock external debt service relative to government revenue would increase to 40 percent in 2018 (from 29 percent in absence of such a shock). In comparison to exchange rate depreciation, other stress tests are more benign although their standard versions in some cases do not capture the risks well at the current juncture. For instance, the standard stress test for GDP growth assumes it to be one standard deviation below historical averages. However, growth during the next years is already projected well below historical averages.[12] If instead a shock to growth relative to the baseline of four standard deviations is modeled,[13] the impact is more modest.

PUBLIC SECTOR DEBT SUSTAINABILITY

12. Total public debt levels have increased in line with external debt, but also due to a significant increase in domestic debt (Table 3 and Figure 2). External public debt is expected to stay slightly below 80 percent of total public debt, as domestic debt is expected to increase to about 26 percent of GDP in 2017 and 2018 (of which, about 60 percent in government securities, while the rest is SOEs domestic debt). Nominal public debt stood at 128.3 percent of GDP at end 2016 (of which 10 percent of GDP in SOEs domestic debt, not previously included in the debt projections due to data availability) (compared to 73 percent of GDP in the previous Article IV DSA). The current DSA update includes in the coverage of public debt a selected number of SOEs for which data was available.[14] In the case of Mozambique, staff has assessed strong macro-financial linkages between the government on the one hand and SOEs, banks, on the other. Given the identified vulnerabilities in the SOEs sector, their indebtedness towards both external creditors and domestic banks has been

[12] Similarly, while Table 2 identifies shocks to non-debt creating external inflows (such as FDI) to have a higher impact, these figures cannot be taken at face value. This stress test assumes that imports would remain constant, even if FDI were to underperform. In the case of Mozambique, however, FDI flows are mainly driven by LNG investment over the medium term and most of them go toward imports. Thus, if these flows were to be lower, imports would also be lower by the same proportion, and there would not be the large impact on debt displayed in Table 2.

[13] In this stress test, real GDP growth is 2.3 percent in 2018 and 2019 (versus a baseline of 3 percent and 2.5 percent, respectively).

[14] The criteria for inclusion of SOEs in the DSA is defined in the Joint Bank-IMF Guidance Note on Low Income Countries Debt Sustainability Framework.

included in the current DSA update. The present value of total public debt at the 5 percent DSA discount rate would be 104 percent of GDP (more than double of the value projected in the previous Article IV DSA), with increasing domestic debt playing an important role. The PV of debt surpasses the 56 percent of GDP prudent benchmark in the near and medium term until 2025.

13. Public debt servicing is expected to continue to be an enormous challenge, with both external and domestic arrears accumulating over the projection period. Rollover of domestic debt instruments needs to be ensured. Total public debt service is projected to consume over 50 percent of public revenue in 2018, 2019 and 2020. As this figure includes the rollover of domestic treasury bills and bonds, it provides a notion of the importance of reassuring holders of these instruments through determined policy action. Under the baseline, domestic arrears to suppliers are expected to accumulate reaching about 20 percent of GDP by 2023.

CONCLUSION

14. Ensuring that LNG production materializes is crucial to underpin Mozambique's long-run debt sustainability. LNG-driven increases to GDP and revenues holds the potential to eventually return debt ratios to prudent levels, aside from providing resources to foster Mozambique's development. But the ongoing challenges with regards to public debt may negatively affect the implementation of LNG prospects. Therefore, re-establishing macroeconomic stability and improving the outlook for debt, including through the careful management of relations with creditors, will support LNG developments and future growth prospects.

15. Restoring macroeconomic stability is paramount. While it will be essential to re-instill confidence and to support the economy at a critical juncture, it will also be important for returning debt to sustainability. The reason is that Mozambique's debt sustainability could be further undermined in response to moderate shocks. Stress tests highlight that Mozambique's debt and its debt service capacity would be adversely affected by higher metical depreciation than is envisaged in the present projections. It is important for the authorities to ambitiously implement fiscal consolidation both to address the economy's external imbalance and to place public debt on a sustained downward trajectory. Moreover, it would help contain downside risks to the financing plans, notably in relation to the still-to-be-contracted concessional official financing.

16. Extreme caution is warranted regarding the contracting of new debt going forward. On external loans, non-concessional terms need to be avoided and the contraction of new loans needs to be strictly limited in line with expectations on the LNG revenues coming on stream. The focus should be on the most urgent projects with high development impacts including maintenance projects to safeguard productive capacity. It is important thus to continue to improve project selection and efficiency of public investment spending by developing a better prioritization of projects and their financing. An increase in the efficiency of the investment process in general would be crucial. In the near-term, this will also imply that some loans for projects for which financing has already been approved and secured may need to be postponed or cancelled if loans for higher-priority projects are to be contracted.

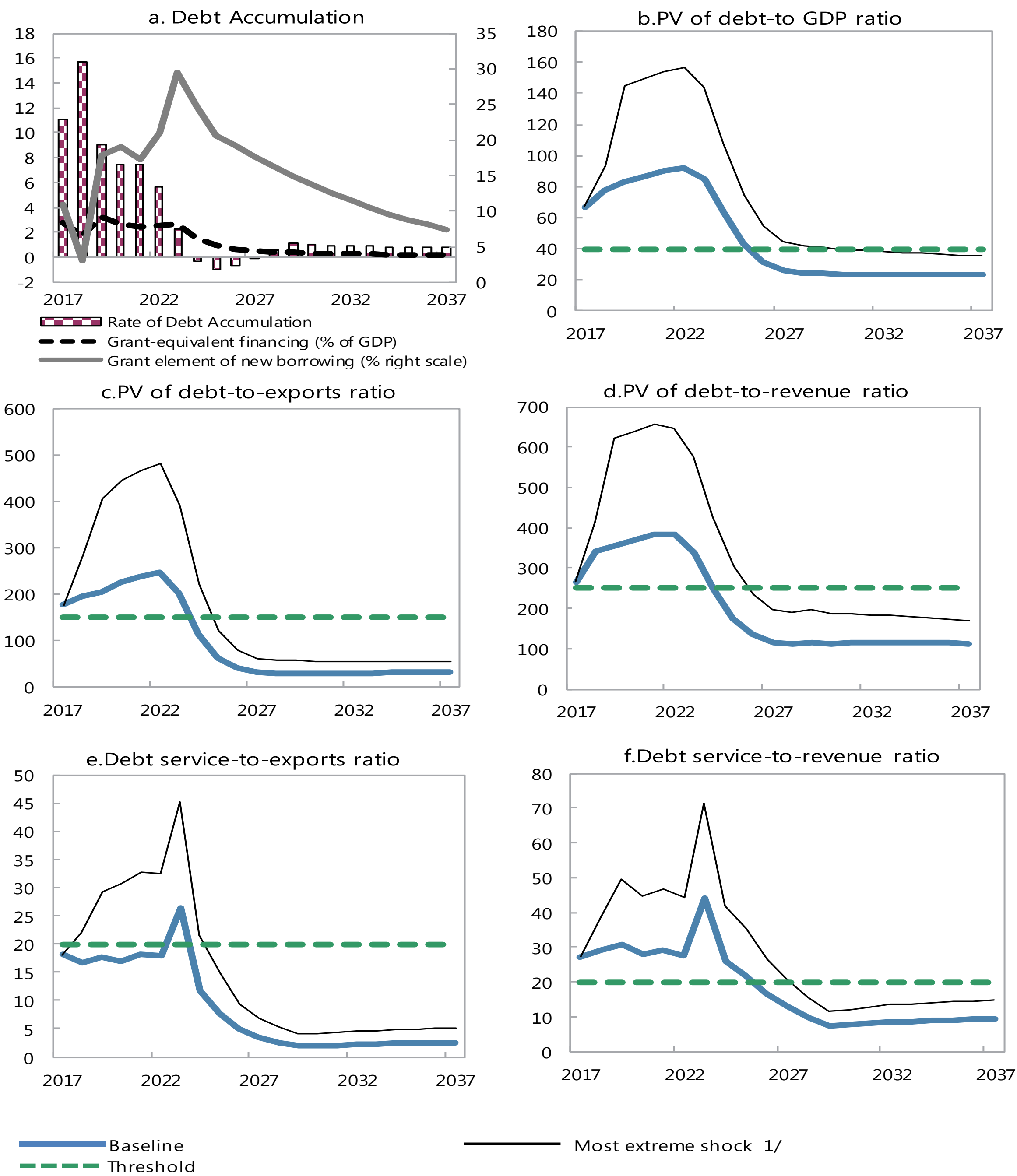
17. Debt management and oversight need to be improved. The debt unit needs to be strengthened (with respect to capacity and clout) to exercise effective oversight over the entire public debt portfolio and to implement strong safeguards. The oversight over SOEs needs to be substantially strengthened.[15]

AUTHORITIES VIEW

18. The authorities concurred with staff's assessment regarding the revision in the external debt risk rating, and the debt sustainability assessment. The authorities recognized the need for reducing financing needs as well as reaching a balanced primary deficit over the medium term. However, they had reservations on the pace of fiscal adjustment recommended by the staff, as well as on the medium-term growth projections under the baseline, which the authorities considered too conservative. To restore debt sustainability, the authorities intend to implement the fiscal measures envisaged in the 2018 Budget and actively resume discussions for the restructuring of external public debt owed to private creditors, initiated in October 2016, as well as bilaterally, the discussions with six official creditors (Libya, Iraq, Angola, Bulgaria and Poland, as well as Brazil).

[15] Please also see the Information Annex, attached to the Article IV Staff Report.

Figure 1. Mozambique: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2017-37[1]



Sources: Mozambique authorities; and IMF staff estimates and projections.

[1] The most extreme stress test is the test that yields the highest ratio on or before 2027. In figure b. it corresponds to a Combination shock; in c. to an Export shock; in d. to a Combination shock; in e. to an Export shock and in figure f. to a GDP deflator shock.

Table 1. Mozambique: External Debt Sustainability Framework, Baseline Scenario, 2014-2037[1]

(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/	Standard Deviation 6/	Projections									
	2014	2015	2016			2017	2018	2019	2020	2021	2022	2017-2022 Average	2027	2037	2023-2037 Average
External debt (nominal) 1/	**93.6**	**124.9**	**167.3**			**142.8**	**148.5**	**156.8**	**165.9**	**178.8**	**278.3**		**136.8**	**37.6**	
of which: public and publicly guaranteed (PPG)	55.8	76.4	103.7			85.2	95.3	101.3	106.0	110.6	114.3		33.1	28.2	
Change in external debt	10.7	31.3	42.4			-24.5	5.7	8.3	9.1	12.9	99.5		-41.7	-0.6	
Identified net debt-creating flows	4.9	27.4	51.2			0.0	0.7	6.6	9.7	12.5	92.9		-54.5	-37.4	
Non-interest current account deficit	**37.3**	**38.7**	**35.9**	**25.8**	**15.5**	**11.1**	**13.1**	**39.0**	**60.3**	**85.7**	**105.8**		**-33.2**	**-37.0**	-17.7
Deficit in balance of goods and services	45.1	43.7	37.7			16.3	14.3	40.4	61.6	84.9	110.4		-51.4	-54.1	
Exports	27.5	27.9	33.4			38.0	40.0	40.6	38.4	37.8	37.2		82.0	74.4	
Imports	72.6	71.7	71.1			54.3	54.4	81.0	100.1	122.7	147.6		30.6	20.4	
Net current transfers (negative = inflow)	-8.1	-5.4	-2.0	-6.6	1.9	-5.6	-1.3	-1.2	-1.2	-1.1	-1.1		-4.5	0.1	-0.4
of which: official	-6.4	-3.6	-0.7			-2.8	-0.1	-0.1	-0.1	-0.1	-0.1		0.0	0.0	
Other current account flows (negative = net inflow)	0.3	0.4	0.2			0.4	0.0	-0.2	-0.1	1.9	-3.6		22.7	16.9	
Net FDI (negative = inflow)	**-29.1**	**-26.1**	**-27.4**	**-21.6**	**12.9**	**-12.1**	**-12.4**	**-34.5**	**-53.4**	**-75.0**	**-19.8**		**0.6**	**-0.8**	-0.7
Endogenous debt dynamics 2/	**-3.4**	**14.8**	**42.8**			**1.0**	**0.0**	**2.1**	**2.8**	**1.8**	**7.0**		**-21.9**	**0.4**	
Denominator: 1+g+r+gr	1.1	0.9	0.8			1.1	1.1	1.0	1.0	1.0	1.0		1.2	1.0	
Contribution from nominal interest rate	0.9	1.7	3.7			5.4	3.7	5.6	6.4	5.4	10.7		6.4	1.1	
Contribution from real GDP growth	-5.9	-7.0	-6.2			-4.4	-3.7	-3.5	-3.6	-3.6	-3.8		-28.3	-0.7	
Contribution from price and exchange rate changes	1.6	20.2	45.3			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**5.8**	**3.9**	**-8.8**			**-24.5**	**5.0**	**1.7**	**-0.6**	**0.4**	**6.5**		**12.8**	**36.8**	
of which: exceptional financing	0.0	0.0	-1.6			-4.1	-3.3	-3.0	-1.9	-1.7	-0.9		0.0	0.0	
PV of external debt 4/	...	...	143.1			124.6	131.0	138.3	146.5	158.6	256.3		129.5	32.9	
In percent of exports	...	...	428.0			328.3	327.3	340.6	381.4	419.8	689.1		157.9	44.2	
PV of PPG external debt	**...**	**...**	**79.5**			**67.1**	**77.8**	**82.8**	**86.6**	**90.3**	**92.4**		**25.8**	**23.5**	
In percent of exports	**...**	**...**	**237.7**			**176.7**	**194.4**	**204.0**	**225.4**	**239.1**	**248.4**		**31.4**	**31.6**	
In percent of government revenues	**...**	**...**	**330.8**			**265.6**	**341.6**	**356.7**	**370.5**	**384.4**	**382.0**		**114.2**	**112.9**	
Debt service-to-exports ratio (in percent)	**14.7**	**17.8**	**27.2**			**29.3**	**24.1**	**28.4**	**29.9**	**28.2**	**42.0**		**23.4**	**3.6**	
PPG debt service-to-exports ratio (in percent)	**4.0**	**8.3**	**16.65**			**18.2**	**16.6**	**17.6**	**16.9**	**18.1**	**17.9**		**3.6**	**2.6**	
PPG debt service-to-revenue ratio (in percent)	**4.0**	**9.3**	**23.18**			**27.3**	**29.1**	**30.7**	**27.7**	**29.1**	**27.5**		**12.9**	**9.3**	
Total gross financing need (Billions of U.S. dollars)	2.1	2.6	2.0			1.3	1.5	2.4	2.9	3.5	17.3		-8.1	-33.4	
Non-interest current account deficit that stabilizes debt ratio	26.6	7.4	-6.5			35.7	7.3	30.7	51.2	72.8	6.3		8.5	-36.4	
Key macroeconomic assumptions															
Real GDP growth (in percent)	7.4	6.6	3.8	6.7	1.1	3.0	3.0	2.5	2.4	2.3	2.2	2.5	19.2	1.9	10.7
GDP deflator in US dollar terms (change in percent)	-1.9	-17.7	-26.6	-2.4	14.2	9.3	9.7	2.3	2.1	2.0	1.9	4.6	2.0	2.0	2.0
Effective interest rate (percent) 5/	1.1	1.6	2.2	1.7	0.8	3.6	3.0	4.0	4.2	3.4	6.2	4.1	4.3	3.1	5.3
Growth of exports of G&S (US dollar terms, in percent)	-2.7	-10.9	-8.9	4.0	14.4	27.7	19.1	6.4	-1.1	2.6	2.5	9.5	27.6	2.7	19.9
Growth of imports of G&S (US dollar terms, in percent)	-5.8	-13.4	-24.4	12.2	29.9	-14.1	13.1	56.3	29.1	27.9	25.3	22.9	-5.2	2.7	-1.6
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	11.0	3.0	17.9	18.9	17.3	21.0	14.9	17.7	7.4	15.0
Government revenues (excluding grants, in percent of GDP)	27.5	25.0	24.0			25.3	22.8	23.2	23.4	23.5	24.2		22.6	20.9	22.0
Aid flows (in Billions of US dollars) 7/	1.4	1.3	0.7			0.5	0.5	0.8	0.6	0.6	0.6		0.5	0.2	
of which: Grants	0.7	0.4	0.2			0.2	0.2	0.2	0.1	0.1	0.1		0.1	0.0	
of which: Concessional loans	0.7	0.8	0.4			0.3	0.3	0.6	0.5	0.5	0.5		0.4	0.2	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			2.7	1.8	3.2	2.7	2.5	2.6		0.5	0.2	0.6
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			22.5	10.9	25.3	24.2	22.0	25.4		21.6	9.0	18.2
Memorandum items:															
Nominal GDP (Billions of US dollars)	16.9	14.8	11.3			12.7	14.3	15.0	15.7	16.4	17.1		60.1	95.1	
Nominal dollar GDP growth	5.4	-12.3	-23.8			12.5	12.9	4.9	4.5	4.3	4.1	7.2	21.6	3.9	12.9
PV of PPG external debt (in Billions of US dollars)			7.7			9.0	11.0	12.2	13.4	14.5	15.5		15.2	22.0	
(PVt-PVt-1)/GDPt-1 (in percent)						**11.1**	**15.7**	**9.0**	**7.4**	**7.5**	**5.7**	**9.4**	-0.1	0.8	0.6
Gross workers' remittances (Billions of US dollars)	0.0	0.0	0.0			0.2	0.0	0.0	0.0	0.0	0.0		2.5	-0.3	
PV of PPG external debt (in percent of GDP + remittances)	...	...	79.7			66.1	77.9	82.9	86.7	90.4	92.5		24.8	23.6	
PV of PPG external debt (in percent of exports + remittances)	...	...	239.4			170.2	194.9	204.5	225.9	239.7	249.0		29.9	31.8	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	16.8			17.5	16.6	17.6	16.9	18.1	17.9		3.4	2.6	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2. Mozambique: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2017-2037

(In Percent)

	Projections							
	2017	2018	2019	2020	2021	2022	**2027**	2037
PV of debt-to GDP ratio								
Baseline	67	77.8	82.9	87	90.3	92	**26**	24
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	67	86	91	92	89	5	**-75**	606
A2. New public sector loans on less favorable terms in 2017-2037 2	67	80	89	97	105	110	**35**	39
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	67	77.1	82.2	85.7	89.4	91	**25**	23
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	67	86	105	108	112	114	**32**	26
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	67	101	131	137	143	146	**40**	37
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	67	77	103	106	110	112	**32**	26
B5. Combination of B1-B4 using one-half standard deviation shocks	67	94	145	149	154	157	**45**	35
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	67	105	112	117	122	125	**35**	31
PV of debt-to-exports ratio								
Baseline	177	194	204	225	239	248	**31**	32
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	177	216	225	241	236	14	**-91**	814
A2. New public sector loans on less favorable terms in 2017-2037 2	177	199	219	252	277	295	**43**	53
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	177	191	201	222	235	243	**31**	31
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	177	285	406	444	467	483	**62**	55
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	177	191	201	222	235	243	**31**	31
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	177	192	253	276	291	301	**39**	35
B5. Combination of B1-B4 using one-half standard deviation shocks	177	245	376	410	430	444	**57**	50
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	177	191	201	222	235	243	**31**	31
PV of debt-to-revenue ratio								
Baseline	266	342	357	371	384	382	**114**	113
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	266	380	394	395	380	21	**-331**	2904
A2. New public sector loans on less favorable terms in 2017-2037 2	266	349	384	415	446	454	**156**	188
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	266	338	354	367	380	377	**112**	110
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	266	377	450	463	476	470	**142**	125
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	266	442	566	587	608	603	**179**	176
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	266	338	442	455	468	462	**140**	125
B5. Combination of B1-B4 using one-half standard deviation shocks	266	412	623	639	656	648	**198**	169
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	266	463	484	501	520	515	**153**	150

Table 2. Mozambique: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2017-2037 (concluded)

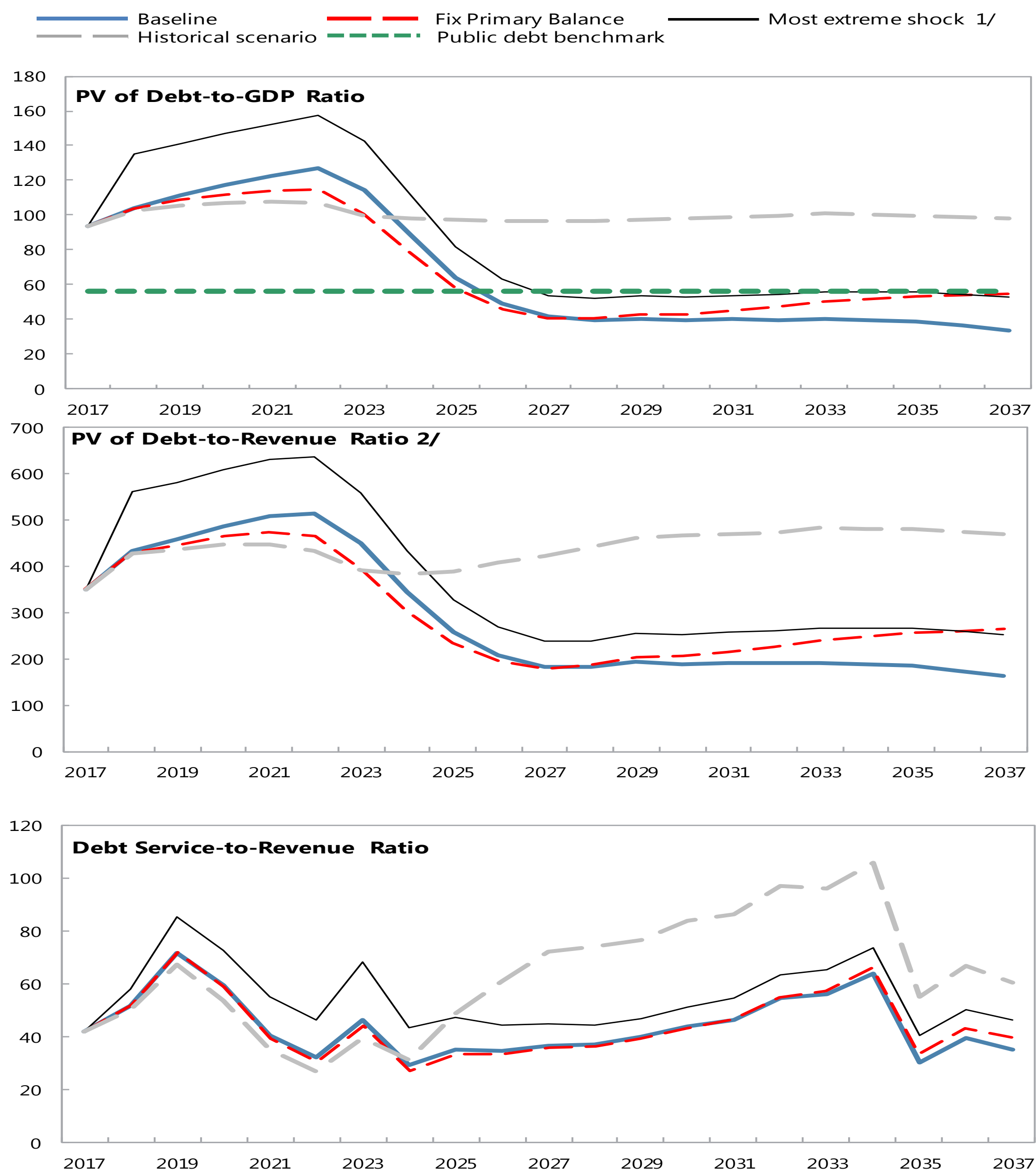
(In percent)

	2017	2018	2019	2020	2021	2022	**2027**	2037
Debt service-to-exports ratio								
Baseline	18	17	18	17	18	18	**4**	3
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	18	18	19	19	20	18	**-1**	44
A2. New public sector loans on less favorable terms in 2017-2037 2	18	17	17	21	22	21	**4**	4
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	18	17	18	17	18	18	**4**	3
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	18	22	29	31	33	33	**7**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	18	17	18	17	18	18	**4**	3
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	18	17	18	19	21	20	**4**	3
B5. Combination of B1-B4 using one-half standard deviation shocks	18	20	24	28	29	29	**6**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	18	17	18	17	18	18	**4**	3
Debt service-to-revenue ratio								
Baseline	27	29	31	28	29.1	28	**13**	9
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	27	32	34	31	31	28	**-3**	158
A2. New public sector loans on less favorable terms in 2017-2037 2	27	29	29	34	36	32	**13**	15
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	27	29	31	28	29	28	**13**	9
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	27	29	32	32	33	32	**16**	12
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	27	38	50	45	47	44	**21**	15
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	27	29	31	32	33	31	**16**	11
B5. Combination of B1-B4 using one-half standard deviation shocks	27	34	40	43	45	43	**22**	16
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	27	40	42	38	40	38	**18**	13
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	7	7	7	7	7	7	**7**	7

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly a an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Figure 2. Mozambique: Indicators of Public Debt Under Alternative Scenarios, 2017-2037[1]



Sources: Mozambique authorities; and IMF staff estimates and projections.

[1] The most extreme stress test is the test that yields the highest ratio on or before 2027.

[2] Revenues are defined inclusive of grants.

Table 3. Mozambique: Public Sector Debt Sustainability Framework, Baseline Scenario, 2014-2037

(In percent of GDP, unless otherwise indicated)

	Actual			Average 5/	Standard Deviation 5/	Estimate	Projections								
	2014	2015	2016			2017	2018	2019	2020	2021	2022	2017-22 Average	2027	2037	2023-37 Average
Public sector debt 1/	62.4	88.1	128.3			112.0	121.8	130.1	136.7	143.0	149.3		48.7	38.7	
of which: foreign-currency denominated	55.8	76.4	103.7			85.2	95.3	101.3	106.0	110.6	114.3		33.1	28.2	
		0.9	0.8			0.8	0.8	0.8	0.8	0.8	0.8				
Change in public sector debt	9.2	25.7	40.2			-16.4	9.9	8.3	6.6	6.3	6.2		-9.2	-2.5	
Identified debt-creating flows	11.1	19.9	32.0			-26.3	1.2	4.4	3.6	3.1	3.4		-9.9	-2.3	
Primary deficit	10.0	6.3	5.0	4.5	2.3	1.7	2.7	4.1	4.3	5.1	5.6	3.9	-0.5	-1.7	0.0
Revenue and grants	31.8	28.1	26.1			26.8	24.1	24.4	24.1	24.1	24.7		22.7	20.9	
of which: grants	4.3	3.0	2.1			1.6	1.3	1.2	0.7	0.6	0.6		0.1	0.0	
Primary (noninterest) expenditure	41.8	34.4	31.2			28.6	26.8	28.5	28.4	29.2	30.3		22.2	19.2	
Automatic debt dynamics	1.1	13.6	26.9			-28.0	-1.5	0.3	-0.7	-2.0	-2.2		-9.4	-0.6	
Contribution from interest rate/growth differential	-3.6	-3.3	-2.5			-3.6	-1.5	0.3	-0.7	-2.0	-2.4		-9.4	-0.6	
of which: contribution from average real interest rate	0.1	0.5	0.7			0.1	1.7	3.3	2.3	1.0	0.7		0.0	0.1	
of which: contribution from real GDP growth	-3.7	-3.9	-3.2			-3.7	-3.2	-3.0	-3.0	-3.0	-3.1		-9.4	-0.8	
Contribution from real exchange rate depreciation	4.7	17.0	29.4			-24.5	0.0	0.0	0.0	0.0	0.2		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-1.9	5.8	8.2			10.0	8.6	3.8	3.0	3.3	2.9		0.7	-0.2	
Other Sustainability Indicators															
PV of public sector debt	...	...	104.1			93.8	104.3	111.6	117.3	122.8	127.3		41.4	34.0	
of which: foreign-currency denominated	...	...	79.5			67.1	77.8	82.8	86.6	90.3	92.4		25.8	23.5	
of which: external	...	...	79.5			67.1	77.8	82.8	86.6	90.3	92.4		25.8	23.5	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	11.7	9.3	11.9			13.0	15.2	21.6	18.6	14.8	13.5		7.7	5.6	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	398.6			349.7	433.3	457.8	487.1	508.8	514.3		182.5	162.7	
PV of public sector debt-to-revenue ratio (in percent)	...	...	433.4			371.5	458.1	480.6	501.9	522.6	526.4		183.4	162.9	
of which: external 3/	...	...	330.8			265.6	341.6	356.7	370.5	384.4	382.0		114.2	112.9	
Debt service-to-revenue and grants ratio (in percent) 4/	5.1	10.5	26.4			42.0	51.7	71.7	59.4	40.5	32.0		36.4	35.1	
Debt service-to-revenue ratio (in percent) 4/	5.9	11.8	28.8			44.6	54.7	75.3	61.2	41.6	32.7		36.6	35.2	
Primary deficit that stabilizes the debt-to-GDP ratio	0.8	-19.4	-35.2			18.1	-7.2	-4.1	-2.3	-1.3	-0.7		8.7	0.8	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	7.4	6.6	3.8	6.7	1.1	3.0	3.0	2.5	2.4	2.3	2.2	2.5	19.2	1.9	10.7
Average nominal interest rate on forex debt (in percent)	1.1	1.4	2.4	1.2	0.7	3.4	3.3	3.4	3.3	3.3	3.2	3.3	2.1	3.0	2.5
Average real interest rate on domestic debt (in percent)	6.7	6.1	-1.0	5.5	3.3	-6.3	3.3	9.3	3.8	-0.9	-2.0	1.2	-0.3	-0.8	-0.2
Real exchange rate depreciation (in percent, + indicates depreciation)	10.8	32.3	39.5	7.6	17.8	-23.9	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	2.6	4.4	12.3	5.8	3.4	13.1	5.9	5.8	5.6	5.6	5.6	6.9	5.5	5.5	5.5
Growth of real primary spending (deflated by GDP deflator, in percent)	34.7	-12.4	-5.9	1.7	12.3	-5.6	-3.5	9.1	1.9	5.2	6.2	2.2	11.2	1.6	7.1
Grant element of new external borrowing (in percent)	...	...	...	...	...	11.0	3.0	17.9	18.9	17.3	21.0	14.9	17.7	7.4	...

Sources: Country authorities; and staff estimates and projections.

1/Gross debt concept is used. Coverage of public sector is general government (central government plus selected SOEs according to the Joint Bank-IMF Guidance Note on LIC DSF for which data was available).

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4. Mozambique: Sensitivity Analysis for Key Indicators of Public Debt, 2017-2037

	Projections							
	2017	2018	2019	2020	2021	2022	2027	2037
PV of Debt-to-GDP Ratio								
Baseline	94	104	112	117	123	127	41	34
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	94	102	106	107	108	107	96	98
A2. Primary balance is unchanged from 2017	94	103	109	112	114	115	41	55
A3. Permanently lower GDP growth 1/	94	105	112	118	124	130	44	44
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	94	101	104	108	112	115	33	16
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	94	108	118	124	129	134	44	36
B3. Combination of B1-B2 using one half standard deviation shocks	94	104	109	113	117	120	34	15
B4. One-time 30 percent real depreciation in 2018	94	135	141	147	152	157	54	53
B5. 10 percent of GDP increase in other debt-creating flows in 2018	94	114	121	127	132	137	45	37
PV of Debt-to-Revenue Ratio 2/								
Baseline	350	433	458	487	509	514	182	163
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	350	426	436	447	448	433	423	469
A2. Primary balance is unchanged from 2017	350	430	445	464	473	465	179	264
A3. Permanently lower GDP growth 1/	350	434	460	492	515	523	194	211
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	350	421	428	450	466	466	147	75
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	350	449	483	513	535	540	192	173
B3. Combination of B1-B2 using one half standard deviation shocks	350	433	448	470	484	484	150	70
B4. One-time 30 percent real depreciation in 2018	350	560	580	610	632	635	237	252
B5. 10 percent of GDP increase in other debt-creating flows in 2018	350	472	496	526	548	552	197	178
Debt Service-to-Revenue Ratio 2/								
Baseline	42	52	72	59	40	32	36	35
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	42	50	67	54	35	27	72	60
A2. Primary balance is unchanged from 2017	42	52	72	59	39	30	36	40
A3. Permanently lower GDP growth 1/	42	52	72	60	41	32	37	39
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2018-2019	42	51	68	56	38	30	33	28
B2. Primary balance is at historical average minus one standard deviations in 2018-2019	42	52	72	61	42	33	37	36
B3. Combination of B1-B2 using one half standard deviation shocks	42	50	68	57	39	30	34	28
B4. One-time 30 percent real depreciation in 2018	42	58	85	72	55	46	45	46
B5. 10 percent of GDP increase in other debt-creating flows in 2018	42	52	74	61	42	34	38	37

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Statement by Mr. Mkwezalamba, Executive Director for Mozambique and Mr. Tivane, Senior Advisor to Executive Director February 27, 2018

1. Introduction

On behalf of our Mozambican authorities, we thank staff for their continued engagement and policy advice as well as the candid policy discussions during the 2017 Article IV Consultation. Despite the challenging macroeconomic environment, the authorities continue to make headway in addressing the multiple shocks the country experienced over the past two years, notably the fall in commodity prices, weather-related shocks, and security concerns predominantly in the central and northern regions of the country. In addition, the steady rise in debt levels resulted in mounting fiscal pressures, weakening in business confidence, and the freezing of budget support by development partners. In this regard, they are intensifying efforts aimed at addressing the macroeconomic imbalances, while invigorating implementation of far-reaching structural reforms to lift potential growth, curbing the incidence of poverty and inequality, and strengthening institutions. They broadly agree with staff that renewed policy efforts are essential to sustain the reform momentum, as well as gather the required support from a wide spectrum of domestic stakeholders, International Financial Institutions (IFIs), and development partners.

2. Recent Economic Developments and Outlook

Economic activity slowed down from a historical average of 7.5 percent to 3.8 percent in 2016, on the back of disruptions to agricultural production caused by floods, subdued commodity prices, bottlenecks in transport and logistics primarily for exportation of coal, and the shortage of foreign exchange to finance critical imports. According to the latest estimates from the National Institute of Statistics, real GDP in 2017 grew by 3.7 percent, broadly in line with the authorities' projections set at 3.8 percent. This performance was driven by improved commodity prices, an uptick in production and exports of coal, a rebound in agriculture activity stemming from a benign rainfall season, and better transportation logistics owing to the cessation of military hostilities across the country. Although staff's growth projections for 2017 and 2018 are set at 3.0 percent, the authorities expect the growth momentum witnessed in 2017 to be maintained in 2018. This is on account of a moderate recovery in the mining, agriculture, and transport sectors; and enhanced business confidence occasioned by declining inflation expectations as well as a rebalanced foreign exchange market.

Inflation declined significantly from 19.2 percent in December 2016 to 15.11 percent in December 2017, reflecting subdued aggregate demand, stable exchange rate, and a tight monetary policy stance. As a result, the average inflation for 2018 is estimated to decline to a single-digit space of 7.7 percent.

The current account deficit is estimated to narrow to 16.1 percent of GDP in 2017, from 39.2 percent of GDP in 2016, owing to a rebound in international commodity prices,

particularly for aluminum and coal. Consequently, the reserve position improved at end-December 2017 to 6 months of non-mega project imports, against an import cover of 4.7 months at end-December 2016. For 2018, the reserve position is expected to remain stable, equivalent to nearly 6 months of import cover.

3. Policy Priorities and Reforms

To tackle the prevailing macroeconomic challenges, the authorities are making determined efforts geared at implementing macro-critical structural reforms to improve the fiscal position, gradually address the bottlenecks to broad-based growth, and upgrade institutions. Concerted policy efforts have been made to improve the macroeconomic conditions, accelerate dialogue with the opposition parties to achieve long-lasting peace, and create an adequate set of institutions to lift the primacy of the rule of law and strengthen democracy in Mozambique.

Fiscal Policy

The authorities are committed to foster fiscal consolidation, through implementation of reforms aimed at improving domestic revenue mobilization, enhancing public financial management, and stepping-up efforts toward achieving timely debt restructuring. They, therefore, broadly agree with staff that steadfast policy actions aimed at accelerating the pace of fiscal consolidation remain critical to ease the fiscal pressures over the short and medium term. In this regard, on the back of limited fiscal space for financing development expenditures and servicing debt, the authorities' 2018 budget approved by the National Assembly in December 2017 seeks to continue efforts to consolidate public finances. The fiscal revenue is projected at 22.5 percent of GDP in 2018, from 23 percent of GDP in 2017, whilst total expenditures and net lending is targeted at 28.1 percent of GDP in 2018, down from an estimate of 31.7 percent of GDP in 2017. In addition, they have undertaken a set of deficit-reducing measures over the past few months, including: (i) phasing out of fuel and wheat subsidies; (ii) adopting an automatic fuel price adjustment formular; and (iii) reducing bonuses, relocation subsidies, and housing allowances. These measures are expected to reduce the wage bill and goods and services by about 0.8 percent of GDP in 2018.

The authorities are also mindful that efforts to ease the fiscal pressures and put debt dynamics on a sustainable path would require sustained efforts to improve fiscal transparency, governance, and accountability. To this end, they have recently undertaken a set of measures, including the following:

i. Strengthening the Debt Management Unit and creating a Fiscal Risk Management Unit in the Ministry of Economy and Finance in the second half of 2016, with IMF and World Bank support. The unit is already staffed and fully functional;

ii. Completion of the Kroll Audit Report and submission of its recommendations to the Attorney General's Office (AGO) in July 2017. The AGO submitted to the Office of Public Prosecutor in January this year matters that warrant further legal action, and

continues with investigations on issues that are under its purview to help address queries on how the proceeds from the undisclosed loans were used;

iii. A Cabinet Decree to regulate the issuance and management of public debt and guarantees was issued in November 2017. The decree requires, among others, that all central government borrowing and contingent liabilities be contracted by the Minister of Economy and Finance on behalf of the central government. The decree also calls for disclosure of loans and guarantees approved, including feasibility studies and assessment of fiscal risks; and regular update of public sector debt records reconciled with creditors on a quarterly basis; and

iv. Completion in December 2017 of the strategy aimed at validating and gradually clearing arrears to suppliers, through securitization. In addition, the authorities are pursuing measures to prevent accumulation of arrears in line with staff's recommendations, including: (i) streamlining the network of expenditures units, (ii) enforcing budget ceilings through measures aimed at increasing regular audits to the budget execution by line ministries; and (iii) strengthening government liquidity management.

To strengthen the implementation of the Government Action Plan which seeks to improve fiscal transparency, governance, and accountability, the authorities intend to undertake the following measures in 2018:

v. Submit to the National Assembly a draft law on Fiscal Responsibility by end-2018;

vi. Approve regulations aimed at implementing the new Public Enterprises Act by end-June 2018;

vii. Submit to the National Assembly a draft law for Public Investment Management by end-2018;

viii. Stepping up efforts aimed at accelerating debt restructuring, while considering the country's financing needs to advance its development agenda. The Ministry of Economy and Finance is scheduled to make a presentation to Mozambique's commercial creditors on Tuesday, March 20, 2018 in London to provide an update on the recent economic developments and present the key elements of the proposed debt restructuring; and

ix. Implementing fiscal structural reforms to improve domestic revenue mobilization, particularly through implementation of measures to widen the tax base, reduce tax exemptions, and improve revenue administration. Further, the authorities have started discussions to establish a sovereign wealth fund to help the country manage the substantial inflow of revenues accruing from the LNG exploration over the medium term.

Monetary, Exchange Rate, and Financial Sector Policies

Monetary and exchange rate policies in the short and medium terms remain geared towards achieving price stability and smoothening exchange rate volatility. Accordingly, the *Banco de Moçambique* (BM) has significantly tightened the monetary policy stance to anchor the heightened inflation pressures coupled with widened external imbalances that crippled the economy since the second quarter of 2016. In this connection, the BM raised its policy rate by 600 basis points (bp) to 23.25 percent in October 2016.

Following a steep decline in inflation expectations coupled with a gradual rebalancing of the foreign exchange market, the BM initiated a cycle of monetary easing in December 2017, and cut its policy rate by 150 bp to 19.5 percent. The Monetary Policy Committee (MPC), at its recent meeting held on Monday, February 26, 2018, further cut the policy rate by 150 bp to 18 percent with the aim of increasing the supply of domestic credit, to stimulate private consumption and investment. The BM is firmly committed to relying on the use of the exchange rate as a shock absorber, and rebuild reserve buffers.

The BM will also continue with efforts aimed at ensuring that monetary policy normalization remains consistent with a faster path of fiscal adjustment needed to achieve debt sustainability. Likewise, to enhance the BM independence and strengthen the legal framework for the conduct of monetary policy, the authorities are currently undertaking reviews of the Central Bank Act, Foreign Exchange Act, and the Credit Institutions Act. To strengthen financial sector resilience, while addressing the risks arising from the increased NPLs as well as the high exposure of the banking sector to sovereign securities and state-owned enterprises (SOEs), the BM will continue to upgrade its institutional capacity for enhanced oversight and enforcement of macro-prudential regulations

Structural Reforms

The authorities attach great importance on the need to calibrate structural priorities to accelerate economic transformation and diversification, reduce the incidence of poverty and inequality, and improve policy institutions. They recognize that the massive production and exportation of natural gas expected from 2023 onwards, while presenting an opportunity to boost growth and accelerate socio-economic development, comes with its own challenges, including the risk of Dutch disease in the absence of adequate institutions to help the country manage revenues from natural resources. In this regard, they intend to implement measures aimed at gradually easing bottlenecks to economic competitiveness, while creating an appropriate set of incentives to improve the business environment, to unlock the country's growth potential and spur job creation. The measures include: (i) easing registration and licensing of economic activities; (ii) expediting the issuance of permits for small businesses; (iii) strengthening the legal framework for enforcement of contracts; (iv) increasing access to electricity, predominantly in rural areas; (v) upgrading the movable collateral registry; and (vi) improving credit access by SMEs.

Further, they will advance efforts to bridge the infrastructure financing gap with a view to foster broad-based growth, accelerate the implementation of the Financial Deepening and Inclusion Strategy (2016–22), and revamp the implementation of the Strategy for Fighting Corruption. Similarly, steps intended to improve the data gaps in fiscal reporting and national

accounts, alongside the steadfast implementation of the AML/CFT framework will continue to be given primacy going forward.

4. Conclusion

The Mozambican authorities are committed to advance their reform and development agenda to achieve sound macroeconomic fundamentals, layout the foundations for accelerated growth, and upgrade institutions. In this regard, they consider the Fund's continued engagement and policy advice essential in supporting their efforts.