



# REPUBLIC OF MOZAMBIQUE

January 2016

## STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION, FIFTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT, REQUEST FOR MODIFICATION OF ASSESSMENT CRITERIA, AND REQUEST FOR AN 18-MONTH ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE REPUBLIC OF MOZAMBIQUE

In the context of the Staff Report for the 2015 Article IV Consultation, fifth review under the Policy Support Instrument, request for modification of assessment criteria, and request for an 18-month arrangement under the Standby Credit Facility, 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 December 18, 2015 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 December 18, 2015, following discussions that ended on October 28, 2015, 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 December 3, 2015.
- 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 Statement** 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:

Letter of Intent sent to the IMF by the authorities of the Republic of Mozambique\*  
Memorandum of Economic and Financial Policies by the authorities of the Republic of Mozambique\*  
Technical Memorandum of Understanding\*  
Selected Issues

\*Also included in Staff Report

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.

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**Washington, D.C.**



Press Release No. 15/580  
FOR IMMEDIATE RELEASE  
December 18, 2015

International Monetary Fund  
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Washington, D. C. 20431 USA

### **IMF Executive Board Completes Fifth PSI Review, Approves US\$282.9 Million Credit Facility and Concludes 2015 Article IV Consultation with Mozambique**

On December 18, 2015, the Executive Board of the International Monetary Fund (IMF) completed the fifth review of Mozambique's economic performance under the program supported by the Policy Support Instrument (PSI)<sup>1</sup>.

In completing the review, the Executive Board approved the authorities request for waiver and modification of three assessment criteria for December 2015 to account for the changed environment and revised microeconomic projections.

The Board also approved Mozambique's request for an SDR 204.5 million, (about US\$282.9 million) Standby Credit Facility to supplement the PSI to augment reserves and maintain macroeconomic stability, with a first SDR 85.2 million disbursement (about US\$117.9 million) available immediately. The SCF aims to alleviate the external balance of payments shocks, and through strengthening macroeconomic stability, to achieve the government's goals on poverty reduction and inclusive growth.

The Executive Board approved the PSI for Mozambique on June 24, 2013 (see [Press Release No. 13/231](#)).

Following the Executive Board's discussion, Mr. Min Zhu, Deputy Managing Director and Acting Chair, issued the following statement:

"Despite challenges, Mozambique's economic growth continues to be robust and inflation remains low. However, lower commodity prices and a decline in foreign exchange inflows have generated a temporary balance of payments gap. The authorities have taken strong policy measures to preserve

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<sup>1</sup> The PSI is an instrument of the IMF designed for countries that do not need balance of payments financial support. The PSI helps countries design effective economic programs that, once approved by the IMF's Executive Board, signal to donors, multilateral development banks, and markets the Fund's endorsement of a member's policies (see <http://www.imf.org/external/np/exr/facts/psi.htm>). Details on Mozambique's PSI program are available at <http://www.imf.org/mozambique>.

macroeconomic stability. Continued implementation of prudent policies under the standby credit facility will be essential to ensure debt sustainability, safeguard against external shocks, as well as promote strong and inclusive growth.

“The authorities’ front-loaded corrective measures, including a tightening of the 2016 budget deficit and of the monetary policy stance in 2015, as well as a reform of the foreign exchange market should help to stabilize the economy. Rigorous implementation of the budget, enhanced VAT management, close monitoring of fiscal risks, and allowing for continued exchange rate flexibility will be key to restoring macroeconomic stability. The central bank should stand ready to further tighten liquidity conditions as needed. Work on an action plan to improve the profitability of the EMATUM fishing company should be fast tracked to reduce its risk to the government budget.

“Significant progress has been made on structural reforms. To make Mozambique’s strong growth performance more inclusive and broad based, the reform agenda needs to focus on enhancing public financial management, including budget controls and fiscal transparency, and developing the institutional framework and building capacity to prepare for the management of natural resource wealth. Priority should also be given to reforming the energy sector, improving access to financial services, and strengthening the business environment. A vigorous debt management strategy will be crucial to address the challenges of significant infrastructure gaps at a time when debt vulnerabilities have been rising.”

The Executive Board also completed the 2015 Article IV Consultation with Mozambique.

Despite lower commodity prices and a weaker global environment, Mozambique’s economic prospects remain positive given planned massive investment in natural resources. While GDP growth averaged 7 percent over the last five years, Mozambique’s per-capita income (\$624 in 2014) and human development index (178 out of 187 countries) remain low. There is a need to continue implementing policies that support fiscal sustainability, infrastructure investment, and inclusive growth.

Mozambique’s economic outlook remains robust. Growth of 6.3 percent is expected in 2015, and remains below potential at 6.5 percent in 2016, mainly due to a stagnant mining sector and substantially tighter fiscal and monetary policies. Over the medium term, growth is projected to recover to 7.5–8 percent, supported by massive investment in natural gas projects and higher coal production if key agreements can be reached for coal and gas sector development. Inflation is expected to increase towards the BM’s medium target of 5–6 percent, due to the recent depreciation of the metical and adjustments in administered prices.

Balance of payments pressures are increasing and the exchange rate has depreciated substantially. While the overall current account is improving due to a decline in import-intensive megaproject investments (given the end of the gas exploration phase), the non-megaproject current account has continued to worsen, intensifying pressures in the foreign exchange market. Foreign exchange

market pressures, first experienced in late 2014 and early 2015, subsided during April–July but have since re-emerged. The non-megaproject current account deficit largely drives these pressures in the domestic foreign exchange market. During July 2014–June 2015, this deficit worsened by \$1.7 billion compared to the previous 12 months. This deterioration was caused by lower commodity prices and declining FDI and external aid, while imports remained dynamic owing to strong domestic demand fueled by expansionary fiscal and monetary policies. The depreciation of the metical has so far not had a noticeable impact on import demand.

The fiscal consolidation agreed under the PSI program has been implemented by the new administration. Following election-related fiscal slippages in 2014, the 2015 budget started to place public finances on a more sustainable path through a reduction of about 1.5 percent of GDP (excluding one-off factors in 2014) in public spending. The main objective of fiscal policy in 2016 is to ensure debt sustainability and contribute to the required external adjustment.

### **Executive Board Assessment<sup>2</sup>**

Executive Directors noted that while Mozambique’s economic growth remains robust, lower commodity prices and a decline in foreign direct investment and donor support have adversely affected the economy and generated a temporary balance of payments gap. Directors commended the actions taken by the authorities to maintain macroeconomic stability and agreed that continued strong commitment to prudent policies and deeper structural reforms under the Fund-supported program is essential to reduce vulnerabilities and foster sustainable and inclusive growth.

Directors supported the tighter monetary policy stance and encouraged the authorities to take further action, as needed, to curb inflationary pressures and improve the foreign exchange market. Continued exchange rate flexibility would help safeguard foreign reserves and absorb the impact of external shocks. Directors supported the efforts to strengthen the financial sector and encouraged the authorities to fully implement their Financial Sector Development Strategy so as to improve access to small and medium-sized enterprises.

Directors commended the authorities for substantially scaling back external borrowing in light of rising risks of debt distress. Going forward, they called for rigorous budget implementation by strengthening the management of VAT, reducing wage bill growth, and closely monitoring fiscal risks, especially those arising from government guarantees and public enterprises. Directors highlighted the urgent need to develop an action plan to improve the profitability of the EMATUM fishing company.

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<sup>2</sup> 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 commended the progress on structural reforms, including on the mining and hydrocarbon legislation which should facilitate further investments in the large natural gas projects. They encouraged a renewed focus on enhancing budget controls and fiscal transparency and developing the institutional framework and building capacity to prepare for the management of natural resource wealth. Directors welcomed the recent adjustments in electricity tariffs and advised the authorities to accelerate fuel subsidy reforms, while protecting the most vulnerable segments of the population.

Directors emphasized that fostering financial inclusion and improving the business environment would help make Mozambique's strong growth more inclusive and broad-based. They called for greater emphasis on the effective use of public resources, transparent investment project analysis and prioritization, and vigorous debt management strategy, given the significant infrastructure gaps and rising debt vulnerabilities.



# REPUBLIC OF MOZAMBIQUE

## STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION, FIFTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT, REQUEST FOR MODIFICATION OF ASSESSMENT CRITERIA, AND REQUEST FOR AN 18-MONTH ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY

December 3, 2015

### KEY ISSUES

**Context and short-term policy challenges.** Despite some deceleration, growth is still robust (in the 6-7 percent range in 2015-16) and inflation remains low. However, the economy has been increasingly affected by lower commodity prices and a decline in foreign exchange inflows. As a result, a balance of payments gap has emerged and the exchange rate has depreciated substantially. While policy commitments undertaken at the time of the 4<sup>th</sup> review were followed, performance under the PSI has been less than satisfactory, NIR declined significantly as a result of external shocks and three quantitative assessment criteria missed at end-June 2015. The monetary policy stance was tightened with delays despite the loss in NIR and proved to be too accommodating. Greater progress has been achieved on structural reforms, despite some implementation delays. Against this backdrop, the authorities requested an arrangement under the standby credit facility (SCF) supported by a strong policy package of corrective measures that includes further fiscal adjustment, continued exchange rate flexibility, and tight liquidity management. These measures are essential in the short term to preserve macroeconomic stability, improve the international reserve position, and continue to attract foreign investment (including in the oil and gas sectors) to support growth. Key structural reform priorities include improving VAT administration, strengthening capacity for transparent public investment management, and deepening financial sector reforms.

**Medium-term reforms.** Maintaining fiscal discipline will be essential to preserve debt sustainability. This will require measures to contain current spending pressures and greater rigor and transparency in the analysis and selection of public investment projects. Structural reforms focusing on public financial management, managing natural resources, modernization of the framework for monetary policy, and further improving the business environment should be implemented vigorously to sustain growth and render it more inclusive.

**Staff supports completion of the review and the request for the SCF arrangement (180 percent of quota or approximately \$285 million, with a first disbursement of 75 percent of quota or about \$120 million).** While quantitative performance was less than satisfactory, the implementation of the structural reform agenda is adequate given

existing capacity constraints. The new government has also demonstrated strong commitment to policy adjustment, including through fiscal consolidation in the 2016 budget, adjustments in monetary policy instruments in late 2015, and new commitments to further structural reforms.



Approved By  
**David Owen and Steve Barnett**

A staff team comprising Mr. Lazare (mission chief), Messrs. Inui, Medina, Xiao (all AFR), and Henn (SPR) visited Maputo during October 14-28, 2015. The mission met with Ministers Maleiane (Economy and Finance), Couto (Natural Resources and Energy), Bank of Mozambique Governor Gove and other senior government officials. The mission also met with the World Bank, development partners and representatives of civil society, and the private sector. It was assisted by Mr. Segura-Ubiergo (resident representative), Ms. Palacio and Messrs. Simione and Sousa (resident representative office).

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## CONTEXT

### 1. Despite lower commodity prices and a weaker global environment, Mozambique's economic prospects remain positive given planned massive investment in natural resources.

While GDP growth averaged 7 percent over the last five years, Mozambique's per-capita income (\$624 in 2014) and human development index (178 out of 187 countries) remain low. There is a need to continue implementing policies that support fiscal sustainability, infrastructure investment, and inclusive growth. Over the medium term, efforts to develop a sound framework to manage natural resource wealth should be stepped up.

**2. Political tension remains a risk factor.** Failure to find a permanent solution to the growing tension between the ruling Frelimo party and the main opposition party (Renamo), which is calling for greater political decentralization, could negatively affect the business environment. While the risk of a return to an outright civil war is low, the government's attempt to disarm Renamo has resulted in violent clashes with the police. Peaceful negotiations are essential to preserve macroeconomic stability and investor confidence at a time when Mozambique is facing new economic challenges.

**3. Following policy slippages in 2014, the economy has been significantly affected by lower commodity prices and a decline in foreign exchange inflows.** This has resulted in slower export growth, lower net international reserves (NIR), and a marked depreciation of the metical vis-à-vis the dollar. While the authorities tightened the fiscal stance and monetary policy following the 4<sup>th</sup> review under the PSI, renewed market pressures since the summer have led to a further depreciation of the metical (see para 7) and lower NIR. As a result, the authorities have requested a standby credit facility (SCF) to supplement the PSI to address the present balance of payments (BOP) need and shore up reserves, which will also provide a strong signal to markets of their intent to stabilize the economic and financial situation.

| Millennium Development Goals                                  |      |      |      |                   | SSA              |
|---|------|------|------|-------------------|------------------|
|   | 1995 | 2005 | 2010 | 2014 <sup>2</sup> | 2015 Est.        |
| Population (millions)   | 16   | 21   | 24   | 27                | 918 <sup>3</sup> |
| National household survey poverty incidence <sup>1</sup>      | 68   | 56   | 52   | ...               | ...              |
| <i>Of which</i> : rural                                       | ...  | 55   | 57   | ...               | ...              |
| <i>Of which</i> : urban                                       | ...  | 52   | 50   | ...               | ...              |
| GDP per capita (constant 2005 US\$)                           | 189  | 311  | 371  | 439               | ...              |
| Primary school enrollment ratio (percent of net)              | 44   | 75   | 89   | 87                | 80               |
| Ratio: girls to boys in primary/secondary education (percent) | 75   | 84   | 89   | 91                | ...              |
| Under 5 mortality rate (per 1000)                             | 215  | 134  | 103  | 81                | 86               |
| Prevalence of HIV, total (percent of population aged 15-49)   | 5    | 11   | 11   | 11                | ...              |
| Access to improved water sources (percent of population)      | 37   | 45   | 49   | 51                | 68               |

Source: World Bank, World Development Indicators.

<sup>1</sup> Revised: national 1996/97 based basket National Poverty Line with 13 location price deflators and 2002/03 and 2008/09 data partially re-estimated. (source: World Bank, *Poverty in Mozambique: New Evidence from Recent Household Surveys, October 2012*)

<sup>2</sup> Data in italics refer to 2013.

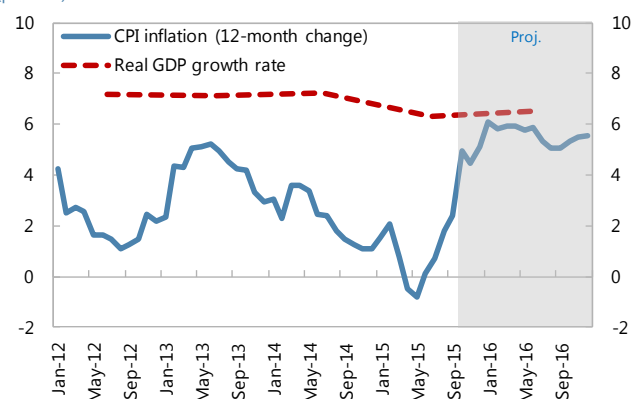
<sup>3</sup> WEO, *World Economic Outlook*, October 2015.

## RECENT ECONOMIC DEVELOPMENTS AND PROGRAM PERFORMANCE

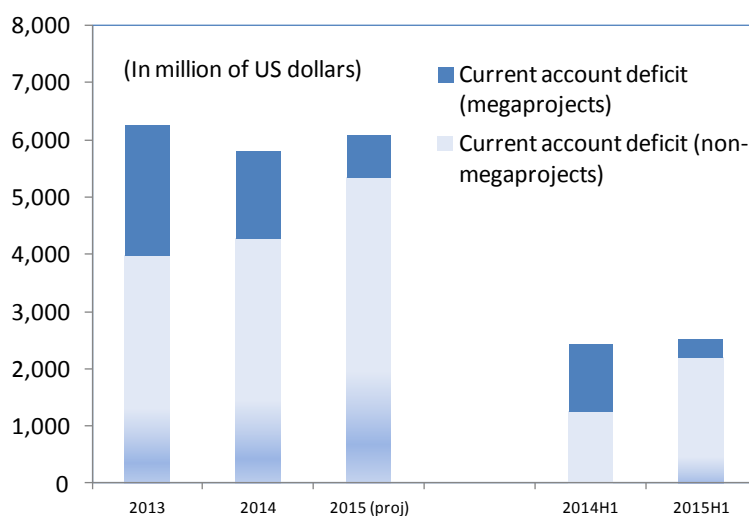
### 4. Robust growth and low inflation continued in 2015, though at a somewhat lower pace than historical averages.

Growth decelerated to 6.3 percent in the first half of the year, owing to floods in early 2015, a slowdown in the mining sector, reflecting lower international commodity prices, and the delay in the approval of the 2015 budget. Despite the sizable depreciation of the metical against the US dollar, 12-month inflation stood at 2.4 percent in September because of a more moderate depreciation against the South African rand, low food prices, and stable administered prices (fuels, public transportation, and utilities). The depreciation and increases in administered prices (bread and electricity) in October–November are likely to push end-2015 inflation to around 5 percent.

Mozambique: GDP growth and CPI inflation projections (percent)



**5. The new administration has been implementing the fiscal consolidation agreed under the PSI program.** Following election-related fiscal slippages in 2014, the 2015 budget started to place public finances on a more sustainable path through a reduction of about 1½ percent of GDP (excluding one-off factors in 2014) in public spending. For the first nine months of the year, spending was broadly in line with program targets while revenues underperformed by a small margin. However, in June, the government made a lump sum payment of about \$100 million (0.6 percent of GDP) to fuel distributors to compensate them for past losses generated by regulated fuel prices, which reflected under-budgeting for fuel subsidies. In addition, delays in donor flows, and the fact that the bulk of government securities received by companies as reimbursements for outstanding VAT credits (MT 8.2 billion) was discounted, pushed net credit to government (NCG) above target at end-June and September. Nonetheless, the government expressed a commitment to restrain spending in the last quarter to ensure that the program fiscal targets and NCG ceilings are met. This should be feasible if donor flows for the rest of the year proceed as planned.



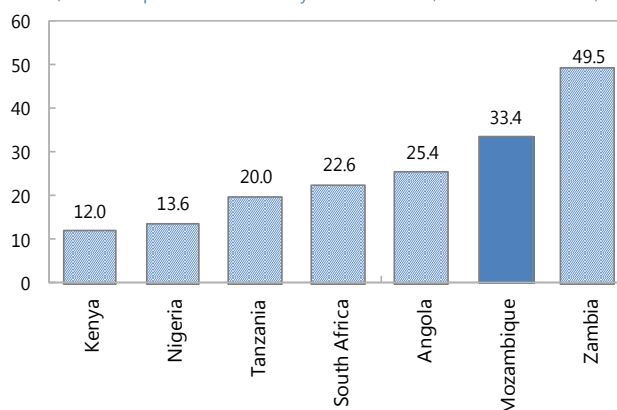
**6. While the overall current account is improving due to a decline in import-intensive megaproject investments (given the end of the gas exploration phase), the non-megaproject current account has continued to worsen, intensifying pressures in the foreign exchange market.**

Foreign exchange market pressures, first experienced in late 2014 and early 2015, subsided during April-July but have since re-emerged. The non-megaproject current account deficit largely drives these pressures in the domestic foreign exchange market.<sup>1</sup>

During July 2014-June 2015, this deficit worsened by \$1.7 billion compared to the previous 12 months. This

deterioration was caused by lower commodity prices and declining FDI and external aid, while imports remained dynamic owing to strong domestic demand fueled by expansionary fiscal and monetary policies. The depreciation of the metical has so far not had a noticeable impact on import demand.

**Nominal depreciation of selected currencies versus the US dollar**  
(Percent ; US dollar per national currency - November 14, 2014- November 16, 2015)



**7. The net international reserves (NIR) of the Bank of Mozambique (BM) continued to decline.** In an attempt to stabilize the foreign exchange market, the BM intervened heavily during late 2014 to early 2015, resulting in a \$700 million decline in NIR. The BM has virtually stopped discretionary intervention since April and allowed the exchange rate to adjust (with a 33 percent year-on-year depreciation against the US dollar by mid-November 2015, the second largest depreciation in sub-Saharan African countries during the same period), but its longstanding commitment to supply US dollars to cover fuel imports<sup>2</sup> and the government's payment of EMATUM debt service falling due in September drove NIR down to \$2.1 billion by end-October.<sup>3</sup> The BM kept reserve money growth in line with commitments in the 4th PSI review, resulting in a gradual deceleration of credit growth, to 23 percent in September compared to 28 percent in end-2014.

<sup>1</sup> Capital flows associated with megaprojects are often used to finance imports. Megaprojects are often exempt from FX legislation and are also allowed in some cases to keep a large share of their dollar earnings offshore.

<sup>2</sup> This is a commitment made by the BM at the time of the 2008-09 global crisis to inject confidence in the thin foreign exchange market.

<sup>3</sup> The government guaranteed the \$850 million bond issued in 2013 by the state-owned enterprise EMATUM. This borrowing financed the purchase of tuna fishing boats and maritime security equipment. Subsequently, \$500 million out of the total \$850 million was incorporated into the budget and became public debt under the responsibility of the treasury. The remaining amount (\$350 million) remains on EMATUM's balance sheet.

**8. Performance under the PSI through September 2015 was less than satisfactory.** The assessment criteria (AC)/indicative targets on NCG, NIR, external arrears, and government revenues for June and September were missed (see above), while those on reserve money, nonconcessional borrowing, and the stock of short-term external public debt were met. The structural reform agenda is being implemented broadly as scheduled: of the ten structural benchmarks falling due before January 2016, 3 have been met, 3 have been completed with slight delays, 2 are expected to be met in time, and the other 2 are experiencing some delays (see paragraph 42).

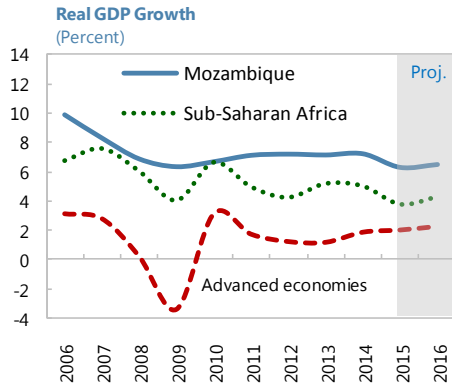
### Program Performance

|  | June 2015 Sep 2015 |     |
|--|--------------------|-----|
|  | AC                 | IT  |
| Assessment Criteria                      |                    |     |
| Net credit to the government             | ▲                  | ▲   |
| Stock of reserve money                   | ●                  | ●   |
| Stock of net international reserves      | ▲                  | ▲   |
| Nonconcessional external debt            | ●                  | ●   |
| Stock of short-term external public debt | ●                  | ●   |
| External payments arrears                | ▲                  | ▲   |
| Indicative Targets                       |                    |     |
| Government revenue                       | ▲                  | ▲   |
| Priority spending                        | ...                | ... |

● met    ▲ not met

**Figure 1. Mozambique: Impact of Global Developments**

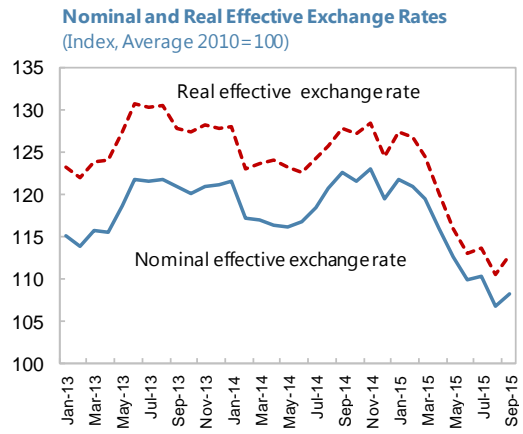
Mozambique's growth outlook remains robust, outperforming other SSA countries.



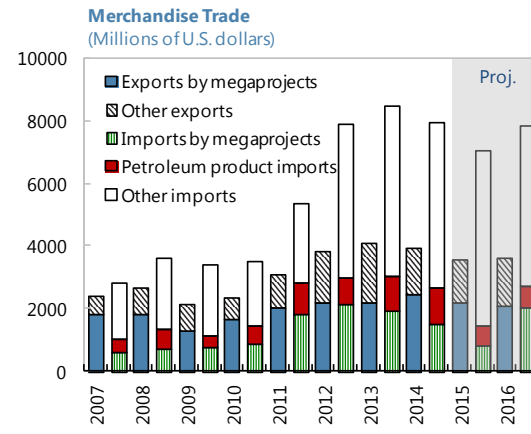
Terms of trade gains reversed since 2011 due to weakening international commodity prices...



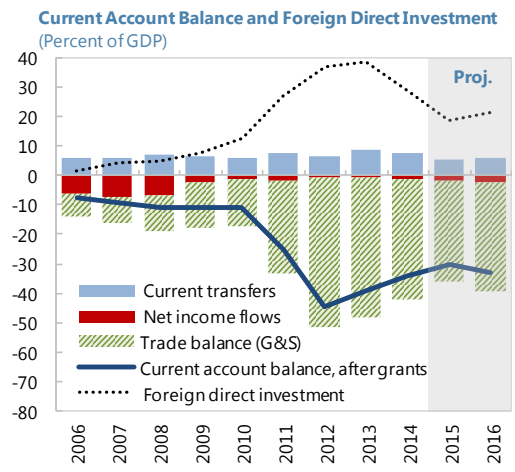
...while the metical has sharply depreciated since the beginning of 2015.



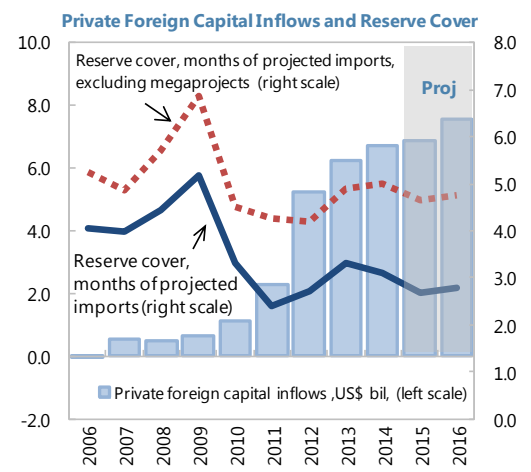
While overall trade deficit has narrowed, the non-megaproject trade deficit has increased due to lower export prices and sizeable fuel imports.



The current account deficit remains large, but continues to reflect sizeable investment imports by the natural resource sector since 2011-12.



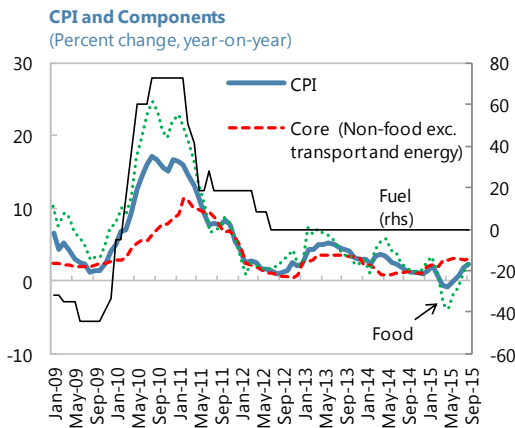
The overall reserve cover declined markedly in 2014, but a large fall in megaproject imports kept reserve coverage (excl. megaprojects) at a still reasonable level.



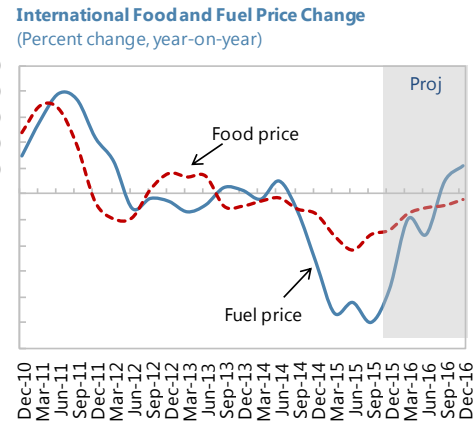
Sources: Mozambican authorities and IMF staff estimates and projections.

**Figure 2. Mozambique: Inflation and Monetary Developments**

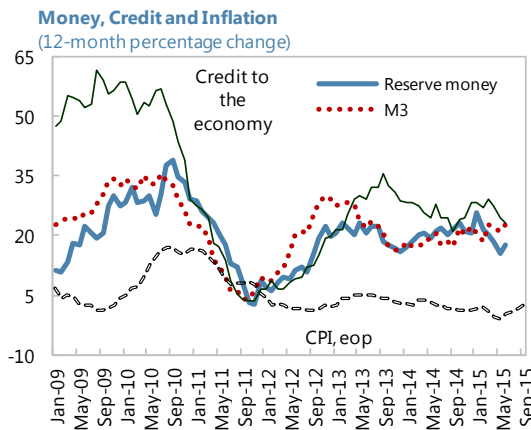
*Inflation has remained well-contained since 2012...*



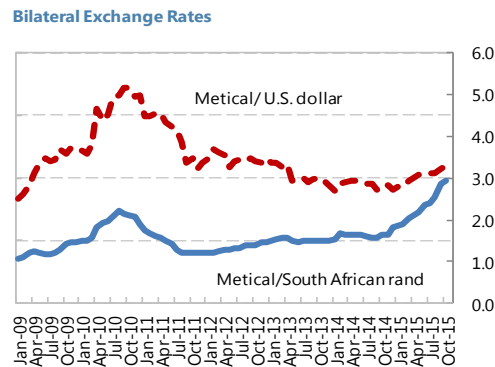
*supported by favorable developments in international food prices.*



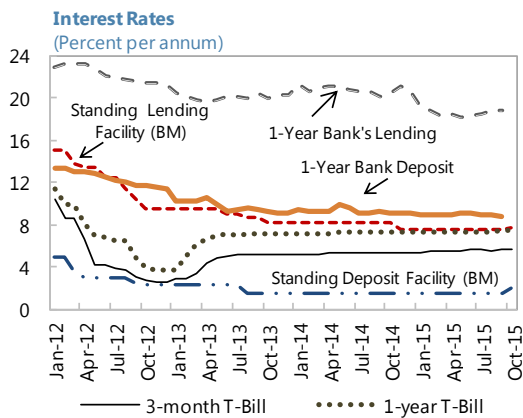
*Strong private sector credit growth signals financial deepening, but loose money growth since 2012 may have aggravated import demand and inflation.*



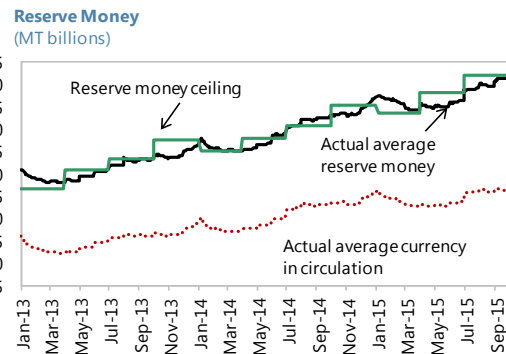
*The Mt/\$ exchange rate started to depreciate in 2014Q4, while the rate against the rand remained stable.*



*The Central Bank's policy rates and the T-bill rates had been stable before the BM raised policy rates in October.*



*The BM's liquidity management kept reserve money below its program target in September 2015.*



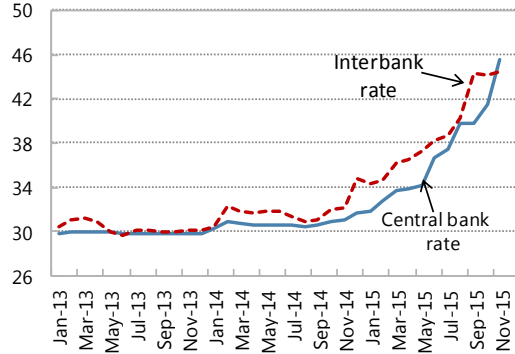
Sources: Mozambican authorities and IMF staff estimates and projections.



**Figure 3. Mozambique: Selected External Sector Developments**

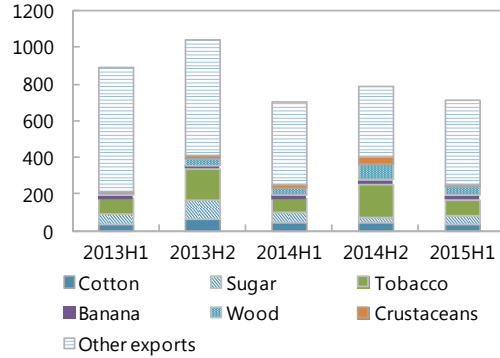
Significant exchange rate pressure emerged in the foreign exchange market in 2014Q4 ...

**Nominal Exchange Rate**  
(Metical/U.S. dollar)



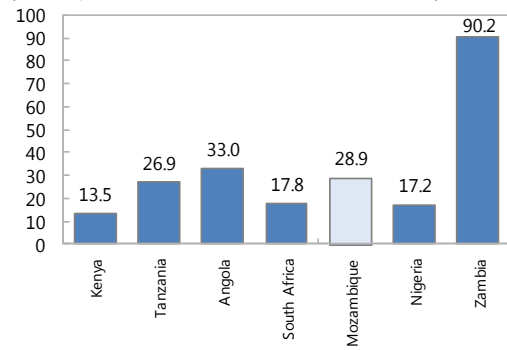
... partly due to a substantial fall in traditional exports,...

**Selected Traditional Exports**  
(Millions of U.S. dollars)



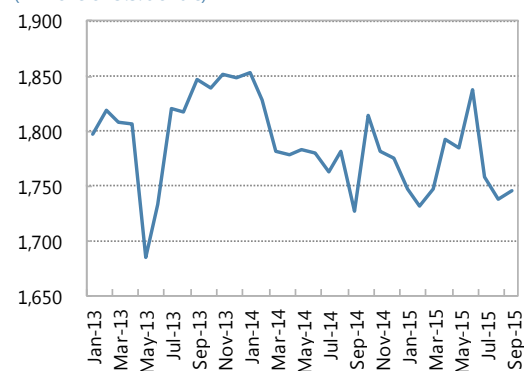
... and partly reflecting the global strengthening of the US dollar, ...

**Nominal depreciation of selected currencies vs. US dollar**  
(Percent ; between December 2014 and October 2015)



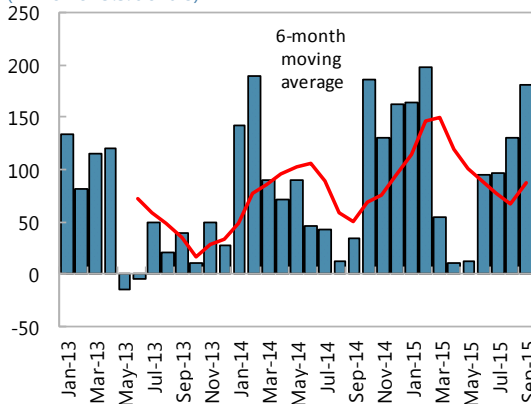
... while dollar deposits in the banking system remained broadly stable.

**Banks Foreign Currency Deposits**  
(Millions of U.S. dollars)



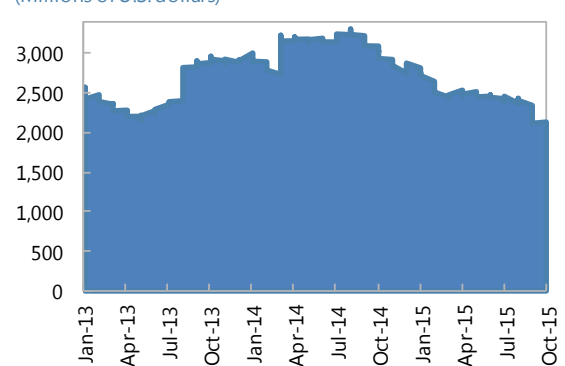
The central bank's recent intervention was mainly for its commitment to finance fuel imports...

**Net Central Bank Foreign Exchange Sales**  
(Million of U.S. dollars)



... but the level of international reserves continue to fall.

**Net International Reserves**  
(Millions of U.S. dollars)



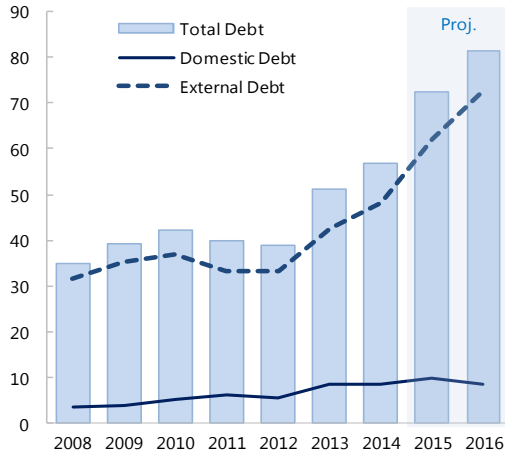
Sources: Mozambican authorities and IMF staff estimates and projections.

**Figure 4. Mozambique: Fiscal Developments**

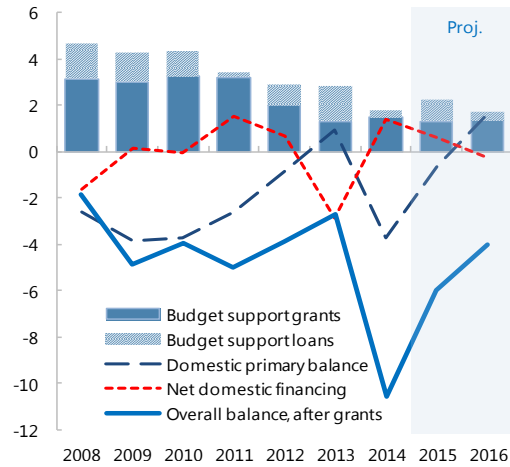
*Public Debt has been rising fast, although 2015-16 increases are mainly driven by metical depreciation.*

*Fiscal consolidation started in 2015 after the overall fiscal stance deteriorated markedly in 2014...*

**Total Public Debt Composition**  
(Percent of GDP)



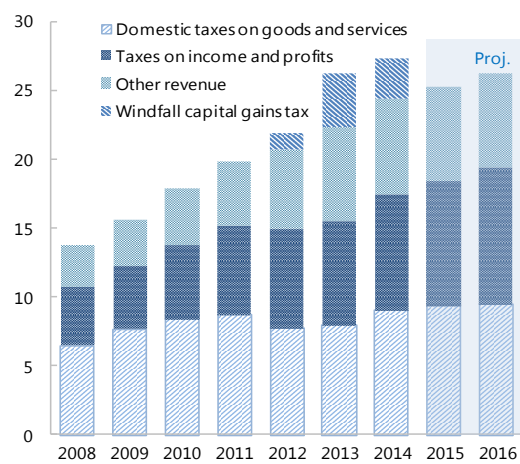
**Budget Financing**  
(Percent of GDP)



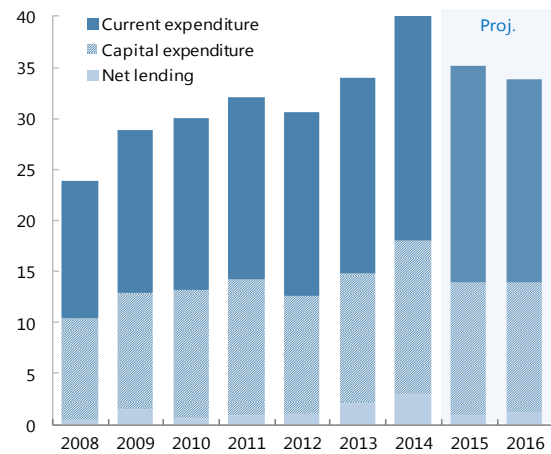
*...when large windfall revenues in 2013-2014...*

*... were used to finance a sharp increase in expenditure.*

**Revenue Collection**  
(Percent of GDP)



**Total Expenditure and Net Lending**  
(Percent of GDP)



Sources: Mozambican authorities and IMF staff estimates and projections.

## ECONOMIC OUTLOOK AND POLICY DISCUSSIONS

Discussions focused on a policy adjustment package underpinning an 18-month SCF arrangement in response to the temporary external shocks and BOP needs. The SCF would supplement but not replace the current PSI. As regards surveillance issues, the discussions focused on medium-term policies to achieve fiscal consolidation, maintain an adequate level of international reserves, strengthen the capacity for managing natural resource wealth, and reinvigorate the structural reform agenda to promote inclusive growth and financial sector development.

### A. Outlook and Risks

**9. Mozambique's economic outlook remains robust.** Growth of 6.3 percent is expected in 2015 (i.e., a 0.7 percent downward revision), and remains below potential at 6.5 percent in 2016, mainly due to a stagnant mining sector and substantially tighter fiscal and monetary policies.

Over the medium term, growth is projected to recover to 7½-8 percent, supported by massive investment in natural gas projects and higher coal production if key agreements can be

reached for coal and gas sector development.<sup>4</sup> Inflation is expected to increase towards the BM's medium target of 5-6 percent, due to the recent depreciation of the metical and adjustments in administered prices.<sup>5</sup>

**10. Economic risks are substantial.** In the short term, construction of liquefied natural gas (LNG) plants could be significantly delayed if the ongoing negotiations between the authorities and gas companies are not completed by the end of the year. Over the longer run, persistently weak international commodity prices and significant slowdowns in China and other key economies might delay the expansion of coal mining projects and dampen growth. If these risks materialize, the recovery of growth to 7-8 percent could be delayed by a few years, while the growth rate would remain above 6 percent owing to the expected growth of non-mining sectors.

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Mozambique: Mining Sector Indicators

|   | 2002-11                               | 2012   | 2013   | 2014   | 2015   | 2016   |
|---|---------------------------------------|--------|--------|--------|--------|--------|
|   | Average                               |        |        |        | Proj.  | Proj.  |
|   | (In percent, unless otherwise stated) |        |        |        |        |        |
| Mining GDP (nominal, in MT million)                               | 3,301                                 | 13,081 | 15,230 | 24,921 | 28,235 | 32,743 |
| Mining GDP (share in total nominal GDP)                           | 1.2                                   | 3.0    | 3.2    | 4.7    | 4.7    | 4.9    |
| Mining real growth  | 20.9                                  | 67.9   | 15.7   | 43.7   | 7.8    | 9.8    |
| Mining contribution to total GDP growth<br>(in percentage points) | 0.2                                   | 1.1    | 0.4    | 1.2    | 0.3    | 0.4    |
| <i>Memorandum items:</i>  |                                       |        |        |        |        |        |
| Total real GDP growth   | 7.7                                   | 7.2    | 7.1    | 7.2    | 6.3    | 6.5    |
| Non-mining real GDP growth  | 7.6                                   | 6.2    | 6.9    | 6.2    | 6.2    | 6.4    |

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

<sup>4</sup> In the natural gas sector, such agreements between the government and concessionaries would trigger massive FDI in LNG processing facilities (starting from the second half of 2016) and pave the way for LNG exports by 2021. In the coal sector, agreements need to be reached to unlock financing for the completion of the Nacala rail corridor, which would triple coal export volumes by 2017. In the latter part of October, negotiations between the government and the investors were in full swing.

<sup>5</sup> Bread prices were adjusted in October and electricity prices in November, with an estimated average increase of about 20 percent in the latter case.

As a tail risk event, low international gas prices could cause significant delays in the gas projects for several years, although the oil and gas companies still remain confident in the feasibility of their projects.<sup>6</sup> In addition, new concessions awarded in October 2015 could generate additional investment in the oil and gas sector.

**11. The depreciation of the metical has heightened Mozambique's debt vulnerability, implying a need for cautious future borrowing.** With most public debt issued in foreign currency, the depreciation raised the present value of external debt to almost 40 percent of GDP at end-2015 (from 30 percent at end-2014). The updated DSA shows that Mozambique's external debt rating remains moderate, but debt level indicators are now closer to a high risk rating, and the risk to overall public debt is now heightened.<sup>7</sup> Maintaining debt sustainability will require vigorous fiscal discipline in line with the authorities' program, a strong focus on contracting debt mostly on concessional terms, and increased prioritization among investment projects. Such prioritization is also important as debt service has started to increase sharply with the start of repayments on EMATUM debt, even if it remains manageable overall. The present value of debt is expected to decrease somewhat below 40 percent of GDP during 2016-19 before declining to less than 20 percent by the mid-2020s because of a higher GDP (LNG production).

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<sup>6</sup> The sizable current account deficits projected in the medium term are driven by large gas projects financed by FDI and private debt. It will not pose a significant BOP risk to the extent that the implied imports are financed directly by these inflows.

<sup>7</sup> The Debt Sustainability Framework applies a method based on probabilities of default to borderline cases within a range of +/- 5 percent of the threshold values. According to this alternative method, Mozambique's probability of default is clearly moderate, implying that its overall moderate rating is maintained.

**Box 1. Mozambique: Risk Assessment Matrix<sup>1</sup>**

| <b>Nature/Source of Risk</b>  | <b>Likelihood in the next three years</b> | <b>Expected impact on the economy</b> | <b>Time Horizon</b> | <b>Policy Response</b>  |
|---|---|---------------------------------------|---------------------|---|
| <b>External</b>   |   |                                       |                     |   |
| Protracted period of slower growth in key advanced and emerging economies                       | M   | H                                     | Short Term          | Accelerate policies to diversify exports and structural reforms to boost competitiveness  |
| Sharp growth slowdown and financial risks in China  | L   | L                                     | Short Term          | Accelerate policies to diversify exports and structural reforms to boost competitiveness  |
| Persistently low global commodity prices affecting Mozambican exports (especially coal and gas) | M   | M                                     | Medium Term         | Exchange rate flexibility as first line of defense, and automatic stabilizers while preserving debt sustainability  |
| <b>Domestic</b>   |   |                                       |                     |   |
| Significant delay in LNG projects   | L   | H                                     | Short Term          | prudent fiscal policy to maintain debt sustainability   |
| Social unrest in connection with lower than expected benefits from natural resource management  | M   | M                                     | Short Term          | Foster inclusive growth and intensify public communication on the long term social benefits of natural resources  |
| Significant aid decline   | L   | M                                     | Short Term          | Continue to seek donor support and maintain consistent policies, with an emphasis on good governance and transparency                                       |
| Climate disasters   | M   | H                                     | Medium Term         | Accelerate prevention and risk management policies. Automatic stabilizers and targeted spending initiatives. Supportive monetary and exchange rate policies |
| Infrastructure bottlenecks hampering exports and economic growth                                | M   | M                                     | Medium Term         | Enhance project selection and financing consistent with debt sustainability   |
| Excessive borrowing leading to unsustainable external public debt                               | M   | H                                     | Medium Term         | Enhance debt management, project selection and assessment process   |

<sup>1</sup> 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 of risks listed is the staff's subjective assessment of the risks surrounding the baseline. The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with authorities.

## B. Short-Term Challenge: Responding to Balance of Payments Shocks

**12. The central bank's NIR have declined markedly in 2015, mostly due to a series of external shocks.** Cumulative losses in NIR amounted to \$1.1 billion between September 2014 and October 2015 as foreign exchange inflows declined substantially due to: (i) Mozambique's exports being hit by sharp declines in international commodity prices from late 2014, both for commodity and traditional exports; (ii) foreign direct investment in the natural gas sector coming to a halt, with the exploration phase concluded and investment in processing facilities awaiting finalization of key production agreements between the government and concessionaires; (iii) absence of revenues from capital gain taxes in 2015 (which had supported the budget and NIR levels in 2013-14) and (iv) declines in external aid flows. Unforeseen renewed pressures since June (Box 2) have rendered the end-2015 target agreed at the time of the fourth review unattainable (see paragraphs 6, 7).

**13. While significant policy adjustment is now underway to ensure that reserves are safeguarded, a more timely policy reaction would have been preferable.** The authorities implemented measures agreed in the fourth review; in particular, the fiscal deficit is projected to decline to 6.0 percent of GDP in 2015 from 10.4 percent in 2014. However, import demand has thus far remained high—partly due to a lingering impact of the major 2014 fiscal policy slippages—although the authorities let the exchange rate depreciate (see above) and the metical is now being broadly fairly valued (Annex 1). Given the adverse shocks to external inflows, import levels have become unsustainable and a more immediate policy reaction would have been preferable to redress the situation. Especially, a tighter monetary stance than agreed at the time of the fourth review would have been desirable to counteract NIR losses. Adherence to the initial reserve money targets meant that the central bank was reinjecting through open market operations part of the domestic currency liquidity that was being withdrawn through foreign exchange sales. This impaired the automatic adjustment mechanism to the balance of payment pressures.

## Box 2. Impact of External Shocks

This box illustrates how renewed external shocks can explain most of the reserve losses in 2015 by causing higher BOP pressures than anticipated at the time of the fourth review of the PSI-supported program:

- Mozambique's exports—having already fallen short of projections by \$170 million during the first half of 2015—are performing worse on account of further declines in key commodity prices, especially for aluminum and natural gas but also affecting traditional exports. Coal companies have reacted to continued low coal prices by limiting export volume growth to contain their losses.

|             | 4th review | 5th review | Export value 2014<br>(US\$ millions) |
|-------------|------------|------------|--------------------------------------|
| Aluminum    | -3.0       | -9.8       | 1,052                                |
| Coal        | -19.5      | -14.1      | 501                                  |
| Electricity | 1.2        | 1.0        | 355                                  |
| Natural gas | -10.3      | -33.4      | 340                                  |
| Titanium    | -16.6      | -22.3      | 191                                  |

- Foreign direct investment for megaprojects has come to a halt—halving during the first semester of 2015—with finalization of key production agreements between the government and concessionaires taking longer than expected previously, delaying investments in coal infrastructure in LNG processing facilities.<sup>1</sup>
- Aid disbursements have continued their longer-term downward trend in 2015, in contrast to fourth review projections which proved too optimistic in projecting a slight rebound.

Finally, the BM's international reserves, when evaluated in US dollars, suffered from further valuation losses after June as a result of continued dollar strength.

### Mozambique: Changes in external inflows during 2015 and potential NIR impact (US\$ millions)

|  | 4th review | 5th review | Change | Estimated<br>impact on NIR 5/ |
|--|------------|------------|--------|-------------------------------|
| Projected change in NIR during 2015      | 8          | -856       | -864   | ...                           |
| Main factors contributing to NIR losses: |            |            |        |                               |
| Goods exports                            | 4,031      | 3,557      | -474   | -200 to -300                  |
| <i>of which:</i> Commodity-related 1/    | 2,544      | 2,186      | -358   |                               |
| Foreign direct investment, net           | 4,048      | 2,880      | -1,168 | -175 to -300                  |
| <i>of which:</i> LNG and coal megaprojec | 2,000      | 858        | -1,143 |                               |
| Program aid inflows 2/                   | 747        | 586        | -161   | -161                          |
| <i>of which:</i> Fungible program aid 3/ | 427        | 346        | -81    |                               |
| Reserve valuation 4/                     | -89        | -205       | -116   | -116                          |

1/ Includes coal, natural gas, aluminum, titanium, and electricity.

2/ Does not include project aid, which is tied to specific projects, typically infrastructure.

3/ Basis for calculation of NIR adjustor under PSI program. It excludes in kind flows and funds tied to specific government programs with limited fungibility in financing the government budget.

4/ Valuation change of net international reserves in US dollars during 2015.

5/ Impacts of exports and FDI on potential NIR accumulation are less than one-to-one: For exports, only 50 percent of revenues have to be repatriated with exceptions for some firms. For FDI, only a relatively small fraction is spent on domestic value added rather than imports.

<sup>1</sup>Although only a relatively small proportion of this investment spent on procurement of domestic value added, the additional impact is notable, given the sheer size of such investment and its steep decline.

**14. Further policy adjustments are required to stabilize the BOP and start rebuilding international reserves.** Policy adjustment is most critical to stabilize the BOP, with Fund financing filling the remaining financing gap and ensuring that other donor support proceeds as planned. Policy adjustment is projected to reduce imports by about \$1 billion per year and will make the BOP sustainable after its full impact has materialized by the end of the 18-month SCF program. Fund financing amounts to SDR 204.5 million (approximately \$285 million) over the course of the program and is expected to serve a catalytic role. In the near term, the authorities' ongoing engagement with the Fund ensures that planned World Bank disbursements, including for budget support, go ahead as planned. In 2016 and beyond, the engagement will continue to underpin confidence of the broader donor community.

**15. Staff and the authorities agreed on a policy mix based on three interrelated pillars designed to allow rebuilding of reserves to commence in 2016.** These three pillars are (1) further fiscal adjustment of two percent of GDP, which will generate a reduction in the overall fiscal deficit to 4 percent of GDP in 2016 (the projected 6.0 percent of GDP in 2015 is already significantly lower than programmed); (2) the monetary policy tightening cycle initiated in October and intensified in November; and (3) reforming the FX market and allow for continued exchange rate flexibility. These policies will be supported by a gradual phasing out of the guaranteed sales of US dollars for fuel imports<sup>8</sup> and minimal discretionary intervention to smooth out exchange rate volatility, with the authorities standing ready to undertake further policy adjustment to safeguard reserves in case BOP pressures remain higher than expected. The front-loaded implementation of this corrective policy package, with the planned adoption of the 2016 budget by mid-December 2015 and the implementation of the monetary and foreign exchange market measures in November 2015, aim at providing support to the shoring up of reserves right from the start of the program. The policy mix will be supported by an ambitious structural reform agenda with an added emphasis on critical PFM reforms and managing fiscal risks on public enterprises (including EMATUM).

**16. As a result of the policy adjustment under the SCF/PSI, NIR are expected to bottom out during the first half of 2016 before resuming a path of gradual recovery that would return import coverage ratios back to comfortable levels.** Given the level of NIR in October 2015 and projected foreign disbursements for the remainder of the year, the end-2015 NIR level is projected to be just above \$2 billion. The tightening of monetary and fiscal policies should restrain imports significantly in 2016, adding to the lagged impact of the substantial depreciation of the metical. Policy adjustment, together with an expected modest resumption of FDI, should result in sufficient dollar liquidity in the domestic foreign exchange market by mid-2016 to allow the BM to discontinue interventions for fuel imports and gradually start purchasing dollars to rebuild reserves. Import coverage of gross international reserves is projected to increase to

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<sup>8</sup> The phasing out results from the impact of the corrective policy package on imports demand, which will materialize with some lags. In the meantime, the BM needs to continue to stand ready to provide sufficient foreign exchange to the commercial banks to avoid any interruption in fuel supplies.



4.5 months of non-megaproject imports by end-2016 (from 4.2 months of imports at end-2015).<sup>9</sup> The shallowness and current illiquidity of the interbank foreign exchange market impair the central bank's ability to purchase significant amounts of foreign exchange in the market and to pursue significantly more ambitious NIR targets in 2016.

## Fiscal Policy

**17. The main objective of fiscal policy in 2016 is to ensure debt sustainability and contribute to the required external adjustment.** In 2016, net domestic financing will be slightly negative (0.2 percent of GDP), which will contribute negatively to money creation and help prevent crowding out pressures. Beyond 2016, the main objective will be to put debt accumulation on a downward path. In that regard, the authorities concurred with staff's recommendation on a more rapid fiscal consolidation in the medium term than envisaged in the 4<sup>th</sup> review. With regards to external borrowing, the program targets are set based on the authorities' appropriately prudent 2016 borrowing plan. Reflecting the Fund's updated debt limits policy, targets are now present-value based and cover total external borrowing instead of non-concessional borrowing only (see the authorities' borrowing plan in Tables 8. 9). By eliminating a rigid concessionality threshold, they should afford the authorities more flexibility in loan negotiations.

|                |                     | 2015   | 2016   | 2017   | 2018   | 2019   | 2020   |
|----------------|---------------------|--------|--------|--------|--------|--------|--------|
| (a) Current    | Grants              | 615.0  | 545.4  | 451.9  | 420.3  | 390.9  | 363.5  |
|                | Loans               | 946.3  | 817.9  | 1086.6 | 1298.5 | 1445.1 | 1602.5 |
|                | Total               | 1561.2 | 1363.3 | 1538.5 | 1718.8 | 1836.0 | 1966.0 |
| (b) 4th Review | Grants              | 824.2  | 654.5  | 608.6  | 566.0  | 526.4  | 489.6  |
|                | Loans               | 1095.6 | 1154.4 | 1544.4 | 1882.2 | 1936.4 | 1937.0 |
|                | Total               | 1919.8 | 1808.8 | 2153.0 | 2448.3 | 2462.8 | 2426.5 |
| (a) - (b)      | Grants              | -209.2 | -109.0 | -156.7 | -145.7 | -135.5 | -126.0 |
|                | Loans               | -149.3 | -336.4 | -457.7 | -583.7 | -491.3 | -334.4 |
|                | Total               | -358.5 | -445.5 | -614.5 | -729.4 | -626.8 | -460.5 |
|                | (in percent of GDP) | -2.4   | -3.0   | -3.7   | -4.0   | -3.1   | -2.0   |

Source: IMF staff estimates.

**18. In light of rising debt levels and persistent BOP pressures, staff and the authorities agreed on a significantly tighter fiscal stance in 2016 (see text table below) to underpin the SCF.** The overall fiscal deficit (after grants) is projected to decline by 2 percentage points of GDP to 4 percent of GDP in 2016 and the domestic primary balance would improve by about 2¼ percent of GDP, significantly more than previously envisaged.

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**19. Total revenues are projected to expand by 1 percent of GDP in 2016.** This increase is expected to be generated by (i) strong performance in international trade taxes—as the

<sup>9</sup> These ratios include disbursements under the SCF-supported program.

depreciation boosts the taxable base in domestic currency, (ii) an increase in gas royalties, and (iii) tax administration reforms to facilitate revenue mobilization (stamp taxes for alcoholic beverages and cigarettes, common custom tariffs and excise duties.)

| Mozambique: Key Fiscal Indicators                         |   |      |       |         |                      |       |                      |       |
|---|---|------|-------|---------|----------------------|-------|----------------------|-------|
|   | 2012                                      | 2013 | 2014  |         | 2015                 |       | 2016                 |       |
|   | Act.                                      | Act. | Act.  | Neutral | 4th Rev.<br>CR15/223 | Proj. | 4th Rev.<br>CR15/223 | Proj. |
|   | (Percent of GDP, unless otherwise stated) |      |       |         |                      |       |                      |       |
| Total revenue   | 21.9                                      | 26.3 | 27.3  | 24.3    | 25.5                 | 25.2  | 25.7                 | 26.2  |
| <i>of which capital gain tax</i>                          | 1.2                                       | 3.9  | 3.0   | 0.0     | 0.0                  | 0.0   | 0.0                  | 0.0   |
| Total expenditure and net lending                         | 30.7                                      | 34.0 | 42.2  | 38.5    | 36.9                 | 35.3  | 34.6                 | 33.9  |
| <i>of which current expenditures</i>                      | 18.1                                      | 19.2 | 23.8  | 20.1    | 20.7                 | 21.3  | 19.7                 | 20.2  |
| <i>of which maritime security</i>                         | 0.0                                       | 0.0  | 2.8   | 0.0     | -1.0                 | 0.0   | 0.0                  | 0.0   |
| <i>of which domestically financed capital expenditure</i> | 5.7                                       | 7.0  | 8.2   | 8.2     | 7.4                  | 6.0   | 6.6                  | 6.1   |
| Overall balance, before grants                            | -8.9                                      | -7.9 | -14.8 | -14.1   | -11.4                | -10.0 | -8.9                 | -7.7  |
| Grants  | 5.1                                       | 5.2  | 4.2   | 4.2     | 4.9                  | 4.0   | 3.4                  | 3.7   |
| Overall balance after grants                              | -3.9                                      | -2.7 | -10.6 | -9.9    | -6.5                 | -6.0  | -5.5                 | -4.0  |
| Net external financing                                    | 3.2                                       | 5.6  | 8.8   | 5.9     | 5.7                  | 5.4   | 5.4                  | 4.2   |
| Net domestic financing                                    | 0.7                                       | -2.9 | 1.4   | 4.0     | 0.8                  | 0.6   | 0.0                  | -0.2  |
| <i>Memorandum items:</i>                                  |   |      |       |         |                      |       |                      |       |
| Domestic primary balance                                  | -1.0                                      | 0.9  | -4.1  | -3.5    | -1.2                 | -0.6  | 0.8                  | 1.6   |
| Real GDP growth (percent)                                 | 7.2                                       | 7.1  | 7.2   | 7.2     | 7.2                  | 6.3   | 8.2                  | 6.5   |
| Average CPI inflation (percent)                           | 2.1                                       | 4.2  | 2.3   | 2.3     | 2.3                  | 1.9   | 5.6                  | 5.6   |

Sources: Mozambican authorities and IMF staff estimates and projections.  
<sup>1</sup> IMF Neutral adjusts for one-off receipts and expenses. Revenues exclude USD 520 million capital gain taxes for the natural resource sector (or 3.1 percent of GDP), while expenditures exclude one-off maritime security spending of 2.8 percent of GDP (EMATUM), and temporary election-related expenditures (0.8 percent of GDP).

**20. Fiscal adjustment is driven by a reduction of about 1½ percent of GDP in public spending relative to 2015.** A substantial part of the fiscal adjustment will fall on current spending, including subsidies and the wage bill, but public investment will be adjusted downward as well in line with implementation capacity and more rigorous selection criteria.

- **The government is committed to further reducing the wage bill by 0.2 percentage point of GDP in 2016 through a deceleration in the pace of new hiring and by stronger administrative controls on salary payments.** The latter will involve (i) requirements to regularly produce "proofs of life" statements for all civil servants, and (ii) strict limits on new hiring in non priority sectors (i.e., excluding the health, education, agriculture and police sectors).
- **At current international oil prices, no provision for fuel subsidies is required in the 2016 budget.** Should international oil prices increase, the government indicated that they will consider adjustments in the price setting formula to prevent the need for new subsidies. If the formula cannot be adjusted in a timely manner for political economy reasons, any subsidies accrued would be financed through downward adjustments in other non-priority spending to ensure the achievement of the budget target.
- **Public investment projects will be subject to more rigorous evaluation procedures to enhance investment efficiency and ensure greater value for money.** No project exceeding \$50 million will be authorized for inclusion in the multi-year list of priority

investment without a prior feasibility study from the sectors and a technical evaluation by the Ministry of Economy and Finance (MEF).

- **The mission and the authorities agreed that the envisaged fiscal adjustment should be implemented without negatively affecting critical social programs.**

| <b>Mozambique: Fiscal Adjustment in 2016</b> |  |   |
|--|--|---|
|  | <b>2016</b> (Change with respect to 2015, in percent of GDP) | <b>Comments</b>   |
| <b>Total Revenue</b>                         | 1.0  | derived from the combination of a higher volume of goods imports in US dollars and a more depreciated exchange rate vis-à-vis the US dollar, increase in gas in-kind royalties, as well as administrative reforms in key areas, for instance, stamp taxes for alcoholic beverages and cigarettes, common custom tariffs and excise duties |
| <b>Total Expenditure and Net Lending</b>     | -1.4   |   |
| <b>Current Expenditure</b>                   | -1.1   | adjustment entails: (1) a deceleration in the public servants hiring rate (which has increased substantially in the last years) and an augmentation of controls on the salary payments system, and (2) decrease in transfer payments, specifically fuel subsidies   |
| <b>Capital Expenditure and Net Lending</b>   | -0.3   | mainly through a reduction in externally financed capital expenditure   |
| <b>Domestic Primary Balance, Before</b>      | 2.3  |   |
| <b>Grants</b>                                | -0.4   |   |
| <b>Overall Balance, After Grants</b>         | 2.0  |   |

Source: IMF staff estimates.

## Monetary and Exchange Rate Policies

**21. Decisive action is required to curb inflationary pressures and help stabilize the foreign exchange market.** Staff commended the BM on its decision to initiate a cycle of monetary tightening in its October Monetary Policy Committee meeting. Staff and the authorities agreed on the need to further tighten monetary policy, given the worsening foreign exchange market conditions and the loss of NIR and to attempt to reduce dollar hoarding behavior by increasing the attractiveness of holding deposits in domestic currency. Depreciation is being passed through to domestic prices, which, together with several expected adjustments in administered prices, is expected to push inflation above the BM's target range of 5-6 percent by end-2016. The BM raised the required reserve requirement by 100 basis points in October and again by 150 basis points in November. It also increased its standing lending (FPC) rate by 25 basis points and its standing deposit (FPD) rates by 50 basis points in October, with a further 50 basis point increase in the FPC rate and 75 basis point increase in the FPD rate in November. It is expected that this tightening will reduce credit growth and the demand for dollars in the

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foreign exchange market. The mission and BM also agreed on the need to keep reserve money growth at 12 percent in 2016, somewhat below nominal GDP growth, representing a significant deceleration compared to previous years, and tightening monetary policy further in 2016 should the pressures on the foreign exchange market and inflation persist.

**22. The BM took action to remove the distortion in the foreign exchange market (MCI), which had previously skewed commercial banks' demand for interventions by the BM.**

MEFP ¶133

The BM intervenes in the market through the MCI computer screen, based on buying and selling quotes posted by 16 participating banks. Besides the MCI system, these banks also negotiated and traded outside the system, at exchange rates that did not always correspond to the MCI rates due to the shallowness and illiquidity of the interbank foreign exchange market. The spread between the BM's intervention rate and the interbank rate increased since the last review under the PSI, generating incentives for commercial banks to mobilize foreign exchange from the BM instead of purchasing them from their clients. In November, banks quoted buy and sale rates on the MCI computer screen consistent with the interbank rate, hence bringing this spread to zero.

## C. Medium-Term Reforms: Strengthening Institutions and Preparing for Managing Natural Resource Wealth

### Fiscal Reforms

**23. The authorities need to continue strengthening budget controls and fiscal transparency.**

The government has expanded gradually the coverage of its integrated information management systems for expenditure tracking (e-SISTAFE) and wage payments (e-Folha), as well as the treasury single account. However, e-SISTAFE is still not used adequately. Most budgetary transactions, in particular commitments and verifications, are not entered in the system in real time, which weakens budgetary controls and may result in line ministries exceeding their budget appropriations and accumulating extra-budgetary spending. To this end, staff stressed the importance of aligning the three traditional stages of expenditure recording (commitment, verification, issuance of the payment order) with the actual timing of the various budgetary transactions by June 2016 (structural benchmark).

MEFP ¶15-19

**24. Although the 2015 budget projected revenues on a net basis and current VAT collections are recorded net of refund payments, the implementation of the net VAT system has encountered difficulties.**

This has led to the accumulation of around \$50 million of arrears by end-October 2015. The authorities agreed on the importance of securing enough funds to reimburse the taxpayers in due time, by creating a dedicated subaccount to be regularly replenished with an amount equivalent to the refund claims received. This should be operational from the beginning of 2016 (proposed structural benchmark). Staff welcomes the authorities' prudent decision to start recording net VAT collections on the basis of the refund claims received, even if these have not yet been verified and paid, by end-2015.

MEFP ¶23

**25. Staff urged the authorities to closely monitor fiscal risks and public enterprises, and to adopt an action plan to improve the profitability of EMATUM.**

MEFP ¶120, 32

In November, the government published a fiscal risks statement to ensure greater transparency and better informed fiscal decisions (structural benchmark). The statement pays special attention to risks associated with government guarantees and public enterprises. Staff is encouraged by the authorities' intention to create a fiscal risk unit in the MEF to provide strategic advice to the minister in a timely manner. The government also intends to adopt an action plan which aims at improving profitability of EMATUM by April 2016 (structural benchmark).

**26. Staff urged the authorities to continue to strengthen debt management.**

MEFP ¶13

Staff commended the new government on the measures taken to slow down new external borrowing, but cautioned on the negative effect of the depreciation of the metical on Mozambique's capacity to service its external debt, as shown in the DSA update (see above). The government is revising its Debt Management Strategy with emphasis on fostering the development of the domestic capital markets, and is regularly producing annual domestic borrowing plans and debt reports. Staff stressed that the government needs to continue to strengthen debt management to avoid further external debt arrears, in particular by improving reconciliation with creditors.

**27. Enhancing public investment efficiency and ensuring greater value for money remains crucial, but reform implementation efforts should be stepped up.**

MEFP ¶12

Staff welcomed the requirement for mandatory assessments by the Investment Evaluation Committee of all public investment projects exceeding \$50 million in the 2016 budget, but stressed the need for the application of more rigorous evaluation procedures to select public investment projects and the improvement of project implementation monitoring and evaluation. The government is expecting to benefit from a forthcoming FAD mission to introduce PIMA, a new tool to assess public investment.

### Energy Sector Reforms

**28. Staff and the authorities agreed on the importance of taking steps to initiate crucial reforms in the energy sector.**

MEFP ¶11

Staff welcomed the long overdue increase in electricity tariffs in November, which should help contain the operational losses of the National Electricity Company (EDM).<sup>10</sup> Fuel prices have not been adjusted since 2011 and the fuel subsidy paid in 2014 showed that the current price mechanism can be costly and inefficient.<sup>11</sup> At current international prices, retail fuel prices are no longer subsidized, which provides an opportunity for reform. Following a recent

<sup>10</sup> The tariff increase ranges from 18 percent (domestic/household tariff) to close to 50 percent (large consumers). The "social" and "agriculture" tariffs have not been changed. It is estimated that the weighted average tariff increase is approximately 20 percent.

<sup>11</sup> About half of the subsidy in 2014 was mis-targeted and only two percent reached the poorest 10 percent of the population.

FAD TA mission, staff recommended streamlining the automatic price-setting formula through the introduction of reference pricing and implementation of an automatic fuel pricing mechanism with a smoothing component as early as possible in 2016. The authorities argued that additional studies on the fuel market, including on the need to reform the centralized fuel importing system, are needed and that they are also considering measures needed to mitigate the impact on the most vulnerable.

## Monetary and Financial Sector Reforms

**29. The BM continues to strengthen its analytical tools and monetary policy operations framework.** An enhanced inflation forecasting model has been developed and is currently being used to inform decisions by the Monetary Policy Committee. Efforts to improve the liquidity forecasting model, with IMF technical assistance, are also ongoing. The law that requires 20 percent withholding tax on interests earned on T-bills, OTs, secured and unsecured interbank transactions has been enforced since May 2015 (structural benchmark). Allowing T-bonds as collateral in money market operations, another important reform for developing domestic financial markets, and enhancing the monetary policy transmission mechanism experienced some further delays due to the need for new regulations. This reform is now expected to become operational in December 2015 (structural benchmark). Staff stressed the need for deepening domestic financial markets, as high degrees of concentration in both the deposit base and credit have contributed to structurally high deposit and lending rates and hampered the adjustment of market interest rates in response to policy rate changes, a key monetary policy transmission channel.<sup>12</sup>

MEFP ¶¶34-38

inform

MEFP ¶¶39-44

**30. Reforms to strengthen bank supervision, crisis management tools, and financial sector development are ongoing.** Despite the depreciation of the metical, bank soundness indicators suggest that banks are well capitalized and profitable, with low non-performing loans (NPLs). This could be due to the limited open positions that most banks have in dollars, and the high provisioning requirements for foreign currency loans to non-exporters that discourages dollar-denominated lending. Stress tests also point to a resilient banking system, with credit concentration remaining the main source of risk. The monetary tightening cycle just initiated should help to slow down the trend of rapid credit expansion.<sup>13</sup> As NPLs could rise during the expected downturn of the credit cycle, staff urged the BM to monitor credit risks closely and require the banks to maintain adequate capitals. Staff welcomed the continued effort in implementing the Financial Sector Contingency Plan, including the BM's intention to adopt an Action Plan aimed at addressing the issues observed during the simulation exercise by March 2016 (proposed structural benchmark). Vigorous implementation of the *Financial Sector Development Strategy 2013-22* is required to solve the perennial difficulty of access to credit by

<sup>12</sup> Selected Issued paper.

<sup>13</sup> Given the less developed financial markets, the interaction between the financial cycle and the real economy appears to be limited. While booming credit could have contributed to growth, the risk of problem loans also increased.

small and medium-sized enterprises and foster financial inclusion. In this regard, the Law on the Creation of Private Credit Registry Bureaus has been adopted in July, while the launch of the National Financial Inclusion Strategy is expected this year.

### Managing Natural Resource Wealth

**31. Negotiations between the authorities and the oil and gas companies should continue to move forward to allow final investment decisions in near future.** Even with recent subdued commodity prices, including LNG prices, gas development companies remain confident in the viability of the LNG projects. However, further delays in the negotiations would result in lower FDI inflows in the short run and delay the expected benefits on growth and fiscal revenues.

**32. Staff updated the analysis on the macroeconomic implication of the LNG projects.** If the LNG projects are implemented along the current schedule, the LNG sector will significantly contribute to growth during the early-2020s and output from the sector will account for more than half of GDP in the mid-2020s. However, the fiscal revenues from the projects would become significant only by the mid-2020s, and current account balance would turn into surplus only in 2025, due to cost recovery of investment. The authorities should initiate work to develop a medium-term fiscal framework and a formal fiscal rule to (i) inform future saving and investment decisions, (ii) manage volatility, and (iii) address exhaustibility concerns. They should take into consideration various risk factors including lower gas prices when the spending and borrowing plans are constructed and implemented. Staff welcomed the ex-ante rule for the use of windfall revenue in the 2015 Budget Law (structural benchmark), which seeks to limit the use of these resources only for public investment, debt repayment, and national emergencies.

MEFP ¶127-30

**33. The authorities agreed with the staff's analysis and remain committed to further strengthening capacity building and enhancing transparency in natural resource wealth management.** With technical assistance from the Fund, the authorities have been strengthening the legal framework for the natural resource sector and the capacity of tax authorities in revenue collection and forecasts. Mozambique has compiled EITI reports and has been enhanced transparency of its natural resource management. The authorities should further strengthen their capacity for developing and operationalizing the medium-term fiscal strategy.

### Other Reforms and Issues

**34. Improving the business environment remains crucial to promote enterprises and job creation.** Mozambique's performance has edged down in the 2016 World Bank's Doing Business index, being ranked at the 133<sup>th</sup> position (128<sup>th</sup> in the previous report). Decisive action is necessary to address difficulties in obtaining credit by SMEs and reduce the excessive time prospective investors devote to starting a new business. Nevertheless, staff commends the authorities for integrating eight provinces into e-BAU, an IT platform aimed at providing online services to the business community. The authorities estimate that, as a result of this reform, the

number of days taken for licensing economic activities was reduced from fifteen to a maximum of three on average in all the affected provinces. By July 2016, the remaining three provinces (Manica, Zambezia, and Niassa) and all municipalities and provincial capitals should also be integrated into the e-BAU platform.

**35. Statistics and data availability.** While the statistical system is broadly adequate to support surveillance and program monitoring, enhanced dissemination and regular transmission of data to the Fund are required. Weaknesses exist, particularly in the areas of national accounts, government finance, balance of payments, and external debt statistics. The authorities should further enhance the quality and frequency of data dissemination, supported by technical assistances from the Fund and other agencies.

## PROGRAM ISSUES

**36. The SCF would have an 18-month duration.** Its objective will be to alleviate the external shock through the first part of 2017, while maintaining the PSI's existing objectives of strengthening macroeconomic stability, investing in infrastructure and social sectors, fostering inclusive growth, and building capacity in investment planning and debt management and management of natural resource wealth. The monitoring of the program would be synchronized with the PSI.

**37. Frontloading.** The BOP need will be highest in 2015 (Table 7) and the beginning of 2016, as imports will gradually adjust to policy tightening and exchange rate depreciation. This justifies a front-loading of the SCF disbursements. Adjustment in 2016 and the tripling of coal export capacity in 2017 (Nacala railways project) will gradually phase out the BOP need in 2017.

**38. The requested access is in line with the new SCF norms, which provide an adequately-sized buffer of 180 percent of quota (approximately \$285 million).** The proposed first disbursement (75 percent of quota or about \$120 million) is proposed to become available upon approval of the arrangement in late 2015, followed by three semi-annual disbursements of 35 percent (about \$55 million) of quota each. A safeguards assessment, required under the Fund's safeguards policy, will be completed before the first review under the SCF arrangement.

**39. The main risks to the program are:** (i) political instability eroding program ownership; (ii) further deterioration of the external environment; (iii) delays in the negotiation of large investment projects in the natural resource sector; (iv) adverse weather conditions which would significantly affect agricultural production; and (v) capacity constraints that can delay reform implementation (including on revenue administration and budget execution).

**40. Small external arrears (totaling about US\$ 1 million) to three different bilateral creditors emerged.** They occurred as a result of imperfect debt reconciliation with creditors and a lapse in debt recording. These arrears have been promptly addressed by the authorities in October after they became aware of their existence. The authorities furthermore envisage taking measures to strengthen debt reconciliation with creditors to prevent any recurrence.



**41. Waivers are requested for the non-observance of three assessment criteria (ACs) for June 2015 and modifications are proposed for four ACs for December 2015, to reflect recent developments.**

A waiver for the non-observance of the AC on net credit to the government at end-June 2015 is requested on the basis that the deviation is expected to be temporary and has not affected the achievement of the program's objectives, and the government is implementing expenditure restraint measures to meet the December target.<sup>14</sup> A waiver for the non-observance of the AC on NIR is requested in light of the authorities' corrective actions. These comprise foreign exchange market reforms and monetary and fiscal tightening, which will contain imports and allow a return to gradual reserve accumulation by mid 2016. Together, these actions are expected to ensure that NIR only temporarily undercut and promptly return to a prudent range of 4-4½ months of non-megaproject imports. A waiver for the non-observance of the AC on external arrears is requested because the deviation has been minor and temporary. Revised ACs on NCG, reserve money, and NIR for December 2015 are proposed to reflect recent developments.

**42. Two structural benchmarks (SBs) are proposed to be rescheduled.** The November benchmark on the submission of the draft law on the establishment of a movable collateral registry is proposed for rescheduling to March 2016 due to the complexity of this reform, which may require the change of some other legislation. The January benchmark on the mandatory requirement on the real-time recording of the commitment and verification of expenditures for all units operating within e-SISTAFE is proposed for rescheduling to June 2016 due to technical limitations.

**43. Performance criteria (PCs) (for end-June 2016), indicative targets (ITs) and new SBs through end-2016 are proposed (MEFP Tables 1 and 2).** The five new SBs proposed are aimed at further strengthening public financial management and deepening financial sector reforms.

## STAFF APPRAISAL

**44. Mozambique's economic performance has been adversely affected by a series of external shocks in 2015 and the lingering effects of the 2014 fiscal slippage.** Lower commodity prices, a decline in external aid, and markedly lower foreign direct investment resulted in a worsening of the (non-megaproject) current account deficit and generated intense balance of payment pressures. Excessively expansionary policies in 2014 (especially on the fiscal side) and a late start in the monetary tightening cycle when BOP pressures intensified over the summer also contributed to the current difficulties. While policy commitments at the time of the 4<sup>th</sup> review temporarily stopped the loss in NIR, renewed BOP pressures over the summer resulted in a further significant drop in NIR and further depreciation in the metical. While reserve money targets were met, monetary policy should have tightened liquidity conditions further at an earlier

<sup>14</sup> The end-2015 NCG target includes a technical adjustment to incorporate the estimated discounting of the treasury securities that were issued for clearing VAT backlogs (MT 8.2 billion, see paragraph 5) as it does not represent new fiscal stimulus beyond the program. The underlying NCG target is MT 3.6 billion, compared to MT 4.9 billion in the 4<sup>th</sup> review.

stage given the continuous drain in international reserves. In addition, payment by the government in September of the first installments of guaranteed debt of the EMATUM company and constraints on institutional capacity also contributed to weaker program performance.

**45. At the same time, staff commends the authorities for adopting a strong package of corrective policy measures aimed at restoring external sustainability and preserving adequate reserve levels.**

The government's 2016 budget approved by Parliament envisages a reduction in the overall fiscal deficit of 2 percent of GDP, returning to the prudent deficit levels observed prior to the 2014 fiscal slippages (around 4 percent of GDP). The authorities are also to be commended for their steps to reintroduce a more prudent borrowing policy and for taking steps to ensure the return to a strong fiscal position. Similarly, the BM's adjustments of reserve requirements and key interest rates, in October and in November, help tighten liquidity conditions and reduce FX pressures. The recent convergence of rates in the foreign exchange market is crucial to prevent further losses of international reserves. The front-loaded implementation of this corrective policy package will provide support to the shoring up of reserves right from the start of the program.

**46. Despite these temporary difficulties, the medium-term macroeconomic outlook remains positive.**

Mozambique's strong track record of high growth is expected to continue over the medium term on account of massive planned investment in natural resources. In that regard, the successful conclusion of the negotiations between the government and the leading concessionaires is of paramount importance. Delays in concluding the negotiations could be quite costly and exacerbate balance of payment pressures in 2016-17 (as capital inflows would be lower than currently projected). The positive medium-term outlook raises challenges of its own, including the need for inclusive policies focusing public spending on social and pro-poor programs and bridging infrastructure gaps. The staff is encouraged by the authorities' commitment to further strengthen capacity building and enhance transparency in natural resource wealth management.

**47. Given the strength of the authorities' package of corrective policy measures, staff recommends the completion of the fifth PSI review and supports the authorities' request for an eighteen-month SCF arrangement.**

While program performance has been less than satisfactory, the authorities have taken corrective measures and committed to a strong policy adjustment package which would help achieve the objectives of the SCF-supported program. In particular, the government submitted a revised 2016 budget to the parliament in line with program commitments, and the BM tightened the monetary policy stance in October and November through increases in reserve requirements and key policy interest rates. The BM also removed the distortions in the foreign exchange market. The authorities also committed to medium term fiscal consolidation to ensure debt sustainability, further liquidity tightening if pressures persist, exchange rate flexibility, and structural reforms aimed at strengthening fiscal management and facilitating financial stability and development.

**48. Staff supports the request for waivers for the non-observance of three ACs at end-June 2015 on the basis that either the deviations were temporary and have not harmed the achievement of the program objectives and that the authorities have made a strong commitment to remedial actions.** Staff also supports the authorities' request to modify the

end-December 2015 ACs, the modification of three structural benchmarks, and the setting of PCs for end-June 2016 and ITs through end-2016, as the new targets better align with recent developments and continue to be consistent with the achievement of the core program objectives under both the SCF and the PSI.

**49. It is proposed that the next Article IV Consultation take place within 24 months subject to the decision on consultation cycles (Decision No. 14747-(10/96), September 28, 2010).**

**Table 1. Mozambique: Selected Economic and Financial Indicators, 2012-20**

|   | 2012   | 2013   | 2014   | 2015      |        | 2016      |        | 2017   | 2018    | 2019    | 2020    |
|---|--------|--------|--------|-----------|--------|-----------|--------|--------|---------|---------|---------|
|   | Act.   | Act.   | Act.   | CR 15/223 | Proj.  | CR 15/223 | Proj.  |        | Proj.   |         |         |
| (Annual percentage change, unless otherwise indicated)                          |        |        |        |           |        |           |        |        |         |         |         |
| National income and prices  |        |        |        |           |        |           |        |        |         |         |         |
| Nominal GDP (MT billion)  | 433    | 482    | 536    | 591       | 598    | 676       | 673    | 762    | 871     | 990     | 1124    |
| Nominal GDP growth  | 13.5   | 11.3   | 11.1   | 12.5      | 11.7   | 14.3      | 12.5   | 13.2   | 14.4    | 13.6    | 13.5    |
| Real GDP growth   | 7.2    | 7.1    | 7.2    | 7.0       | 6.3    | 8.2       | 6.5    | 7.2    | 8.3     | 7.6     | 7.5     |
| GDP per capita (US\$)   | 602    | 620    | 624    | 626       | 544    | 685       | 515    | 556    | 607     | 657     | 712     |
| GDP deflator  | 5.9    | 3.9    | 3.6    | 5.1       | 5.1    | 5.6       | 5.6    | 5.6    | 5.6     | 5.6     | 5.6     |
| Consumer price index (annual average)   | 2.1    | 4.2    | 2.3    | 4.0       | 1.9    | 5.6       | 5.6    | 5.6    | 5.6     | 5.6     | 5.6     |
| Consumer price index (end of period)  | 2.2    | 3.0    | 1.1    | 5.5       | 5.1    | 5.6       | 5.6    | 5.6    | 5.6     | 5.6     | 5.6     |
| Exchange rate, MT per US dollar, eop  | 29.8   | 30.1   | 33.6   | ...       | ...    | ...       | ...    | ...    | ...     | ...     | ...     |
| Exchange rate, MT per US dollar, per.avg.                                       | 28.5   | 30.1   | 31.5   | ...       | ...    | ...       | ...    | ...    | ...     | ...     | ...     |
| External sector   |        |        |        |           |        |           |        |        |         |         |         |
| Merchandise exports   | 23.6   | 6.9    | -4.8   | 2.9       | -9.4   | 11.7      | 2.4    | 12.7   | 19.5    | 17.0    | 13.0    |
| Merchandise exports, excluding megaprojects                                     | 52.5   | 14.3   | -22.6  | 0.0       | -7.7   | 19.5      | 14.8   | 12.3   | 14.4    | 11.4    | 13.7    |
| Merchandise imports   | 47.2   | 7.3    | -6.2   | 7.7       | -10.8  | 17.4      | 10.9   | 42.2   | 32.0    | 17.8    | 16.9    |
| Merchandise imports, excluding megaprojects                                     | 63.9   | 13.6   | -1.2   | -6.5      | -2.7   | 7.5       | -7.7   | 4.9    | 9.0     | 8.7     | 12.5    |
| Terms of trade  | -5.7   | -0.7   | -1.7   | -0.1      | 0.0    | 0.7       | -1.6   | -1.0   | -0.7    | -0.6    | -0.4    |
| Nominal effective exchange rate (annual average)                                | 7.6    | -1.7   | 0.3    | ...       | ...    | ...       | ...    | ...    | ...     | ...     | ...     |
| Real effective exchange rate (annual average)                                   | 7.1    | -1.2   | -1.4   | ...       | ...    | ...       | ...    | ...    | ...     | ...     | ...     |
| (Annual percentage change, unless otherwise indicated)                          |        |        |        |           |        |           |        |        |         |         |         |
| Money and credit  |        |        |        |           |        |           |        |        |         |         |         |
| Reserve money   | 19.7   | 15.7   | 20.5   | 16.5      | 22.6   | 15.2      | 12.0   | 15.1   | 15.3    | 15.2    | 15.2    |
| M3 (Broad Money)  | 29.4   | 16.3   | 22.2   | 17.1      | 21.2   | 15.5      | 12.3   | 15.3   | 15.6    | 15.5    | 15.5    |
| Credit to the economy   | 19.9   | 28.7   | 28.4   | 17.5      | 19.8   | 15.5      | 12.3   | 15.3   | 15.2    | 15.2    | 15.2    |
| (Percent of GDP)  | 27.2   | 31.5   | 36.4   | 38.7      | 39.0   | 39.1      | 38.9   | 39.7   | 39.9    | 40.5    | 41.1    |
| (Percent of GDP)  |        |        |        |           |        |           |        |        |         |         |         |
| Investment and saving   |        |        |        |           |        |           |        |        |         |         |         |
| Gross domestic investment   | 47.4   | 54.5   | 46.9   | 48.6      | 32.1   | 51.6      | 40.6   | 65.8   | 84.1    | 91.6    | 102.2   |
| Government  | 12.7   | 14.8   | 18.0   | 16.2      | 14.0   | 14.9      | 13.9   | 14.2   | 14.3    | 14.1    | 14.0    |
| Other sectors   | 34.7   | 39.6   | 28.9   | 32.4      | 18.1   | 36.7      | 26.7   | 51.6   | 69.8    | 77.4    | 88.2    |
| o/w Megaprojects  | 28.2   | 31.6   | 15.3   | ...       | 5.0    | ...       | 13.2   | 35.4   | 53.0    | 61.2    | 72.3    |
| o/w non-Megaprojects  | 6.5    | 8.0    | 13.6   | ...       | 13.0   | ...       | 13.5   | 16.2   | 16.8    | 16.3    | 15.9    |
| Gross domestic savings (excluding grants)                                       | -0.9   | 12.5   | 9.5    | 7.2       | -1.1   | 7.2       | 4.6    | 8.2    | 9.1     | 9.3     | 10.5    |
| Government  | 3.8    | 7.0    | 3.6    | 4.8       | 4.0    | 6.2       | 6.2    | 7.1    | 7.7     | 8.0     | 8.1     |
| Other sectors   | -4.7   | 5.5    | 6.0    | 2.4       | -5.0   | 1.0       | -1.7   | 1.1    | 1.4     | 1.3     | 2.4     |
| External current account, before grants   | -48.3  | -41.9  | -37.4  | -41.4     | -33.1  | -44.3     | -36.1  | -57.6  | -75.0   | -82.3   | -91.7   |
| External current account, after grants  | -44.7  | -39.1  | -34.1  | -38.2     | -30.2  | -42.1     | -33.1  | -55.4  | -73.2   | -80.8   | -90.4   |
| Government budget   |        |        |        |           |        |           |        |        |         |         |         |
| Total revenue <sup>1</sup>  | 21.9   | 26.3   | 27.3   | 25.5      | 25.2   | 25.7      | 26.2   | 26.7   | 26.8    | 26.9    | 27.0    |
| Total expenditure and net lending   | 30.7   | 34.0   | 42.2   | 36.9      | 35.3   | 34.6      | 33.9   | 33.8   | 33.4    | 33.0    | 32.8    |
| Overall balance, before grants  | -8.9   | -7.9   | -14.8  | -11.4     | -10.0  | -8.9      | -7.7   | -7.1   | -6.6    | -6.1    | -5.9    |
| Total grants  | 5.1    | 5.2    | 4.2    | 4.9       | 4.0    | 3.4       | 3.7    | 2.8    | 2.3     | 1.9     | 1.6     |
| Overall balance, after grants   | -3.9   | -2.7   | -10.6  | -6.5      | -6.0   | -5.5      | -4.0   | -4.3   | -4.4    | -4.2    | -4.3    |
| Domestic primary balance, before grants   | -1.0   | 0.9    | -4.1   | -1.2      | -0.6   | 0.8       | 1.6    | 2.7    | 3.4     | 3.7     | 3.7     |
| External financing (incl. debt relief)  | 3.2    | 5.6    | 7.9    | 5.6       | 5.4    | 5.4       | 4.2    | 5.2    | 5.7     | 5.7     | 5.8     |
| Net domestic financing  | 0.7    | -2.9   | 1.4    | 0.9       | 0.6    | 0.0       | -0.2   | -0.9   | -1.3    | -1.5    | -1.5    |
| Privatization   | 0.0    | 0.0    | 0.0    | 0.0       | 0.0    | 0.0       | 0.0    | 0.0    | 0.0     | 0.0     | 0.0     |
| Total nominal public debt <sup>2</sup>  | 39.9   | 50.9   | 56.6   | 61.0      | 73.6   | 61.7      | 69.5   | 65.9   | 63.9    | 62.7    | 61.9    |
| Of which: external  | 34.5   | 42.4   | 48.1   | 50.6      | 63.6   | 52.7      | 60.8   | 59.1   | 57.9    | 57.5    | 57.3    |
| Of which: domestic  | 5.5    | 8.6    | 8.5    | 10.4      | 10.0   | 9.1       | 8.6    | 6.8    | 5.9     | 5.2     | 4.6     |
| (Millions of U.S. dollars, unless otherwise indicated)                          |        |        |        |           |        |           |        |        |         |         |         |
| External current account, before grants   | -7,328 | -6,713 | -6,355 | -7,033    | -5,038 | -8,445    | -5,342 | -9,459 | -13,803 | -16,855 | -20,880 |
| External current account, after grants  | -6,790 | -6,253 | -5,787 | -6,481    | -4,597 | -8,016    | -4,901 | -9,104 | -13,473 | -16,548 | -20,594 |
| Overall balance of payments   | 375    | 393    | -110   | 40        | -823   | 418       | 258    | 520    | 420     | 429     | 722     |
| Net international reserves (end of period) <sup>3</sup>                         | 2,604  | 2,995  | 2,881  | 2,889     | 2,026  | 3,273     | 2,251  | 2,737  | 3,125   | 3,521   | 4,241   |
| Gross international reserves (end of period) <sup>3</sup>                       | 2,798  | 3,191  | 3,071  | 3,079     | 2,467  | 3,463     | 2,768  | 3,277  | 3,632   | 3,995   | 4,714   |
| Months of projected imports of goods and nonfactor services                     | 2.7    | 3.3    | 3.9    | 2.7       | 3.0    | 2.8       | 2.3    | 2.0    | 1.9     | 1.8     | 1.9     |
| Months of projected imports of goods and nonfactor services, excl. megaprojects | 4.2    | 4.9    | 4.8    | 4.7       | 4.2    | 4.8       | 4.5    | 4.9    | 5.0     | 4.9     | 5.2     |

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

<sup>1</sup> Net of verified VAT refund requests.<sup>2</sup> Estimate consistent with DSA definition, the nonconcessional Portuguese credit line is included under the external debt. Domestic debt projections include planned securitization<sup>3</sup> Includes disbursements of IMF resources under the ESF and August 2009 SDR allocation.

Table 2. Mozambique: Government Finances, 2012-16

(Billions of Meticaís)

|  | 2012  | 2013  | 2014  | 2015     |       | 2016     |       |
|--|-------|-------|-------|----------|-------|----------|-------|
|  | Act.  | Act.  | Act.  | CR15/223 | Proj. | CR15/223 | Proj. |
| Total revenue <sup>1</sup>   | 94.8  | 126.6 | 146.4 | 151.0    | 151.0 | 173.5    | 176.4 |
| Tax revenue  | 80.9  | 107.6 | 125.2 | 128.6    | 128.6 | 147.9    | 151.2 |
| Income and profits   | 36.8  | 55.8  | 61.3  | 54.0     | 54.0  | 66.8     | 67.1  |
| <i>Of which:</i>   |       |       |       |          |       |          |       |
| Capital gain tax   | 5.0   | 18.6  | 16.2  | 0.0      | 0.0   | 0.0      | 0.0   |
| Others   | 31.7  | 37.3  | 45.1  | 54.0     | 54.0  | 66.8     | 67.1  |
| Goods and services <sup>1</sup>                                      | 33.3  | 38.3  | 48.3  | 55.8     | 55.8  | 62.5     | 63.6  |
| <i>Of which: on petroleum products</i>                               | 1.3   | 2.2   | 1.8   | 2.9      | 2.9   | 13.9     | 15.9  |
| International trade  | 7.6   | 10.0  | 11.4  | 12.2     | 12.2  | 13.9     | 15.9  |
| Other  | 3.2   | 3.5   | 4.1   | 6.6      | 6.6   | 4.7      | 4.7   |
| Nontax revenue   | 14.0  | 19.0  | 21.2  | 22.4     | 22.4  | 25.6     | 25.2  |
| Total expenditure and net lending                                    | 133.1 | 164.2 | 225.8 | 218.2    | 211.1 | 233.7    | 228.2 |
| Current expenditure  | 78.3  | 92.6  | 127.4 | 122.3    | 127.3 | 133.2    | 136.2 |
| Compensation to employees  | 41.5  | 49.5  | 59.8  | 64.4     | 64.4  | 71.1     | 71.5  |
| Goods and services <sup>1</sup>                                      | 15.1  | 20.4  | 41.1  | 26.0     | 25.4  | 25.0     | 31.0  |
| <i>Of which: Maritime security</i>                                   | ...   | ...   | 14.9  | 0.0      | 0.0   | 0.0      | ...   |
| Interest on public debt  | 4.1   | 4.0   | 5.4   | 8.2      | 8.4   | 10.1     | 12.5  |
| Domestic   | 2.9   | 2.2   | 2.8   | 4.2      | 4.2   | 4.4      | 7.2   |
| External   | 1.2   | 1.7   | 2.6   | 4.1      | 4.2   | 5.7      | 5.3   |
| Transfer payments  | 17.5  | 18.8  | 21.0  | 23.6     | 29.0  | 27.0     | 21.2  |
| Capital expenditure  | 50.4  | 61.6  | 80.3  | 84.6     | 78.1  | 87.1     | 83.8  |
| Domestically financed  | 24.7  | 33.6  | 44.0  | 43.7     | 35.7  | 44.5     | 41.3  |
| Externally financed  | 25.6  | 28.0  | 36.3  | 40.9     | 42.4  | 42.6     | 42.5  |
| Net lending  | 4.5   | 10.0  | 16.1  | 11.3     | 5.7   | 13.4     | 8.2   |
| Domestically financed  | -0.4  | -0.3  | 0.3   | 0.3      | 0.3   | 0.4      | 0.6   |
| Externally financed loans to public enterprises                      | 4.9   | 10.3  | 15.9  | 11.0     | 5.4   | 13.0     | 7.6   |
| Unallocated revenue (+)/expenditure (-) <sup>2</sup>                 | -0.4  | -0.5  | -1.9  | 0.0      | 0.0   | 0.0      | 0.0   |
| Domestic primary balance, before grants, above the line <sup>3</sup> | -4.1  | 4.2   | -21.8 | -7.0     | -3.9  | 5.6      | 10.8  |
| Overall balance, before grants                                       | -38.7 | -38.1 | -79.4 | -67.2    | -60.1 | -60.1    | -51.8 |
| Grants received  | 21.9  | 24.9  | 22.7  | 28.7     | 24.2  | 23.2     | 24.8  |
| Project support  | 13.3  | 18.5  | 14.7  | 20.7     | 16.3  | 16.5     | 15.8  |
| Budget support   | 8.7   | 6.4   | 8.0   | 8.0      | 7.9   | 6.8      | 9.0   |
| Overall balance, after grants  | -16.8 | -13.1 | -56.7 | -38.5    | -35.9 | -36.9    | -27.0 |
| Net external financing   | 13.8  | 27.1  | 47.0  | 33.6     | 32.3  | 36.6     | 28.5  |
| Project  | 15.4  | 29.6  | 50.2  | 38.1     | 37.2  | 41.8     | 37.2  |
| Project  | 6.7   | 12.2  | 16.1  | 20.3     | 26.2  | 26.1     | 26.8  |
| Nonproject support   | 8.7   | 17.5  | 18.5  | 17.9     | 11.1  | 15.7     | 10.4  |
| Other disbursements  | ...   | ...   | 15.6  | 0.0      | 0.0   | ...      | ...   |
| Cash amortization  | -1.6  | -2.5  | -3.2  | -4.5     | -4.9  | -5.1     | -8.7  |
| Net domestic financing   | 2.9   | -13.9 | 7.6   | 4.9      | 3.6   | 0.3      | -1.5  |
| <i>Memorandum items:</i>   |       |       |       |          |       |          |       |
| Overall balance excluding windfall receipt and one-off expenses      | -21.8 | -31.7 | -57.2 | -38.5    | -35.9 | -36.9    | -27.0 |
| Gross aid flows  | 37.4  | 47.4  | 36.5  | 58.9     | 56.2  | 57.2     | 55.0  |
| Budget support   | 12.5  | 13.6  | 9.7   | 14.9     | 13.6  | 9.4      | 11.8  |
| Nonbudget support  | 24.8  | 33.8  | 42.6  | 46.3     | 46.2  | 51.0     | 46.6  |
| Project support  | 20.0  | 30.7  | 30.9  | 40.9     | 42.4  | 42.6     | 42.5  |
| Concessional   | 20.0  | 30.7  | 15.1  | 38.7     | 38.8  | 39.4     | 39.1  |
| Nonconcessional  | 0.0   | 0.0   | 15.8  | 2.2      | 3.7   | 3.2      | 3.5   |
| Concessional loans to public enterprises                             | 4.9   | 3.1   | 11.7  | 5.4      | 3.8   | 8.4      | 4.1   |

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

<sup>1</sup> VAT presented on a net basis (collection minus requested VAT refunds).<sup>2</sup> Residual discrepancy between identified sources and uses of funds.<sup>3</sup> Revenue minus noninterest current expenditure minus locally financed capital expenditure and locally financed net lending.

**Table 3. Mozambique: Government Finances, 2012-20**  
(Percent of GDP)

|  | 2012 | 2013 | 2014  | 2015     |       | 2016     | 2017        | 2018 | 2019 | 2020 |      |
|--|------|------|-------|----------|-------|----------|-------------|------|------|------|------|
|  | Act. | Act. | Act.  | CR15/223 | Proj. | CR15/223 | Projections |      |      |      |      |
| Total revenue <sup>1</sup>   | 21.9 | 26.3 | 27.3  | 25.5     | 25.2  | 25.7     | 26.2        | 26.7 | 26.8 | 26.9 | 27.0 |
| Tax revenue  | 18.7 | 22.3 | 23.4  | 21.7     | 21.5  | 21.9     | 22.5        | 22.9 | 23.0 | 23.2 | 23.2 |
| Capital gain tax   | 1.2  | 3.9  | 3.0   | 0.0      | 0.0   |          | 0.0         | 0.0  | 0.0  | 0.0  | 0.0  |
| Nontax revenue   | 3.2  | 3.9  | 4.0   | 3.8      | 3.7   | 3.8      | 3.7         | 3.7  | 3.7  | 3.7  | 3.7  |
| Total expenditure and net lending                                    | 30.7 | 34.0 | 42.2  | 36.9     | 35.3  | 34.6     | 33.9        | 33.7 | 33.4 | 32.9 | 32.8 |
| Current expenditure  | 18.1 | 19.2 | 23.8  | 20.7     | 21.3  | 19.7     | 20.2        | 19.8 | 19.3 | 19.1 | 19.1 |
| Compensation to employees  | 9.6  | 10.3 | 11.2  | 10.9     | 10.8  | 10.5     | 10.6        | 10.4 | 10.0 | 9.8  | 9.7  |
| Goods and services <sup>1</sup>                                      | 3.5  | 4.2  | 7.7   | 4.4      | 4.3   | 3.7      | 4.6         | 4.4  | 4.3  | 4.3  | 4.3  |
| Of which: Maritime security  | 0.0  | 0.0  | 2.8   | 0.0      | 0.0   |          | 0.0         | 0.0  | 0.0  | 0.0  | 0.0  |
| Interest on public debt  | 1.0  | 0.8  | 1.0   | 1.4      | 1.4   | 1.5      | 1.9         | 1.8  | 1.8  | 1.9  | 1.8  |
| Transfer payments  | 4.0  | 3.9  | 3.9   | 4.0      | 4.8   | 4.0      | 3.2         | 3.2  | 3.2  | 3.2  | 3.2  |
| Capital expenditure  | 11.6 | 12.8 | 15.0  | 14.3     | 13.1  | 12.9     | 12.5        | 11.4 | 11.7 | 10.2 | 10.5 |
| Domestically financed  | 5.7  | 7.0  | 8.2   | 7.4      | 6.0   | 6.6      | 6.1         | 5.9  | 5.9  | 5.9  | 5.9  |
| Externally financed  | 5.9  | 5.8  | 6.8   | 6.9      | 7.1   | 6.3      | 6.3         | 5.5  | 5.8  | 4.3  | 4.6  |
| Net lending  | 1.0  | 2.1  | 3.0   | 1.9      | 0.9   | 2.0      | 1.2         | 2.5  | 2.4  | 3.7  | 3.2  |
| Domestically financed  | -0.1 | -0.1 | 0.1   | 0.1      | 0.1   | 0.1      | 0.1         | 0.1  | 0.1  | 0.1  | 0.1  |
| Externally financed loans to public enterprises                      | 1.1  | 2.1  | 3.0   | 1.9      | 0.9   | 1.9      | 1.1         | 2.5  | 2.4  | 3.6  | 3.1  |
| Unallocated revenue (+)/expenditure (-) <sup>2</sup>                 | -0.1 | -0.1 | -0.4  | 0.0      | 0.0   | 0.0      | 0.0         | 0.0  | 0.0  | 0.0  | 0.0  |
| Domestic primary balance, before grants, above the line <sup>3</sup> | -1.0 | 0.9  | -4.1  | -1.2     | -0.6  | 0.8      | 1.6         | 2.7  | 3.4  | 3.7  | 3.8  |
| Overall balance, before grants                                       | -8.9 | -7.9 | -14.8 | -11.4    | -10.0 | -8.9     | -7.7        | -7.1 | -6.6 | -6.1 | -5.8 |
| Grants received  | 5.1  | 5.2  | 4.2   | 4.9      | 4.0   | 3.4      | 3.7         | 2.8  | 2.3  | 1.9  | 1.6  |
| Project Support  | 3.1  | 3.8  | 2.7   | 3.5      | 2.7   | 2.4      | 2.3         | 1.6  | 1.3  | 1.1  | 0.9  |
| Investment projects  | 1.7  | 2.1  | 1.1   | 1.8      | 1.2   | 1.2      | 1.2         | 0.7  | 0.6  | 0.5  | 0.4  |
| Special programs   | 1.4  | 1.8  | 1.7   | 1.7      | 1.5   | 1.3      | 1.1         | 0.9  | 0.8  | 0.6  | 0.5  |
| Budget support   | 2.0  | 1.3  | 1.5   | 1.4      | 1.3   | 1.0      | 1.3         | 1.1  | 0.9  | 0.8  | 0.7  |
| Overall balance, after grants  | -3.9 | -2.7 | -10.6 | -6.5     | -6.0  | -5.5     | -4.0        | -4.3 | -4.3 | -4.2 | -4.2 |
| Net external financing   | 3.2  | 5.6  | 8.8   | 5.7      | 5.4   | 5.4      | 4.2         | 5.2  | 5.7  | 5.7  | 5.8  |
| Disbursements  | 3.6  | 6.1  | 9.4   | 6.5      | 6.2   | 6.2      | 5.5         | 6.6  | 7.1  | 7.1  | 7.0  |
| Project  | 1.6  | 2.5  | 3.0   | 3.4      | 4.4   | 3.9      | 4.0         | 3.8  | 4.4  | 3.2  | 3.7  |
| Nonproject support   | 2.0  | 3.6  | 3.4   | 3.0      | 1.8   | 2.3      | 1.5         | 2.8  | 2.6  | 3.8  | 3.3  |
| Other disbursement   | 0.0  | 0.0  | 2.9   | 0.0      | 0.0   | ...      | ...         | ...  | ...  | ...  | ...  |
| Cash amortization  | -0.4 | -0.5 | -0.6  | -0.8     | -0.8  | -0.8     | -1.3        | -1.4 | -1.4 | -1.4 | -1.3 |
| Net domestic financing   | 0.7  | -2.9 | 1.4   | 0.8      | 0.6   | 0.0      | -0.2        | -0.9 | -1.3 | -1.5 | -1.5 |
| <i>Memorandum items:</i>   |      |      |       |          |       |          |             |      |      |      |      |
| Overall balance excluding windfall receipt and one-off expens        | -5.0 | -6.7 | -10.7 | -6.5     | -6.0  |          | ...         | ...  | ...  | ...  | ...  |
| Gross aid flows  | 8.2  | 10.1 | 6.8   | 10.0     | 9.4   | 8.5      | 8.2         | 7.3  | 7.9  | 6.9  | 7.3  |
| Budget support   | 2.9  | 2.9  | 1.8   | 2.5      | 2.3   | 1.4      | 1.8         | 1.4  | 1.2  | 1.0  | 0.8  |
| Nonbudget support  | 5.3  | 7.2  | 8.0   | 7.8      | 7.7   | 7.5      | 6.9         | 6.7  | 7.8  | 6.6  |      |
| Project support  | 4.6  | 6.5  | 5.8   | 6.9      | 7.1   | 6.3      | 6.3         | 5.5  | 5.8  | 4.3  | 4.6  |
| Nominal GDP  | 433  | 470  | 536   | 591      | 598   | 676      | 673         | 762  | 871  | 990  | 1124 |

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

<sup>1</sup> VAT presented on a net basis (collection minus requested VAT refunds).

<sup>2</sup> Residual discrepancy between identified sources and uses of funds.

<sup>3</sup> Revenue minus noninterest current expenditure minus locally financed capital expenditure and locally financed net lending.

Table 4. Mozambique: Monetary Survey, 2012-16

(Billions of Meticaís, unless otherwise specified)

|   | 2012  | 2013  | 2014  | 2015  |           |       |           |           |       | 2016      |       |       |           |       |       |
|---|-------|-------|-------|-------|-----------|-------|-----------|-----------|-------|-----------|-------|-------|-----------|-------|-------|
|   | Act.  | Act.  | Act.  | Q1    | Q2        | Q3    | Q4        | CR 15/223 | Est.  | CR 15/223 | Proj. | Q1    | Q2        | Q3    | Q4    |
|   |       |       |       | Act.  | CR 15/223 | Act.  | CR 15/223 |           |       |           |       | Est.  | CR 15/223 | Proj. | Proj. |
| <b>Bank of Mozambique</b>                       |       |       |       |       |           |       |           |           |       |           |       |       |           |       |       |
| Net foreign assets                              | 73.1  | 85.7  | 91.5  | 86.8  | 83.8      | 95.7  | 86.8      | 93.0      | 95.5  | 84.0      | 81.1  | 85.5  | 88.5      | 96.0  |       |
| (US\$ billions)                                 | 2.5   | 2.8   | 2.7   | 2.3   | 2.4       | 2.5   | 2.5       | 2.2       | 2.7   | 1.9       | 1.8   | 1.9   | 1.9       | 2.1   |       |
| Net international reserves                      | 77.5  | 90.1  | 96.8  | 92.8  | 89.3      | 101.4 | 92.8      | 99.3      | 101.1 | 91.2      | 88.6  | 92.3  | 95.3      | 103.3 |       |
| (US\$ billions)                                 | 2.6   | 3.0   | 2.9   | 2.5   | 2.6       | 2.6   | 2.7       | 2.3       | 2.9   | 2.0       | 1.9   | 2.0   | 2.1       | 2.3   |       |
| Net domestic assets                             | -32.0 | -38.1 | -34.2 | -32.4 | -24.6     | -37.2 | -24.7     | -31.0     | -28.8 | -13.8     | -14.6 | -18.5 | -18.3     | -17.4 |       |
| Credit to government (net)                      | -27.6 | -45.7 | -51.0 | -50.8 | -52.5     | -50.8 | -53.4     | -40.8     | -50.7 | -51.8     | -53.1 | -57.8 | -52.9     | -53.3 |       |
| Credit to banks (net)                           | -12.7 | -10.0 | -4.4  | -0.6  | 21.6      | -4.6  | 18.0      | -6.4      | 4.6   | 19.8      | 15.7  | 18.6  | 16.4      | 15.8  |       |
| Credit to the economy                           | 1.3   | 1.3   | 1.7   | 1.6   | 1.7       | 1.6   | 1.5       | 1.7       | 1.7   | 1.7       | 1.6   | 1.6   | 1.7       | 1.7   |       |
| Other items (net; assets +)                     | 6.9   | 16.2  | 19.4  | 17.4  | 4.6       | 16.7  | 9.3       | 14.6      | 15.7  | 16.5      | 21.3  | 19.1  | 16.5      | 18.5  |       |
| Reserve money                                   | 41.1  | 47.5  | 57.3  | 54.4  | 59.2      | 58.5  | 62.1      | 62.0      | 66.7  | 70.2      | 66.6  | 67.0  | 70.2      | 78.7  |       |
| Currency in circulation                         | 26.2  | 30.4  | 36.3  | 32.7  | 37.5      | 35.0  | 39.5      | 36.3      | 42.5  | 36.5      | 32.5  | 32.6  | 34.2      | 40.8  |       |
| Bank deposits in BM                             | 14.8  | 17.2  | 21.0  | 21.7  | 21.7      | 23.5  | 22.6      | 25.7      | 24.2  | 33.7      | 34.1  | 34.3  | 36.0      | 37.8  |       |
| <b>Commercial Banks</b>                         |       |       |       |       |           |       |           |           |       |           |       |       |           |       |       |
| Net foreign assets                              | 21.3  | 14.3  | 13.3  | 18.0  | 18.4      | 13.1  | 15.3      | 20.9      | 21.6  | 13.0      | 24.2  | 14.5  | 28.7      | 22.0  |       |
| (Millions of U.S. dollars)                      | 0.7   | 0.5   | 0.4   | 0.5   | 0.5       | 0.3   | 0.4       | 0.5       | 0.6   | 0.3       | 0.5   | 0.3   | 0.6       | 0.5   |       |
| Net domestic assets                             | 143.9 | 178.1 | 222.2 | 222.0 | 227.0     | 239.7 | 231.0     | 247.6     | 256.5 | 279.0     | 268.5 | 283.0 | 282.5     | 302.5 |       |
| Banks' reserves                                 | 22.2  | 24.3  | 32.2  | 30.5  | 29.8      | 34.1  | 31.5      | 31.5      | 35.1  | 41.7      | 42.3  | 42.3  | 43.9      | 43.3  |       |
| Credit to BM (net)                              | 12.3  | 10.1  | 2.5   | 1.0   | -21.6     | 0.9   | -18.0     | 7.5       | -4.6  | -19.8     | -15.7 | -18.6 | -16.4     | -15.8 |       |
| Credit to government (net)                      | 27.5  | 31.7  | 42.1  | 39.3  | 28.6      | 50.8  | 31.0      | 52.1      | 37.0  | 55.0      | 45.6  | 49.3  | 41.4      | 45.2  |       |
| Credit to the economy                           | 116.5 | 150.3 | 193.0 | 202.2 | 209.1     | 207.5 | 207.4     | 214.3     | 227.0 | 231.6     | 238.6 | 240.7 | 244.4     | 260.3 |       |
| Other items (net; assets +)                     | -34.5 | -38.3 | -47.6 | -51.0 | -18.8     | -53.7 | -21.0     | -57.8     | -38.0 | -29.5     | -42.4 | -30.7 | -30.8     | -30.5 |       |
| Deposits  | 165.3 | 192.4 | 235.5 | 240.0 | 245.5     | 252.7 | 246.3     | 268.5     | 278.1 | 292.0     | 292.7 | 297.5 | 311.2     | 324.5 |       |
| Demand and savings deposits                     | 108.4 | 122.0 | 152.7 | 152.8 | 156.8     | 156.5 | 156.4     | 164.7     | 175.8 | 186.1     | 182.3 | 192.9 | 200.9     | 204.9 |       |
| Time deposits                                   | 56.8  | 70.4  | 82.9  | 87.2  | 88.6      | 96.2  | 89.9      | 103.8     | 102.3 | 105.9     | 110.4 | 104.6 | 110.3     | 119.7 |       |
| <b>Monetary Survey</b>                          |       |       |       |       |           |       |           |           |       |           |       |       |           |       |       |
| Net foreign assets                              | 94.4  | 100.0 | 104.8 | 104.8 | 102.2     | 108.7 | 102.1     | 113.9     | 117.1 | 97.0      | 105.3 | 100.0 | 117.3     | 118.1 |       |
| (US\$ billions)                                 | 3.2   | 3.3   | 3.1   | 2.8   | 2.9       | 2.8   | 2.9       | 2.7       | 3.3   | 2.2       | 2.3   | 2.2   | 2.6       | 2.6   |       |
| Net domestic assets                             | 91.6  | 116.5 | 159.7 | 160.7 | 172.6     | 172.5 | 174.8     | 184.8     | 192.6 | 223.4     | 211.6 | 222.3 | 220.2     | 241.8 |       |
| Domestic credit                                 | 117.7 | 137.6 | 185.8 | 192.3 | 186.8     | 209.1 | 186.5     | 227.3     | 215.0 | 236.4     | 232.6 | 233.8 | 234.5     | 253.8 |       |
| Credit to government (net)                      | -0.1  | -14.0 | -8.9  | -11.5 | -23.9     | 0.0   | -22.4     | 11.3      | -13.7 | 3.2       | -7.6  | -8.5  | -11.5     | -8.2  |       |
| Credit to the economy                           | 117.8 | 151.7 | 194.7 | 203.8 | 210.7     | 209.1 | 208.9     | 216.0     | 228.7 | 233.3     | 240.2 | 242.3 | 246.0     | 262.0 |       |
| Cred. economy in foreign currency               | 28.8  | 34.4  | 39.5  | 39.7  | 43.6      | 43.6  | 46.0      | 42.5      | 46.6  | 47.5      | 51.0  | 49.4  | 53.2      | 52.5  |       |
| Other items (net; assets +)                     | -26.1 | -21.2 | -26.1 | -31.6 | -14.2     | -36.6 | -11.7     | -42.5     | -22.4 | -13.0     | -21.1 | -11.6 | -14.3     | -12.0 |       |
| Money and quasi money (M3)                      | 186.0 | 216.4 | 264.5 | 265.5 | 274.9     | 281.2 | 276.9     | 298.7     | 309.7 | 320.5     | 316.9 | 322.3 | 337.5     | 359.9 |       |
| Foreign currency deposits                       | 53.3  | 55.6  | 59.7  | 64.7  | 66.9      | 68.2  | 62.4      | 74.7      | 69.9  | 75.1      | 82.0  | 79.4  | 85.3      | 85.4  |       |
| (US\$ billions)                                 | 1.8   | 1.8   | 1.8   | 1.7   | 1.9       | 1.7   | 1.8       | 1.7       | 2.0   | 1.7       | 1.8   | 1.7   | 1.9       | 1.9   |       |
| M2  | 132.7 | 160.8 | 204.8 | 200.7 | 213.2     | 213.0 | 238.8     | 224.0     | 272.6 | 245.4     | 234.9 | 242.9 | 252.2     | 274.5 |       |
| Currency outside banks                          | 19.7  | 22.7  | 27.3  | 24.5  | 29.4      | 27.1  | 30.6      | 28.2      | 31.6  | 28.5      | 24.2  | 24.7  | 26.3      | 35.3  |       |
| Domestic currency deposits                      | 113.1 | 138.1 | 177.5 | 176.3 | 183.8     | 185.9 | 208.2     | 195.8     | 241.0 | 216.9     | 210.6 | 218.1 | 225.9     | 239.1 |       |
| <b>Memorandum Items</b>                         |       |       |       |       |           |       |           |           |       |           |       |       |           |       |       |
| Avg daily reserve money in 3rd month of quarter | 40.3  | 46.5  | 57.0  | 54.3  | 58.2      | 56.6  | 61.9      | 61.5      | 64.4  | 69.8      | 66.4  | 64.8  | 69.6      | 78.2  |       |
| 12-month percent change                         | 21.1  | 15.4  | 22.6  | 20.7  | 19.0      | 15.6  | 17.5      | 16.6      | 16.5  | 22.6      | 22.3  | 14.6  | 13.2      | 12.0  |       |
| NCG stock (prog def.)                           | -9.8  | -27.2 | -23.1 | -25.6 | -25.9     | -15.1 | -26.9     | -4.7      | -18.2 | -11.1     | -12.1 | -13.0 | -16.0     | -12.6 |       |
| NCG flow (prog def.) cum from end-year          | 2.9   | -17.4 | 4.1   | -2.5  | -2.8      | 8.0   | -3.8      | 18.4      | 4.9   | 12.0      | -0.9  | -1.9  | -4.9      | -1.5  |       |
| 12-month percent change                         |       |       |       |       |           |       |           |           |       |           |       |       |           |       |       |
| Reserve money                                   | 19.7  | 15.7  | 20.5  | 20.2  | 19.0      | 17.5  | 17.5      | 17.4      | 16.5  | 22.6      | 22.3  | 14.6  | 13.2      | 12.0  |       |
| Currency in circulation                         | 19.8  | 15.7  | 19.7  | 20.0  | 20.0      | 11.9  | 18.0      | 8.5       | 17.1  | 0.5       | -0.7  | -6.8  | -5.8      | 11.9  |       |
| Bank reserves                                   | 19.6  | 15.8  | 22.0  | 20.6  | 17.3      | 27.1  | 16.6      | 32.7      | 15.5  | 60.9      | 57.1  | 46.4  | 40.0      | 12.1  |       |
| M2  | 25.6  | 21.2  | 27.3  | 25.3  | 20.0      | 22.9  | 18.0      | 23.3      | 17.1  | 19.8      | 17.0  | 14.0  | 12.6      | 11.9  |       |
| Domestic deposits                               | 28.1  | 22.2  | 28.5  | 26.9  | 20.4      | 25.4  | 18.4      | 26.1      | 17.4  | 22.2      | 19.5  | 17.3  | 15.4      | 10.3  |       |
| M3  | 29.4  | 16.3  | 22.2  | 22.7  | 20.0      | 22.8  | 17.6      | 26.9      | 17.1  | 21.2      | 19.4  | 14.6  | 13.0      | 12.3  |       |
| Credit to the economy                           | 19.9  | 28.7  | 28.4  | 29.0  | 24.1      | 23.2  | 19.4      | 23.5      | 17.5  | 19.8      | 17.9  | 15.9  | 13.9      | 12.3  |       |
| Money multiplier (M2/reserve money)             | 3.23  | 3.38  | 3.58  | 3.69  | 3.51      | 3.64  | 3.45      | 3.61      | 3.59  | 3.49      | 3.53  | 3.63  | 3.59      | 3.49  |       |
| Velocity (GDP/M2)                               | 3.26  | 3.00  | 2.61  | ...   | ...       | ...   | ...       | ...       | 2.47  | 2.44      | 2.86  | 2.77  | 2.67      | 2.45  |       |
| Nominal GDP                                     | 433   | 482   | 536   | 598   | 591       | 598   | 591       | 598       | 591   | 598       | 673   | 673   | 673       | 673   |       |
| Nominal GDP growth                              | 13.5  | 11.3  | 11.1  | 11.7  | 12.5      | 11.7  | 12.5      | 11.7      | 12.5  | 11.7      | 12.5  | 12.5  | 12.5      | 12.5  |       |
| Policy lending rate (end-of-period)             | 9.5   | 8.3   | 7.5   | 7.5   | ...       | 7.5   | ...       | 7.5       | ...   | ...       | ...   | ...   | ...       | ...   |       |
| T-bill 91 days rate                             | 2.6   | 5.2   | 5.4   | 5.5   | ...       | 5.6   | ...       | ...       | ...   | ...       | ...   | ...   | ...       | ...   |       |

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

**Table 5. Mozambique: Balance of Payments, 2012-20**

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

|   | 2012   | 2013   | 2014   | 2015      |        | 2016      |        | 2017        | 2018    | 2019    | 2020    |
|---|--------|--------|--------|-----------|--------|-----------|--------|-------------|---------|---------|---------|
|   | Act.   | Act.   | Est.   | CR/15/223 | Proj.  | CR/15/223 | Proj.  | Projections |         |         |         |
| <b>Current account balance</b>                                | -6,790 | -6,253 | -5,787 | -6,481    | -4,597 | -8,016    | -4,901 | -9,104      | -13,473 | -16,548 | -20,594 |
| <i>Trade balance for goods</i>                                | -4,048 | -4,357 | -4,025 | -4,531    | -3,532 | -5,551    | -4,219 | -7,070      | -9,846  | -11,641 | -13,836 |
| <i>Of which: Megaprojects</i>                                 | 30     | 267    | 953    | 27        | 1,384  | -830      | 11     | -2,747      | -5,228  | -6,672  | -8,271  |
| Exports, f.o.b.   | 3,856  | 4,123  | 3,927  | 4,031     | 3,557  | 4,501     | 3,643  | 4,107       | 4,908   | 5,743   | 6,487   |
| Megaprojects  | 2,173  | 2,201  | 2,440  | 2,544     | 2,186  | 2,724     | 2,069  | 2,340       | 2,886   | 3,491   | 3,926   |
| Other   | 1,682  | 1,922  | 1,487  | 1,487     | 1,372  | 1,777     | 1,574  | 1,768       | 2,021   | 2,252   | 2,561   |
| Imports, f.o.b.   | 7,903  | 8,480  | 7,952  | 8,562     | 7,090  | 10,052    | 7,863  | 11,178      | 14,754  | 17,384  | 20,323  |
| Megaprojects  | 2,143  | 1,934  | 1,487  | 2,516     | 802    | 3,554     | 2,058  | 5,087       | 8,114   | 10,163  | 12,197  |
| Other   | 5,760  | 6,546  | 6,465  | 6,046     | 6,288  | 6,498     | 5,805  | 6,091       | 6,640   | 7,221   | 8,126   |
| <i>Services (net)</i>   | -3,706 | -3,259 | -2,932 | -2,546    | -1,699 | -2,762    | -1,231 | -2,297      | -3,662  | -4,758  | -5,699  |
| <i>Primary income (net)</i>                                   | -75    | -59    | -202   | -246      | -232   | -459      | -344   | -574        | -807    | -997    | -1,930  |
| <i>Of which: Interest on public debt (net)</i>                | -40    | -49    | -76    | ...       | -104   | ...       | -101   | -114        | -136    | -160    | -186    |
| <i>Of which: Megaprojects (Net Interest and Dividends)</i>    | -48    | -42    | -46    | 0         | -50    | -70       | -82    | -218        | -338    | -437    | -1,292  |
| <i>Secondary income (net)</i>                                 | 1,039  | 1,421  | 1,372  | 842       | 867    | 755       | 894    | 837         | 843     | 848     | 871     |
| <i>Of which: External grants</i>                              | 538    | 460    | 568    | 551       | 441    | 429       | 442    | 356         | 331     | 308     | 286     |
| <b>Capital account balance</b>                                | 490    | 423    | 372    | 499       | 424    | 478       | 368    | 378         | 390     | 400     | 420     |
| <b>Financial account balance</b>                              | -6,644 | -6,202 | -5,279 | -6,022    | -3,350 | -7,955    | -4,790 | -9,245      | -13,503 | -16,576 | -20,896 |
| Net foreign direct investment                                 | -5,626 | -6,175 | -4,902 | -4,048    | -2,880 | -4,706    | -3,188 | -7,376      | -11,407 | -13,300 | -4,491  |
| Loans (net) by the general government                         | -544   | -1,056 | -1,398 | -942      | -925   | -1,055    | -754   | -956        | -1,180  | -1,326  | -1,466  |
| Loans (net) by the nonfin private sector <sup>1</sup>         | -32    | -125   | -76    | -412      | -298   | -1,447    | -1,538 | -1,638      | -1,694  | -2,768  | -15,803 |
| Other <sup>1</sup>  | -441   | 1,154  | 1,097  | -621      | 752    | -748      | 690    | 726         | 779     | 818     | 864     |
| <b>Net errors and omissions</b>                               | 32     | 22     | 26     | 0         | 0      | 0         | 0      | 0           | 0       | 0       | 0       |
| <b>Overall balance</b>  | 375    | 393    | -110   | 40        | -823   | 418       | 258    | 520         | 420     | 429     | 722     |
| <b>Financing</b>  | 375    | 393    | -120   | -40       | 703    | -418      | -368   | -575        | -420    | -429    | -722    |
| Reserve assets (- = increase)                                 | 378    | 396    | -117   | -7        | 735    | -384      | -335   | -542        | -387    | -396    | -720    |
| Net use of credit   | -2     | -3     | -3     | -33       | -32    | -34       | -33    | -33         | -32     | -33     | -2      |
| <i>Of which: Repayments to the Fund (-)</i>                   | -2     | -3     | -3     | -33       | -32    | -34       | -33    | -33         | -32     | -33     | -2      |
| Exceptional financing   | 0      | 0      | 0      | 0         | 0      | 0         | 0      | 0           | 0       | 0       | 0       |
| <b>Financing Gap</b>  | 0      | 0      | 0      | 0         | 120    | 0         | 110    | 55          | 0       | 0       | 0       |
| Financing from IMF (SCF disbursements)                        | 0      | 0      | 0      | 0         | 120    | 0         | 110    | 55          | 0       | 0       | 0       |
| <i>Memorandum items:</i>                                      |        |        |        |           |        |           |        |             |         |         |         |
| Current account balance (percent of GDP)                      | -44.7  | -39.1  | -34.1  | -38.2     | -30.2  | -42.1     | -33.1  | -55.4       | -73.2   | -80.8   | -90.4   |
| Excluding external grants                                     | -48.3  | -41.9  | -37.4  | -43.1     | -33.1  | -46.1     | -36.1  | -57.6       | -75.0   | -82.3   | -91.7   |
| Excluding Mega-Projects                                       | -23.9  | -24.7  | -25.1  | -28.4     | -31.5  | -26.1     | -26.5  | -25.2       | -25.0   | -24.7   | -25.5   |
| Excluding Mega-Projects and indirect MP imports <sup>3/</sup> | -8.1   | -10.2  | -13.5  | ...       | -13.9  | ...       | -9.8   | -9.7        | -9.5    | -9.6    | -9.8    |
| Net foreign assets  | 2,457  | 2,849  | 2,723  | 2,762     | 1,867  | 3,180     | 2,092  | 2,579       | 2,966   | 3,362   | 4,082   |
| Net international reserves <sup>4/</sup>                      | 2,604  | 2,995  | 2,881  | 2,889     | 2,026  | 3,273     | 2,251  | 2,737       | 3,125   | 3,806   | 4,471   |
| Gross international reserves <sup>2</sup>                     | 2,798  | 3,191  | 3,071  | 3,079     | 2,467  | 3,463     | 2,768  | 3,277       | 3,632   | 3,995   | 4,714   |
| Months of projected imports of goods and nonfactor services   | 2.7    | 3.3    | 3.9    | 2.7       | 3.0    | 2.8       | 2.3    | 2.0         | 1.9     | 1.8     | 1.9     |
| Months of projected G&S imports (excl. megaproject import)    | 4.2    | 4.9    | 4.8    | 4.7       | 4.2    | 4.8       | 4.5    | 4.9         | 5.0     | 4.9     | 5.2     |
| Percent of broad money (M2)                                   | 62.7   | 59.7   | 50.4   | 44.9      | 45.2   | 44.9      | 46.3   | 48.5        | 47.5    | 46.3    | 48.3    |

Sources: Data from Government of Mozambique and projections by IMF s

<sup>1</sup> Other financial account flows now 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. This included only net portfolio investment and other investment assets in the BPM5 concept used in CR/15/223. Thereby, the figure in the nonfinancial private sector net foreign loans line also varies from that reported for nonfinancial private sector net foreign borrowing in CR/15/223.

<sup>2</sup> The ratio to short term debt is not presented due to availability of the data.

<sup>3/</sup> Also excludes imports by domestic firms that are used to supply megaprojects (estimated).

<sup>4/</sup> NIR do not include any disbursements by the IMF.



**Table 6. Mozambique: Financial Soundness Indicators for Banking Sector, 2009-15**

|   | 2009  | 2010  | 2011  | 2012  | 2013  | 2014  | Sept 2015 |
|---|-------|-------|-------|-------|-------|-------|-----------|
| <b>Capital adequacy</b>                                       |       |       |       |       |       |       |           |
| Regulatory capital to risk-weighted assets                    | 15.1  | 14.4  | 17.1  | 17.9  | 16.9  | 15.1  | 16.5      |
| Regulatory Tier I capital to risk-weighted assets             | 13.0  | 13.7  | 16.1  | 16.9  | 16.0  | 13.6  | 15.0      |
| Capital (net worth) to assets                                 | 7.7   | 8.0   | 9.0   | 9.5   | 9.5   | 9.6   | 9.8       |
| <b>Asset composition and quality</b>                          |       |       |       |       |       |       |           |
| Foreign exchange loans to total loans                         | 32.4  | 29.5  | 25.1  | 28.1  | 21.9  | 22.2  | 22.6      |
| Nonperforming loans to gross loans <sup>1</sup>               | 1.8   | 1.9   | 2.6   | 3.2   | 2.3   | 3.2   | 4.3       |
| Nonperforming loans net of provisions to capital <sup>1</sup> | 5.9   | 5.6   | 6.6   | 6.8   | 4.5   | 3.8   | ...       |
| <b>Earnings and profitability</b>                             |       |       |       |       |       |       |           |
| Return on assets  | 3.0   | 2.6   | 2.5   | 1.9   | 2.0   | 2.1   | 2.3       |
| Return on equity  | 36.6  | 32.9  | 26.5  | 19.6  | 21.0  | 21.6  | 23.4      |
| Interest margin to gross income                               | 55.7  | 59.4  | 64.9  | 58.9  | 55.6  | 55.4  | 52.5      |
| Noninterest expenses to gross income                          | 58.4  | 59.7  | 61.3  | 66.1  | 65.3  | 62.4  | 61.3      |
| Personnel expenses to noninterest expenses                    | 45.9  | 45.5  | 47.1  | 49.1  | 47.6  | 47.1  | 47.5      |
| Trading and fee income to gross income                        | 44.3  | 23.8  | 17.2  | 19.5  | 17.0  | 20.8  | 26.9      |
| <b>Funding and liquidity</b>                                  |       |       |       |       |       |       |           |
| Liquid assets to total assets <sup>2</sup>                    | 27.9  | 22.4  | 27.8  | 33.4  | 30.7  | 28.2  | 31.1      |
| Customer deposits to total (non-interbank) loans              | 138.2 | 131.2 | 131.6 | 143.8 | 132.5 | 127.0 | 125.2     |

Source: Bank of Mozambique (BM).

<sup>1</sup> Prior to 2014, nonperforming loans are defined according to Mozambican accounting standards (they include only part of the past-due loans).

<sup>2</sup> Includes deposits at parent banks.

**Table 7. Mozambique: External Financing Needs and Sources, 2012-20**

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

|   | 2012         | 2013         | 2014         | 2015         | 2016         | 2017          | 2018          | 2019          | 2020          |
|---|--------------|--------------|--------------|--------------|--------------|---------------|---------------|---------------|---------------|
|   | Act.         | Act.         | Est.         | Projections  |              |               |               |               |               |
| <b>Financing requirements</b>                             | <b>7,817</b> | <b>7,218</b> | <b>6,908</b> | <b>5,671</b> | <b>6,077</b> | <b>10,299</b> | <b>14,695</b> | <b>17,798</b> | <b>21,862</b> |
| Current account deficit excl. grants                      | 7,328        | 6,713        | 6,355        | 5,038        | 5,342        | 9,459         | 13,803        | 16,855        | 20,880        |
| <i>of which: Public sector interest payments 1/</i>       | 40           | 49           | 76           | 104          | 101          | 114           | 136           | 160           | 186           |
| <i>of which: Private sector interest payments</i>         | 63           | 52           | 62           | 69           | 117          | 277           | 426           | 546           | 1,410         |
| Public sector loan amortization                           | 57           | 72           | 102          | 178          | 247          | 290           | 301           | 322           | 353           |
| <i>of which: EMATUM Bond amortization</i>                 | 0            | 0            | 0            | 77           | 153          | 153           | 153           | 153           | 162           |
| Non-financial private sector loan amortizations           | 429          | 430          | 449          | 423          | 454          | 516           | 558           | 588           | 627           |
| Interest and amortization payments on existing Fund loans | 2            | 3            | 3            | 32           | 33           | 33            | 32            | 33            | 2             |
| <b>Financing sources</b>                                  | <b>7,817</b> | <b>7,218</b> | <b>6,908</b> | <b>5,551</b> | <b>5,967</b> | <b>10,244</b> | <b>14,695</b> | <b>17,798</b> | <b>21,862</b> |
| Capital account balance                                   | 490          | 423          | 372          | 424          | 368          | 378           | 390           | 400           | 420           |
| Net foreign direct investment                             | 5,626        | 6,175        | 4,902        | 2,880        | 3,188        | 7,376         | 11,407        | 13,300        | 4,491         |
| Public sector loan disbursements                          | 603          | 1,130        | 1,514        | 1,026        | 849          | 1,094         | 1,329         | 1,495         | 1,658         |
| Public sector grants                                      | 538          | 460          | 568          | 441          | 442          | 356           | 331           | 308           | 286           |
| Non-financial private sector loan disbursements           | 459          | 576          | 489          | 711          | 1,983        | 2,146         | 2,244         | 3,347         | 16,420        |
| Other capital flows (net)                                 | 474          | -1,155       | -1,059       | -666         | -529         | -564          | -617          | -655          | -692          |
| Change in reserves (+ decrease)                           | -373         | -390         | 123          | 735          | -335         | -542          | -387          | -396          | -720          |
| <b>Financing Gap</b>                                      | <b>0</b>     | <b>0</b>     | <b>0</b>     | <b>120</b>   | <b>110</b>   | <b>55</b>     | <b>0</b>      | <b>0</b>      | <b>0</b>      |
| Financing from IMF (SCF disbursements)                    | 0            | 0            | 0            | 120          | 110          | 55            | 0             | 0             | 0             |

Source: Mozambican authorities and IMF staff estimates and projections.

1/ Includes payments on EMATUM bond but excludes interest on Fund loans.

**Table 8. Mozambique: Summary Table of Projected External Borrowing Program**  
December 1, 2015 to December 31, 2016

| PPG external debt                      | Volume of new debt in 2016 |            | PV of new debt in 2016<br>(program purposes) |            |
|--|----------------------------|------------|--|------------|
|  | USD million                | Percent    | USD million                                  | Percent    |
| <b>By sources of debt financing</b>    | <b>403.3</b>               | <b>100</b> | <b>179.0</b>                                 | <b>100</b> |
| <b>Concessional debt, of which</b>     | <b>319.5</b>               | <b>79</b>  | <b>106.8</b>                                 | <b>60</b>  |
| Multilateral debt                      | 230.8                      | 57         | 82.3   | 46         |
| Bilateral debt                         | 88.7                       | 22         | 24.5   | 14         |
| Other                                  | 0.0                        | 0          | 0.0  | 0          |
| <b>Non-concessional debt, of which</b> | <b>83.8</b>                | <b>21</b>  | <b>72.2</b>                                  | <b>40</b>  |
| Semi-concessional                      | 83.8                       | 21         | 72.2   | 40         |
| Commercial terms                       | 0.0                        | 0          | 0.0  | 0          |
| <b>By Creditor Type</b>                | <b>403.3</b>               | <b>100</b> | <b>179.0</b>                                 | <b>100</b> |
| Multilateral                           | 261.2                      | 65         | 105.8  | 59         |
| Bilateral - Paris Club                 | 53.4                       | 13         | 48.7   | 27         |
| Bilateral - Non-Paris Club             | 88.7                       | 22         | 24.5   | 14         |
| Other                                  | 0.0                        | 0          | 0.0  | 0          |
| <b>Uses of debt financing</b>          | <b>403.3</b>               | <b>100</b> | <b>179.0</b>                                 | <b>100</b> |
| Infrastructure                         | 230.5                      | 57         | 124.2  | 69         |
| Social Spending                        | 0.0                        | 0          | 0.0  | 0          |
| Budget Financing                       | 84.1                       | 21         | 30.3   | 17         |
| Other                                  | 88.7                       | 22.0       | 24.5   | 13.7       |
| <b>Memo Items</b>                      |                            |            |  |            |
| <b>Indicative projections</b>          |                            |            |  |            |
| Year 2017                              | <b>997.6</b>               |            | <b>459.4</b>                                 |            |
| Year 2018                              | <b>968.6</b>               |            | <b>653.1</b>                                 |            |

Sources: Mozambique authorities and IMF staff projections.

**Table 9. Mozambique: Type of New External Debt, USD million**  
**December 1, 2015 to December 31, 2016**

| <b><i>By the type of interest rate</i></b> |       |
|--|-------|
| Fixed Interest Rate                        | 372.9 |
| Variable Interest Rate                     | 0.0   |
| Unconventional Loans                       | 30.4  |
| <b><i>By currency</i></b>                  |       |
| USD denominated loans                      | 210.9 |
| Loans denominated in other currency        | 192.4 |

Sources: Mozambique authorities and IMF staff projections.

**Table 10. Mozambique: Disbursements and Timing of Reviews Under the SCF Arrangement<sup>1</sup>**

| Date of Availability <sup>2</sup>       | Conditions   | Amount (SDR millions) | Percent of quota | Amount (\$m) <sup>3</sup> |
|---|--|-----------------------|------------------|---------------------------|
| Upon Board Approval (December 18, 2015) | Board approval of the arrangement  | 85.2                  | 75               | 120                       |
| March 31, 2016                          | Observance of end-december performance criteria and structural benchmarks and completion of first SCF arrangement review (sixth PSI review) <sup>4</sup> | 39.76                 | 35               | 55                        |
| September 30, 2016                      | Observance of end-june performance criteria and structural benchmarks and completion of second SCF arrangement review                                    | 39.76                 | 35               | 55                        |
| March 31, 2017                          | Observance of end-december performance criteria and structural benchmarks and completion of third SCF arrangement review                                 | 39.76                 | 35               | 55                        |
| Total                                   |  | 204.48                | 180              | 285                       |

<sup>1</sup> Mozambique's quota is SDR 113.6 million.

<sup>2</sup> Financing would become available based on the completion of the associated SCF arrangement review, which would be conducted at the time as the PSI review.

<sup>3</sup> At an assumed exchange rate of \$1 = SDR 0.717

<sup>4</sup> Mozambique's PSI arrangement expires on June 23, 2016 and the SCF arrangement Expires on June 17, 2017.

Table 11. Mozambique: Indicators of Capacity to Repay the Fund

|  | Projections |        |        |        |        |        |        |        |       |       |       |      |
|--|-------------|--------|--------|--------|--------|--------|--------|--------|-------|-------|-------|------|
|  | 2015        | 2016   | 2017   | 2018   | 2019   | 2020   | 2021   | 2022   | 2023  | 2024  | 2025  |      |
| <b>Fund obligations based on existing credit</b><br>(in millions of SDRs)                                    |             |        |        |        |        |        |        |        |       |       |       |      |
| Principal  | 3.00        | 23.70  | 23.21  | 22.72  | 22.72  | 1.42   | 0.00   | 0.00   | 0.00  | 0.00  | 0.00  | 0.00 |
| Charges and interest   | 0.00        | 0.02   | 0.15   | 0.10   | 0.04   | 0.02   | 0.02   | 0.02   | 0.02  | 0.02  | 0.02  | 0.02 |
| <b>Obligations to the Fund based on existing and prospective credit<sup>1</sup></b><br>(in millions of SDRs) |             |        |        |        |        |        |        |        |       |       |       |      |
| Principal  | 3.00        | 23.70  | 23.21  | 22.72  | 32.19  | 33.61  | 45.44  | 45.44  | 45.44 | 22.09 | 4.42  |      |
| Charges and interest   | 0.00        | 0.02   | 0.62   | 0.61   | 1.06   | 0.95   | 0.76   | 0.54   | 0.31  | 0.11  | 0.03  |      |
| <b>Obligations to the Fund from existing and prospective credit</b>  |             |        |        |        |        |        |        |        |       |       |       |      |
| In millions of U.S. dollars  | 4.20        | 33.41  | 33.82  | 33.33  | 47.76  | 50.08  | 66.95  | 66.63  | 66.30 | 32.17 | 6.45  |      |
| In percent of gross international reserves   | 0.17        | 1.21   | 1.03   | 0.92   | 1.20   | 1.06   | 1.24   | 1.08   | 0.91  | 0.36  | 0.06  |      |
| In percent of exports of goods and services  | 0.10        | 0.76   | 0.68   | 0.58   | 0.72   | 0.67   | 0.59   | 0.44   | 0.26  | 0.09  | 0.01  |      |
| In percent of GDP  | 0.03        | 0.23   | 0.21   | 0.18   | 0.23   | 0.22   | 0.21   | 0.18   | 0.14  | 0.05  | 0.01  |      |
| In percent of quota  | 2.64        | 20.88  | 20.98  | 20.54  | 29.27  | 30.42  | 40.67  | 40.48  | 40.27 | 19.54 | 3.92  |      |
| <b>Outstanding Fund credit based on existing drawings (end-of-period, all PRGT)</b>                          |             |        |        |        |        |        |        |        |       |       |       |      |
| In millions of SDRs  | 93.60       | 70.07  | 46.86  | 24.14  | 1.42   | 0.00   | 0.00   | 0.00   | 0.00  | 0.00  | 0.00  | 0.00 |
| In percent of quota  | 82.40       | 61.68  | 41.25  | 21.25  | 1.25   | 0.00   | 0.00   | 0.00   | 0.00  | 0.00  | 0.00  | 0.00 |
| <b>Outstanding Fund credit based on existing and prospective drawings (end-of-period)</b>                    |             |        |        |        |        |        |        |        |       |       |       |      |
| In millions of U.S. dollars  | 250.61      | 330.66 | 356.71 | 326.57 | 282.17 | 235.97 | 170.12 | 104.27 | 38.42 | 6.41  | 0.00  |      |
| In percent of gross international reserves   | 10.16       | 11.94  | 10.88  | 8.99   | 7.06   | 5.01   | 3.15   | 1.70   | 0.53  | 0.07  | 0.00  |      |
| In percent of exports of goods and services  | 0.24        | 0.27   | 0.22   | 0.16   | 0.11   | 0.07   | 0.03   | 0.01   | 0.00  | 0.00  | 0.00  |      |
| In percent of GDP  | 0.00        | 0.00   | 0.00   | 0.00   | 0.00   | 0.00   | 0.00   | 0.00   | 0.00  | 0.00  | 0.00  |      |
| In percent of quota  | 157.40      | 206.68 | 221.25 | 201.25 | 172.92 | 143.33 | 103.33 | 63.33  | 23.33 | 3.89  | 0.00  |      |
| <b>Memorandum items:</b>   |             |        |        |        |        |        |        |        |       |       |       |      |
| Nominal GDP (in billions of U.S. dollars)  | 15.21       | 14.81  | 16.42  | 18.40  | 20.48  | 22.78  | 31.39  | 36.66  | 48.21 | 58.66 | 75.81 |      |
| Exports of goods and services (in billions of us dollars)  | 4.23        | 4.42   | 4.94   | 5.79   | 6.68   | 7.50   | 11.28  | 14.99  | 25.80 | 35.51 | 52.68 |      |
| Gross international reserves (in billions of us dollars)   | 2.47        | 2.77   | 3.28   | 3.63   | 4.00   | 4.71   | 5.40   | 6.14   | 7.25  | 9.03  | 10.45 |      |
| Quota (in millions of SDRs)  | 113.6       | 113.6  | 113.6  | 113.6  | 113.6  | 113.6  | 113.6  | 113.6  | 113.6 | 113.6 | 113.6 |      |

Sources: IMF staff estimates, and projections.

<sup>1</sup> Assumes access of 180 of the quota during 2015-17 and semi-annual disbursements.

## Annex I. Mozambique: External Balance Assessment<sup>1</sup>

**Data limitations surrounding megaproject-related activities imply that external stability assessments for Mozambique are subject to considerable uncertainty.** These limitations relate in particular to identifying a current account and net international investment position unrelated to megaprojects, which would describe accurately the country's core economy. While the Mozambican authorities produce accurate external sector data for megaprojects, only exploratory data is available on domestic firms whose operations exclusively relate to megaprojects.<sup>2</sup> Based on this exploratory data and other considerations, staff has estimated current account and IIP balances excluding all megaproject-related activities.<sup>3</sup>

**Staff estimates on a non-megaproject-related external position illustrate that the current account deteriorated after 2013.** Like many LIDCs, Mozambique has traditionally run a current account deficit, which stood at around 5 percent of GDP during 2006-09 and around 10 percent of GDP more recently during 2010-13. The latter has been broadly consistent with a stable net international investment position (IIP), while Mozambique's IIP improved considerably during the earlier period. However, there has been a considerable recent worsening of non-MP-related current account deficits to 13½ and 14 percent of GDP in 2014 and 2015, respectively.

**In absence of high megaproject investment activity, such higher non-megaproject-related current account deficits are not sustainable.** Megaproject inflows have collapsed and are projected at less than \$1 billion in 2015, given temporarily lower investment in the coal and gas sectors while agreements between the government and private sector are negotiated. Although the vast majority of these FDI inflows go into imports, their sheer size (of \$4 billion on average during 2012-14) implied that the even small leakage into domestic goods and services constituted significant financing.

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<sup>1</sup> Prepared by Christian Henn.

<sup>2</sup> For instance, there are domestic firms engaged in extraction and processing steps for coal and exclusively sell their services to megaprojects. The available data relates only to the coal sector for 2013 and suggests that, in light of high outsourcing, the imports by MP-related domestic firms was likely larger than that of the coal MPs themselves.

<sup>3</sup> These other considerations include a doubling of "unclassified" non-MP imports between 2011 and 2012, as megaprojects were strongly expanding, which can hardly be explained by the traditional economy alone.

**In contrast, the non-megaproject financial account has remained comparably resilient.**

Although they are expected to slow going forward, private sector FDI and loan inflows have thus far maintained their pace of 2014, offsetting lower disbursements for public investment projects, partly resulting from a slower pace of contracting external debt in the recent past. The non-megaproject financial account in 2015 is therefore expected to net over \$3.2 billion in inflows, outstripping the 2012 (\$3.2 billion) and 2013 totals (\$2.7 billion)<sup>4</sup> but falling short in magnitude relative to 2014 (\$3.7 billion).

**Notably, there is no evidence of capital flight.** Domestic agents retained their savings in the country, although they have reportedly been keen to retain existing dollar deposits, possibly in anticipation of further metical depreciation. While this has made the domestic foreign exchange market more illiquid, there has not been capital flight. Capital flight would typically occur through acquisition of portfolio investments or bank deposits abroad and would be registered under “other” financial account flows (in Table 5). Rather, these “other” flows continue to be heavily driven by megaprojects’ transactions (and changes in their trade credit positions in particular). Of \$1.1 billion in net outflows in this category in 2014, the non-megaproject economy accounted for only for \$100 million.<sup>5</sup> This pattern has persisted in the first half of 2015 with the non-megaproject economy only accounting for \$16 million of the total \$370 million in such outflows.<sup>6</sup>

**During 2016, macroeconomic adjustment is projected to reverse the current account deterioration and thereby halt the decline in 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 -47 percent of GDP in 2013. The deterioration resulted from overly expansive fiscal policies in the run up to the 2014 elections, an overvalued exchange rate in the recent past, and relatively loose monetary policy. With large capital gains tax windfalls and related boosts to international reserves allowing considerable FX intervention, adjustment has been delayed. However, the decisive adjustment started by the authorities in late 2015 is expected to return the current account to below 10 percent of GDP from 2016 onwards and drive a gradual recovery in the IIP from a projected 2016 level of -78 percent of GDP.

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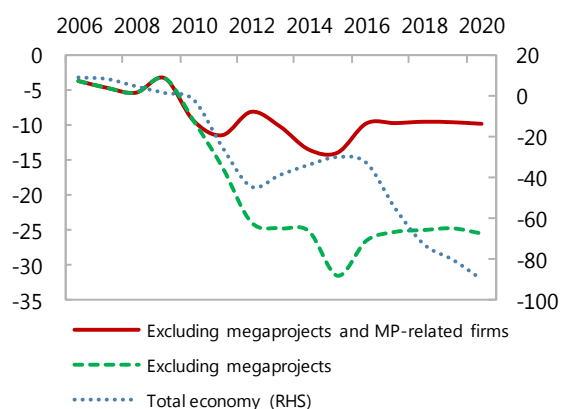
<sup>4</sup> Adjusted to exclude the disbursement of the EMATUM bond of \$782 million.

<sup>5</sup> In each 2012 and 2013, the non-megaproject economy registered large inflows exceeding \$1 billion in this category, but this was driven by special factors: the contracting of the \$780 million EMATUM bond in 2013 and data issues in 2012, related to the ramping up of (MP-related) imports by domestic firms supplying exclusively megaprojects. Meanwhile, in the decade up to 2011 the non-MP economy registered relatively stable inflows in this category of about \$100 million per year.

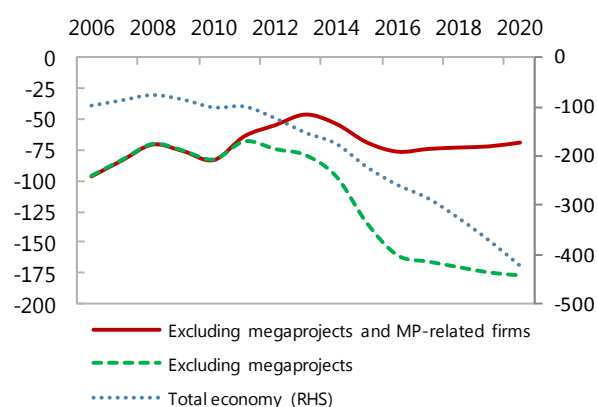
<sup>6</sup> A reduction in such “other” outflows had already been projected previously, with net trade credits given by megaprojects to importers of their products expanding at a much more moderate pace given lower commodity prices. Nonetheless, such flows are difficult to project as they can be driven by lumpy transactions by megaprojects. Thereby the magnitude of the reversal has thus far not been as strong as expected at the time of the fourth review (which expected inflows in 2015), partly because reductions in megaprojects’ investment activity would lead to a reduction in trade credit liabilities.



**Current Account Balance  
(Percent of GDP)**



**Net International Investment Position  
(Percent of GDP)**



**The metical depreciation since late 2014 is expected to assist the rebalancing.** After having been mostly stable during 2012-14, the nominal and real effective exchange rates depreciated by about 10 percent between end-December 2014 and end-September 2015. Depreciation through mid-November was more pronounced vis-à-vis the US dollar (25 percent), but more limited versus the South African Rand (13 percent) in which many imports are invoiced. Impacts on imports are still expected to materialize, including because some of the depreciation has occurred in recent months.<sup>7</sup>

**The External Balance Assessment (EBA) concludes that the metical is broadly fairly valued.** Although data limitations impose some uncertainty, the latest metical depreciation and effects of adjustment measures are likely to have corrected much of the 5-10 percent overvaluation assessed at the last review. Once their effects pass fully through into trade flows, the current account deficit (excluding megaproject-related flows) is projected to contract from its 2015 level of 14 percent of GDP to 9.8 percent in 2016 and remain in that range over the medium term. This is in line with the current account norms derived under EBA-lite's Current Account and External Sustainability Approaches of 10 and 11½ percent of GDP, respectively. The Index REER Approach, which is more responsive by directly evaluating exchange rates, supports this conclusion by suggesting that the metical is at present broadly fairly valued.

<sup>7</sup> During May to mid-November, depreciation was 19 percent versus the US dollar and 2½ percent versus the Rand. The real effective exchange rate depreciated by 4 percent during May to September.

**Estimates of the Valuation of the Metical using EBA-lite Approaches**

| Approach   | Current Account Gap<br>(percent of GDP) 1/ | Overvaluation (+) /<br>Undervaluation (-)<br>(percent) 2/ |
|--|--|---|
| Current Account Approach                         |  |   |
| 2015   | -4.7                                       | 9.5   |
| 2016 (after exchange rate pass-through to trade) | -0.6                                       | 1.2   |
| Index REER Approach (2015)                       | ...  | -2.2  |
| External Sustainability Approach 3/              |  |   |
| 2015   | -2.4                                       | 4.9   |
| 2016 (after exchange rate pass-through to trade) | 1.7  | -3.5  |

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-2014 level of 83 percent of GDP.

**The Fund-supported program is designed to ensure that international reserves remain at comfortable levels.** The conclusions of the 4<sup>th</sup> review's reserve adequacy assessment continue to hold. This assessment judged 4.5 month of non-megaproject imports to be a prudent reserve cover. End-2015 reserves are projected to cover 4.2 months of prospective imports, down from 5.0 months at end-2014. Under the program, reserves are projected to bottom out at 3.8 months in early 2016, before recovering to 4.5 months by end-2016. More importantly, the program sets the stage for Mozambique to return to a path of gradual long-run reserve accumulation to withstand increasing amplitude of shocks that may result as its exports continue to shift toward natural resources.

## Arrangement Under the Standby Credit Facility

Attached hereto is a letter dated December 2, 2015 (the “Letter”), with its attached Memorandum of Economic and Financial Policies (the “MEFP”) and Technical Memorandum of Understanding (the “TMU”), from the Minister of Economy and Finance and the Governor of the Bank of Mozambique requesting from the International Monetary Fund, as Trustee of the Poverty Reduction and Growth Trust (the “Trustee”), an 18-month arrangement under the Standby Credit Facility (“SCF”), and setting forth:

- (a) the objectives and policies of the program that the authorities of the Republic of Mozambique intend to pursue during the 18-month period of the arrangement;
- (b) the objectives, policies and measures that the authorities of the Republic of Mozambique intend to pursue during the first year of the arrangement; and
- (c) understandings of the Republic of Mozambique with the Trustee regarding reviews that will be made of progress in realizing the objectives of the program and of the policies and measures that the authorities of the Republic of Mozambique will pursue during the remaining period of the arrangement.

To support these objectives and policies, the Trustee grants the requested 18-month arrangement in accordance with the following provisions, and subject to the provisions applying to assistance under the Poverty Reduction and Growth Trust (the “PRG Trust”).

1. (a) For a period of 18 months from the date of approval of this arrangement, the Republic of Mozambique will have the right to obtain disbursements from the Trustee in a total amount equivalent to SDR 204.48 million, subject to the availability of resources in the PRG Trust.
- (b) Disbursements under this arrangement shall not exceed the equivalent of SDR 164.72 million in the first twelve months of the arrangement.
2. During the period of the arrangement:
  - (a) the first disbursement, in an amount equivalent to SDR 85.2 million, will be available upon approval of the arrangement, at the request of the Republic of Mozambique and subject to paragraphs 4 and 5 below;
  - (b) the second disbursement, in an amount equivalent to SDR 39.76 million, will be available on or after March 31, 2016, at the request of the Republic of Mozambique and subject to paragraphs 3, 4, and 5 below;

- (c) the third disbursement, in an amount equivalent to SDR 39.76 million, will be available on or after September 30, 2016, at the request of the Republic of Mozambique and subject to paragraphs 3, 4, and 5 below.

3. The Republic of Mozambique will not request:

A. The second and third disbursements under this arrangement specified in paragraphs 2(b) and 2(c) above respectively:

- (a) if the Managing Director of the Trustee finds that, with respect to the second disbursement, the data as of December 31, 2015, and with respect to the third disbursement, the data as of June 30, 2016, indicate that:

- (i) the ceiling on the net credit to the central government; or

- (ii) the ceiling on the stock of reserve money; or

- (iii) the floor on the stock of net international reserves of the Bank of Mozambique;

as set out in Table 1 of the MEFP and further specified in the TMU, was not observed; or

- (b) after March 30, 2016, until the Trustee has determined, with respect to the second disbursement, that the first program review has been completed and, after September 29, 2016, until the Trustee has determined, with respect to the third disbursement, that the second program review has been completed.

4. The Republic of Mozambique will not request a disbursement if at any time during this arrangement:

- (a) The ceiling on the present value of new external debt contracted or guaranteed by the central government or the Bank of Mozambique or selected state-owned enterprises with maturity of one year or more; or

- (b) The ceiling on the stock of short-term external debt contracted or guaranteed by the central government; or

- (c) The ceiling on the external payments arrears of the central government;

as set out in Table 1 of the MEFP and further specified in the TMU, was not observed; or

- (d) the Republic of Mozambique imposes or intensifies restrictions on the making of payments and transfers for current international transactions; or

- (e) the Republic of Mozambique introduces or modifies multiple currency practices; or
  - (f) the Republic of Mozambique concludes bilateral payments agreements that are inconsistent with Article VIII; or
  - (g) the Republic of Mozambique imposes or intensifies import restrictions for balance of payments reasons.
5. The Republic of Mozambique will not request a disbursement that has become available under this arrangement upon the satisfaction of the conditions for such disbursement set out in paragraphs 3 and 4 above and that remains undrawn:
- (i) after March 30, 2016, until the first review referred to in paragraph 3.A(b) above has been completed;
  - (ii) after September 29, 2016, until the second review referred to in paragraph 3.A(b) above has been completed;
6. When the Republic of Mozambique is prevented from requesting disbursements under this arrangement because of paragraphs 3, 4, and 5 above, such disbursements may be made available only after consultation has taken place between the Trustee and the Republic of Mozambique and understandings have been reached regarding the circumstances in which the Republic of Mozambique may request the disbursements.
7. In accordance with paragraph 6 of the Letter, the Republic of Mozambique will provide the Trustee with such information as the Trustee requests in connection with the progress of the Republic of Mozambique in implementing the policies and reaching the objectives of the program supported by this arrangement.
8. During the period of this arrangement, the Republic of Mozambique shall remain in close consultation with the Trustee. In accordance with paragraph 5 of the Letter, the Republic of Mozambique shall consult with the Trustee on the adoption of any measures that may be appropriate at the initiative of the government or whenever the Managing Director of the Trustee requests such a consultation. Moreover, after the period of this arrangement and while the Republic of Mozambique has outstanding financial obligations to the Trustee arising from loan disbursements under this arrangement, the Republic of Mozambique will consult with the Trustee from time to time, at the initiative of the government or whenever the Managing Director of the Trustee requests consultation on the Republic of Mozambique economic and financial policies. These consultations may include correspondence and visits of officials of the Trustee to the Republic of Mozambique or of representatives of the Republic of Mozambique to the Trustee.

## Appendix I. Letter of Intent

Maputo, Mozambique  
December 2, 2015

Ms. Christine Lagarde  
Managing Director  
International Monetary Fund  
Washington, D.C. 20431  
U.S.A.

Dear Ms. Lagarde:

Since late 2014, the Mozambican economy has been increasingly affected by the decline in international commodity prices, resulting in falling export receipts and FDI, significant depreciation of the metical, and loss of international reserves. Despite severe challenges, the growth outlook is robust and inflation remains low, and the Government of Mozambique is taking policy measures to cope with the external shocks, including through fiscal adjustment and tightening of monetary policy stance. To support our effort, we are requesting an eighteen-month standby credit facility (SCF) arrangement to supplement the Policy Support Instrument (PSI) to augment reserves and provide a strong signal of our intention to maintain macroeconomic stability. The main objective of the SCF arrangement will be to alleviate the external balance of payments shocks, and through strengthening macroeconomic stability, to achieve the Government's goals on poverty reduction and inclusive growth.

The Government of Mozambique requests the completion of the fifth review under the PSI and the approval of the SCF arrangement. We also request the modification of three assessment criteria for December 2015 to account for the changed environment and our revised macroeconomic projections: the substantial decline in net international reserves amid strong balance of payment pressures, the impact of private companies' discounting of the treasury securities for clearing VAT refund backlog on net credit to government, and the effects of the increase in reserve requirement on reserve money. We also request (i) to set performance criteria and indicative targets for end-June 2016, and indicative targets for end-March, end-September, and end-December, (ii) to reschedule two existing structural benchmark and set new structural benchmarks for 2015-16, in part reflecting the complexities in the implementation of structural benchmarks. In support of this request, we are transmitting the attached Memorandum of Economic and Financial Policies (MEFP), which reviews the implementation of the program supported by the current PSI and establishes policy objectives and assessment criteria and indicative targets for the short and medium term.

The Government is of the view that the policies outlined in the MEFP are adequate to achieve the objectives of the PSI/SCF-supported program. We stand ready to take any further measures that may become appropriate for this purpose.

The Government will consult with the IMF on the adoption of these measures—at its own initiative or whenever the Managing Director requests such a consultation—in advance of any revision to the policies contained in the MEFP, in accordance with the Fund’s policies on such consultation.

The Government will provide the IMF with such information as the IMF may request to be able to assess the progress made in implementing the economic and financial policies and achieving the objectives of the program.

The Government authorizes the publication of this Letter of Intent, its attachments and the associated staff report.

Sincerely yours,

/s/

**Adriano Maleiane**  
**Minister of Economy and**  
**Finance**

/s/

**Ernesto Gouveia Gove**  
**Governor**  
**Bank of Mozambique**

Attachments: Memorandum of Economic and Financial Policies  
Technical Memorandum of Understanding

## Memorandum of Economic and Financial Policies (MEFP)

December 2, 2015

1. This MEFP (i) describes recent developments and performance of the Government's economic program under the three-year Policy Support instrument (PSI) to date, and (ii) elaborates on economic and structural policy intentions. It builds on the MEFP underlying the Fourth PSI Review of June 2015.

### I. Recent Economic Developments and Performance Under the Program

2. **In 2015, the performance of the Mozambican economy has remained robust.** However, the economy is facing in the short term growing challenges arising from lower commodity prices, temporarily subdued foreign direct investments, and sharp appreciation of the US dollar internationally.
  - **Economic growth has moderated in 2015. Real GDP grew by 6.3 percent in the first half of 2015, compared to an average 8 percent in the same period in the last two years.** This deceleration was partly driven by the floods in early 2015 and the slower execution of fiscal expenditure due to the delay in the budget approval, although growth in the agriculture and manufacturing sectors was better than anticipated. Mining sector growth decelerated to 17 percent in the first half of 2015 from 29 percent in the first half of 2014, reflecting lower international commodity prices and transportation constraints that prevented the scaling up in coal production and exports. Performance also weakened in the commerce and transport sectors due to the impact of the floods on traffic flows of people and merchandise along the north-south highway in early 2015.
  - **Inflation and monetary policy.** In the past nine months, inflation has remained stable and low, with a year-on-year rate of 2.4 percent in September 2015. The low inflationary pressure reflects the increase in domestic food supply, the decline in the international commodity prices and the relatively stable exchange rate of the Metical vis-à-vis the South African Rand. Sound liquidity management in the banking system and unchanged administered prices were other key drivers of low inflation by September.
  - **Exchange rate.** Since the last quarter of 2014, the Metical-dollar exchange rate has been under pressure because of the strengthening of the US dollar in international markets, a widening of the current account deficit exacerbated by the decline in commodity prices, and continuously strong domestic demand for foreign currency, including for external debt payment and fuel imports. Depreciation pressures were aggravated by lower foreign aid and foreign direct investment in the context of an uncertain political environment that followed the elections in late 2014.



- **External current account.** In the first half of 2015, the current account deficit excluding megaprojects deteriorated to \$2.2 billion from \$1.2 billion compared to the same period last year, due to a 17 percent increase in imports and an absence of capital gains tax inflows which contained the current account deficit in the first half of 2014. In light of the international environment, traditional exports, which remained stable, could not provide a counterweight. Including megaproject operations, the current account deficit deteriorated only slightly. Total exports declined by 4.2 percent to \$1.8 billion reflecting the impact of lower commodity prices, including for heavy sands, coal and gas. Total imports fell by 4.5 percent to \$3.5 billion due to imports of megaprojects declining steeply in line with a slowdown in their investment activities. This investment slowdown is driving a decline in FDI and other financing inflows weighing on the external balance.
- **FDI, aid/loan disbursements, reserves.** FDI flows into the country registered a year-on-year decline of 17 percent in the first half of 2015, mainly related to the slowdown of investments in the mining industry, particularly gas and coal. External aid inflows declined by 14 percent in the first half of the year. As a result, net international reserves declined to \$2.2 billion at end-September 2015 (corresponding to about 3.9 months of coverage of gross international reserves of current imports of goods and non-factor services excluding megaprojects).

### **Budget implementation.**

- Revenues were slightly below the program target. Among other factors, this performance was due to (i) the verification and continuous controls on annual income statements by individuals and corporates; and (ii) increased control of investment project tax benefits by the Tax Directorate (DGI).
- Expenditures reached 84.5 percent of the program in the first semester. This under-execution is explained by the late approval (end-April 2015) of the 2015 State budget. In the first four months the Operational Budget was implemented in compliance with the principle of twelfths (setting monthly expenditure ceilings equal to 1/12 of the previous year budget), and the Investment Budget was executed only for projects registered in 2014 which have continued in the financial year 2015.
- The budget deficit was lower than expected by 0.3 percent of GDP as externally-financed expenditure decreased by 50.7 percent, due to delays in aid disbursements and the late approval of the budget. Grant and loan disbursements represented 45.3 percent and 40.3 percent, respectively, of the initially committed amounts for the year.

### **3. Program Performance**

- **Quantitative targets through end-September 2015:** Performance of the program at end-June is mixed. Three assessment criteria (AC) on net credit to government (NCG), Net International Reserves (NIR) and external arrears and an indicative target (IT) on government revenue were missed, while all the other ACs were met. The deviation in

NCG reflected one-off factors and is expected to be temporary: the government made a lump sum payment of about \$100 million (0.6 percent of GDP) to fuel distributors to compensate for past under-payments, which reflected under-budgeting. This, together with a speedy discounting of the bulk of government securities received by companies as reimbursements for outstanding VAT credits (MT 8.4 billion), pushed net credit to government (NCG) above target at end-June. The NIR target was missed by a small margin at end-June, partly reflecting valuation loss. The reserve money indicative target was met in September 2015. Failure to meet the indicative NIR target by a substantial amount at end-September reflects continued BOP pressures including lower export proceeds, higher external debt service, and negative exchange rate valuation changes resulting from a stronger US Dollar. Imperfect coordination with creditors and a legacy lapse of debt management caused small external arrears, but these arrears have since been resolved.

- **Structural benchmarks (SB):** The end-June SB on inclusion in the draft 2016 budget of a fiscal rule on the use of windfall revenue was met. The SB on the operationalization of an IT application for payments of VAT, ISPC, corporate and personal income taxes through banks was not met, though considerable progress was achieved and this SB was met by end-November. The end-July benchmark on the issuance of budget guidelines making mandatory the technical assessment by the Investment Evaluation Committee for new public investment projects to be included in the 2016 and subsequent budgets of a value of \$50 million or more was met. The SB on allowing the use of T-bonds as collateral in money market operations was not met by end-September as envisaged. However, the related IT issues have been resolved and related draft regulations have been approved by the BM Board and the SB was fully met in November 2015. The remaining benchmarks for December 2015 and January 2016 are advancing as planned and are expected to be met.

## II. Macroeconomic Policies

### A. Economic Objectives

#### 4. Economic outlook for 2015-19.

- **Macroeconomic policy.** Fiscal policy will be geared toward fostering strong and inclusive growth while preserving sustainability and supporting the external adjustment. In this regard, the overall fiscal deficit is expected to decline from 6 percent of GDP in 2015 to 4 percent of GDP in 2016 and remain at this level over the medium term. Revenue collection is expected to remain strong in the period and expenditures are expected to decrease by 1.4 percent of GDP in 2016 and stabilize around 32-33 percent of GDP over the medium term. Access to non concessional borrowing will be limited to projects that cannot be financed through concessional loans, do not endanger debt sustainability and have been subject to a rigorous cost benefit analysis. Monetary policy will be consistent with the overall development of the economy, while ensuring price stability and maintaining adequate reserve levels.

- **GDP growth** in 2015 is expected to reach 7 percent though there are downside risks that might warrant a further reduction of about 0.7 percentage points depending on the performance in the second half of the year.<sup>1</sup> Downward revisions could be needed if the weaker performances of the mining, commerce, financial, transport and tourism sectors continue until the end of the year. Nevertheless, growth will accelerate towards the 7-8 percent range during 2016-2020, supported by agriculture, construction and financial services, and spearheaded by expanding coal production and construction works for LNG projects.
- **Inflation.** Based on recent developments, inflation is expected to rise to about 5 percent by end-2015 (2 percent in average terms) due to the recent adjustment of some administered prices and depreciation of the metical, although it remains below the year-on-year target of 5.5 percent. In 2016-17, inflation is expected to rise somewhat to our medium-term objective of an annual average of 5-6 percent per annum.
- **External Current account.** The balance of payments 2015-17 will remain characterized by the negative impact of persistently low international commodity prices, which keeps exports subdued. Our macroeconomic adjustment measures are thereby designed to retain sustainability by containing non-megaproject imports. New investment inflows for coal infrastructure and LNG processing facilities, which could start in 2016, are expected to underpin the external position further, including over the medium term. These measures will halt declines in international reserves and return them to a path of gradual expansion. For end 2015, we expect a gross reserve cover ratio of about 4.2 months of projected imports of goods and services excluding megaprojects. After bottoming out in the first half of 2016, the ratio is projected to recover to 4.5 months at end 2016 and further to 4.9 by end 2017.
- **Fiscal policy.** The overall fiscal deficit will continue to narrow in 2016 to support external adjustment to 4 percent of GDP. The budget deficit is expected to remain at the same level over the medium term.

## B. Monetary and Exchange Rate Policy

**5. The monetary policy stance will be less accommodative in the last quarter of 2015 and remain tight in 2016.** Given a rising inflation outlook (partly driven by the depreciation of the metical), the Bank of Mozambique (BM) has already started to tighten its monetary policy stance in the Monetary Policy Committee meeting in October. It will continue to intervene in the interbank markets in order to ensure reserve money growth consistent with our price stability objective and the policy adjustments to preserve adequate levels of net international reserves. The BM will devote efforts toward containing reserve money growth around 12 percent in 2016.

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<sup>1</sup> To be prudent, the program is based on the more conservative growth assumption.

The BM will also stand ready to monitoring risks internally and abroad, and to take appropriate actions to maintain overall price stability.

**6. We remain committed to a flexible exchange rate regime.** The BM will allow the exchange rate to adjust freely to evolving patterns of trade and financial flows.

**7. The Mozambican authorities remain committed to their obligations under Article VIII, sections 2, 3, and 4 of the Fund's Articles of Agreement.** The BM will continue to monitor the implementation of the new foreign exchange regulations, its implementation norms, as well as the functioning of the foreign exchange market, with a view to avoiding practices that could turn out to be inconsistent with Article VIII principles. We will keep IMF staff informed of any developments that could potentially run against those principles. The Bank of Mozambique confirms that it will ensure that the exchange rates at which the central bank sells foreign exchange to commercial banks for oil imports, or any official exchange rates used by the Bank of Mozambique for any other spot transactions, and the interbank market rates, will not deviate by more than two percent at any given time and will take any measures necessary to that effect.

### C. Fiscal Policy

**8. Budget execution in 2015.** We will execute the 2015 budget consistent with the program. In particular, we will offset fuel subsidy payment of MT 3.8 billion by reducing expenditures in other categories.

**9. Fiscal policy objectives.** In 2016, the government will ensure that the overall fiscal deficit after grants will decline to 4 percent of GDP, while the domestic primary surplus reaches 1.6 percent of GDP. Revenues are expected to reach 26.2 percent of GDP, an increase of 1 percent of GDP compared to the 2015 target. This increase in revenues is expected to result from: a strong performance in international trade taxes (derived from the combination of a higher volume of goods imports in US dollars and a more depreciated exchange rate vis-à-vis the US dollar), increase in gas in-kind royalties, as well as administrative reforms in key areas, for instance, stamp taxes for alcoholic beverages and cigarettes, common custom tariffs and excise duties. Expenditures are expected to decline by 1.4 percent of GDP, to 33.9 percent of GDP consistent with the consolidation path over the medium term that was set up in early 2015.

**10. Revenue outlook.** We will continue our efforts to improve revenue performance through reforms in tax and customs administration. The state budget for 2016 does not consider inflows from capital gain taxes, however if they are reported during the financial year, Article 5 of the Budget Law authorizes the government to use them for the realization of investment expenses, debt reduction and mitigate effects of emergencies.

**11. Expenditure policy.** Even though expenditures are expected to decline to 33.9 percent of GDP, the budget will continue to contribute to poverty reduction by prioritizing the resource allocation to economic and social infrastructure, human capital and diversification of public goods and services, and public sector reforms.

- **Wage bill policy.** We will reduce the wage bill by 0.2 percent of GDP in 2016, compared to 2015. This will be achieved through measures to contain the pressure on salaries, such as: (i) the implementation of the "Proof of Life" for all employees and State agents, and (ii) the limitation of new hiring, excluding the health, education, agriculture and police sectors.
- **Strengthening social protection.** Social Protection Programmes are planned to reach around 0.5 percent of GDP in 2016, which will cover 507,902 beneficiaries, or 16 percent higher than 2014.
- **Subsidies for petroleum products.** Subsidies paid in 2015 amounted Mt 3.8 billion, or 0.6 percent of GDP that would be accounted for in the 2015 executed budget. The government is considering a reform of the fuel pricing mechanism and a rationalization of the fuel subsidies. At current international oil prices, no fuel subsidies exist. In the mean time, the government deems that no fuel subsidies will be necessary in 2016. If subsidies were needed, the government would take offsetting budgetary measures to achieve its budget target.
- **Other subsidies.** We will continue to allocate resources to subsidize non-fuel prices, such as wheat, flour, and transport to minimize the cost of living of the population. Therefore, we expect to spend roughly 0.4 percent of GDP on non-fuel price subsidies and enterprises.
- **Electricity tariffs.** The revised tariff proposal is still under consideration by the Government. It is envisaged that the new tariff has become effective in November.
- **EDM performance contract.** The performance contract was not signed in July as envisaged due to the high financing need for investment projects, which cannot be secured by the budget. The performance contract is under revision by the company and is expected to be signed by June 2016.

### III. Public Finance Structural Reforms

#### Investment Planning and Debt Management

**12. Public Investment Management.** We issued budget guidelines through a notice to all line ministries to make mandatory the technical assessment for investment projects exceeding the \$50 million in the 2016 and subsequent budgets in July 2015 (4th review structural benchmark). We also developed the manual for project selection to be included in the Integrated Investment Program (IIP) and we expect to organize training activities to line ministries on the use of the manual. The Government will continue to improve public investment management, including through a closer analysis of the relationship between public investment and debt sustainability. In addition, institutions in charge of the design and implementation of public investment projects will be strengthened so that public investment project selection and evaluation conforms to sound practices.

**13. Strengthening public debt management:** Despite the adverse effect of the US dollar appreciation on debt-to-GDP ratios, Mozambique's external debt remains sustainable and the country risk of debt vulnerability continues to be moderate. We revised our Debt Management Strategy with technical assistance from the World Bank and IMF, which include considerations on how to help the development of the domestic capital markets. This strategy was submitted to the Cabinet in November 2015. The 2015 domestic borrowing plan was finalized by end June 2015. The annual debt reports include the analysis of the cost and risk associated with the public debt portfolio.

**14. Guarantee management policy.** The projects that benefit from guarantees are regularly monitored by the Ministry of Economy and Finance to minimize the risk of default. We have built a database to manage all guarantees and we plan to develop capacity to assess the probability and impact of potential default of this exposure with technical assistance from the World Bank and IMF. A comprehensive list of all the guarantees outstanding has been communicated to IMF.

### Public Financial Management (PFM)

**15. Expenditure coverage and tracking.** We made progress in the coverage of the integrated financial management system (e-SISTAFE). By end-August 2015 the share of expenditures paid through e-SISTAFE directly to the beneficiary reached 70.7 percent of total spending from the target of 70 percent for 2015. Coverage is expected to reach 75 percent in 2016.

**16. Real time registration of commitments.** The reform is expected to allow greater control of budget execution through greater efficiency in the use of e-SISTAFE. We implemented the procedures set out in the Ministerial Diploma No 210/2014, of December 9, for wage processing and payment to all civil servants and State Agents observing the three stages of expenditure execution in June 2015. We are conducting training and awareness campaigns for the users of e-SISTAFE to facilitate the implementation of the mandatory real-time recording of the commitment and verification of expenditures for all units operating within e-SISTAFE by end-June 2016 (Structural benchmark)..

**17. Wage bill management.** We remain committed to expanding the e-Folha to all State agencies and institutions that have e-SISTAFE. By end-September 2015, from the total of 302,800 civil servants and State agents registered in e-CAF, 270,612 had their wages and salaries processed and paid by e-Folha, which corresponds to 89.3%. From July to September 2015 we carried out 245,607 proof of life in the country, corresponding to 81.1% of civil servants and State agents registered in e-CAF.

**18. Cash management.** We remain committed to extending the use of the treasury single account (CUT). We concluded the identification and evaluation of the accounts held outside the CUT in order to reduce the number of bank accounts outside the CUT (Circular No. 02/GAB-MF/2014). A new Budget Circular was issued in November 2015 to ensure that all revenues are transferred into the CUT, including own revenues of budgetary institutions.

**19. Scope of the public sector.** The revision of the SISTAFE Law which is expected to take place by December 2016 will broaden the scope of the public sector and make it consistent with international standards. In addition, a new law defining the statute of public funds and autonomous entities has been drafted and is under revision and expected to be submitted to Cabinet by May 2016.

**20. Fiscal risk management.** The National Directorate of Economic and Financial Studies was established in the new structure of the Ministry of Economy and Finance. The Directorate incorporates a fiscal risk management unit and will be responsible to deal with all fiscal risk related matters. We drafted the initial statement of fiscal risks with IMF technical assistance, and published it on the website of MEF in November 2015 (4th review structural benchmark for October 2015). The statement highlighted general risks to the budget stemming from possible changes in macroeconomic assumptions, and possible risks associated with state guarantees, PPPs, and large public sector, or public sector participated corporations to. We remain committed to implement the recommendations of the 2014 fiscal transparency evaluation report with technical assistance from the IMF.

**21. Fiscal rule for windfall revenue.** Large and regular influx of natural resource revenue from LNG is expected to start in a decade. But we expect that additional capital gain taxes associated with transactions involving transfers of ownership stakes in large natural resource projects might occur in the next few years. To ensure the use of these resources only for public investment, debt repayment, and national emergencies<sup>2</sup>, the above fiscal rule will be included in the 2016 budget law. We intend to develop a medium-term fiscal framework and a formal fiscal rule to (i) inform future saving and investment decisions, (ii) manage volatility, and (iii) address exhaustibility concerns before significant natural resource revenues materialize.

**22. Public Expenditure and Financial Accountability (PEFA).** We carried out the PEFA evaluation this year based on the current PEFA methodology using information over the period 2012-2014 and comparing the results with the 2011 last PEFA exercise. The main findings of the report suggested that Mozambique is being successful in consolidating progress achieved on PFM reforms since 2010, particularly in the areas of budget execution, accounting, e-SISTAFE system coverage, reporting and internal and external audit. At the same time, the report recommended improvements, especially in the area of public procurement.

## Revenue administration

**23. VAT administration.** The 2015 budget projected VAT revenues on a net basis. In addition, VAT arrears from previous budget years amounting to 8.2 billion Mt were securitized. These were two key components of the VAT reform. However, implementation of the net VAT system has encountered some difficulties, which have led to the accumulation of new arrears

<sup>2</sup> In case of temporary severe cash constraints generated by unexpected shortfalls in budget support, windfall deposits could be used on a temporary basis.

projected at 6.5-7 billion Mt by end-2015, of which part are claims from years before 2015. To prevent these problems in the execution of the 2016 budget, we will create in the TSA a dedicated subaccount to pay VAT refunds, by end-December 2015. This account will be regularly replenished by an amount equivalent to the amount of claims received. In addition, to compute net VAT collections, we will adjust gross VAT collections by the amount of refund claims received minus any claims that have been rejected.

**24. Implementation of e-Tax.** The registration of taxpayers into the new electronic system advanced considerably, reaching so far 76 percent of all VAT taxpayers more than the 65 percent of the target for end-December 2015. The e-tax collection system for VAT and ISPC currently covers 19 of the tax offices. Progress was registered towards the launch of the online taxpayers' portal connected to e-tax, which is expected to be fully operational by end-2015.

**25. Tax payment through banks.** We made progress to facilitate tax payments through banks by developing an IT application and signing agreements with 13 commercial banks. The whole reform process was finalized by end-November 2015. (Structural Benchmark)

**26. Modernizing the Revenue Authority (AT) to improve revenue collection.** We assessed the revenue administration using the TADAT diagnostic tool with technical assistance from the IMF and a report was concluded in May 2015. The recommendations of the TADAT diagnosis were included in the AT Strategic Plan 2015-2019. The main weaknesses are related to the integrity of the data base of registered taxpayers, and delays in filing tax returns.

## Natural Resource Management

**27. Extractive Industry Transparency Initiative (EITI).** The 6th Report is expected to be completed by end-December 2015 and will cover information on the extractive industry and the payments made by companies in the mining sector, oil and gas, as well as the revenue collected by government agencies in the period from 1 January 2013 to 31 December 2013 and 1 January 2014 to 31 December 2014. The 6th EITI report will be the basis for the next Validation of Mozambique as Country Compliant or not the EITI.

**28. Mining and Hydrocarbon Legislation.** The Regulation of the Mining Law was approved by the cabinet in October 2015 and the Regulation of the Petroleum Law was approved in November 2015.

**29. Strengthening the Mining and Hydrocarbon Tax Regime.** The regulations of the mining and hydrocarbon fiscal regimes which benefited from IMF technical assistance were submitted to the Cabinet and approved in October 2015.

**30. Development of natural gas liquefaction.** After the Decree-Law was approved to operationalize the development of natural gas liquefaction plants in the Rovuma Basin, negotiations continue to amend the Exploration, Production and Concession Contracts (EPCC), as requested by the Concessionaires of Area 1 and 4. With respect to the Concessionaire for Area 1,



negotiations are in the final stage, and preliminary agreement has been reached on modalities for the financing of the participation of ENH, amount of gas to be reserved for domestic purposes and the structure of marketing activities. A unitization agreement for the exploration of the greatest gas field that straddles Areas 1 and 4 (Prosperidade/Mamba) has also been reached. The government expects that recent progress will allow the concessionaires for Areas 1 and 4 to reach a final investment decision in 2016.

## Public Enterprises and Enterprises with State Participation

### 31. Strengthening supervision of public enterprises.

- The 2014 Annual Reports and audited financial accounts of the 8 largest State Owned Enterprises (SOE's) were published, and the summary report on the operations and fiscal risks of all 14 SOEs was elaborated, is under harmonization and then will be submitted to the Council of Ministers.
- The proposal for a Law on the Corporate Sector of the State, with a focus on the companies where the state has a participation below 100 percent, was submitted to the Ministry of Finance at end-2014, then it will be submitted to the Council of Ministers by end-March 2016.
- Regarding the process to consolidate the State's portfolio of enterprises, by October 2015 the following activities were completed (i) Sale of State Shares reserved for managers, technicians and workers in 4 SOE's, (ii) preparation for the sale of state participation in 2 more entities are in advanced stages, (iii) 4 are on the stage of getting the approval from respective line Ministers, (iv) 6 are on negotiation process with private investors.
- The new software to report financial information on state corporations became operational in July 2015, with the financial information of the pilot companies. Since July IGEPE is monitoring and managing the challenges of shifting from the previous process of presenting financial information to the current one (software – SIMAP). At this stage, a significant number of SOE's have submitted their financial information regarding 2014 and 2015 (second submission cycle). Note that each cycle has 4 months.
- Portfolio managers have been trained on the SIMAP tool with a view to improve the monitoring of the state portfolio and enhance its performance.

**32. EMATUM.** The EMATUM business plan was revised and is under consideration by the Ministry of Economy and Finance. Work is ongoing to restructure the EMATUM debt. An action plan which aims at improving profitability of EMATUM will be adopted by end-April 2016 (structural benchmark).

## IV. Financial Sector Policies

### Enhance the Functioning of Foreign Exchange Market

**33. The BM will enhance the intervention mechanism in the MCI market by trading foreign exchange at a rate that better reflects interbank market conditions.** From November, for its interventions in the market, the BM will intervene at the prices that the commercial banks are actually trading.

### Strengthen Monetary Policy Formulation and Implementation

**34. Monetary policy framework.** The BM will continue to strengthen the monetary policy framework and to improve the analytical capacity and communication in the monetary policy decision-making process, including by improving its inflation forecast model with technical assistance from IMF.

**35. Inflation forecasting model.** Under the new forecasting system, two forecasting rounds have been implemented and further model refinements are in place. As a complement, the BM is working on communication issues aiming at improving the degree of monetary policy transparency and communication with markets and the public.

**36. The BM has made considerable progress towards improving its liquidity management framework.** All steps recommended by the technical assistance mission to improve the forecasts of currency in circulation and government cash flow, as well as deepening the money markets were fully observed within the considered time. It includes (i) compilation of a new database under the new liquidity management spreadsheet; (ii) effective use of the new liquidity forecast spreadsheet; (iii) data collection on factors related to Government and Notes and Coins in Circulation; and (iv) initiating contacts with the MEF aiming at making more effective the information sharing mechanism. Initially, the liquidity forecasting horizon will be bounded to one day and, as the forecasting accuracy of the model improves, the time horizon will be enlarged.

**38. Money market management.** The remaining IT tests on the SAP platform toward allowing the use of T-bonds as collateral in the money market (**Structural Benchmark for end-September**) were completed by September. A regulatory amendment allowing the use of T-bonds as collateral has been issued in November 2015 under the BM Notice No. 8/GBM/2015. The equalization of fiscal treatment between secured and unsecured interbank transactions is in implementation since May 2015, under the Law No. 19/2013 (structural benchmark for end-January 2016). We expect this measure to help increasing the level of trading activity in the monetary market, especially for the secured transactions.

### Financial Sector Surveillance

**39. Stress testing and non-performing loans (NPLs).** The terms of reference for data collection process under the stress testing framework have been elaborated and incorporated

into the Bank's Business Intelligence Plan. The BM has conducted new rounds of stress testing exercises in June and September 2015. The latest results indicate that the largest banking system vulnerabilities include high credit concentration and insufficient capital buffer to cope with potential failure of the largest borrowers. The system is also vulnerable to funding liquidity risk, as the sources of funds are concentrated in large depositors. Other vulnerabilities are associated with the negative impact on NPLs of the metical-dollar exchange rate depreciation in cases where borrowers are not exporters. However, the overall NPL ratio remains relatively low at 4.3 at end-September.

**40. Risk-based supervision and Basel II implementation.** All inspections planned for the first half of 2015 were finalized. In addition, one institution was subject to an ad-hoc inspection. As for the second half of 2015, the inspection of one bank with high systemic relevance is underway. Two small and one medium size institutions were subject to inspection based on each bank's risk profile. The process will continue throughout the year, on a regular basis.

**41. Financial Sector Contingency Plan.** The World Bank draft report on the results of the simulation exercise has been discussed with the BM in a workshop held in September 2015. As the result of the workshop, a joint BM-World Bank proposal to elaborate an Action Plan addressing the issues observed during the simulation exercise and improving the legal and operational framework of crisis management was proposed. The approval of the Action Plan by the Board of BM is envisaged by end-March 2016.

**42. Deposit Insurance Fund (DIF).** In the first half of 2015, participating institutions and the government have already deposited the initial contribution (105 million MT) on behalf of the Fund. In August 2015 the Board of BM approved the Steering Committee Report of FGD. The Steering Committee will make further effort to work with KfW to secure its contribution in order to begin the operation of the FGD.

## Financial Sector Development

**43. Financial Sector Development.** The main objectives of the Financial Sector Development Strategy (FSDS) 2013-2022 are to: (i) maintain financial sector stability; (ii) increase access to financial services and products, eliminating structural constraints in the economy, specifically those that limit financial intermediation and access to financial services; and (iii) increase the supply of private capital to support private sector development.

- **Promoting financial inclusion.** A public consultation workshop on the National Financial Inclusion Strategy (FINS) took place in July 2015 which allowed the BM to gathering contributions to the draft FINS from stakeholders. The draft FINS was further submitted to the peer review and discussed during the Financial Inclusion Strategy Peer Learning Group (FISPLG) under the Alliance for Financial Inclusion (AFI) forum, held in Maputo, in September 2015. The process of encompassing the contribution from both meetings in the document, as well as the experiences learnt from other countries, is underway, before its submission to the Cabinet (**Structural Benchmark for end-**

- December).** The notice on cash recirculation is in the process of submission to the Board for appreciation.
- **Establishing credit registry bureaus (CRB).** The Law on the creation of private credit registry bureaus was approved by Parliament in July 2015. Its implementation of regulation is expected to be approved by end-March 2016.
  - **Promotion of mobile banking.** The Notice No.6/GBM/2015 which establishes the rules on the protection of funds from the issuance of electronic money was approved in July 2015, awaiting its publication in the State Gazette.
  - **Promotion of competition within the banking sector.** The draft Notice on the list and denomination of prices and commissions for financial products and services was concluded in December 2014 and is expected to be submitted to the BM Board for approval by December 2015.
  - **Capital Market Development.** The Stock Exchange (BVM) has been implementing a financial education program.
  - **Moveable collateral framework.** Preparation work on the draft law is ongoing. (structural benchmark for November 2015 proposed to be rescheduled to March 2016).

## Payment System

### 44. Reforms of the Payment System

- **Developing the retail payments network (SIMO).** As of October 15, thirteen banks out of eighteen have been connected to the single national electronic payment network. Work is in progress in the remaining five banks aiming at completing the transition by end-April 2016, within the migration schedule established in the Notice 02/GBM/2015.

## Business Environment

### 45. Improving the business environment:

- The e-BAU platform aims to providing quality online services to all segments of society, with greater focus on the citizens and business community, through automation and re-use of data and systems, improving provision of services and the business environment in the country. So they were integrated into electronic platform eight (8) Single Service desks in the provinces of Maputo City, Maputo Province, Gaza, Inhambane, Sofala, Nampula, Tete and Cabo Delgado. This action will have an impact on the reduction of procedures, costs and time.

- As a direct result of the implementation of the Platform, the number of days for licensing of economic activity was reduced from fifteen days and currently it can be done within three days on average for all computerized e-BAU's.
- The revision of the Policy and Strategy for the Industry is under public consultation phase for its harmonization and submission to the Cabinet by end-December 2015. The Strategy for Small and Medium Enterprises was presented to the Cabinet in November 2014, and recommended further consultations with relevant stakeholders for subsequent submission to the Economic Committee. The process of interoperability between institutions has been produced and is being tested.
- By July 2016 we expect to (i) Integrate the e-BAU's missing in the Electronic Platform (sectors of Commerce, Industry, and Simplified Touring in Manica, Zambezia and Niassa); (ii) Enter the Application System on line; and Integrate all organic Provincial Capital, including the municipalities that intervening in the licensing process, the Electronic Platform e-BAU nationwide.

### **Program Monitoring**

**46. The proposed assessment/performance criteria and indicative targets up to December 2016 are shown in Table 1. Tables 2, 3, and 4 include a list of existing and proposed structural benchmarks and corrective policy measures. The 6<sup>th</sup> PSI review is expected to be completed by June 15, 2016 (as specified in the MEFP dated June 12, 2015).**

Table 1: Assessment/Performance Criteria and Indicative Targets

|  | 2015                         |        |        |        | 2015                       |        |         |        | 2016                        |          |                             |        | 2016                          |         |                                 |       |                           |  |
|--|------------------------------|--------|--------|--------|----------------------------|--------|---------|--------|-----------------------------|----------|-----------------------------|--------|-------------------------------|---------|---------------------------------|-------|---------------------------|--|
|  | End-June Assessment Criteria |        |        |        | End-Sept Indicative Target |        |         |        | End-Dec Assessment Criteria |          | End-March Indicative Target |        | End-June Performance Criteria |         | End-September Indicative Target |       | End-Dec Indicative Target |  |
|  | Prog.                        | Adj.   | Actual | Status | Prog.                      | Adj.   | Actual  | Status | Prog.                       | Proposed | Proj.                       | Proj.  | Proj.                         | Proj.   | Proj.                           | Proj. |                           |  |
| <b>Assessment Criteria for end-June/December</b>   |                              |        |        |        |                            |        |         |        |                             |          |                             |        |                               |         |                                 |       |                           |  |
| Net credit to the central government (cumulative ceiling)  | -2,826                       | 1,074  | 8,047  | NM     | -3,785                     | ...    | 18,387  | NM     | 4,895                       | 11,999   | -940                        | -1,876 | -4,889                        | -1,526  |                                 |       |                           |  |
| Stock of reserve money (ceiling)   | 58,230                       | 58,230 | 56,575 | M      | 61,938                     | 61,938 | 61,489  | M      | 64,411                      | 69,850   | 66,443                      | 64,815 | 69,612                        | 78,232  |                                 |       |                           |  |
| Stock of net international reserves of the BM (floor, US\$ millions)   | 2,550                        | 2,521  | 2,470  | NM     | 2,650                      | ...    | 2,173   | NM     | 2,889                       | 2,025    | 1,925                       | 2,000  | 2,075                         | 2,250   |                                 |       |                           |  |
| Present value of new external debt contracted or guaranteed by the central government or the BM or selected state-owned enterprises with maturity of one year or more (ceiling covering the period December 18, 2015 (board date) through December 31, 2016, US\$ millions) <sup>2</sup> | ...                          | ...    | ...    | ...    | ...                        | ...    | ...     | ...    | ...                         | 180      | 180                         | 180    | 180                           | 180     |                                 |       |                           |  |
| New nonconcessional external debt contracted or guaranteed by the central government or the BM or selected state-owned enterprises with maturity of one year or more (cumulative ceiling over the duration of the program, US\$ millions) <sup>2</sup>                                   | 1,500                        | 1,500  | 1,498  | M      | 1,500                      | 1,500  | 1,498   | M      | 1,500                       | ...      | ...                         | ...    | ...                           | ...     |                                 |       |                           |  |
| Stock of short-term external debt contracted or guaranteed by the central government (ceiling) <sup>2</sup>  | 0                            | 0      | 0      | M      | 0                          | 0      | 0       | M      | 0                           | 0        | 0                           | 0      | 0                             | 0       |                                 |       |                           |  |
| External payments arrears of the central government (ceiling, US\$ millions) <sup>2</sup>  | 0                            | 0      | 0.3    | NM     | 0                          | 0      | 1.0     | NM     | 0                           | 0        | 0                           | 0      | 0                             | 0       |                                 |       |                           |  |
| <b>Indicative targets</b>  |                              |        |        |        |                            |        |         |        |                             |          |                             |        |                               |         |                                 |       |                           |  |
| Government revenue (cumulative floor)  | 70,093                       | 70,093 | 68,211 | NM     | 110,230                    | ...    | 108,516 | NM     | 151,000                     | 151,000  | 35,289                      | 81,164 | 128,804                       | 176,444 |                                 |       |                           |  |
| Priority spending (cumulative floor) <sup>3</sup>  | ...                          | ...    | ...    | ...    | ...                        | ...    | ...     | ...    | ...                         | ...      | ...                         | ...    | ...                           | ...     |                                 |       |                           |  |

Sources: Mozambican authorities and IMF staff estimates.  
<sup>1</sup> For definition and adjustors, see the Program Monitoring Section of the Memorandum of Economic and Financial Policies and the Technical Memorandum of Understanding.  
<sup>2</sup> Assessed on a continuous basis.  
<sup>3</sup> Targets will be set in the 6th PSI review after the authorities revise the definition.

**Table 2. Mozambique: Structural Benchmarks for 2015-16**

| <b>Structural Benchmarks</b>  | <b>Date of Implementation</b> | <b>Comment</b>                                     | <b>Macroeconomic Relevance</b>                 |
|---|-------------------------------|--|--|
| The Government will finalize and fully operationalize the IT application for payments of VAT, ISPC, and corporate and personal income taxes through banks. (¶129 of the MEFP dated December 12, 2014)   | End-June 2015                 | Not met. Completed with delay in November 2015.    | Strengthening tax administration               |
| The Government will include in the draft 2015 budget a fiscal rule on the use of windfall revenue only for investment spending, debt reduction and exceptional needs. (¶126 of the MEFP dated December 12, 2014)  | End-June 2015                 | Met  | Ensuring fiscal sustainability                 |
| The Government will issue budget guidelines requiring a mandatory technical assessment by the Investment Evaluation Committee for new public investment projects to be included in the 2016 and subsequent budgets of a value of \$50 million or more. (¶117 of the MEFP dated December 12, 2014) | End-July 2015                 | Met  | Strengthening public investment management     |
| The use of T-bonds as collateral in money market operations will become operational. (¶141 of the MEFP dated December 12, 2014)   | End-September 2015            | Not met. Completed with delay in November 2015.    | Deepening capital markets                      |
| Produce an assessment on fiscal risks for inclusion in the 2016 budget documents. (¶121 of the MEFP dated June 12, 2015)  | End-October 2015              | Not met. Completed with delay in November 2015.    | Improving the management of fiscal risks (PFM) |
| The draft law on the establishment of a movable collateral registry will be submitted to the Council of Ministers. (¶147 of the MEFP dated December 12, 2014 and ¶144 of the MEFP dated June 12, 2015)  | End- November 2015            | Not met. Proposed to be rescheduled to March 2016. | Deepening financial markets                    |

**Table 2. Mozambique: Structural Benchmarks for 2015-16 (concluded)**

| <b>Structural Benchmarks</b>  | <b>Date of Implementation</b> | <b>Comment</b>   | <b>Macroeconomic Relevance</b>                        |
|---|-------------------------------|--|---|
| Complete mandatory assessments by the Investment Evaluation Committee (or any other government body created to replace this Committee in the new MEF structure) of all public investment projects exceeding \$50 million that are included in the 2016 budget and/or the revised integrated investment program (IIP). (¶12 of the MEFP dated June 12, 2015) | End-December 2015             | Approved in 4 <sup>th</sup> Review                               | Strengthening public investment management (PFM)      |
| Submit to the Council of Ministers the National Financial Inclusion Strategy by the Bank of Mozambique. (¶44 of the MEFP dated June 12, 2015)   | End-December 2015             | Approved in 4 <sup>th</sup> Review                               | Increasing access to financial services               |
| Issue a decree or administrative order that makes the real-time recording of the commitment and verification of expenditures mandatory for all units operating within e-SISTAFE. (¶17 of the MEFP dated June 12, 2015)  | End-January 2016              | Not expected to be met. Proposed to be rescheduled to June 2016. | Strengthening expenditure coverage and tracking (PFM) |
| Enforce the law that requires 20 percent withholding tax on interests earned on T-bills, OTs, secured and unsecured interbank transactions. (¶38 of the MEFP dated June 12, 2015)   | End-January 2016              | Met  | Developing the Interbank Money Market                 |

Sources: IMF staff and the Mozambique authorities.



**Table 3. Mozambique: Corrective Policy Measures Implemented in November and December 2015**

| <b>Policy Measures</b>  | <b>Date of Implementation</b> |
|---|-------------------------------|
| Approval by the National Assembly of a revised 2016 Budget consistent with the fiscal framework agreed under the 5 <sup>th</sup> PSI review.  | December 13, 2015             |
| Increase reserve requirements by 150 basis points and the FPC reference rate by 50 basis points and the FPD rate by 75 basis points in the November meeting of the Monetary Policy Committee. | November 17, 2015             |
| Ensuring that central bank interventions take place at the effective interbank foreign exchange market rate.  | November 30, 2015             |

Sources: IMF staff and the Mozambican authorities.

**Table 4. Mozambique: Proposed New Structural Benchmarks for 2015-2016**

| <b>Structural Benchmarks</b>  | <b>Date of Implementation</b> | <b>Comment</b> | <b>Macroeconomic Relevance</b>                 |
|---|-------------------------------|----------------|--|
| Create a dedicated subaccount to pay VAT refunds, to be regularly replenished by the refund claims received to prevent the accumulation of new arrears. (¶23 of this MEFP)  | End-December 2015             | Proposed       | Strengthening PFM and tax administration       |
| The BM will approve and publish the regulations on the law on private credit registry bureaus. (¶43 of this MEFP)   | End-March 2016                | Proposed       | Increasing access to credit                    |
| The BM will approve an Action Plan aimed at addressing the issues observed during the simulation exercise on the Financial Sector Contingency Plan in April 2015 and improving the legal and operational framework of crisis management. (¶41 of this MEFP) | End-March 2016                | Proposed       | Enhancing stability of the financial system    |
| Adopt an action plan which aims at improving profitability of EMATUM. (¶32 of this MEFP)  | End-April 2016                | Proposed       | Improving the management of fiscal risks (PFM) |
| Sources: IMF staff and the Mozambican authorities.  |                               |                |  |

## Attachment II. Technical Memorandum of Understanding

December 2, 2015

1. This Technical Memorandum of Understanding (TMU) defines the quantitative assessment criteria, indicative targets, and structural benchmarks on the basis of which the implementation of the Fund-supported program under the Policy Support Instrument (PSI) will be monitored. In addition, the TMU establishes the terms and timeframe for transmitting the data that will enable Fund staff to monitor program implementation.

### Definitions

#### A. Net credit to the central government

2. Net credit to the central government (NCG) by the banking system is defined as the difference between the outstanding amount of bank credits to the central government and the central government's deposits with the banking system, excluding deposits in project accounts with the banking system, recapitalization bonds issued to the Bank of Mozambique (BM), and proceeds from the signing fee for mineral resource exploration. Credits comprise bank loans, advances to the central government and holdings of central government securities and promissory notes. NCG will be calculated based on data from balance sheets of the monetary authority and commercial banks as per the monetary survey. The limits on the change in NCG by the banking system will be cumulative from end-December of the previous year.

3. The central government encompasses all institutions whose revenue and expenditure are included in the state budget (*Orçamento do Estado*): central government ministries, agencies without financial autonomy, and the administration of 11 provinces. Although local governments (43 municipalities or *autarquias*) are not included in the definition because they are independent, part of their revenue is registered in the state budget as transfers to local governments.

4. For program purposes, net disbursements on the nonconcessional Portuguese credit line are excluded from the assessment criterion of NCG since the corresponding expenditure is not covered under the definition of central government specified in paragraph 3.

#### B. Government revenue and financing

5. Revenue is defined to include all receipts of the General Directorate of Tax (*Direcção Geral dos Impostos, DGI*), the General Directorate of Customs (*Direcção Geral das Alfândegas, DGA*), and nontax revenue, including certain own-generated revenues of districts and some line ministries, as defined in the budget. Revenue is gross revenue net of verified VAT refund requests (*pedidos verificadas de reembolsos solicitados*). Net receipts from privatization received by the National Directorate of State Assets (*Direcção Nacional do Património do Estado*) and unrealized profits transferred by the central bank to the treasury will not be considered as revenue (above the line) and will be accounted for as other domestic financing (below the line).

6. For the purpose of program monitoring, revenue is considered as collected at the time when it is received by the relevant government collecting agencies, in cash or checks, or through transfers into the respective bank account.

### C. Priority social spending

7. Priority social spending is based on the PARPA program categories expanded to incorporate all areas under the new PARP. Accordingly, it will include total spending in the following sectors: (i) education; (ii) health; (iii) HIV/AIDS; (iv) infrastructure development; (v) agriculture; (vi) rural development; a (vii) governance and judicial system, and (viii) social action, labor and employment.

### D. Reserve money

8. For the purposes of program monitoring reserve money is defined as the sum of currency issued by the BM and commercial banks' holdings at the BM. The target is defined in terms of the average of the daily end-of-day stocks in the month of the test date, and its foreign currency component is evaluated at the program exchange rate specified in Table 1. The reserve money stock will be monitored and reported by the BM.

### E. Net international reserves

9. Net international reserves (NIR) of the BM are defined as reserve assets minus reserve liabilities. The BM's reserve assets include (a) monetary gold; (b) holdings of SDRs; (c) reserve position at the IMF; (d) holdings of foreign exchange; and (e) claims on nonresidents, such as deposits abroad (excluding the central government's savings accounts related to mineral resource extraction concessions). Reserve assets exclude assets pledged or otherwise encumbered (such as swaps) and include but are not limited to assets used as collateral or guarantee for a third-party external liability (assets not readily available). The BM's reserve liabilities include: (a) all short-term foreign exchange liabilities to nonresidents with original maturity of up to and including one year; and (b) all liabilities to the IMF.

### F. Debt

#### Definition of debt

For program purposes, the definition of debt is set out in paragraph 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to Executive Board Decision No. 15688-(14/107), adopted December 5, 2014.<sup>1</sup>

(a) For the purpose of this guideline, the term "debt" will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the

<sup>1</sup> [www.imf.org](http://www.imf.org).

obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:

- (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
- (ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and
- (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.

(b) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

## Coverage of debt

10. For the purposes of this debt limit ceiling, public sector debt covers public and publicly guaranteed debt contracted or guaranteed by the public sector. Contracting of credit lines with no predetermined disbursement schedules or with multiple disbursements will be also considered as contracting of debt.

11. The public sector comprises the central government, the BM, the Road Fund, the water authorities (FIPAG), the electricity company (EDM), and the hydrocarbon company (ENH), or by enterprises and agencies in which the above entities hold a majority stake. The debt limit ceiling also applies to debt contracted by these four state-owned enterprises from domestic banks or from other state-owned enterprises that is contractually inter-related to external nonconcessional loans.

12. For program purposes, the guarantee of a debt arises from any explicit legal or contractual obligation of the public sector to service a debt owed by a third party debtor (involving payments in cash or in kind).

### **Concessional**

For program purposes, a debt is concessional if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt.<sup>2</sup> For debts with a grant element equal or below zero, the PV will be set equal to the nominal value of the debt. The discount rate used for this purpose is the unified discount rate of 5 percent set forth in Executive Board Decision No. 15248-(13/97).

13. For debts carrying a variable interest rate in the form of a benchmark interest rate plus a fixed spread, the PV of the debt would be calculated using a program reference rate plus the fixed spread (in basis points) specified in the debt contract. The program reference rate for the six-month USD LIBOR is 3.02 percent and will remain fixed for the duration of the program. Where the variable rate is linked to a benchmark interest rate other than the six-month USD LIBOR, a spread reflecting the difference between the benchmark rate and the six-month USD LIBOR (rounded to the nearest 50 bps) will be added. Specifically, the spread of six-month Euro LIBOR over six-month USD LIBOR is -250 basis points. The spread of six-month JPY LIBOR over six-month USD LIBOR is -250 basis points. The spread of six-month GBP LIBOR over six-month USD LIBOR is -100 basis points. For interest rates on currencies other than Euro, JPY, and GDP, the spread over six-month USD LIBOR is -200 basis points.<sup>3</sup>

### **Assessment criterion on the PV of new external debt**

14. An assessment criterion (ceiling) applies to the PV of new external debt. The concept of external debt is defined on the basis of the residency of the creditor. The ceiling also applies to debt contracted or guaranteed for which value has not yet been received, including private debt for which official guarantees have been extended. This assessment criterion will be assessed on a continuous basis. The ceiling is subject to an adjustor defined below.

### **Stock of short-term external debt contracted or guaranteed by the central government**

15. The central government will not contract or guarantee external debt with original maturity of less than one year. The concept of external debt is defined on the basis of the

<sup>2</sup>The calculation of concessionality takes into account all aspects of the debt agreement, including maturity, grace period, payment schedule, upfront commissions, and management fees.

<sup>3</sup>The program reference rate and spreads are based on the "average projected rate" for the six-month USD LIBOR over the following 10 years from the Fall 2015 World Economic Outlook (WEO).

residency of the creditor. Excluded from this assessment criterion are short-term, import-related trade credits. This assessment criterion will be assessed on a continuous basis.

### **External payments arrears of the central government**

16. The government undertakes not to incur payments arrears on external debt contracted or guaranteed by the central government, with the exception of external payments arrears arising from central government debt that is being renegotiated with creditors. This assessment criterion will be assessed on a continuous basis.

### **G. Foreign program assistance**

17. Foreign program assistance is defined as grants and loans received by the Ministry of Finance through BM accounts excluding those related to projects (Table 1).

### **H. Actual external debt service payments**

18. Actual external debt service payments are defined as cash payments on external debt service obligations of the central government and central bank, including obligations to Paris Club and other bilateral creditors rescheduled under enhanced HIPC Initiative completion point terms, multilateral creditors, and private creditors, but excluding obligations to the IMF (Table 1).

## **Adjusters**

### **I. Net international reserves**

19. The quantitative targets (floors) for net international reserves (NIR) will be adjusted:

- downward by the shortfall in external program aid less debt service payments (up to US\$200 million), compared to the program baseline (Table 1);
- upward by any windfall capital gain tax receipts in excess of US\$30 million collected during the program period;
- downward/upward for any revision made to the end-year figures corresponding to the previous year; and
- downward to accommodate higher external outlays because of natural disasters, up to US\$20 million.
- Upward for any implicit or explicit reimbursement of past public or publicly guaranteed debt service as a result of refinancing of obligations. This in particular applies to a potential refinancing of the international bond originally issued by EMATUM.

### **J. Net credit to central government**

20. The quantitative targets (ceilings) for net credit to the central government (NCG) will be adjusted:

- upward by the shortfall in the MT value of external program aid receipts less debt service payments (up to the MT equivalent of US\$200 million at exchange rates prevailing at the respective test dates), compared to the program baseline (Table 1);
- downward by any windfall capital gain tax receipts in excess of US\$ 30 million collected during the program period;
- downward by privatization proceeds in excess of those envisaged in the program, unless these proceeds are deposited in the government's savings accounts abroad;
- downward (upward) for any increase (decrease) in the discounted amount of the government securities issued for VAT refund backlogs compared to the program baseline (MT 8,200 million) for December 2015;
- downward (upward) for any increase (decrease) in domestic financing from the nonfinancial private sector; and
- upward to accommodate the higher locally-financed outlays because of natural disasters, up to the MT equivalent of US\$20 million at exchange rates prevailing at the respective test dates.

#### **K. Reserve money**

21. The ceiling on reserve money for every test date will be adjusted downward/upward to reflect decreases/increases in the legal reserve requirement on the liabilities in commercial banks. The adjuster will be calculated as the change in the reserve requirement coefficient multiplied by the amount of commercial banks' liabilities subject to reserve requirement, considered at the end of the period of constitution of the required reserves prior to the change in regulation.

#### **L. Government revenue**

22. The quantitative targets (floors) for government revenue will be adjusted upward by any windfall capital gain tax receipts in excess of US\$ 30 million collected during the program period.

#### **M. Debt**

23. An adjuster of up to 5 percent of the external debt ceiling set in PV terms applies to this ceiling, in case deviations from the performance criterion on the PV of new external debt are prompted by a change in the financing terms (interest, maturity, grace period, payment schedule, upfront commissions, management fees) of a debt or debts. The adjuster cannot be applied when deviations are prompted by an increase in the nominal amount of total debt contracted or guaranteed.

### **Data and other Reporting**

24. The Government will provide Fund staff with:

- monthly and quarterly data needed to monitor program implementation in relation to the program's quantitative targets and broader economic developments;



- weekly updates of the daily data set out in Table 1;
- weekly data set out in Table 4 of the TMU dated May 26, 2005;
- monthly updates of the foreign exchange cash flow of the BM;
- monthly data on government revenues (in detail according to the fiscal table) with a lag not exceeding one month;
- monthly data on verified VAT refund requests;
- monthly information on the balance of government savings accounts abroad;
- monthly data on domestic arrears;
- monthly data on external arrears;
- monthly budget execution reports (that will also be published) with a time lag not exceeding 45 days;
- the “mapa fiscal” with a time lag not exceeding 60 days;
- monthly monetary survey data with a time lag not exceeding 30 days;
- monthly data on gross international reserves, with the composition by original currencies and converted to US dollars at the actual exchange rates; and
- quarterly balance-of-payments data with a time lag not exceeding 65 days;
- monthly disbursements on the nonconcessional Portuguese credit line with a time lag not exceeding 30 days.

25. The monetary survey made available by the BM will clearly identify donor-financed project deposits (with a breakdown between foreign and domestic currency) included in net credit to the government in both the central bank’s and commercial banks’ balance sheets.

26. The Government will provide Fund staff with documentation concerning external loan agreements once these have been signed and become effective.

27. The Government will provide Fund staff with an annual borrowing plan for external debt contraction for the upcoming year as well as any updates to the borrowing plan for the ongoing year. The annual borrowing plan should list individually all new loans that are planned to be contracted with their prospective financing terms (nominal amount, interest, maturity, grace period, payment schedule, upfront commissions, management fees, grants included).

TMU Table 1. Mozambique: Net Foreign Assistance, 2015Q1-2016Q4

|   | 2015    |        |       |        | 2016        |        |        |        |
|---|---------|--------|-------|--------|-------------|--------|--------|--------|
|   | Q1      | Q2     | Q3    | Q4     | Q1          | Q2     | Q3     | Q4     |
|   | Actuals |        |       | Proj.  | Projections |        |        |        |
| Net foreign program assistance (US\$ mn)                  | 47      | -36    | -2    | 105    | -62         | 27     | -72    | 59     |
| Gross foreign program assistance                          | 91      | 5      | 110   | 140    | 54          | 66     | 43     | 98     |
| Program grants  | 67      | 5      | 63    | 66     | 43          | 66     | 43     | 48     |
| Program loans   | 24      | 0      | 48    | 74     | 12          | 0      | 0      | 50     |
| External debt service                                     | 44      | 41     | 112   | 34     | 116         | 39     | 115    | 38     |
| Cumulative net foreign program assistance in US dollars   | 47      | 11     | 9     | 114    | -62         | -35    | -107   | -48    |
| Gross foreign program assistance                          | 91      | 96     | 206   | 346    | 54          | 120    | 163    | 260    |
| External debt service                                     | 44      | 85     | 197   | 232    | 116         | 155    | 270    | 308    |
| Net foreign program assistance (MT mn)                    | 1,654   | -1,348 | -78   | 4,690  | -2,802      | 1,224  | -3,275 | 2,721  |
| Gross foreign program assistance                          | 3,182   | 181    | 4,507 | 6,218  | 2,442       | 2,972  | 1,968  | 4,469  |
| Program grants  | 2,343   | 181    | 2,555 | 2,948  | 1,918       | 2,972  | 1,968  | 2,179  |
| Program loans   | 840     | 0      | 1,951 | 3,271  | 523         | 0      | 0      | 2,289  |
| External debt service                                     | 1,528   | 1,528  | 4,585 | 1,528  | 5,244       | 1,748  | 5,244  | 1,748  |
| Cumulative Net foreign program assistance in MTN millions | 1,654   | 307    | 229   | 4,919  | -2,802      | -1,578 | -4,853 | -2,132 |
| Gross foreign program assistance                          | 3,182   | 3,363  | 7,870 | 14,088 | 2,442       | 5,414  | 7,382  | 11,851 |
| External debt service                                     | 1,528   | 3,056  | 7,641 | 9,169  | 5,244       | 6,991  | 12,235 | 13,983 |
| Program exchange rate for reserve money calculation       | ...     | ...    | ...   | 45.0   | 45.9        | 45.9   | 45.9   | 45.9   |

Source: Mozambican authorities and IMF staff estimates.



# REPUBLIC OF MOZAMBIQUE

STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION,  
FIFTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT  
AND REQUEST FOR MODIFICATION OF ASSESSMENT  
CRITERIA, AND REQUEST FOR AN 18-MONTH  
ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY—  
INFORMATIONAL ANNEX

December 3, 2015

Prepared By

African Department

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## RELATIONS WITH THE FUND

(As of September 30, 2015)

**Membership Status:** Joined: September 24, 1984; Article VIII

| <b>General Resources Account:</b> | <b>SDR Million</b> | <b>%Quota</b> |
|-----------------------------------|--------------------|---------------|
| Quota                             | 113.60             | 100.00        |
| Fund holdings of currency         | 113.58             | 99.98         |
| Reserve Tranche Position          | 0.03               | 0.02          |

| <b>SDR Department:</b>    | <b>SDR Million</b> | <b>%Allocation</b> |
|---------------------------|--------------------|--------------------|
| Net cumulative allocation | 108.84             | 100.00             |
| Holdings                  | 82.05              | 75.38              |

| <b>Outstanding Purchases and Loans:</b> | <b>SDR Million</b> | <b>%Allocation</b> |
|---|--------------------|--------------------|
| ESF Arrangements                        | 95.14              | 83.75              |
| ECF Arrangements                        | 1.63               | 1.43               |

### Latest Financial Arrangements:

|                  | Date of      | Expiration   | Amount Approved | Amount Drawn  |
|------------------|--------------|--------------|-----------------|---------------|
| Type             | Arrangement  | Date         | (SDR Million)   | (SDR Million) |
| ESF              | Jun 30, 2009 | Jun 28, 2010 | 113.60          | 113.60        |
| ECF <sup>1</sup> | Jul 06, 2004 | Jul 05, 2007 | 11.36           | 11.36         |
| ECF <sup>1</sup> | Jun 28, 1999 | Jun 27, 2003 | 87.20           | 78.80         |

<sup>1</sup>Former PRGF.

**Projected Payments to Fund<sup>1</sup>****(SDR Million; based on existing use of resources and present holdings of SDRs):**

|                      | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> |
|----------------------|-------------|-------------|-------------|-------------|-------------|
| Principal            | 3.00        | 23.70       | 23.21       | 22.72       | 22.72       |
| Charges/<br>Interest | 0.00        | 0.02        | 0.15        | 0.10        | 0.04        |
| <b>Total</b>         | 3.01        | 23.71       | 23.36       | 22.82       | 22.76       |

**Implementation of HIPC Initiative:**

|  | <u>Original<br/>Framework</u> | <u>Enhanced<br/>Framework</u> | <u>Total</u> |
|--|-------------------------------|-------------------------------|--------------|
| Commitment of HIPC assistance  |                               |                               |              |
| Decision point date  | Apr 1998                      | Apr 2000                      |              |
| Assistance committed<br>by all creditors (US\$ Million) <sup>2</sup> | 1,716.00                      | 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                     |              |
| 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 <sup>3</sup>              | --                            | 1.10                          | 1.10         |
| <b>Total disbursements</b>   | 93.17                         | 14.83                         | 108.00       |

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

<sup>2</sup> 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.

<sup>3</sup> 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):**

|  |        |
|--|--------|
| DRI-eligible debt (SDR Million) <sup>4</sup> | 106.56 |
| Financed by: MDRI Trust                      | 83.05  |
| Remaining HIPC resources                     | 23.51  |

Debt Relief by Facility (SDR Million)

| <u>Eligible Debt</u> |            |             |              |
|----------------------|------------|-------------|--------------|
| <u>Delivery Date</u> | <u>GRA</u> | <u>PRGF</u> | <u>Total</u> |
| January 2006         | N/A        | 106.56      | 106.56       |

**Implementation of Catastrophe Containment and Relief (CCR):** Not Applicable**Safeguards assessment**

As required under the safeguards policy, the Bank of Mozambique (BM) will be subject to an update safeguards assessment. The previous assessment, completed in 2010, found improvements in financial reporting practices. However, vulnerabilities in the oversight mechanism for external and internal auditing, controls, and in the BM's legal structure were noted. It recommended amendments to the law to address the need for independent oversight, including through the establishment of an Audit Committee comprising non-executive Board members and external experts.

**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.

On May 20, 2011, Mozambique accepted its obligations under Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement ([www.imf.org](http://www.imf.org)). A new foreign exchange law—"Foreign Exchange Law" Law No. 11/2009—came into effect on March 11, 2009. A new foreign exchange regulation to implement the foreign exchange law—the "Regulation for the Foreign Exchange Law" (the "Regulation") (Decreto No. 83/2010)—was issued on December 31, 2010. The Regulation, in conjunction with the implementing norms subsequently issued by the BM, fully removed the existing exchange restrictions subject to Article

<sup>4</sup>The MDRI provides 100 percent debt relief to eligible member countries 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 outstanding at the time the member qualifies for debt relief.

VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement as of July 11, 2011. The two existing multiple currency practices (MCP) were also removed. The MCP arising from the foreign exchange auction system was removed on April 27, 2011 through the adoption of a new regulation on the interbank exchange market and that discontinued the previous multiple price foreign exchange auction system, which in any case had not been used since 2009. The MCP arising from the absence of a mechanism to prevent potential deviations between the rate used by the BM in its foreign exchange transactions in the interbank foreign exchange market and in its transactions with the government, public entities and the World Bank was removed on July 1, 2011 through the adoption of a new mechanism for the determination of the exchange rate for such transactions of which the relevant parties have been notified on August 11, 2011.

### **AML/CFT framework**

Mozambique has taken a number of 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 ML 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 and are scheduled to be tabled in Parliament in the session commencing October 2015. The Financial Intelligence Unit (GIFIM) continues to work towards membership of the Egmont Group of Financial Intelligence Units. The IMF is currently providing assistance in developing a supervisory framework for real estate agents and dealers in precious metals and stones. Going forward, the authorities should build on progress achieved and focus their attention on strengthening their capacity to effectively implement the legal and regulatory framework.

### **Article IV Consultation**

Mozambique is on a 24-month consultation cycle, in accordance with Decision No. 14747-(10/96). The 2013 Article IV consultation was completed by the Executive Board on June 24, 2013 (Country Report No. 13/200).

In concluding the 2013 Article IV consultation, Executive Directors commended the authorities for their policies, which have translated into a strong macroeconomic performance in recent years. While the medium-term growth outlook is favorable, it will be important to manage risks stemming from the external and internal environments. Directors called for continued commitment to sound policies and structural reforms to preserve macroeconomic stability, foster inclusive growth, and reduce poverty. Recognizing the need to support public investment and social development, Directors emphasized the importance of fiscal prudence as revenues from extractive industries will remain modest in the near term. To limit fiscal risks, they advised prioritization of current spending, in particular containing the wage bill. They also called for steps to modernize revenue administration, strengthen public financial management, and ensure timely settlement of VAT refunds. Directors also saw merit in developing a fiscal policy framework that incorporates the anticipated natural resource receipts over the medium term. Directors acknowledged that the current high level of public investment can make an important

contribution to improving infrastructure and enabling Mozambique to access its natural resource wealth. However, they recommended careful monitoring of the pace and effectiveness of these investments in order to maximize returns, avoid hitting absorptive capacity constraints, and preserve debt sustainability. In this context, Directors encouraged the authorities to continue to strengthen their medium-term debt strategy as well as project selection and monitoring. Directors encouraged the authorities to continue to implement their Poverty Reduction Strategy. A renewed focus on job creation, improvements in agricultural productivity, and economic diversification hold the key to more inclusive growth in the period ahead.

### **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.

### **FSAP participation and ROSCs**

A Financial Sector Assessment Program (FSAP) for Mozambique was undertaken during the first quarter of 2003. The related Financial Sector Stability Assessment was circulated to the Executive Board on November 19, 2003 (Country Report No. 04/52). An update to the FSAP took place in February 2009 and the related Financial Sector Stability Assessment circulated to the Board on June 19, 2009 (Country Report No. 10/12). A ROSC on fiscal transparency was issued on February 22, 2001. This ROSC was updated in the context of the 2002 Article IV consultation (Country Report No. 02/140) and the 2003 Article IV Consultation (Country Report No. 04/50). The ROSC on fiscal transparency was updated in May 2008. A Report on the Observance of Standards and Codes (ROSC) data module was prepared in June 2002 and issued on March 5, 2003. This data module was updated in August 2005.

### **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. Alex Segura-Ubierno has been the IMF's resident representative to Mozambique since August 1, 2013.



**Technical Assistance (2013–2015)**

| <b>IMF Technical Assistance Provided to Mozambique (2013–15)</b><br>(As of December, 2015) |                    |                            |   |   |
|--|--------------------|----------------------------|---|---|
| <b>Departments</b>   | <b>Timing</b>      | <b>Form</b>                | <b>Purpose</b>  | <b>Counterparts</b>   |
| Fiscal Affairs   | December 2015      | Mission                    | MNRW-TTF – Follow-up on natural resources tax administration  | AT/Ministry of Economy and Finance  |
|  | November 2015      | Mission                    | Annual follow-up on PFM reforms (including fiscal risks and public investment, PIMA)                              | Ministry of Economy and Finance   |
|  | November 2015      | Mission                    | Follow-up on Revenue Administration   | AT/ Ministry of Economy and Finance                                       |
|  | October 2015       | Mission                    | Fuel imports and subsidies  | Ministry of Economy and Finance, Ministry of Mineral Resources and Energy |
|  | April 2015         | Mission                    | Follow-up on PFM reforms  | Ministry of Economy and Finance   |
|  | March 2015         | Mission                    | Tax administration performance assessment (TADAT)   | AT/ Ministry of Economy and Finance                                       |
|  | March 2015         | Mission (jointly with AFR) | MNRW-TTF – Update on natural resources tax projections  | AT/ Ministry of Economy and Finance                                       |
|  | August 2014        | Mission                    | Public accounting   | Ministry of Finance   |
|  | August 2014        | Mission (jointly with AFS) | Net VAT   | AT/Ministry of Finance  |
|  | July 2014          | Joint IMF WB mission       | Medium-term debt strategy   | Ministry of Finance   |
|  | June 2014          | Mission                    | MNRW-TTF – Mining and petroleum fiscal regime reform and tax projections  | AT/Ministry of Finance  |
|  | April 2014         | Mission                    | Annual follow-up on revenue administration (including experts specialized in IT tax systems and internal control) | AT/Ministry of Finance  |
|  | March – April 2014 | Mission                    | MNRW-TTF - Follow-up on natural resources tax administration  | AT/Ministry of Finance  |
|  | January 2014       | Mission                    | Annual follow-up on PFM reforms   | Ministry of Finance   |

| <b>IMF Technical Assistance Provided to Mozambique, 2013–15 (continued)</b> |                  |                     |  |   |
|---|------------------|---------------------|--|---|
| <b>(As of December, 2015)</b>   |                  |                     |  |   |
| <b>Departments</b>  | <b>Timing</b>    | <b>Form</b>         | <b>Purpose</b>   | <b>Counterparts</b>                                   |
|   |                  |                     |  |   |
|   | November 2013    | Mission             | Fiscal transparency evaluation   | Ministry of Finance                                   |
|   | November 2013    | Mission             | Follow-up on revenue Administration  | AT/Ministry of Finance                                |
|   | November 2013    | Peripatetic experts | Net VAT system   | AT/Ministry of Finance                                |
|   | July 2013        | Mission             | MNRW-TTF - Follow-up on natural resources tax administration   | AT/Ministry of Finance                                |
|   | July 2013        | Mission             | MNRW-TTF - Follow-up on mining and petroleum fiscal regime reform  | AT/Ministry of Finance                                |
|   | May 2013         | Mission             | MNRW-TTF - Public consultation of the revised fiscal regime for mining and petroleum   | AT/Ministry of Finance, Ministry of Mineral Resources |
|   | April 2013       | Mission             | Annual follow-up on PFM reforms  | Ministry of Finance                                   |
|   | April 2013       | Peripatetic expert  | Public accounting  | Ministry of Finance                                   |
|   | March-April 2013 | Mission             | Follow-up on revenue administration (including experts specialized in natural resources tax collection, HR, net VAT, taxpayer's services)                                | AT/Ministry of Finance                                |
|   | March-April 2013 | Peripatetic expert  | Taxpayer service (jointly with FAD annual follow-up on revenue administration)   | AT/Ministry of Finance                                |
|   | March-April 2013 | Mission             | MNRW-TTF – Tax administration action plan for effectively managing increased natural resources collections (jointly with FAD annual follow-up on revenue administration) | Ministry of Finance, Ministry of Mineral Resources    |
|   | March 2013       | Peripatetic expert  | Transfer pricing   | Ministry of Finance                                   |
| Legal   | September 2015   | Mission             | AML/CFT diagnostic project (Phase II, follow up)   | GIFIM/Bank of Mozambique                              |
|   | April 2015       | Mission             | AML/CFT diagnostic project (Phase II, follow up)   | GIFIM/Bank of Mozambique                              |

| <b>IMF Technical Assistance Provided to Mozambique, 2013–15 (continued)</b> |                  |                    |   |  |
|---|------------------|--------------------|---|--|
| <b>(As of December, 2015)</b>   |                  |                    |   |  |
| <b>Departments</b>  | <b>Timing</b>    | <b>Form</b>        | <b>Purpose</b>  | <b>Counterparts</b>                                    |
|   | April 2014       | Mission            | AML/CFT diagnostic project (Phase II)   | GIFIM/Bank of Mozambique                               |
|   | September 2013   | Mission            | AML/CFT diagnostic project (Follow up)  | GIFIM/Bank of Mozambique                               |
|   | April 2013       | Mission            | AML/CFT diagnostic project  | GIFIM/Bank of Mozambique                               |
| Monetary and Financial Sectors  | November 2015    | Peripatetic expert | Liquidity forecasting framework (Follow up)                                       | Bank of Mozambique                                     |
|   | November 2014    | Peripatetic expert | Liquidity forecasting framework   | Bank of Mozambique                                     |
|   | April 2014       | Peripatetic expert | Payment and settlement systems oversight (Follow Up)                              | Bank of Mozambique                                     |
|   | November 2013    | Mission            | Assessing technical assistance needs in monetary policy design and implementation | Bank of Mozambique                                     |
| Statistics  | March 2015       | Peripatetic expert | Follow-up on balance of payments statistics reform                                | Bank of Mozambique                                     |
|   | February 2015    | Mission            | MNRW-TTF - Statistics for managing natural resources                              | INE/ Ministry of Economy and Finance                   |
|   | February 2014    | Peripatetic expert | Follow-up on balance of payments statistics reform                                | Bank of Mozambique                                     |
|   | October 2013     | Peripatetic expert | Public finances statistics (GFS)  | Ministry of Finance                                    |
|   | February 2013    | Peripatetic expert | Follow-up on balance of payments statistics reform                                | Bank of Mozambique                                     |
| AFRITAC South (AFS)   | October 2015     | Peripatetic expert | Procedures for Central Bank communication   | Bank of Mozambique                                     |
|   | August 2015      | Peripatetic expert | Strengthening macro-fiscal forecasts and fiscal risks management                  | Ministry of Economy and Finance                        |
|   | April – May 2015 | Peripatetic expert | Follow-up on compliance with Basel core principles                                | Bank of Mozambique                                     |
|   | April 2015       | Mission            | Technical assistance and training priorities going forward                        | Ministry of Economy and Finance and Bank of Mozambique |
|   | April 2015       | Peripatetic expert | Follow-up on national accounts statistics   | INE/ Ministry of Economy and Finance                   |

**IMF Technical Assistance Provided to Mozambique, 2013–15 (concluded)**

(As of December, 2015)

| <b>Departments</b> | <b>Timing</b>       | <b>Form</b>                           | <b>Purpose</b>   | <b>Counterparts</b>                                       |
|--------------------|---------------------|---------------------------------------|--|---|
|                    | May 2015            | Peripatetic expert                    | Follow-up on post control audit reform   | AT/ Ministry of Economy and Finance                       |
|                    | September 2014      | Peripatetic expert                    | National accounts statistics   | INE/Ministry of Finance                                   |
|                    | August 2014         | Peripatetic expert (jointly with FAD) | Implementation of net VAT  | AT/Ministry of Finance                                    |
|                    | June 2014           | Peripatetic expert                    | Cash management and banking arrangements   | Ministry of Finance                                       |
|                    | April 2014          | Peripatetic expert                    | Follow-up on post control audit reform   | AT/Ministry of Finance                                    |
|                    | April 2014          | Peripatetic expert                    | Basel II capital adequacy framework  | Bank of Mozambique  |
|                    | December 2013       | Peripatetic expert                    | Monetary policy framework operations   | Bank of Mozambique  |
|                    | October 2013        | Peripatetic expert                    | Follow-up on public investment management reforms                                    | Ministry of Finance                                       |
|                    | October 2013        | Peripatetic expert                    | Development of a compliance management framework                                     | AT/Ministry of Finance                                    |
|                    | June-July 2013      | Peripatetic expert                    | Follow-up on public investment management reforms                                    | Ministry of Finance                                       |
|                    | April-May 2013      | Peripatetic expert                    | Post control audit (mainly focused on customs but also on joint auditing with taxes) | AT/Ministry of Finance                                    |
|                    | April-May 2013      | Peripatetic expert                    | Audit Training in specialized sectors of activity (taxes)                            | AT/Ministry of Finance                                    |
|                    | March-April 2013    | Peripatetic expert                    | VAT refunds system   | AT/Ministry of Finance                                    |
|                    | February–March 2013 | Peripatetic expert                    | Public Investment Management   | Ministry of Finance, Ministry of Planning and Development |

# WORLD BANK-IMF COLLABORATION

(As of November 9, 2015)

1. **The Fund Mozambique team met with the World Bank Mozambique team in Maputo during the fifth PSI review mission in October 2015.** The objective was to identify macro-critical structural reforms and to coordinate the two teams' work for the period May 2015 to April 2016.
2. **The teams agreed that Mozambique's main macroeconomic challenge is to sustain higher and more inclusive economic growth going forward.** To meet this challenge, Mozambique needs to enable broader-based economic activity led by the private sector, in particular in areas where it has competitive advantages, such as agriculture, trade-related services in support of booming commodity export sectors, labor-intensive manufacturing, and tourism. Given the low level of infrastructure, this will entail policies and reforms to boost public investment, coupled with enhancements in the business environment. As traditional aid is on a gradual declining trend, increasing public investment may require resorting to non concessional financing and stepping up capacity in the investment selection and debt management areas.
3. **Based on this shared assessment, the teams 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 and a series of other projects in the coming years, 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 identify 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 secure 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 program review missions will provide further 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, so as 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 s 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.

5. **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 at least semiannually during Fund program review 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 program review and other missions, and at least semi-annually.

6. **The table below lists the teams' separate and joint work programs from May 2015 to April 2016.**



| <b>Mozambique: Bank and Fund Planned Activities in Macro-Critical Structural Reform Areas, May 2015-April 2016</b> |   |                           |                               |
|--|---|---------------------------|-------------------------------|
| <b>Title</b>   | <b>Products</b>   | <b>Timing of Missions</b> | <b>Expected delivery date</b> |
| <b>1. Bank Work Program</b>  | 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                       |
| <b>2. Fund Work Program</b>  | Annual TA follow-up mission on PFM  | Nov. 2015                 | Jan. 2016                     |
|  | Annual TA follow-up on tax administration   | 2016                      | 2016                          |
|  | MNRW-TTF: FARI, macro fiscal issues   | 2016                      | 2016                          |
|  | TA on Natural Resources Tax Administration  | Dec. 2015                 | Feb. 2016                     |
|  | TA on Natural Resources Statistics  | 2016                      | 2016                          |
|  | TA on price statistics  | 2016                      | 2016                          |
|  | TA on GDP by production and by expenditure  | 2016                      | 2016                          |
|  | TA on risk Based supervision framework  | 2016                      | 2016                          |
| <b>3. Joint Work Program</b>   | 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

### 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 Fund's General Data Dissemination System (GDDS) and 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 new household income and expenditure survey being conducted in 2015-2016 still need 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 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:** 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 and 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 GDDS regional project, the BM has made significant progress toward compiling and disseminating balance of payments (BOP) and international investment position (IIP) statistics. The migration process from the *Balance of Payments Manual, fifth edition (BPM5)* to the *Balance of Payments Manual, sixth edition (BPM6)* has been progressed substantially. BOP and IIP statistics are now disseminated based on BPM6, with only detailed data on megaprojects remaining to be migrated. 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 and consistency with BPM6 methodology for several specific areas (especially in the services account); starting the compilation of quarterly IIP while 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 with regard to price and volume indices, also merits attention. Work is currently ongoing to identify imports of domestic firms that are directly related to providing services to megaprojects. When this work is completed (currently expected in mid-2016), it is expected to allow enhanced analysis of the impact of megaprojects and allow improved estimation of the economy's underlying (non-megaproject) current account position.

## II. Data Standards and Quality

Mozambique commenced its participation in the General Data Dissemination System (GDDS) in November 2003; but has since then not updated much of its metadata.

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 as a result of these efforts.

## III. Reporting to STA

Mozambique does not report fiscal data for publication in the *IFS* or 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 *International Financial Statistics (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 November 4, 2015)

|   | Date of latest observation | Date received | Frequency of Data <sup>7</sup> | Frequency of Reporting <sup>7</sup> | Frequency of publication <sup>7</sup> | Memo Items:  |  |
|---|----------------------------|---------------|--------------------------------|-------------------------------------|---------------------------------------|--|--|
|   |                            |               |                                |                                     |                                       | Data Quality – Methodological soundness <sup>8</sup> | Data Quality Accuracy and reliability <sup>9</sup> |
| Exchange Rates  | Nov. 2015                  | Nov. 2015     | D                              | W                                   | D                                     |  |  |
| International Reserve Assets and Reserve Liabilities of the Monetary Authorities <sup>1</sup>             | Oct. 2015                  | Oct. 2015     | W                              | W                                   | W                                     |  |  |
| Reserve/Base Money  | Nov. 2015                  | Nov. 2015     | D                              | W                                   | D                                     | LO, O, LO, O   | LO, LO, O, O, LO                                   |
| Broad Money   | Sep. 2015                  | Oct. 2015     | M                              | M                                   | M                                     |  |  |
| Central Bank Balance Sheet  | Sep. 2015                  | Oct. 2015     | M                              | M                                   | M                                     |  |  |
| Consolidated Balance Sheet of the Banking System  | Sep. 2015                  | Oct. 2015     | M                              | M                                   | M                                     |  |  |
| Interest Rates <sup>2</sup>   | Sep. 2015                  | Oct. 2015     | M                              | M                                   | M                                     |  |  |
| Consumer Price Index  | Sep. 2015                  | Oct. 2015     | M                              | M                                   | M                                     | O, LO, LNO, O  | LNO, LO, LO, O, O                                  |
| Revenue, Expenditure, Balance and Composition of Financing <sup>3</sup> – General Government <sup>4</sup> | 2015 Q2                    | Oct. 2015     | M,Q                            | Q                                   | Q                                     | LO, LNO, LO, O                                       | LO, O, LO, O, LNO                                  |
| Stocks of Central Government and Central Government-Guaranteed Debt <sup>5</sup>                          | 2015 Q2                    | Oct. 2015     | Q                              | Q                                   | Q                                     |  |  |
| External Current Account Balance  | 2015 Q2                    | Sep. 2015     | Q                              | I                                   | I                                     | LO, LNO, LO, O                                       | LO, LNO, LO, LO, LNO                               |
| Exports and Imports of Goods and Services   | 2015 Q2                    | Sep. 2015     | Q                              | I                                   | I                                     |  |  |
| GDP/GNP   | 2015 Q2                    | Sep. 2015     | Q                              | Q                                   | I                                     | O, LO, O, LO   | LNO, LO, LO, O, LO                                 |
| Gross External Debt   | Dec. 2014                  | March 2015    | A                              | I                                   | I                                     |  |  |
| International Investment Position <sup>6</sup>  | 2014                       | Sep. 2015     | A                              | A                                   | A                                     |  |  |

<sup>1</sup>Any reserve assets that are pledged or 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.

<sup>2</sup>Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.

<sup>3</sup>Foreign, domestic bank, and domestic nonbank financing.

<sup>4</sup>The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

<sup>5</sup>Including currency and maturity composition.

<sup>6</sup>Includes external gross financial asset and liability positions vis-à-vis nonresidents.

<sup>7</sup>Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).

<sup>8</sup>Reflects the assessment provided in the data ROSC published in August, 2008, and based on the findings of the mission that took place during November 29–December 7, 2007 for the dataset corresponding to the variables in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).

<sup>9</sup>Same as footnote 8, except referring to international standards concerning source data, assessment and validation of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.



# REPUBLIC OF MOZAMBIQUE

December 3, 2015

## STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION, FIFTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT AND REQUEST FOR MODIFICATION OF ASSESSMENT CRITERIA, AND REQUEST FOR AN 18-MONTH ARRANGEMENT UNDER THE STANDBY CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

Approved By  
**David Owen and Steven Barnett (IMF) and Seynabou Sakho (IDA)**

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

*This debt sustainability analysis (DSA) provides a further update to the joint IMF/IDA DSA from April 2014 and June 2015 update.<sup>1</sup> Mozambique remains at moderate risk of external public debt distress, but risks have heightened considerably as the metical depreciation vis-à-vis the US dollar of about 25 percent between end-2014 and mid-November 2015 has increased debt level indicators.<sup>2</sup> Relative to GDP and exports, debt levels stand only barely below thresholds in 2015 and will remain elevated in the next few years, though debt service remains manageable. Going forward, downward trajectories in debt ratios should be ensured by the authorities' commendable policy response to strictly limit external and non-concessional borrowing and fiscal consolidation agreed under the program. Meanwhile, improvements in investment planning capacity are important to identify those projects most important for development. In light of upwardly-revised assumptions on the size of investments in the natural gas sector, private external debt will peak above 150 percent of GDP in the early*

<sup>1</sup>The DSA presented in this document is based on the standard low-income countries (LIC) DSA framework. See "Staff Guidance Note on the Application of the Joint Bank-Fund Debt Sustainability Framework for Low-Income Countries" (<http://www.imf.org/external/pp/longres.aspx?id=4827>) and World Bank Report No. ACS6956, 10/23/13). Under the World Bank Country Policy and Institutional Assessment (CPIA); updated on July 25, 2014 with the 2013 CPIA rating, Mozambique maintains the medium policy performer rating, albeit close to the threshold of 3.75 for strong performers, with an average rating of 3.64 during 2012–14; the DSA uses the indicative thresholds for medium performers.

<sup>2</sup> Computed based on US dollars per metical exchange rates; computation based on meticais per US dollar would return a 33 percent depreciation instead.

*2020s. The authorities were in broad agreement with the DSA outlook and presentation. They emphasized that any changes in risk of debt distress rating should not occur purely in response to exogenous factors beyond the authorities' control, such as exchange rate depreciation.*

## UNDERLYING DSA ASSUMPTIONS

**1. There have been significant changes in assumptions compared to the previous DSA.** This DSA is consistent with the macroeconomic framework outlined in the Staff Report for the Fifth Review under the PSI (Box 1). Compared to the previous DSA,<sup>3</sup> the main changes are threefold. First, the continued depreciation of the metical has led to a significant upward shift in debt and debt service ratios in the short term. Second, updated assumptions reflect considerably larger planned investments in the natural gas sector (Box 1 provides details). Third, following the government's new policy, there has been a considerable scaling back of public sector external borrowing plans, which is projected to result in a lower profile of external disbursement over the next years.

**a. The medium-term macroeconomic framework has been updated, including to reflect the metical's depreciation and larger planned size of investments in the natural gas sector** (Text Table 1). The economic outlook remains robust, although somewhat less buoyant than previously projected, with economic growth projected at 6.3 percent in 2015 and 6.5 percent in 2016 (compared to 7.0 and 8.2 percent respectively in the last DSA). The main reasons being slower-than-expected increases in coal production and substantial tightening of fiscal and monetary policies to address external imbalances. Nevertheless, growth is expected to accelerate over the medium term on the back of extractive industries and infrastructure investments. To ensure debt sustainability and alleviate external imbalances, substantial fiscal consolidation is underway and programmed to continue in 2016. After an election-year deficit of over 10 percent of GDP, the fiscal deficit is expected to contract to 6 percent in 2015 and further to 4 percent in 2016—the level at which it would stabilize over the medium term. The current account deficit is projected to increase to 90 percent of GDP by 2020 reflecting significant imports of goods and services, mainly related to construction of processing facilities for liquefied natural gas (LNG). Approximately one third of these imports are financed by FDI with the remainder financed by private debt.

**Text Table 1. Evolution of Selected Macroeconomic Indicators between DSA Updates**

|  | 2013 | 2014 | 2015        | 2016 | 2017 |
|--|------|------|-------------|------|------|
|  |      |      | Projections |      |      |
| <b>Real GDP growth (%)</b>             |      |      |             |      |      |
| Previous DSA                           | 7.4  | 7.4  | 7.0         | 8.2  | 7.9  |
| Current DSA                            | 7.1  | 7.2  | 6.3         | 6.5  | 7.2  |
| <b>Nominal GDP (US\$ billion)</b>      |      |      |             |      |      |
| Previous DSA                           | 15.6 | 16.7 | 17.0        | 19.0 | 21.2 |
| Current DSA                            | 16.0 | 17.0 | 15.2        | 14.8 | 16.4 |
| <b>Overall fiscal deficit (%GDP)</b>   |      |      |             |      |      |
| Previous DSA                           | 2.7  | 10.3 | 6.5         | 5.1  | 5.5  |
| Current DSA                            | 2.7  | 10.6 | 6.0         | 4.0  | 4.3  |
| <b>Current account deficit (% GDP)</b> |      |      |             |      |      |
| Previous DSA                           | 40.0 | 34.7 | 38.2        | 42.1 | 39.9 |
| Current DSA                            | 39.1 | 34.1 | 30.2        | 33.1 | 55.4 |
| <b>FDI (% of GDP)</b>                  |      |      |             |      |      |
| Previous DSA                           | 39.5 | 29.4 | 23.8        | 24.7 | 22.9 |
| Current DSA                            | 38.6 | 28.9 | 25.2        | 30.6 | 28.3 |

<sup>3</sup> See IMF Country Report No. 15/223.

### Box 1. Macroeconomic Assumptions 2015–35

*The medium-term assumptions in the baseline scenario for 2015–35 are consistent with the medium-term macroeconomic framework underlying the Staff Report for the Fifth Review under the Policy Support Instrument and the request for a new arrangement under the Stand By Credit Facility.*

**Real GDP growth** is expected to accelerate to 7–8 percent range over the medium term, supported by the expansion in coal mining and infrastructure investments, including support for coal exports and LNG manufacturing. A sharp increase in growth in 2021 reflects the assumed coming on line of the first natural gas production plant (“train”) and related exports in that year. While growth of the non-LNG sector is sustained in the long term by strong population/labor force growth, continued infrastructure investment, and related productivity gains, overall GDP growth rate will moderate once the LNG production reaches its full capacity in 2028. Risks to 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 are assumed to be under construction during 2016–27. The projection has significantly updated assumptions on this investment in line with information from the private developers and now assumes that 13 onshore LNG manufacturing units (“trains”) and 4 floating trains (FLNG) would be built (versus only 4 onshore trains assumed in the previous DSA). The first onshore train and the first floating train are assumed to start production in 2021, followed by remaining trains sequentially starting production. The final train will start production in 2028. Total investment from 2016 is projected at \$110 billion. The sector’s contribution to GDP is expected to be small during the construction period due to high import content. Annual LNG output will reach 89 million tons in 2028, constituting more than 50 percent of nominal GDP by then. The schedule and size of the projects depend on the timing and content of final investment decisions expected to be made by the investors by end-2016.

**Consumer price inflation** is projected to remain in the authorities’ target range of 5–6 percent over the medium term.<sup>4</sup>

**Export value growth** is considerably higher than in the previous DSA due to revised assumptions on the size of LNG production facilities. On average exports are projected to be 18 percent on average over the projection period, but show large intertemporal variation. Exports are expected to resume modest growth in 2016 before increasing to around 14 percent during 2017–20 as coal exports expand with completion of the Nacala rail corridor. Average annual growth rates are then projected peak around 50 percent during 2021–25 as LNG exports come onstream, before falling back to around 4½ percent when traditional export growth (of 13 percent) becomes their main driver.

**Imports** are projected to contract in the near term in response to metical depreciation and economic adjustment measures, before recovering gradually and reaching 18 percent annual growth during 2023–27, as LNG production increases available resources. Subsequently, import value growth is projected to return to around 10½ percent.

**The non-interest external current account balance** is projected to record a deficit of over 80 percent of GDP in the medium term largely driven by imports for LNG investment.<sup>5</sup> The 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, projected to exceed 10 percent of GDP during the late 2020s and early 2030s.

**The non-interest primary fiscal deficit** is projected to contract in 2015 to 4¾ percent of GDP and further to a range of 2–2½ percent during 2016–20 in response to the fiscal consolidation envisaged under the authorities’ program. The fiscal balance is expected to improve further beyond 2020 as LNG revenue ramps up. The total fiscal revenues from the LNG project throughout the entire project period until 2045 could reach about \$500 billion.<sup>6</sup> 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.

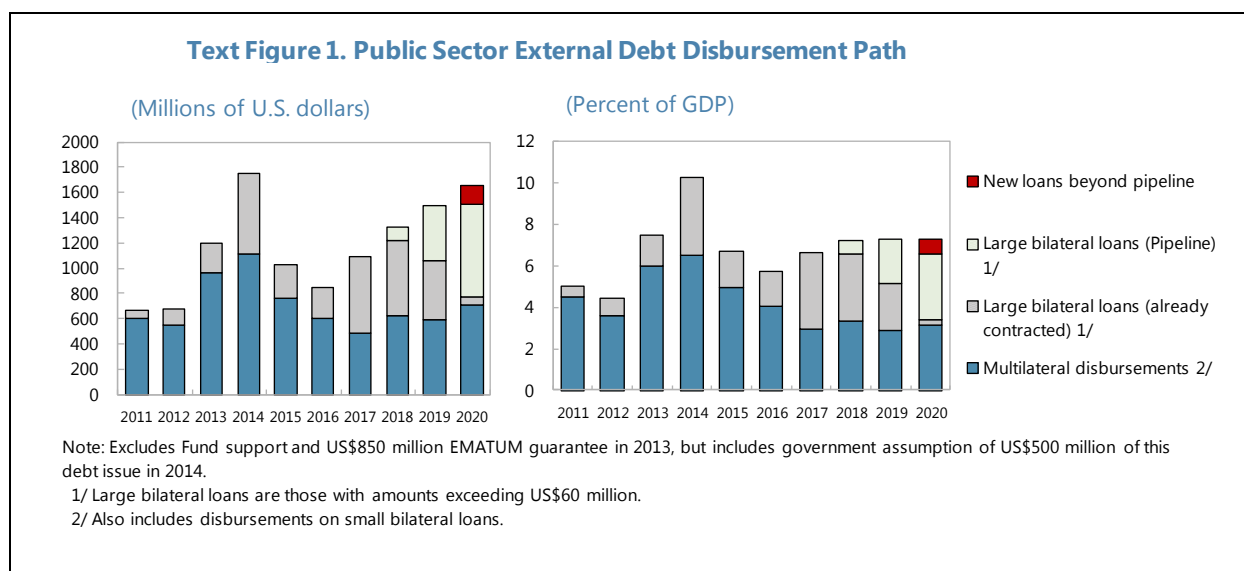
<sup>4</sup> Gas and coal prices, which are important determinants of export receipts, are throughout the projection period expected to remain relatively subdued relative to recent peaks in line with Fall 2015 WEO assumptions.

<sup>5</sup> Meanwhile, the non-megaproject current account is expected to remain on the order of 11–12 percent during the next years.

<sup>6</sup> Main sources of the fiscal revenues are (i) the government’s share of gas profits, (ii) the corporate income tax on the concessionaires, and (iii) the dividends paid by the state-owned hydrocarbon company (ENH), which owns 10 and 15 percent stakes in the two exploration areas where gas has been found.



- b. The external borrowing profile is now considerably more benign, as the authorities have taken strong measures to slow contracting of new debt.** These measures more than offset decreasing donor support, which continues its steady downward trend.<sup>7</sup> In 2015, new borrowing has continued to be limited with face value of new external debt contraction expected to total less than US\$750 million by year-end, of which US\$200 million are non-concessional borrowing.<sup>8</sup> Moreover, the authorities have suspended negotiations on the vast majority of loans, which were considered in the pipeline by the last DSA and totaled US\$ 2.2 billion. These loans have been sent back to line ministries for reevaluation and prioritization. There is currently no clear timeline when (some of) these pipeline loan negotiations may recommence, but any contraction is expected only in 2017 or later and at a more measured pace than in the last DSA. As a result, the external borrowing plan for 2016 envisages lower contraction than in 2015 with loans amounting to US\$400 million, of which about 80 percent are expected at concessional terms (see Staff Report Tables 8, 9). Finally, the updated profile of future disbursements is further reduced by the authorities' decisions to delay implementation of a few projects for which financing has already been obtained (Text Figure 1).
- c. Private sector medium-term borrowing has been considerably revised further upwards, in line with the higher assumptions on LNG investment.** The International Investment Position data now puts private external debt at 31 per-cent of GDP in 2014. It is projected to rise to some 132 percent by 2020, compared to 85 percent in the previous DSA. Debt will also increase further until its peak in 2022 as net repayments commence. The ratio is expected to fall back quickly to below 50 percent by 2030 as LNG revenues are utilized to amortize this private borrowing. This debt is mobilized and repaid entirely through offshore SPVs, which limits risk to the domestic financial system.



<sup>7</sup> Total donor disbursements have fallen from 12 percent of GDP in 2010-11 to a projected 9½ percent in 2015, mainly on account of lower program aid. This declining trend is projected to continue throughout the projection period.

<sup>8</sup> Thereby, total non-concessional borrowing under the PSI program has reached US\$ 1,498 million.

## EXTERNAL DEBT SUSTAINABILITY ANALYSIS

**2. Total external debt is projected to rise more rapidly during this decade than previously projected, reflecting higher private sector investment in the natural gas sector.** External debt (both public and private) is expected to peak at 232 percent of GDP in 2022. By that time private sector debt will represent more than 80 percent of total external debt with its increase mostly driven by investments in the natural gas sector. In the near term, coal sector investment to complete the

Nacala rail corridor project will also have a small impact as it is now expected to be financed by debt rather than FDI. The significant build up of private sector external debt needs to be monitored by the authorities to contain vulnerabilities, though risks (as noted above) are limited due to the financing structures through SPVs offshore. With renowned global companies leading investments in the natural resource sector, vulnerabilities are expected to be limited to those specific to the natural resource operations. Likewise, the risk for government contingent liabilities is deemed modest, though the authorities are well advised to remain vigilant, including in complex negotiation with private sector concessionaires and their prospective lenders.

**3. All public external debt indicators remain below their respective thresholds in the baseline, but two indicators relating to debt levels barely so** (Figure 1).<sup>9</sup> These level indicators are those of external debt relative to GDP and exports. Meanwhile, debt service indicators remain benign although debt service which has started on the US\$850 million EMATUM bond will amount to approximately US\$200 million per year from 2016, effectively doubling public debt service and weighing on Mozambique's international reserves.<sup>10</sup>

- **The PV of debt in terms of GDP** now stands at 39.9 percent in 2015 (Table 1),<sup>11</sup> compared to 31.9 percent in the previous DSA and a threshold of 40 percent. This increase is completely attributable to the depreciation of the metical, as external disbursements during 2015 have been lower than expected in the last DSA. In contrast, its medium-term trajectory is now more benign as a result of public borrowing restraint with ratios projected to consistently decrease to 36½ percent by 2020, while the previous DSA forecasted increases throughout the remainder of the 2010s. Thereafter, strong GDP expansion related to LNG production is expected to stabilize the ratio at a lower level of around 20 percent of GDP.

<sup>9</sup> As in the previous DSAs, the historical scenario has been excluded from Figures 1 and 3. 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 of 19.3 percent of GDP. This is much lower than the average projected deficit of 67 percent of GDP during 2017-22. With private debt accumulation assumed to remain unchanged compared to the baseline, this assumption then results in unrealistically fast declines of public debt ratios.

<sup>10</sup> The government is currently exploring options for refinancing this debt with an aim to *inter alia* lengthen its maturity, which could reduce near term debt service requirements.

<sup>11</sup> Large residuals in Table 1 after 2020 result from large debt service and dividend payments on LNG investment, which are not included in the identified net debt-creating flows. They ramp up in line with LNG production and increasing from about 20 percent of GDP per year in the mid-2020s to over 25 percent of GDP in the early 2030s.

- **The PV of debt in terms of exports** in 2015 has increased considerably relative to the previous DSA (143 percent versus 112 percent) as a result of downward revisions to exports on account of weak commodity prices, which is also slowing expansion in export volumes, particularly with regards to coal. Nonetheless, exports are expected to recover over the medium term, partly as the delayed completion of the Nacala rail corridor project underpins coal exports. This should return the ratio to below 120 percent during the next years, with further considerable declines and stabilization below 40 percent as a result of LNG production.

**4. Mozambique’s risk of debt distress remains moderate.** In cases such as Mozambique, whose debt ratios are within 5 percent of thresholds, it is useful to consider also an alternate methodology in determining the final classification.<sup>12</sup> Instead of specifying thresholds based on past experiences of debt distress across LIDCs, this methodology takes into account Mozambique-specific factors such as higher than average GDP growth and a CPIA rating toward the upper end of the medium range. Its results provide support for Mozambique’s risk of debt distress indeed remaining moderate at this juncture (Figure 3). Nonetheless, the authorities are well advised to retain their current prudent borrowing strategy, while continuing to make progress in investment selection to ensure that those projects with high development impacts are appropriately prioritized.

**5. External debt ratios are sensitive to exchange rate shocks and terms of trade shocks.**<sup>13</sup> The thresholds for the PV of debt relative to GDP, exports and revenues are breached under various stress tests for a sustained period.<sup>14</sup> A combination shock consisting of reductions in non-debt creating flows such as FDI, export prices and growth in 2016-2017 would push ratios well above their prudent thresholds in the near term, with peaks of about 70 percent in the debt-to-GDP and 260 percent in the debt-to-export ratio (Figure 1).<sup>15</sup> Apart from this combination shock, a further sharp depreciation of the metical in 2016 could push the debt-to-GDP ratio well above the 50 percent mark in the medium term. Unlike in the previous DSA, ratios in all the stress scenarios would return below the thresholds during the early 2020s in light of the now higher increases in GDP and exports because of larger size of the LNG facilities. A shock to FDI is also shown to lead to considerable breaches of thresholds; however, this scenario should not be overemphasized as a fall in FDI, and particularly megaproject FDI, would mainly be linked to lower imports rather than higher borrowing as implicitly assumed in this shock scenario.

**6. Ensuring that LNG production materializes remains important to underpin Mozambique’s long-run debt sustainability.** The same applies for completion of coal investment.

<sup>12</sup> For more information see IMF (2013), “Staff Guidance Note on the Application of the Joint Bank-Fund Debt Sustainability Framework for Low-Income Countries”.

<sup>13</sup> The impact the of the standard shocks in the DSA template is heightened by the fact that the standard stress tests revert to historical values, which are significantly different from current and expected values because of the structural change in the Mozambican economy resulting from the large-scale exploitation of coal and natural gas since 2011.

<sup>14</sup> The scenario in which variables are at their historical levels has been omitted given that it generates negative debt as a result of the large changes in variables in the baseline arising from LNG activities.

<sup>15</sup> The charts in Figure 1 display the stress test with the most adverse outcome in 2025.

The authorities have made significant progress in establishing legal frameworks for the sector. Negotiations with private operators on outstanding issues recently regained momentum after some delays. It is crucial that jointly satisfactory agreements are reached soon to ensure that LNG investment can move forward.

## PUBLIC SECTOR DEBT SUSTAINABILITY

**7. Risks to total public debt have heightened in line with external debt** (Table 3 and Figure 2). With over 80 percent of public debt being external, the evolution of total public debt mirrors its trajectory. PV of public debt is expected to stand at 50 percent of GDP at end 2015. Debt-to-GDP and debt-to-revenue ratios are expected to consistently decline over the projection period, in line with external debt, and reinforced by envisaged fiscal consolidation leading to a reduction in net domestic debt. Under the baseline scenario, the PV of public debt remains below the indicative 56 percent of GDP benchmark that research has linked to increased probability of debt distress. However, and in contrast to the previous DSA, public debt ratios would now exceed the benchmark briefly during 2016 and 2017, if the metical were to suffer another sharp depreciation in the upcoming year. Thereby Mozambique's overall risk of public debt distress is now considered heightened. The debt service-to-revenue ratio experiences a pronounced upward shift starting in 2016 as a result of debt service having commenced on the \$850 million commercial borrowing related to defense spending and the state-owned tuna fishing company EMATUM.

**8. These increased risks underline the importance of the authorities' planned fiscal consolidation, including to safeguard future borrowing space for priority public investment.** In light of the tighter constraints, rigorous evaluation and prioritization of investment projects and building increased capacity in this area is becoming even more important. Over the medium and long term, underpinning development will require considerable further public investment, including in the energy sector. With prospective revenue increases tied to LNG production only expected to materialize from the mid to late 2020s, careful resource management is needed to create space for such investments while safeguarding macroeconomic stability.

## AUTHORITIES' VIEWS

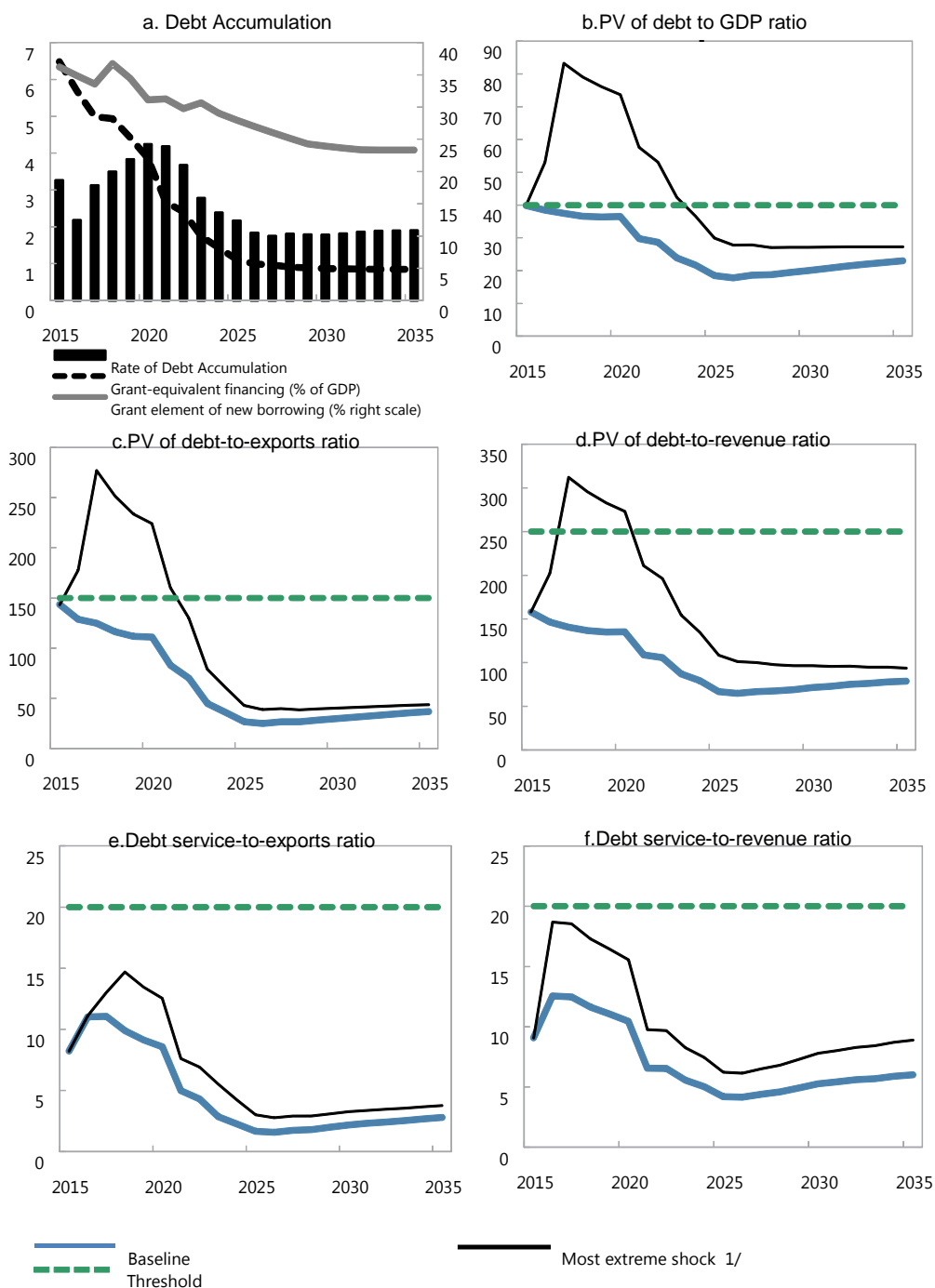
**9. The authorities, were in broad agreement with the DSA's results, but emphasized that an elevation of debt vulnerability rating should not result from purely external factors, such as exchange rate devaluation.** They were mindful that a degradation of Mozambique's rating could arise in the future, particularly if the metical were to depreciate further. They emphasized that any changes in risk of debt distress rating should not occur purely in response to such exogenous factors beyond the authorities' control. In addition, they expressed that the government's capacity to service its debt should be the main factor in making the assessment.

## CONCLUSION

**10. Debt remains manageable, but heightened vigilance—as demonstrated by the authorities—is indeed essential.** Not surprisingly, exchange rate depreciation has had a sizable adverse impact on public debt ratios, given that most public debt is external and denominated in foreign currency. Debt service has become more challenging as the beginning of repayments on the EMATUM bond has doubled debt service commitments in nominal terms, placing some strain on a balance of payments already weakened by commodity price shocks and a temporary slowdown in investment inflows. It is thus important to exercise caution in contraction of new external debt, particularly on non-concessional terms, as well as limit domestic debt issuance to ensure that the fiscal sector supports the external adjustment, as envisaged in the program. In addition, limiting issuance of public guarantees and enhancing monitoring of financial positions of state-owned enterprises are crucial. Shock scenarios highlight that Mozambique's debt remains vulnerable to a general deterioration in economic conditions and the terms-of-trade as well as to further currency depreciation. As some further currency depreciation could be a possibility in light of the balance of payments position, it is comforting that—despite recent increases—public debt service overall remains manageable, given that the vast majority of Mozambique's debt features concessional terms.

**11. The conclusions for strategic debt management are fourfold and similar to those of the previous DSA.** First, debt management and investment planning capacity should continue to be improved to ensure that the most deserving public investment projects are selected and yield their desired payoff. This has become more important as higher debt level ratios resulting from depreciation prescribe a more cautious borrowing path, which the authorities have already charted out, underpinned by sending many projects back to line ministries for reevaluation and prioritization. Second, it is important for the authorities to implement the fiscal consolidation envisaged in their program, both to address the economy's external imbalance and to place public debt on a gradual downward trajectory over the medium term while addressing key public investment priorities. Third, it remains crucial—including from a debt sustainability perspective—to bring the negotiations with the private gas companies to a jointly satisfactory conclusion to ensure that LNG investment moves forward, so that production and its beneficial effects on GDP and fiscal revenue can be realized. They would ensure that, even in case of further adverse shocks explored in the stress scenarios, Mozambique's debt indicators would revert to prudent levels soon thereafter. Fourth, while Mozambique had made substantial progress in debt management under the previous PSI-supported program and debt management capacity has been adequate, reinvigorating improvements in this area is becoming more important in light of heightened risks.

**Figure 1. Mozambique: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2015-2035 1/**



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2025. In figure b. it corresponds to a Non-debt flows shock; in c. to a Non-debt flows shock; in d. to a Non-debt flows shock; in e. to a Combination shock and in figure f. to a One-time depreciation shock

**Table 1. Mozambique: External Debt Sustainability Framework, Baseline Scenario, 2012-2035 1/**  
(In percent of GDP, unless otherwise indicated)

|   | Actual       |              |              | Historical<br>Average <sup>6/</sup> | Standard<br>Deviation <sup>6/</sup> | Projections  |              |              |              |              |              | 2015-2020 |      | 2021-2035    |              |       |
|---|--------------|--------------|--------------|-------------------------------------|-------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|-----------|------|--------------|--------------|-------|
|   | 2012         | 2013         | 2014         |                                     |                                     | 2015         | 2016         | 2017         | 2018         | 2019         | 2020         | Average   | 2025 | 2035         | Average      |       |
| <b>External debt (nominal) 1/</b>                                       | <b>70.9</b>  | <b>78.3</b>  | <b>84.5</b>  |                                     |                                     | <b>106.3</b> | <b>115.6</b> | <b>118.6</b> | <b>120.2</b> | <b>126.8</b> | <b>188.7</b> |           |      | <b>115.5</b> | <b>76.8</b>  |       |
| <i>of which: public and publicly guaranteed (PPG)</i>                   | 34.5         | 42.4         | 48.1         |                                     |                                     | 63.4         | 60.9         | 59.1         | 57.7         | 57.0         | 56.5         |           |      | 26.7         | 30.8         |       |
| Change in external debt   | 0.3          | 7.4          | 6.2          |                                     |                                     | 21.8         | 9.3          | 3.0          | 1.6          | 6.6          | 61.9         |           |      | -36.3        | 2.7          |       |
| Identified net debt-creating flows                                      | -1.9         | -3.2         | 0.7          |                                     |                                     | 5.4          | 4.6          | 3.0          | 2.5          | 7.7          | 62.2         |           |      | -54.9        | -23.2        |       |
| <b>Non-interest current account deficit</b>                             | <b>44.1</b>  | <b>38.4</b>  | <b>33.2</b>  | <b>19.3</b>                         | <b>14.6</b>                         | <b>29.1</b>  | <b>31.4</b>  | <b>52.9</b>  | <b>70.1</b>  | <b>77.3</b>  | <b>83.4</b>  |           |      | <b>-9.9</b>  | <b>-4.3</b>  | 1.7   |
| Deficit in balance of goods and services                                | 51.1         | 47.6         | 40.9         |                                     |                                     | 34.4         | 36.8         | 57.0         | 73.4         | 80.1         | 85.8         |           |      | -26.9        | -15.8        |       |
| Exports   | 30.6         | 29.8         | 27.4         |                                     |                                     | 27.8         | 29.9         | 30.1         | 31.5         | 32.6         | 32.9         |           |      | 69.5         | 62.4         |       |
| Imports   | 81.7         | 77.3         | 68.3         |                                     |                                     | 62.2         | 66.7         | 87.1         | 104.9        | 112.6        | 118.7        |           |      | 42.6         | 46.6         |       |
| Net current transfers (negative = inflow)                               | -6.8         | -8.9         | -8.1         | -7.0                                | 1.1                                 | -5.7         | -6.0         | -5.1         | -4.6         | -4.1         | -3.8         |           |      | -1.5         | -1.8         | -2.0  |
| <i>of which: official</i>   | -4.7         | -6.8         | -6.4         |                                     |                                     | -2.9         | -3.0         | -2.2         | -1.8         | -1.5         | -1.3         |           |      | -0.3         | -0.1         |       |
| Other current account flows (negative = net inflow)                     | -0.2         | -0.3         | 0.4          |                                     |                                     | 0.4          | 0.7          | 1.0          | 1.3          | 1.4          | 1.5          |           |      | 18.6         | 13.2         |       |
| <b>Net FDI (negative = inflow)</b>                                      | <b>-37.1</b> | <b>-38.6</b> | <b>-28.9</b> | <b>-16.5</b>                        | <b>14.8</b>                         | <b>-18.9</b> | <b>-21.5</b> | <b>-44.9</b> | <b>-62.0</b> | <b>-64.9</b> | <b>-19.7</b> |           |      | <b>-19.5</b> | <b>-18.9</b> | -20.1 |
| <b>Endogenous debt dynamics 2/</b>                                      | <b>-8.9</b>  | <b>-3.0</b>  | <b>-3.7</b>  |                                     |                                     | <b>-4.8</b>  | <b>-5.3</b>  | <b>-5.0</b>  | <b>-5.7</b>  | <b>-4.8</b>  | <b>-1.5</b>  |           |      | <b>-25.5</b> | <b>0.1</b>   |       |
| Contribution from nominal interest rate                                 | 0.7          | 0.7          | 0.8          |                                     |                                     | 1.1          | 1.8          | 2.5          | 3.1          | 3.5          | 7.0          |           |      | 5.2          | 2.6          |       |
| Contribution from real GDP growth                                       | -4.4         | -4.8         | -5.3         |                                     |                                     | -5.9         | -7.1         | -7.5         | -8.8         | -8.2         | -8.6         |           |      | -30.7        | -2.6         |       |
| Contribution from price and exchange rate changes                       | -5.1         | 1.1          | 0.8          |                                     |                                     | ...          | ...          | ...          | ...          | ...          | ...          |           |      | ...          | ...          |       |
| <b>Residual (3-4) 3/</b>  | <b>2.1</b>   | <b>10.6</b>  | <b>5.5</b>   |                                     |                                     | <b>16.4</b>  | <b>4.7</b>   | <b>0.0</b>   | <b>-0.8</b>  | <b>-1.0</b>  | <b>-0.3</b>  |           |      | <b>18.7</b>  | <b>25.9</b>  |       |
| <i>of which: exceptional financing</i>                                  | 0.0          | 0.0          | 0.0          |                                     |                                     | 0.0          | 0.0          | 0.0          | 0.0          | 0.0          | 0.0          |           |      | 0.0          | 0.0          |       |
| PV of external debt 4/  | ...          | ...          | 66.2         |                                     |                                     | 82.8         | 93.1         | 97.0         | 99.1         | 106.2        | 168.8        |           |      | 107.3        | 69.0         |       |
| In percent of exports   | ...          | ...          | 242.0        |                                     |                                     | 297.6        | 311.8        | 322.7        | 315.0        | 326.0        | 512.9        |           |      | 154.3        | 110.7        |       |
| <b>PV of PPG external debt</b>  | <b>...</b>   | <b>...</b>   | <b>29.8</b>  |                                     |                                     | <b>39.9</b>  | <b>38.4</b>  | <b>37.5</b>  | <b>36.6</b>  | <b>36.4</b>  | <b>36.5</b>  |           |      | <b>18.4</b>  | <b>23.0</b>  |       |
| <b>In percent of exports</b>  | <b>...</b>   | <b>...</b>   | <b>108.9</b> |                                     |                                     | <b>143.4</b> | <b>128.7</b> | <b>124.7</b> | <b>116.3</b> | <b>111.6</b> | <b>111.1</b> |           |      | <b>26.5</b>  | <b>36.8</b>  |       |
| <b>In percent of government revenues</b>                                | <b>...</b>   | <b>...</b>   | <b>109.0</b> |                                     |                                     | <b>158.1</b> | <b>146.6</b> | <b>140.6</b> | <b>136.8</b> | <b>135.1</b> | <b>135.5</b> |           |      | <b>66.9</b>  | <b>78.9</b>  |       |
| <b>Debt service-to-exports ratio (in percent)</b>                       | <b>12.5</b>  | <b>12.8</b>  | <b>14.3</b>  |                                     |                                     | <b>19.9</b>  | <b>23.9</b>  | <b>27.1</b>  | <b>26.9</b>  | <b>26.1</b>  | <b>35.8</b>  |           |      | <b>20.6</b>  | <b>8.4</b>   |       |
| <b>PPG debt service-to-exports ratio (in percent)</b>                   | <b>2.0</b>   | <b>2.7</b>   | <b>3.6</b>   |                                     |                                     | <b>8.2</b>   | <b>11.0</b>  | <b>11.1</b>  | <b>9.9</b>   | <b>9.1</b>   | <b>8.6</b>   |           |      | <b>1.7</b>   | <b>2.8</b>   |       |
| <b>PPG debt service-to-revenue ratio (in percent)</b>                   | <b>2.8</b>   | <b>3.1</b>   | <b>3.6</b>   |                                     |                                     | <b>9.1</b>   | <b>12.6</b>  | <b>12.5</b>  | <b>11.6</b>  | <b>11.1</b>  | <b>10.5</b>  |           |      | <b>4.2</b>   | <b>6.0</b>   |       |
| Total gross financing need (Billions of U.S. dollars)                   | 1.6          | 0.6          | 1.4          |                                     |                                     | 2.4          | 2.5          | 2.7          | 3.1          | 4.3          | 17.2         |           |      | -11.5        | -26.8        |       |
| Non-interest current account deficit that stabilizes debt ratio         | 43.8         | 31.0         | 27.1         |                                     |                                     | 7.3          | 22.2         | 49.9         | 68.5         | 70.7         | 21.5         |           |      | 26.4         | -7.0         |       |
| <b>Key macroeconomic assumptions</b>                                    |              |              |              |                                     |                                     |              |              |              |              |              |              |           |      |              |              |       |
| Real GDP growth (in percent)  | 7.2          | 7.1          | 7.2          | 7.5                                 | 1.1                                 | 6.3          | 6.5          | 7.2          | 8.3          | 7.6          | 7.5          | 7.2       | 26.2 | 3.7          | 11.0         |       |
| GDP deflator in US dollar terms (change in percent)                     | 7.8          | -1.5         | -1.0         | 2.4                                 | 9.3                                 | -15.8        | -8.6         | 3.5          | 3.4          | 3.5          | 3.5          | -1.8      | 2.4  | 2.4          | 2.5          |       |
| Effective interest rate (percent) 5/                                    | 1.1          | 1.1          | 1.1          | 1.8                                 | 0.8                                 | 1.2          | 1.6          | 2.4          | 2.9          | 3.2          | 6.1          | 2.9       | 4.4  | 3.8          | 5.0          |       |
| Growth of exports of G&S (US dollar terms, in percent)                  | 33.4         | 2.6          | -2.4         | 11.1                                | 14.9                                | -9.1         | 4.5          | 11.7         | 17.3         | 15.3         | 12.3         | 8.7       | 48.3 | 4.5          | 20.0         |       |
| Growth of imports of G&S (US dollar terms, in percent)                  | 62.8         | -0.1         | -6.3         | 19.4                                | 25.3                                | -18.5        | 4.3          | 44.9         | 34.9         | 19.6         | 17.1         | 17.1      | 3.0  | 8.8          | 6.5          |       |
| Grant element of new public sector borrowing (in percent)               | ...          | ...          | ...          | ...                                 | ...                                 | 36.2         | 34.9         | 33.6         | 36.7         | 34.5         | 31.1         | 34.5      | 28.0 | 23.4         | 26.1         |       |
| Government revenues (excluding grants, in percent of GDP)               | 21.9         | 26.3         | 27.3         | ...                                 | ...                                 | 25.2         | 26.2         | 26.7         | 26.8         | 26.9         | 27.0         | ...       | 27.6 | 29.1         | 28.0         |       |
| Aid flows (in Billions of US dollars) 7/                                | 1.3          | 1.7          | 1.4          | ...                                 | ...                                 | 1.2          | 1.0          | 1.1          | 1.2          | 1.2          | 1.0          | ...       | 1.3  | 2.1          | ...          |       |
| <i>of which: Grants</i>   | 0.8          | 0.8          | 0.7          | ...                                 | ...                                 | 0.6          | 0.5          | 0.5          | 0.4          | 0.4          | 0.4          | ...       | 0.3  | 0.1          | ...          |       |
| <i>of which: Concessional loans</i>                                     | 0.5          | 0.9          | 0.7          | ...                                 | ...                                 | 0.6          | 0.4          | 0.6          | 0.8          | 0.8          | 0.7          | ...       | 1.1  | 2.0          | ...          |       |
| Grant-equivalent financing (in percent of GDP) 8/                       | ...          | ...          | ...          | ...                                 | ...                                 | 6.5          | 5.7          | 5.0          | 4.9          | 4.4          | 3.9          | ...       | 1.1  | 0.8          | 1.2          |       |
| Grant-equivalent financing (in percent of external financing) 8/        | ...          | ...          | ...          | ...                                 | ...                                 | 60.1         | 60.4         | 53.0         | 51.9         | 48.0         | 43.5         | ...       | 35.7 | 25.2         | 31.9         |       |
| <b>Memorandum items:</b>  |              |              |              |                                     |                                     |              |              |              |              |              |              |           |      |              |              |       |
| Nominal GDP (Billions of US dollars)                                    | 15.2         | 16.0         | 17.0         | ...                                 | ...                                 | 15.2         | 14.8         | 16.4         | 18.4         | 20.5         | 22.8         | ...       | 75.8 | 148.4        | ...          |       |
| Nominal dollar GDP growth   | 15.6         | 5.5          | 6.1          | ...                                 | ...                                 | -10.5        | -2.7         | 10.9         | 12.0         | 11.3         | 11.2         | 5.4       | 29.2 | 6.2          | 13.8         |       |
| PV of PPG external debt (in Billions of US dollars)                     | ...          | ...          | 4.7          | ...                                 | ...                                 | 5.3          | 5.6          | 6.1          | 6.7          | 7.4          | 8.2          | ...       | 13.8 | 33.6         | ...          |       |
| (Pvt-Pvt-1)/GDPt-1 (in percent)   | ...          | ...          | ...          | ...                                 | ...                                 | 3.3          | 2.2          | 3.1          | 3.5          | 3.8          | 4.2          | 3.3       | 2.2  | 1.9          | 2.2          |       |
| Gross workers' remittances (Billions of US dollars)                     | 0.0          | 0.0          | 0.0          | ...                                 | ...                                 | 0.1          | 0.1          | 0.1          | 0.1          | 0.1          | 0.1          | ...       | 0.1  | 0.2          | ...          |       |
| PV of PPG external debt (in percent of GDP + remittances)               | ...          | ...          | 29.8         | ...                                 | ...                                 | 39.8         | 38.3         | 37.4         | 36.5         | 36.2         | 36.4         | ...       | 18.4 | 22.9         | ...          |       |
| PV of PPG external debt (in percent of exports + remittances)           | ...          | ...          | 109.4        | ...                                 | ...                                 | 141.7        | 127.1        | 123.3        | 115.1        | 110.5        | 110.0        | ...       | 26.5 | 36.7         | ...          |       |
| Debt service of PPG external debt (in percent of exports + remittances) | ...          | ...          | 3.6          | ...                                 | ...                                 | 8.1          | 10.9         | 10.9         | 9.8          | 9.0          | 8.5          | ...       | 1.7  | 2.8          | ...          |       |

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as  $[r - g - p(1+g)] / (1+g+p+gp)$  times previous period debt ratio, with  $r$  = nominal interest rate;  $g$  = real GDP growth rate, and  $p$  = 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, 2015-2035**

(In Percent)

|  | Projections |      |      |      |      |      |            | 2035 |
|--|-------------|------|------|------|------|------|------------|------|
|  | 2015        | 2016 | 2017 | 2018 | 2019 | 2020 | 2025       |      |
| <b>PV of debt-to GDP ratio</b>   |             |      |      |      |      |      |            |      |
| <b>Baseline</b>  | 40          | 38   | 37   | 37   | 36   | 37   | <b>18</b>  | 23   |
| <b>A. Alternative Scenarios</b>  |             |      |      |      |      |      |            |      |
| A1. Key variables at their historical averages in 2015-2035 1/                                     | 40          | 29   | 25   | 22   | 17   | -25  | <b>-6</b>  | 215  |
| A2. New public sector loans on less favorable terms in 2015-2035 2                                 | 40          | 40   | 40   | 41   | 43   | 44   | <b>25</b>  | 36   |
| <b>B. Bound Tests</b>  |             |      |      |      |      |      |            |      |
| B1. Real GDP growth at historical average minus one standard deviation in 2016-2017                | 40          | 38   | 37   | 36   | 36   | 36   | <b>18</b>  | 23   |
| B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/         | 40          | 40   | 43   | 42   | 41   | 41   | <b>20</b>  | 23   |
| B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017         | 40          | 37   | 40   | 39   | 39   | 39   | <b>20</b>  | 25   |
| B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/ | 40          | 53   | 83   | 79   | 76   | 74   | <b>30</b>  | 27   |
| B5. Combination of B1-B4 using one-half standard deviation shocks                                  | 40          | 43   | 72   | 68   | 66   | 64   | <b>27</b>  | 26   |
| B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/                   | 40          | 57   | 55   | 54   | 53   | 54   | <b>27</b>  | 33   |
| <b>PV of debt-to-exports ratio</b>   |             |      |      |      |      |      |            |      |
| <b>Baseline</b>  | 143         | 129  | 125  | 116  | 112  | 111  | <b>27</b>  | 37   |
| <b>A. Alternative Scenarios</b>  |             |      |      |      |      |      |            |      |
| A1. Key variables at their historical averages in 2015-2035 1/                                     | 143         | 97   | 85   | 71   | 51   | -75  | <b>-8</b>  | 345  |
| A2. New public sector loans on less favorable terms in 2015-2035 2                                 | 143         | 132  | 134  | 131  | 130  | 134  | <b>36</b>  | 57   |
| <b>B. Bound Tests</b>  |             |      |      |      |      |      |            |      |
| B1. Real GDP growth at historical average minus one standard deviation in 2016-2017                | 143         | 127  | 123  | 115  | 110  | 110  | <b>26</b>  | 36   |
| B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/         | 143         | 145  | 182  | 169  | 160  | 158  | <b>36</b>  | 47   |
| B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017         | 143         | 127  | 123  | 115  | 110  | 110  | <b>26</b>  | 36   |
| B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/ | 143         | 178  | 277  | 251  | 234  | 224  | <b>43</b>  | 44   |
| B5. Combination of B1-B4 using one-half standard deviation shocks                                  | 143         | 157  | 262  | 239  | 223  | 215  | <b>43</b>  | 46   |
| B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/                   | 143         | 127  | 123  | 115  | 110  | 110  | <b>26</b>  | 36   |
| <b>PV of debt-to-revenue ratio</b>   |             |      |      |      |      |      |            |      |
| <b>Baseline</b>  | 158         | 147  | 141  | 137  | 135  | 135  | <b>67</b>  | 79   |
| <b>A. Alternative Scenarios</b>  |             |      |      |      |      |      |            |      |
| A1. Key variables at their historical averages in 2015-2035 1/                                     | 158         | 110  | 96   | 84   | 62   | -91  | <b>-20</b> | 738  |
| A2. New public sector loans on less favorable terms in 2015-2035 2                                 | 158         | 151  | 151  | 154  | 158  | 164  | <b>90</b>  | 122  |
| <b>B. Bound Tests</b>  |             |      |      |      |      |      |            |      |
| B1. Real GDP growth at historical average minus one standard deviation in 2016-2017                | 158         | 145  | 140  | 136  | 134  | 135  | <b>66</b>  | 78   |
| B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/         | 158         | 152  | 163  | 157  | 154  | 153  | <b>71</b>  | 79   |
| B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017         | 158         | 142  | 152  | 148  | 146  | 146  | <b>72</b>  | 84   |
| B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/ | 158         | 202  | 312  | 296  | 283  | 273  | <b>108</b> | 94   |
| B5. Combination of B1-B4 using one-half standard deviation shocks                                  | 158         | 165  | 269  | 256  | 245  | 238  | <b>98</b>  | 89   |
| B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/                   | 158         | 215  | 207  | 201  | 198  | 199  | <b>97</b>  | 115  |



**Table 2. Mozambique: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2015-2035 (concluded)**

(In percent)

| <b>Debt service-to-exports ratio</b>   |    |    |    |    |    |    |    |    |
|--|----|----|----|----|----|----|----|----|
| <b>Baseline</b>  | 8  | 11 | 11 | 10 | 9  | 9  | 2  | 3  |
| <b>A. Alternative Scenarios</b>  |    |    |    |    |    |    |    |    |
| A1. Key variables at their historical averages in 2015-2035 1/                                     | 8  | 10 | 9  | 8  | 7  | 6  | -1 | 17 |
| A2. New public sector loans on less favorable terms in 2015-2035 2                                 | 8  | 11 | 11 | 10 | 9  | 9  | 2  | 4  |
| <b>B. Bound Tests</b>  |    |    |    |    |    |    |    |    |
| B1. Real GDP growth at historical average minus one standard deviation in 2016-2017                | 8  | 11 | 11 | 10 | 9  | 9  | 2  | 3  |
| B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/         | 8  | 12 | 14 | 13 | 12 | 11 | 2  | 4  |
| B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017         | 8  | 11 | 11 | 10 | 9  | 9  | 2  | 3  |
| B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/ | 8  | 11 | 13 | 15 | 13 | 12 | 3  | 4  |
| B5. Combination of B1-B4 using one-half standard deviation shocks                                  | 8  | 11 | 13 | 15 | 13 | 13 | 3  | 4  |
| B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/                   | 8  | 11 | 11 | 10 | 9  | 9  | 2  | 3  |
| <b>Debt service-to-revenue ratio</b>   |    |    |    |    |    |    |    |    |
| <b>Baseline</b>  | 9  | 13 | 12 | 12 | 11 | 10 | 4  | 6  |
| <b>A. Alternative Scenarios</b>  |    |    |    |    |    |    |    |    |
| A1. Key variables at their historical averages in 2015-2035 1/                                     | 9  | 11 | 10 | 10 | 9  | 8  | -2 | 36 |
| A2. New public sector loans on less favorable terms in 2015-2035 2                                 | 9  | 13 | 12 | 11 | 11 | 11 | 5  | 9  |
| <b>B. Bound Tests</b>  |    |    |    |    |    |    |    |    |
| B1. Real GDP growth at historical average minus one standard deviation in 2016-2017                | 9  | 13 | 13 | 12 | 11 | 11 | 4  | 6  |
| B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/         | 9  | 13 | 13 | 12 | 12 | 11 | 5  | 6  |
| B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017         | 9  | 12 | 14 | 13 | 12 | 11 | 5  | 7  |
| B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/ | 9  | 13 | 14 | 17 | 16 | 15 | 8  | 8  |
| B5. Combination of B1-B4 using one-half standard deviation shocks                                  | 9  | 12 | 13 | 16 | 15 | 14 | 7  | 7  |
| B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/                   | 9  | 19 | 19 | 17 | 16 | 16 | 6  | 9  |
| <i>Memorandum item:</i>  |    |    |    |    |    |    |    |    |
| Grant element assumed on residual financing (i.e., financing required above baseline) 6/           | 24 | 24 | 24 | 24 | 24 | 24 | 24 | 24 |

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.

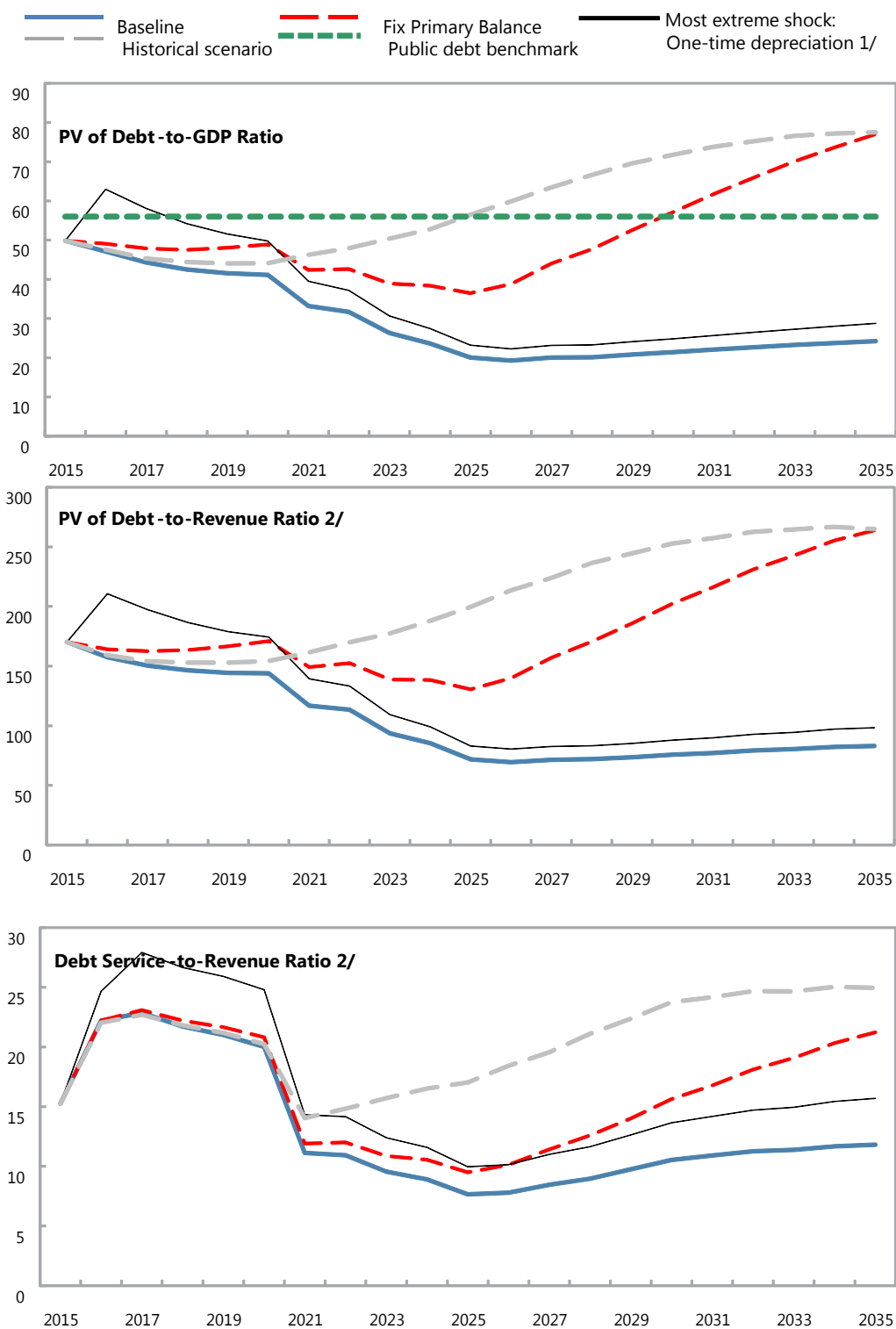
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly a an offsetting adjustment in import levels).

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, 2015-2035 1/**



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2025.

2/ Revenues are defined inclusive of grants.

**Table 3. Mozambique: Public Sector Debt Sustainability Framework, Baseline Scenario, 2012-2035**  
(In percent of GDP, unless otherwise indicated)

|  | Actual |      |       | Average <sup>5/</sup> | Standard<br>Deviation <sup>5/</sup> | Estimate |       |       |       |       |       | Projections        |      |      |                    |
|--|--------|------|-------|-----------------------|-------------------------------------|----------|-------|-------|-------|-------|-------|--------------------|------|------|--------------------|
|  | 2012   | 2013 | 2014  |                       |                                     | 2015     | 2016  | 2017  | 2018  | 2019  | 2020  | 2015-20<br>Average | 2025 | 2035 | 2021-35<br>Average |
| <b>Public sector debt 1/</b>   | 39.9   | 50.9 | 56.6  |                       |                                     | 73.4     | 69.5  | 65.9  | 63.6  | 62.2  | 61.1  |                    | 28.3 | 32.0 |                    |
| <i>of which: foreign-currency denominated</i>                          | 34.5   | 42.4 | 48.1  |                       |                                     | 63.4     | 60.9  | 59.1  | 57.7  | 57.0  | 56.5  |                    | 26.7 | 30.8 |                    |
| Change in public sector debt   | 2.0    | 11.0 | 5.6   |                       |                                     | 16.8     | -3.9  | -3.7  | -2.3  | -1.4  | -1.1  |                    | -5.4 | 0.5  |                    |
| Identified debt-creating flows   | 1.8    | -1.1 | 10.0  |                       |                                     | 14.7     | -3.0  | -2.7  | -2.8  | -2.4  | -2.1  |                    | -8.4 | -1.7 |                    |
| Primary deficit  | 2.9    | 1.8  | 9.6   | 3.3                   | 2.4                                 | 4.7      | 2.1   | 2.4   | 2.5   | 2.4   | 2.5   | 2.8                | -1.4 | -0.7 | -0.9               |
| Revenue and grants   | 27.0   | 31.4 | 31.6  |                       |                                     | 29.3     | 29.9  | 29.4  | 29.0  | 28.8  | 28.6  |                    | 27.9 | 29.2 |                    |
| <i>of which: grants</i>  | 5.1    | 5.2  | 4.2   |                       |                                     | 4.0      | 3.7   | 2.8   | 2.3   | 1.9   | 1.6   |                    | 0.3  | 0.1  |                    |
| Primary (noninterest) expenditure                                      | 29.8   | 33.2 | 41.2  |                       |                                     | 34.0     | 32.0  | 31.9  | 31.6  | 31.2  | 31.0  |                    | 26.5 | 28.5 |                    |
| Automatic debt dynamics  | -1.1   | -2.9 | 0.4   |                       |                                     | 10.0     | -5.1  | -5.1  | -5.3  | -4.7  | -4.6  |                    | -7.0 | -0.9 |                    |
| Contribution from interest rate/growth differential                    | -2.5   | -2.5 | -3.3  |                       |                                     | -3.0     | -3.9  | -4.3  | -4.7  | -4.1  | -3.9  |                    | -6.9 | -0.8 |                    |
| <i>of which: contribution from average real interest rate</i>          | 0.0    | 0.2  | 0.1   |                       |                                     | 0.3      | 0.6   | 0.4   | 0.4   | 0.4   | 0.5   |                    | 0.1  | 0.3  |                    |
| <i>of which: contribution from real GDP growth</i>                     | -2.5   | -2.7 | -3.4  |                       |                                     | -3.4     | -4.5  | -4.7  | -5.0  | -4.5  | -4.3  |                    | -7.0 | -1.1 |                    |
| Contribution from real exchange rate depreciation                      | 1.4    | -0.4 | 3.7   |                       |                                     | 13.0     | -1.1  | -0.8  | -0.7  | -0.6  | -0.7  |                    | ...  | ...  |                    |
| 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                                      | 0.2    | 12.1 | -4.4  |                       |                                     | 2.1      | -0.9  | -1.0  | 0.6   | 1.0   | 1.0   |                    | 3.0  | 2.2  |                    |
| <b>Other Sustainability Indicators</b>                                 |        |      |       |                       |                                     |          |       |       |       |       |       |                    |      |      |                    |
| <b>PV of public sector debt</b>  | ...    | ...  | 38.3  |                       |                                     | 49.9     | 47.1  | 44.3  | 42.5  | 41.6  | 41.1  |                    | 20.0 | 24.2 |                    |
| <i>of which: foreign-currency denominated</i>                          | ...    | ...  | 29.8  |                       |                                     | 39.9     | 38.4  | 37.5  | 36.6  | 36.4  | 36.5  |                    | 18.4 | 23.0 |                    |
| <i>of which: external</i>  | ...    | ...  | 29.8  |                       |                                     | 39.9     | 38.4  | 37.5  | 36.6  | 36.4  | 36.5  |                    | 18.4 | 23.0 |                    |
| PV of contingent liabilities (not included in public sector debt)      | ...    | ...  | ...   |                       |                                     | ...      | ...   | ...   | ...   | ...   | ...   |                    | ...  | ...  |                    |
| Gross financing need 2/  | 4.5    | 3.5  | 11.6  |                       |                                     | 9.2      | 8.7   | 9.2   | 8.8   | 8.4   | 8.2   |                    | 0.7  | 2.7  |                    |
| PV of public sector debt-to-revenue and grants ratio (in percent)      | ...    | ...  | 121.3 |                       |                                     | 170.3    | 157.4 | 150.4 | 146.4 | 144.2 | 144.0 |                    | 71.8 | 83.1 |                    |
| PV of public sector debt-to-revenue ratio (in percent)                 | ...    | ...  | 140.1 |                       |                                     | 197.6    | 179.5 | 165.9 | 158.9 | 154.5 | 152.5 |                    | 72.6 | 83.3 |                    |
| <i>of which: external 3/</i>   | ...    | ...  | 109.0 |                       |                                     | 158.1    | 146.6 | 140.6 | 136.8 | 135.1 | 135.5 |                    | 66.9 | 78.9 |                    |
| Debt service-to-revenue and grants ratio (in percent) 4/               | 6.0    | 5.4  | 6.4   |                       |                                     | 15.3     | 22.2  | 22.9  | 21.7  | 21.0  | 20.0  |                    | 7.6  | 11.8 |                    |
| Debt service-to-revenue ratio (in percent) 4/                          | 7.3    | 6.5  | 7.3   |                       |                                     | 17.7     | 25.3  | 25.2  | 23.6  | 22.5  | 21.2  |                    | 7.7  | 11.8 |                    |
| Primary deficit that stabilizes the debt-to-GDP ratio                  | 0.9    | -9.2 | 4.0   |                       |                                     | -12.1    | 6.0   | 6.1   | 4.8   | 3.8   | 3.5   |                    | 4.0  | -1.3 |                    |
| <b>Key macroeconomic and fiscal assumptions</b>                        |        |      |       |                       |                                     |          |       |       |       |       |       |                    |      |      |                    |
| Real GDP growth (in percent)   | 7.2    | 7.1  | 7.2   | 7.5                   | 1.1                                 | 6.3      | 6.5   | 7.2   | 8.3   | 7.6   | 7.5   | 7.2                | 26.2 | 3.7  | 11.0               |
| Average nominal interest rate on forex debt (in percent)               | 0.9    | 1.2  | 1.1   | 0.9                   | 0.6                                 | 1.3      | 1.5   | 1.5   | 1.5   | 1.5   | 1.5   | 1.5                | 2.0  | 2.8  | 2.3                |
| Average real interest rate on domestic debt (in percent)               | 5.2    | 5.3  | 2.7   | 4.6                   | 3.6                                 | 2.8      | 6.0   | 7.9   | 11.7  | 14.0  | 15.8  | 9.7                | 4.6  | 4.6  | 4.6                |
| Real exchange rate depreciation (in percent, + indicates depreciation) | 4.8    | -1.3 | 9.4   | 3.1                   | 12.1                                | 28.7     | ...   | ...   | ...   | ...   | ...   | ...                | ...  | ...  | ...                |
| Inflation rate (GDP deflator, in percent)                              | 5.9    | 3.9  | 3.6   | 5.5                   | 2.4                                 | 5.1      | 5.6   | 5.6   | 5.6   | 5.6   | 5.6   | 5.5                | 5.6  | 5.6  | 5.6                |
| Growth of real primary spending (deflated by GDP deflator, in percent) | 2.5    | 19.2 | 33.1  | 5.6                   | 11.3                                | -12.2    | 0.1   | 6.8   | 7.3   | 6.2   | 7.0   | 2.5                | 23.0 | 5.3  | 10.2               |
| Grant element of new external borrowing (in percent)                   | ...    | ...  | ...   | ...                   | ...                                 | 36.2     | 34.9  | 33.6  | 36.7  | 34.5  | 31.1  | 34.5               | 28.0 | 23.4 | ...                |

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

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 2015-2035**

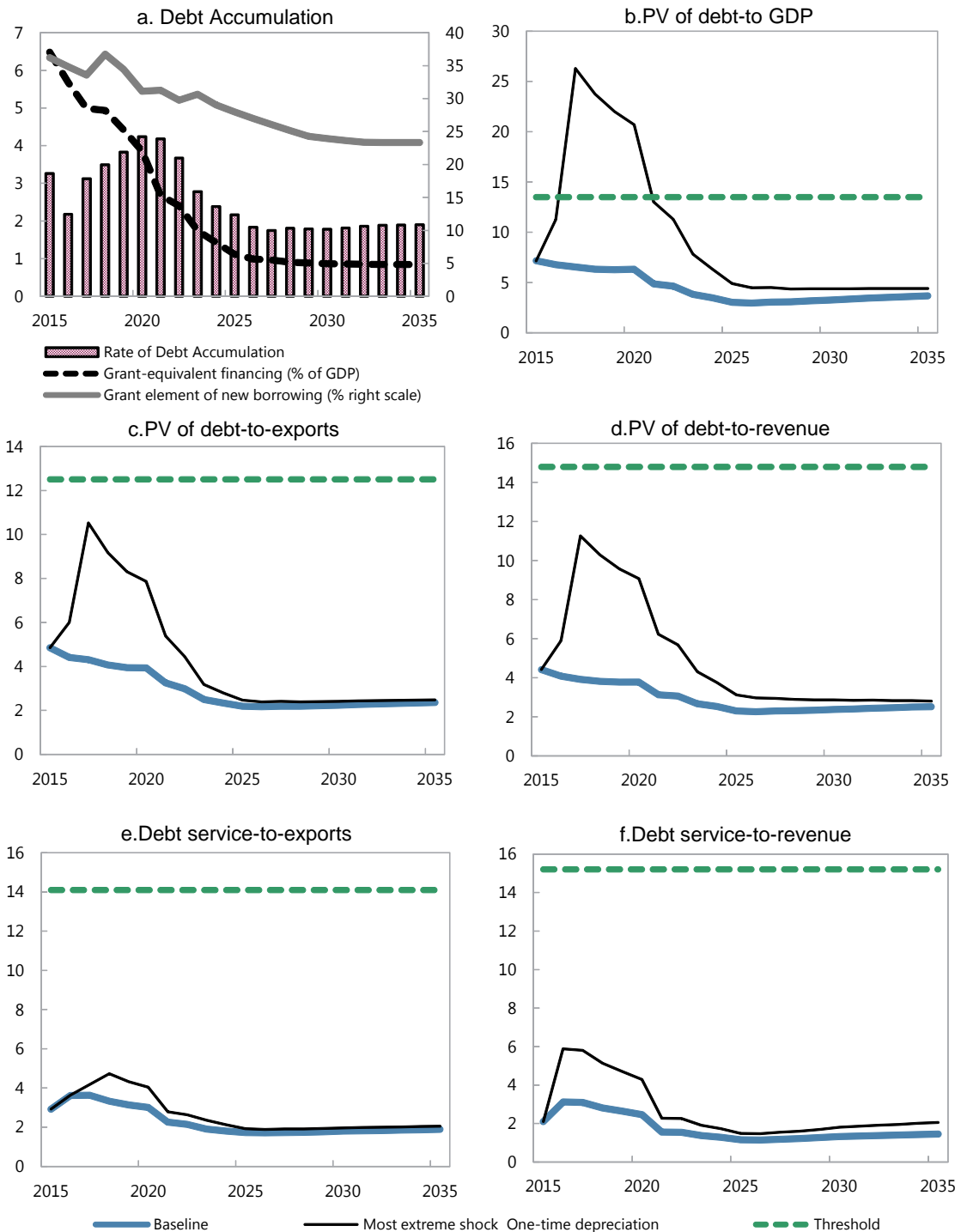
|   | Projections |      |      |      |      |      |      |      |
|---|-------------|------|------|------|------|------|------|------|
|   | 2015        | 2016 | 2017 | 2018 | 2019 | 2020 | 2025 | 2035 |
| <b>PV of Debt-to-GDP Ratio</b>  |             |      |      |      |      |      |      |      |
| <b>Baseline</b>   | 50          | 47   | 44   | 43   | 42   | 41   | 20   | 24   |
| <b>A. Alternative scenarios</b>   |             |      |      |      |      |      |      |      |
| A1. Real GDP growth and primary balance are at historical averages                      | 50          | 48   | 45   | 44   | 44   | 44   | 56   | 78   |
| A2. Primary balance is unchanged from 2015  | 50          | 49   | 48   | 48   | 48   | 49   | 36   | 77   |
| A3. Permanently lower GDP growth 1/   | 50          | 47   | 45   | 43   | 42   | 42   | 22   | 33   |
| <b>B. Bound tests</b>   |             |      |      |      |      |      |      |      |
| B1. Real GDP growth is at historical average minus one standard deviations in 2016-2017 | 50          | 47   | 45   | 43   | 42   | 42   | 21   | 26   |
| B2. Primary balance is at historical average minus one standard deviations in 2016-2017 | 50          | 50   | 49   | 47   | 46   | 45   | 22   | 25   |
| B3. Combination of B1-B2 using one half standard deviation shocks                       | 50          | 49   | 47   | 45   | 44   | 44   | 21   | 24   |
| B4. One-time 30 percent real depreciation in 2016                                       | 50          | 63   | 58   | 54   | 52   | 50   | 23   | 29   |
| B5. 10 percent of GDP increase in other debt-creating flows in 2016                     | 50          | 55   | 51   | 49   | 48   | 47   | 22   | 26   |
| <b>PV of Debt-to-Revenue Ratio 2/</b>   |             |      |      |      |      |      |      |      |
| <b>Baseline</b>   | 170         | 157  | 150  | 146  | 144  | 144  | 72   | 83   |
| <b>A. Alternative scenarios</b>   |             |      |      |      |      |      |      |      |
| A1. Real GDP growth and primary balance are at historical averages                      | 170         | 159  | 154  | 153  | 153  | 154  | 200  | 265  |
| A2. Primary balance is unchanged from 2015  | 170         | 164  | 163  | 164  | 167  | 171  | 131  | 264  |
| A3. Permanently lower GDP growth 1/   | 170         | 158  | 151  | 148  | 147  | 148  | 79   | 113  |
| <b>B. Bound tests</b>   |             |      |      |      |      |      |      |      |
| B1. Real GDP growth is at historical average minus one standard deviations in 2016-2017 | 170         | 157  | 152  | 148  | 147  | 147  | 75   | 90   |
| B2. Primary balance is at historical average minus one standard deviations in 2016-2017 | 170         | 167  | 168  | 163  | 160  | 158  | 77   | 87   |
| B3. Combination of B1-B2 using one half standard deviation shocks                       | 170         | 163  | 161  | 156  | 153  | 152  | 74   | 82   |
| B4. One-time 30 percent real depreciation in 2016                                       | 170         | 211  | 197  | 187  | 179  | 174  | 83   | 98   |
| B5. 10 percent of GDP increase in other debt-creating flows in 2016                     | 170         | 182  | 174  | 169  | 165  | 164  | 79   | 88   |
| <b>Debt Service-to-Revenue Ratio 2/</b>   |             |      |      |      |      |      |      |      |
| <b>Baseline</b>   | 15          | 22   | 23   | 22   | 21   | 20   | 8    | 12   |
| <b>A. Alternative scenarios</b>   |             |      |      |      |      |      |      |      |
| A1. Real GDP growth and primary balance are at historical averages                      | 15          | 22   | 23   | 22   | 21   | 20   | 17   | 25   |
| A2. Primary balance is unchanged from 2015  | 15          | 22   | 23   | 22   | 22   | 21   | 9    | 21   |
| A3. Permanently lower GDP growth 1/   | 15          | 22   | 23   | 22   | 21   | 20   | 8    | 14   |
| <b>B. Bound tests</b>   |             |      |      |      |      |      |      |      |
| B1. Real GDP growth is at historical average minus one standard deviations in 2016-2017 | 15          | 22   | 23   | 22   | 21   | 20   | 8    | 12   |
| B2. Primary balance is at historical average minus one standard deviations in 2016-2017 | 15          | 22   | 23   | 22   | 22   | 21   | 8    | 12   |
| B3. Combination of B1-B2 using one half standard deviation shocks                       | 15          | 22   | 23   | 22   | 21   | 20   | 8    | 12   |
| B4. One-time 30 percent real depreciation in 2016                                       | 15          | 25   | 28   | 27   | 26   | 25   | 10   | 16   |
| B5. 10 percent of GDP increase in other debt-creating flows in 2016                     | 15          | 22   | 24   | 23   | 22   | 21   | 8    | 12   |

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.

**Figure 3. Mozambique: Probability of Debt Distress of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2015-2035 1/**



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2025. In figure b. it corresponds to a Non-debt flows shock; in c. to a Non-debt flows shock; in d. to a Non-debt flows shock; in e. to a Combination shock and in figure f. to a One-time depreciation shock

**Statement by the Staff Representative on the Republic of Mozambique  
December 18, 2015**

1. Since the issuance of the staff report ([www.imf.org](http://www.imf.org)) the following information has become available. This information does not alter the thrust of the report's Staff Appraisal.
2. **Inflation has increased in November largely as expected.** Annual inflation for the 12 months ending in November rose to 5.7 percent, reflecting the expected pass through of the depreciation of the metical during the year on imported food prices and the impact of the increase in electricity tariffs in November.
3. **After weakening significantly in late November/early December, the exchange rate has been recovering in recent days.** Reflecting uncertainties surrounding the negotiations on large natural gas projects and a seasonal peak in import demand, the exchange rate depreciated further by about 20 percent (to reach about 56-57 meticals per US dollar in the first days of December). Since then, in part as a result of positive developments in the energy sector (below) and as a sign that the corrective policy measures are starting to bear fruit, the meticals appreciated by about 18 percent (to 48-49 meticals per dollar). Preliminary data suggest that the end-December target for net international reserves is within reach.
4. **The authorities have completed all the front-loaded corrective measures.** On December 14, the 2016 budget that is consistent with the fiscal framework agreed in the program was formally approved by the National Assembly, thus completing all the corrective measures set out in Table 3 of the MEFP.
5. **The December 14, 2015 Monetary Policy Committee meeting of the Banco de Mozambique took additional policy tightening actions.** In line with the policy advice, it raised the interest rate on the standing lending facility (FPC) by a further 150 basis points and the rate on the standing deposit facility (FPD) rate by a further 100 basis points.
6. **Favorable developments in megaproject negotiations bode well for FDI in the coming years.** The authorities, ENI and Anadarko, the two largest companies investing in Mozambique's massive offshore natural gas resources, reached an agreement in November for the joint development of the natural gas resources that straddle two offshore blocks. In addition, a preliminary Memorandum of Understanding (MOU) was reached to provide natural gas for domestic use. These agreements pave the way for final investment decisions in 2016 and will help improve the supply of foreign exchange in 2016.

**Statement by Ms. Kapwepwe, Executive Director for Mozambique  
and Mr. Tivane, Senior Advisor to Executive Director  
December 18, 2015**

**1. Introduction**

The Mozambican authorities are appreciative of the Fund's continued engagement and support in advancing their economic reform agenda aimed at safeguarding macroeconomic stability, gradually removing binding constraints to economic competitiveness, and strengthening policy institutions. Economic performance has remained broadly in line with the targets envisaged under the Policy Support Instrument (PSI), amidst heightened downside risks related to protracted low commodity prices, the slowdown in FDI inflows, restrained donor support, and the weakened global demand. However, in spite of timely actions to contain increased depreciation pressures that have emerged since completion of the Fourth PSI Review, BOP pressures have remained significant. This has led to a draw down in reserve buffers and a robust adjustment of the macroeconomic policy stance to address short term vulnerabilities while accelerating the pace of external adjustment. In view of this, the authorities seek the Executive Board's approval for completion of the fifth review under the PSI and modification of assessment criteria, as well as the request for an 18-month arrangement under the Standby Credit Facility.

**2. Recent Economic Developments and Outlook**

The challenging environment, primarily related to the protracted commodity price slump coupled with the adverse impact of floods earlier in 2015, prompted a slight downward revision of the macroeconomic policy objectives set for 2015-2017. GDP growth receded to 6.3 percent in the first half of 2015, compared to an average of 8 percent over the past two years. This slowdown is primarily attributed to a significant decline of mining sector growth from 29 percent in the first half of 2014 to 17 percent during the same period of 2015. There was also weak performance in the commerce, transportation and agriculture sectors, the latter mostly reflecting the impact of the floods. Recent developments indicate that in the first three quarters of the year, real GDP grew by 6.2 percent, broadly in line with the projected growth of 6.3 percent in 2015. Real GDP growth is forecast to reach on average 7-8 percent over the medium term, in consonance with the goal set forth in the Five-Year Government Plan. This performance improvement will be driven by projected increases in infrastructure investments to boost competitiveness in labor intensive sectors including agriculture and manufacturing, and by massive logistic investments in preparation of the exploration phase in the hydrocarbon sector.

Consumer price inflation is forecast to average 2.4 percent in 2015, and is expected to remain at the Bank of Mozambique's (BM) target of 5-6 percent, in the short and medium term. To lessen the impact of heightened depreciation pressures on the economy, the Monetary Policy Committee increased its reserve requirements by 100 basis points in October and by 150 basis points in November 2015. The BM also raised both its standing lending facility rate and its standing deposit facility rate by 225 basis points, cumulatively in October, November and

December, 2015, in an effort to further tighten the monetary policy stance. This should help achieve a rapid adjustment of the external position, while preserving net international reserves, consistent with the goal of maintaining comfortable levels of 4.5-5 month of import cover over the near term.

The current account deficit excluding megaprojects deteriorated slightly in the first half of 2015, on account of weaker performance of traditional exports, lower commodity prices and declining FDI and external aid. In the medium term, the current account deficit including mega projects is expected to increase significantly, from around 42 percent of GDP in 2015, to 55.5 and 81 percent of GDP, in 2017 and 2019, respectively, due to large projected imports to support logistic investment in extractive sector. In the longer-term, however, once the gas production begins, the current account balance could steadily improve and reach a surplus of around 10 percent of GDP, in 2025.

### **3. Program Performance**

The authorities have stepped up efforts to mitigate the adverse impact of short term vulnerabilities arising from the lingering low commodity prices and terms of trade shocks, coupled with weather related shocks, with mixed program performance under the PSI through September 2015. Performance on three AC related to net credit to the government (NCG), net international reserves (NIR), and external payment of arrears was mixed, while government revenue fell short of the indicative target. Deviation in the NCG reflected transitory factors, particularly the need to clear payment arrears (0.6 percent of GDP) of subsidies to fuel distributors to compensate for the past losses, which have been underestimated in the budget, coupled with accelerated pace of discounting of bulk of government securities issued to clear outstanding VAT arrears. The NIR was missed by a small margin mostly reflecting significant BOP pressures and continued valuation losses due to a stronger US Dollar. Coordination constraints in reconciling information with donors led to small amount of arrears, which has since been resolved. On the structural front, significant progress has been achieved; all measures have been implemented broadly as planned.

### **4. Fiscal Policy**

The implementation of the authorities' fiscal strategy in the short and medium term aims to foster fiscal consolidation, support the needed external adjustment, and rebalance expenditure towards growth-enhancing sectors, while safeguarding debt sustainability. Total revenue for 2015 is projected to reach 25.2 percent of GDP, the total expenditure including net lending to amount to 35.3 percent of GDP, with the implied overall fiscal deficit projected around 6.0 percent of GDP. The targeted 2015 fiscal adjustment is expected to lead to a reduction of around 1.5 percent of GDP, through containment of current expenditure, mostly the wage bill, and subsidies, while scaling back public investment based on implementation capacity.



The authorities will continue to step up fiscal structural reforms to broaden the tax base, enhancing the efficiency of tax administration, and set a robust legal framework to enable an optimal intergenerational redistribution of the revenues from natural resource taxes. In addition, strengthening of institutional capacity to monitor implementation of investment programs, and upgrading the selection criteria to ensure adequate value for money of capital expenditures will continue.

While cognizant of the risks posed by heightened depreciation pressures to debt sustainability, the authorities remain committed to invigorate the implementation of policy measures to improve debt management, and upgrade the institutional capacity on financial oversight of public enterprises. This set of policy priorities will contribute to prevent escalation of fiscal risks, and safeguard debt sustainability, over the medium and long term. At the same time, an elevation of the debt vulnerability rating should not result purely from external factors, such as exchange rate depreciation. Changes in the risk of debt distress rating should also take into account exogenous factors which are beyond the authorities' control.

## **5. Monetary and Exchange Rate Policies**

The monetary and exchange rate policies continues to be geared towards achieving price stability and smoothening exchange rate volatility in the short and medium term. The BM will gradually fine tune its policy instruments to contain the current depreciation pressures, while curbing the second round effects exerted on inflation expectations prompted by adjustment in administered electricity, bread and water prices in October 2015. More specifically, measures directed to enhance the monetary policy framework, particularly through improved analytical capacity on inflation forecasting and liquidity management will be given a priority. Swift implementation of policy measures aimed at strengthening crisis management tools to contain risks for financial stability, stemming from significant concentration of loans in the banking system, will also be critical.

Restoring reserve buffers is paramount to improve the ability of the economy to absorb future external shocks. In this regard, the BM will continue to pursue actions directed at rebuilding international reserves while allowing exchange rate flexibility.

## **6. Financial Sector Development Policies**

Enhancing financial deepening and inclusion remain a critical challenge to address the limited access to financial services in the economy. The authorities remain committed to foster the implementation of ongoing reforms aimed at achieving the main objectives of the Financial Sector Development Strategy (FSDS 2013-2022): (i) maintain financial stability; (ii) increase access to financial services and products, and eliminating structural constraints to the economy; and (iii) increase the supply of private capital to support private development. To this end, a set of measures have been deployed, including the establishment

of credit registry bureaus, promotion of mobile banking and implementation of a moveable collateral registry.

## **7. Structural Reforms**

Fostering broad based-growth and achieving productivity gains in traditional sectors of the economy such as agriculture and manufacturing, remain a challenge for Mozambique in the next decade. The weak growth elasticity of poverty reduction, estimated at 0.1 percent, side by side with still sub-optimal patterns of income distribution, call for accelerating structural reforms to reinforce the growth-poverty- nexus, while addressing the outstanding bottlenecks to economic competitiveness and productivity. The implementation of the authorities' reform agenda going forward, as stated in their Five Year Government Plan (2014-2019), seek to foster economic transformation and diversification and swiftly deploy a set of policy measures to tackle binding constraints to growth, through continued investment in infrastructure projects to unlock the country's growth potential and augment job creation.

Further, to improve the business climate, the authorities will revamp steps underway to expedite the process of starting up a new business, particularly through improved online provision of integrated services for facilitating "*start ups*", in addition to expanding the geographical coverage of one-stop shops.

## **8. Conclusion**

Going forward the authorities stand ready to advance the implementation of policy reforms aimed at restoring market confidence and safeguarding macroeconomic stability. They will continue to implement measures which mitigate the adverse impact of short term vulnerabilities. In line with these commitments, the authorities look forward to continued constructive engagement with the Fund in order to support enhanced institutional capacity on policy design and implementation.