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ECONOMIC OUTLOOK AND INFLATION FORECASTS



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AND INFLATION FORECASTS

May 2021

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¹ Internal and/or external guests may also participate in Monetary Policy Committee meetings, whenever necessary, at the invitation of the body's Chairman.

Foreword

The primary mandate of the Banco de Moçambique (BM) is to maintain price stability so as to ensure the protection of the purchasing power of citizens. This implies keeping inflation low, at one digit, and stable in the medium term. The mandate to make this objective possible is exercised by the Monetary Policy Committee (MPC), a body composed of the Governor, Vice-Governor, BM Board Members and permanent guests. The BM is equally responsible for supervising and maintaining the stability of the financial system.

Price stability also fosters balanced and sustainable economic growth. Price stability reduces the degree of uncertainty of economic agents and makes it possible to ensure more attractive interest rates, enabling a favorable environment for savings and investment.

To ensure price stability, the MPC defines the policy interest rate, known as the Mozambique interbank money market rate (MIMO). This rate, introduced on April 17, 2017, signals the stance of monetary policy and serves as an anchor for operations in the Interbank Money Market (MMI). It is expected that, through its influence on overnight interest rates formed in the MMI, the MIMO rate will affect inflation through the expectations, exchange rate and credit channels.

The decision on the MIMO rate is primarily based on inflation projections, always weighing the risks and uncertainties associated with such projections and the economic outlook. The MPC recognizes that its decisions affect the economy with a certain time lag, so it adopts a monetary policy stance based on an assessment of the economic and financial outlook and its risks and uncertainties over a time horizon of at least eight quarters. Where inflation projections deviate materially from the primary monetary policy objective set for the medium term, the MPC shall take appropriate policy measures to reverse the trend.

The MPC convenes ordinarily once every two months and, exceptionally, whenever economic conditions so require. The calendar of ordinary MPC meetings is announced at the beginning of each year. However, the body may convene extraordinarily to deliberate on monetary policy aspects, whenever macroeconomic circumstances so require.

The BM values transparency in the communication of its monetary policy. Monetary policy decisions are announced publicly, through an MPC Communiqué and / or a Press Conference Communiqué led by the BM Governor, on the same day of the committee meeting.

The Economic Outlook and Inflation Forecasts (CEPI) Report is an additional means for communicating the Monetary Policy Committee's (MPC) decisions. The CEPI report discloses the factors and rationale behind measures taken by the MPC, broadening the public's understanding of objectives and conduct of monetary policy.

Rogério Lucas Zandamela

Governor

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Executive Summary

The Monetary Policy Committee (MPC) of the Banco de Moçambique decided to keep unchanged the monetary policy rate, MIMO rate, at 13.25%. The decision is based on the worsening of the risks and uncertainties, notwithstanding the downward revision of the inflation forecasts for the short and medium term, reflecting mainly the recent appreciation of the Metical.

The MPC has also decided to keep unchanged the interest rates on the Standing Deposit Facility (SDF) at 10.25% and the Standing Lending Facility (SLF) at 16.25%, as well as the Reserve Requirement ratio for liabilities in domestic and foreign currency at 11.50% and 34.50%, respectively.

The risks and uncertainties associated with the inflation forecasts have worsened. At the domestic level, the intensification of military instability in the northern areas of the country stands out with an impact on the fiscal pressure and the suspension of Mozambique's LNG project, in addition to the increased volatility of the exchange rate. This volatility stems from the prevailing high uncertainties and asymmetries in forming expectations by operators in the foreign exchange market. In the external environment, the key risks are the increased fluctuation in the financial assets and commodities prices, as well as the emergence of new variants of the coronavirus.

The inflation forecasts have been revised downward, despite the worsening risks. Annual inflation decelerated to 5.19% in April from 5.76% in March, reflecting the recent appreciation of the Metical, and the fading impact of the natural disasters that hit the country at the beginning of the year. Core inflation, which excludes goods and services with administered prices and fruits and vegetables, slowed down as expected. For the short and medium term, a slower pace of acceleration in inflation is anticipated, mostly due to the recent dynamic in the exchange rate in a context of weak economic activity.

A slower recovery of the economy is anticipated for 2021. This prospect is underpinned by the weak domestic demand, coupled with the suspension of Mozambique's LNG project, despite the forecast of a gradual upturn in external demand, and the expected containment of the spread of COVID-19. Thus, given the limited space of monetary policy and State Budget the deepening of the structural reforms in the economy remains relevant aimed at strengthening institutions, improving the business environment, attracting investment and creating jobs.

Domestic public debt remains high. Since the end of March, domestic public debt, excluding loans and lease agreements and overdue liabilities, increased slightly by 310 million to 205.5 billion meticaïs.

International reserves remain at comfortable levels. Gross international reserves stand at USD 3,987 million, sufficient to cover more than 6 months of imports of goods and services.

The MPC will continue to monitor the domestic and international macroeconomic environment, as well as the prevailing risks, and will not hesitate to take the necessary corrective measures before the next ordinary meeting scheduled for July 21, 2021.

Chapter I. Recent Developments in International Economy

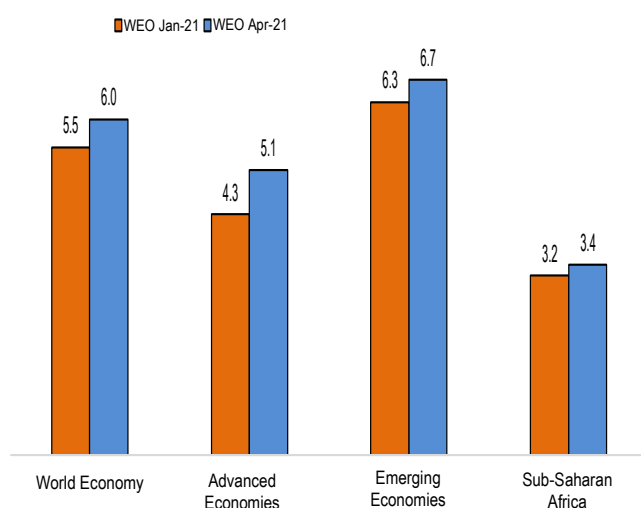
In light of the advances of vaccination programs against COVID-19 and the effect of fiscal stimulus measures, prospects for recovery of the global economy remain high, especially in advanced countries. In turn, since the last MPC, inflation has continued to accelerate in most economies, in the face of a recovering external demand and reflected in the increase in the prices of main commodities.

Table 1-1: Global GDP Growth Projections - 2021 (%)

Region	Achieved	Projection		Difference to January/21's WEO	
	2020	2021	2022	2021	2022
World Economy	-3.3	6.0	4.4	0.5	0.2
Advanced	-4.7	5.1	3.6	0.8	0.5
United States	-3.5	6.4	3.5	1.3	1.0
Euro Area	-6.6	4.4	3.8	0.2	0.2
Germany	-4.9	3.6	3.4	0.1	0.3
Japan	-4.8	3.3	2.5	0.2	0.1
United Kingdom	-9.9	5.3	5.1	0.8	0.1
Emerging and Developing	-2.2	6.7	5.0	0.4	0.0
Brazil	-4.1	3.7	2.6	0.1	0.0
India	-8.0	12.5	6.9	1.0	0.1
China	2.3	8.4	5.6	0.3	0.0
Sub-Saharan Africa	-1.9	3.4	4.0	0.2	0.1

Source: IMF, WEO (January 2021)

Chart 1-1: Real GDP Growth in 2021 (%)



Source: IMF

1.1. Recent Economic Activity and Forecasts

Optimism about the resumption of global economic growth prevails.

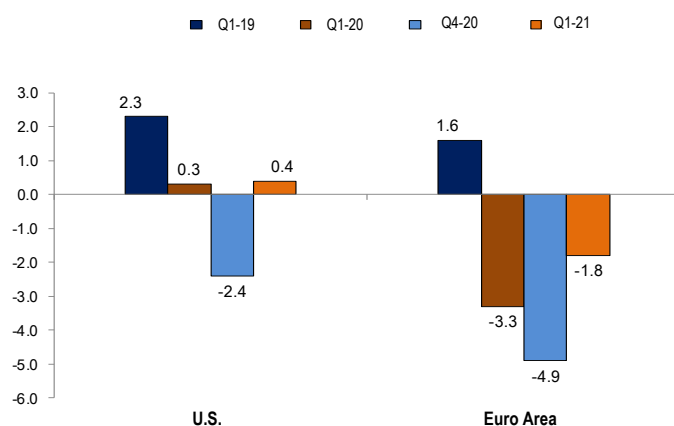
In the April edition of the World Economic Outlook (WEO), the International Monetary Fund (IMF) updated the growth forecasts of the world economy for 2021 to 6.0% from 5.5% of January 2020 (Table 1-1 and Chart 1-1). This review stems from worldwide progress of the vaccination program and the additional economic stimulus packages in the United States of America (USA). However, the IMF warns of heterogeneity in the recovery, with a trend of less significant performance in countries relying on tourism and in those with limited access to vaccines against COVID-19.

Fiscal stimulus drives economic growth in the U.S.

Preliminary data indicate that in the first quarter of 2021 the US grew by 0.4%, in annual terms, after a contraction of 2.4% in the previous quarter, reflecting the impact of fiscal and monetary stimulus, amid the reopening of the economy associated with the progress in the vaccination program (Chart 1-2).

However, the renewal of restrictive measures to control the health crisis continued to limit economic activity in

Chart 1-2: US and Euro Area Real GDP (%)



Source: Reuters and Trading Economics

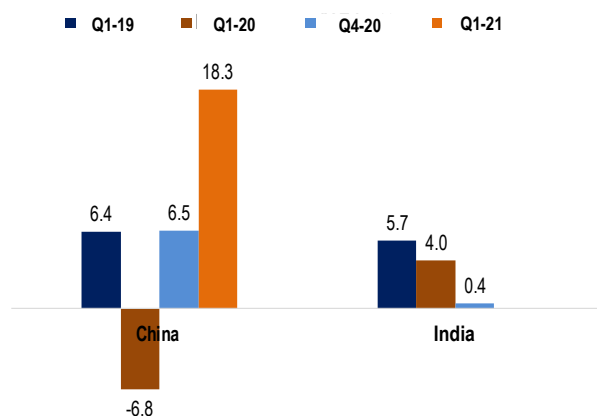
the Eurozone, which, despite the GDP improvement, was still contracting in the first quarter of 2021.

The acceleration of economic growth in China continues to reflect the combined effect of the recovery in domestic and foreign demand and the positive impact of fiscal and monetary stimulus on the economy (Chart 1-3).

1.2. Inflation and Interest Rates

For Mozambique's main trading partners, annual inflation maintains the upward trend.

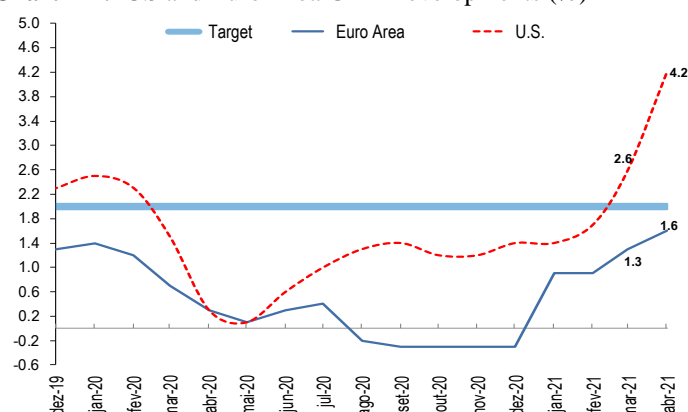
Chart 1-3: Real GDP of China and India (%)



Source: Reuters and Trading Economics

In advanced economies, annual inflation accelerated in April, reflecting the base effect, against a backdrop of rising costs of liquid fuels and electricity, in line with the gradual reopening of economies. Thus, inflation in the US and the Euro Zone stood at 4.2% and 1.6%, respectively (Chart 1-4).

Chart 1-4: US and Euro Area GDP Developments (%)



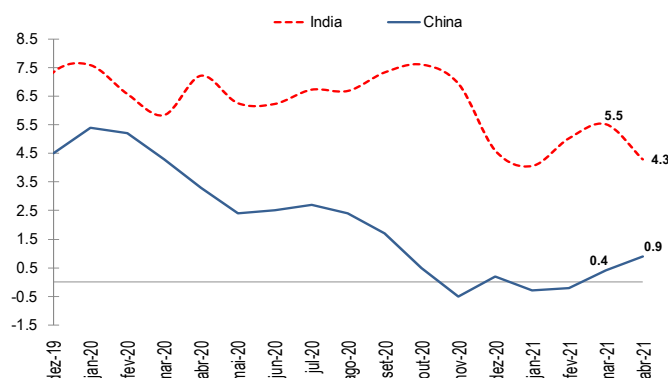
Source: Reuters and Trading Economics

In the same period, in emerging economies, prices showed a mixed pattern. In China, annual inflation accelerated to 0.9%, as a result of the increase in the price of fuel and services, while in India, it slowed to 4.3%, reflecting the reduction in food (Chart 1-5).

In South Africa, annual inflation accelerated by 120bp to 4.4%. The rise in prices stems from the rise in food and liquid fuel prices (Chart 1-6).

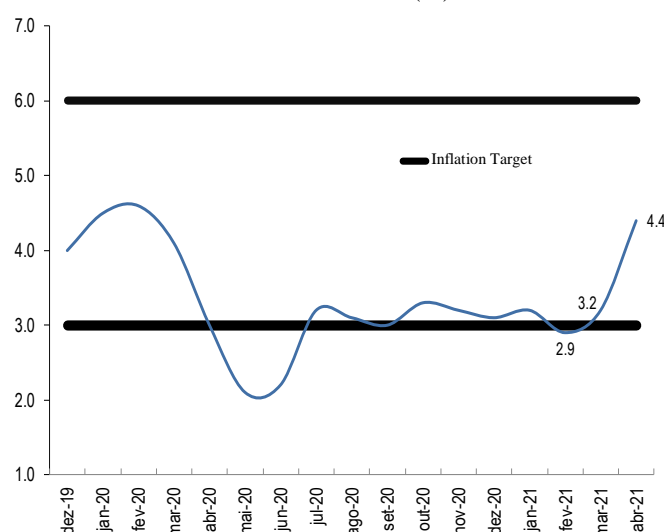
Central banks kept monetary policy interest rates unchanged. This position is justified by expectations of inflation that shall fall within the targets, despite the upward prices trend.

Chart 1-5: Inflation in China and India (%)



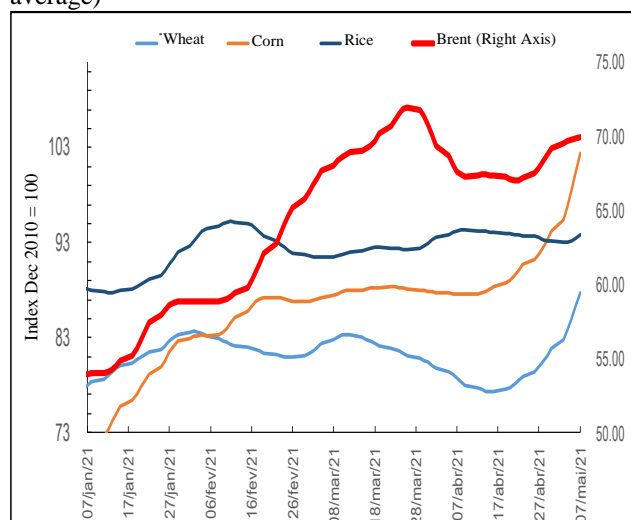
Source: Reuters and Trading Economics

Chart 1-6: Inflation in South Africa (%)



Source: Reuters and Trading Economics

Chart 1-7: Price Index of Imported Goods (7-day moving average)



Source: Reuters

1.3. Main Commodities Prices and US Dollar Dynamics

The progressive opening-up of economies, linked to the tendency to control the pandemic, favors the continuous increase in the prices of the main export and import goods.

Between mid-March and the first week of May, the price of Brent recorded cumulative gains of 31.8%, raising its price on the international market to 68.28 USD/barrel (Chart 1-7). This increase is essentially explained by the prospects for a resumption of global economic growth.

In the same period, grain prices increased as a result of the combined effect of climate shocks in South America and the imposition of the export surcharge by Russia.

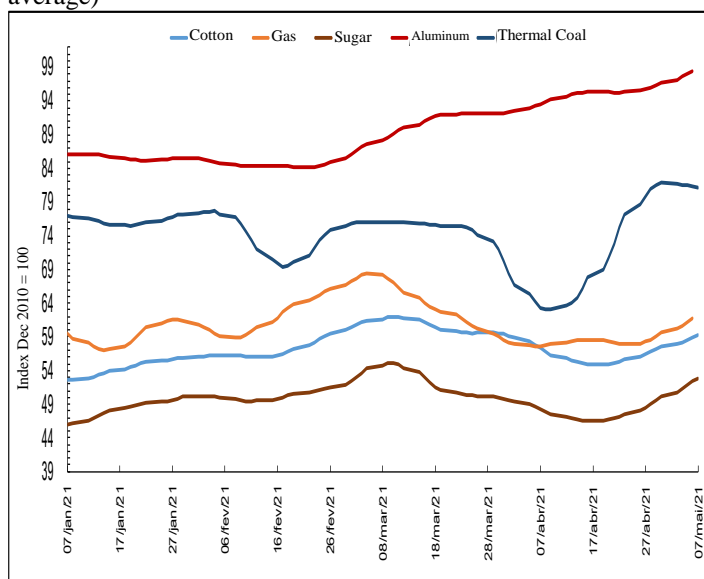
The upward trend in prices was also observed in Mozambique's main export products (Chart 1-8) and could favor the country's export revenues, from the second quarter of 2021.

Specifically, the price of coal increased due to supply restrictions (especially from India and China) following the imposition of strong sanitary control measures to contain the COVID-19 spread. In turn, the strengthening of the aluminum price stems from the largest economies transitioning to green energy, a dynamic that is expected to prevail in the medium term.

The US dollar (USD) has weakened against major currencies.

In the foreign exchange market, and between March and May this year, the composite index shows the weakening

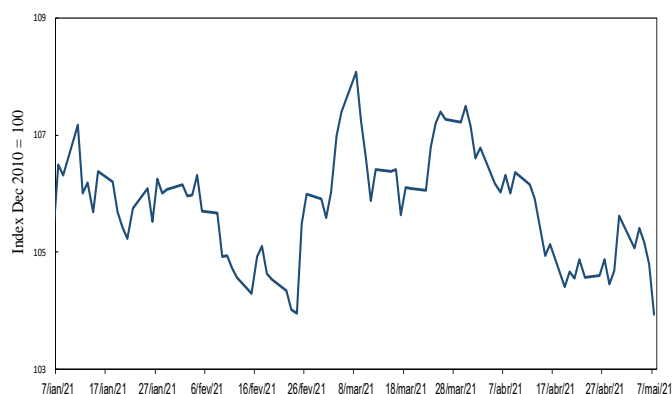
Chart 1-8: Price Index of Imported Goods (7-day moving average)



Source: Reuters

of the USD against the main trading currencies (Euro, Rand, Pound and Yen). During the period, the USD recorded losses of 1.6%, partly due to FED's accommodative monetary policy (Chart 1-9).

Chart 1-9: Composite Index of USD against Currencies of Major Trading Partners



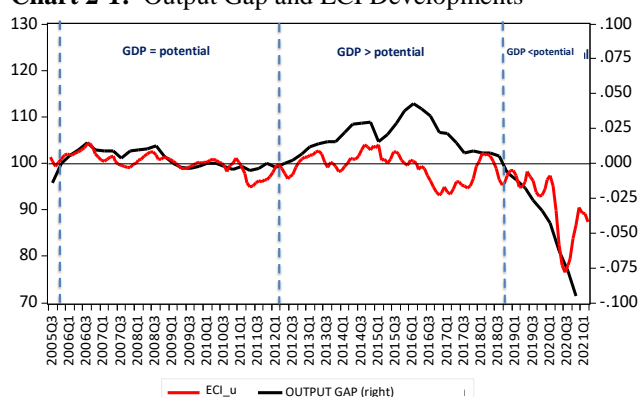
Source: Reuters

Chapter II. Recent Developments in Domestic Economy and Short-Term Prospects

Moderate GDP growth prospects remain for the year's second quarter, supported by the recovery in external demand and the effects of additional fiscal stimulus and domestic trend towards pandemic control. However, the worsening military instability that led to the suspension of the Mozambique LNG project in the Rovuma basin may limit the economic performance in the year. Regarding prices, the recent appreciation of Metical and the dissipation of the effects of the climate shocks that occurred at the beginning of the year in the country translated into lower inflation in April, and led to a downward revision of its prospects for the short and medium term.

II.1. Short-term Economic Activity

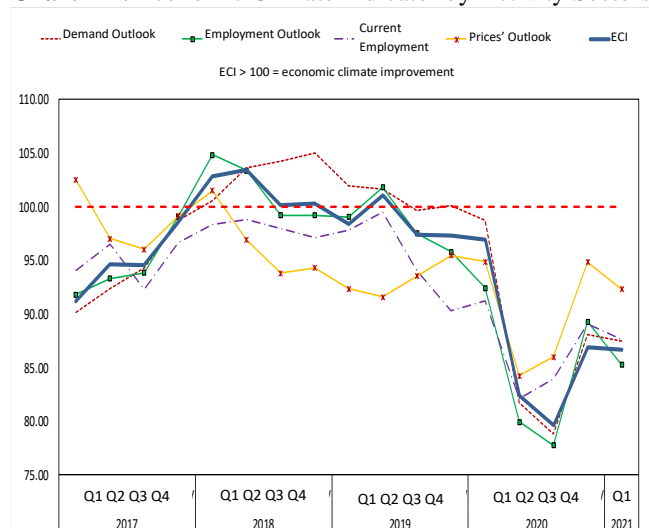
Chart 2-1: Output Gap and ECI Developments



Source: INE

The unfavorable assessment of the economic climate supports the prospects for deterioration of economic activity in the first quarter of 2021. The confidence of economic agents fell in the first quarter of 2021, following signs of recovery in the previous quarter. This fact, combined with a more weakened aggregate demand, in the face of i) the extension of restrictive measures to mitigate the increase in COVID-19 infections; and ii) the negative effects of climate shocks, both observed at the beginning of the year, reinforce the prospects of deterioration of economic activity in the period in question (Charts 2-1 and 2-2).

Chart 2-2: Economic Climate Indicator by Activity Sectors



Source: INE

The limited aggregate demand is supported by weak dynamics in foreign trade and credit to the economy, despite the increase in public spending. In fact, in the first quarter of the year there was a significant reduction in the import of intermediate goods and capital, which, in the face of a slight increase in exports, corroborates the poor performance of economic activity in the same period (Tables 2-1 and 2-3). In the quarter in question, credit to the private sector decreased in annual terms, especially for the foreign currency component, considering the Metical appreciation observed in the period (Chart 2-3).

On the other hand, public spending increased by 11% in annual terms, and the current – with greater weight in total spending, increased by about 13% (Table 2-4). In a context where total revenue grew less than expenditure, the overall fiscal deficit widened by 18%, largely financed by domestic resources. Compared to March,

Table 2-1: Developments in Balance of Payments (million USD)

	Incl. GP			
	Q1 20	Q1 21	Var. (USD)	Var. (%)
Current Account	-1,205	-795	410	-34
Balance of Goods	-890	-457	434	-49
Exports	893	921	27	3
Imports	1,784	1,377	-406	-23
Balance of Services	-299	-288	11	-4
Balance of Primary Income	-114	-123	-9	8
Balance of Secondary Income	98	73	-25	-26
Capital Account	46	27	-19	-41
Financial Account	962	668	-295	-31
FDI	714	334	-380	-53
Other investments	247	345	98	40

Source: BM

domestic debt increased by 310 million meticaïs, to a balance of 205,489 million meticaïs, reflecting the increase in Treasury Bonds issuance (Table 2-5).

For the second quarter of 2021, the prospects for a modest improvement in economic activity remain. In light of the containment of COVID-19 infections and the trend of increasing prices of main export goods, the gradual recovery of the global and domestic economy support better operating conditions of the economy in the second quarter of 2021, compared to the same period in 2020.

Table 2-2: Main Exported Goods (million USD)

	Q1 2020	Q1 2021
Aluminum Bars	230	269
Heavy Sands	53	100
Electric Power	117	129
Mineral Coal	195	154
Tobacco	31	21

Source: BM

The prospect of recovery is in line with the assessment of economic agents in the industrial sector, which report increased production and new orders. However, the temporary suspension of the Mozambique LNG project may result in relatively more limited growth, given its negative impact on companies supplying goods and services to the project (Chart 2-4).

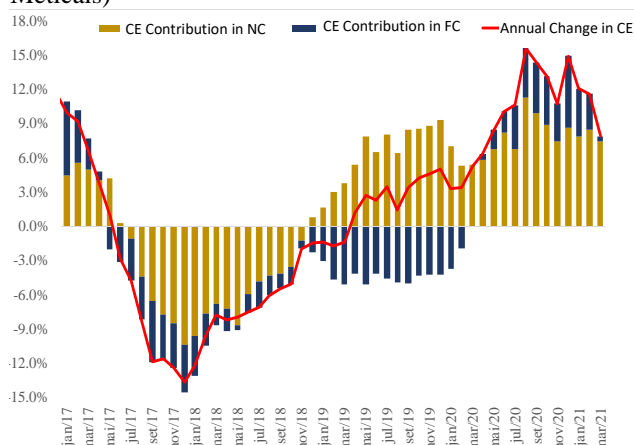
Table 2-3: Main imported goods (million USD)

	Q1 2020	Q1 2021
Machinery	314	246
Cars	10	8
Fuels	213	130
Raw aluminum	95	84
Wheat	45	63

Source: BM

The country's external position, as measured by gross international reserves (RIB), remains at comfortable levels. In the first week of May, the GIR balance was set at USD 4,017 million, which is sufficient to cover over 6.0 months of imports of goods and services, excluding imports from major projects.

From March to May, Metical experienced greater volatility against the US dollar (USD). This volatility resulted from the high uncertainties and asymmetries in the process of forming traders' expectations in the foreign exchange market, in addition to the effect of the greater fluctuation in the prices of financial assets on the international market.

Chart 2-3: Developments in Credit to the Economy (million Meticaïs)

Source: BM

Indeed, despite the recent depreciation trend, relating to the latest MPC data, the Metical appreciated against the Dollar by 21.0%, against the Euro by 18.8%, and depreciated slightly against the Rand by 0.4%. (Chart 2-5).

In real effective terms, as measured by the Real Effective Exchange Rate Index (REER), in the period under review, the Metical recorded losses

Table 2-4: Public Expenditure in 2021 (10⁶ MT)

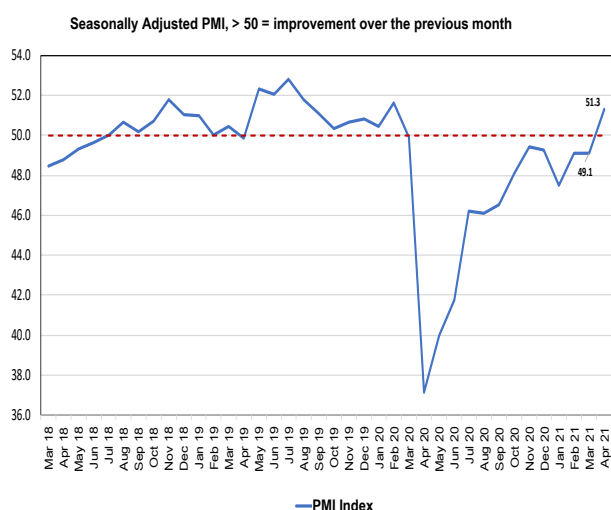
(million meticaís)	Q1/20 Paid-In	2021 Law	Q1/21 Paid-In	Annual Change
Total Revenue	54,632	265,596	59,867	9.6%
Net expenditure and loans	68,177	367,595	75,921	11.4%
Current Expenditure	50,713	238,291	57,157	12.7%
Staff	33,229	134,157	35,982	8.3%
Goods and Services	3,940	37,542	6,158	56.3%
Debt Service	5,253	35,115	5,691	8.3%
Current transfers	7,762	28,672	8,747	12.7%
Subsidies	332	113	442	32.9%
End of fiscal years+Capital Deposits+ Other	197	1,692	138	-29.7%
Investment Deposits	6,031	83,782	9,487	57.3%
Net loans	11,433	45,523	9,277	-18.9%
Balance before Donations	(13,545)	(101,999)	(16,054)	18.5%
Donations	1,513	34,006	3,126	106.6%
Balance after Donations	(12,032)	(63,557)	(12,928)	7.4%
Foreign Financing (net)	5,243	25,536	2,012	-61.6%
Domestic Loans	9,352	40,958	13,392	43.2%
Use for Added Value	5,275	2,500	2,500	-52.6%
Total Resources	76,015	368,595	80,897	6.4%

Source: Ministry of Economy and Finance (MEF)

Table 2-5: Domestic Public Debt as Treasury Bills and Bonds and BM advances (million MT)

	Use of T-Bills	Treasury Bonds	In the BM	Total Debt	Debt as GDP %
Dec – 2017	21,634	39,566	41,226	102,425	12.8%
Dec - 2018	20,957	50,986	44,477	116,420	13.0%
Dec - 2019	29,671	61,817	48,067	139,555	14.6%
Dec – 2020	44,220	88,100	54,885	187,205	21.0%
Jan – 2021	44,220	88,100	59,822	192,142	16.9%
Feb – 2021	44,220	92,238	60,105	196,563	17.3%
Mar – 2021	50,220	96,445	58,514	205,179	18.1%
Apr – 2021	50,208	98,390	56,891	205,489	18.1%
Flow (Mar-April)	-12	1,945	-1,623	310	

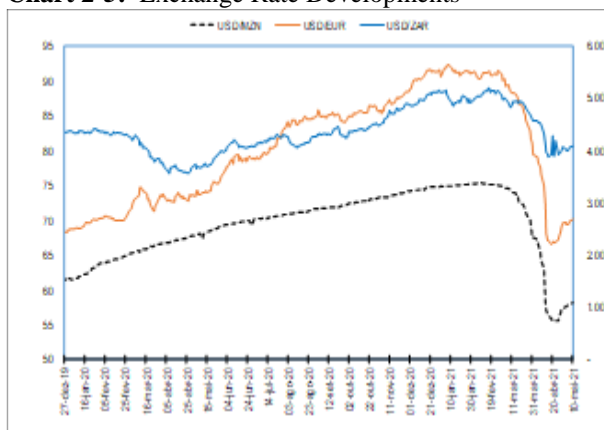
Source: BM

Chart 2-4: Purchasing Managers Index' (PMI)

Source: HIS, Markit

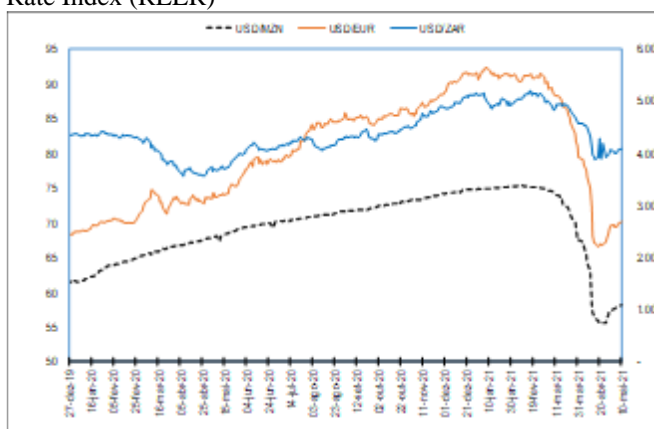
of competitiveness, resulting from the appreciation of the Nominal Effective Exchange Rate Index by (2.04%), in cumulative terms, against a background of a slight reduction in the difference between domestic prices and those of the country's main trading partners (Chart 2-6).

Chart 2-5: Exchange Rate Developments



Source: BM

Chart 2-6: Developments of the Real Effective Exchange Rate Index (REER)



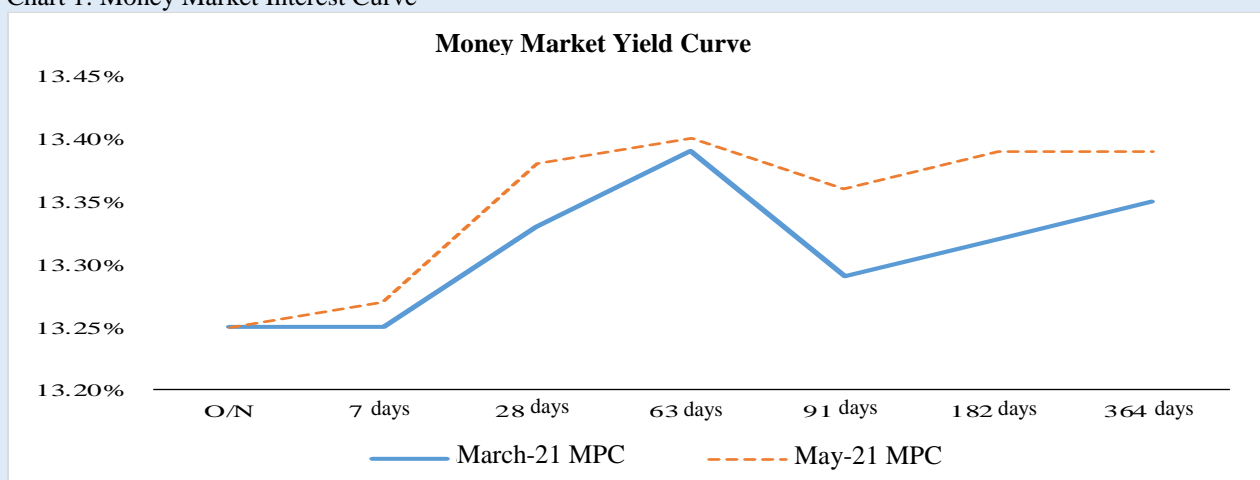
Source: BM

Box 1: Developments in Money and Capital Market Interest Rates

I. Yield Curve Developments

Between March and May, the upward trend of Interbank Money Market interest rates (MMI) remained at all maturities, in line with the upward adjustment of the monetary policy interest rate, the MIMO rate, observed in the first MPC session, held in January 2021. Indeed, except for the overnight term, all market interest rates increased by magnitudes ranging from 1 to 7 bp, as illustrated in Chart 1.

Chart 1: Money Market Interest Curve

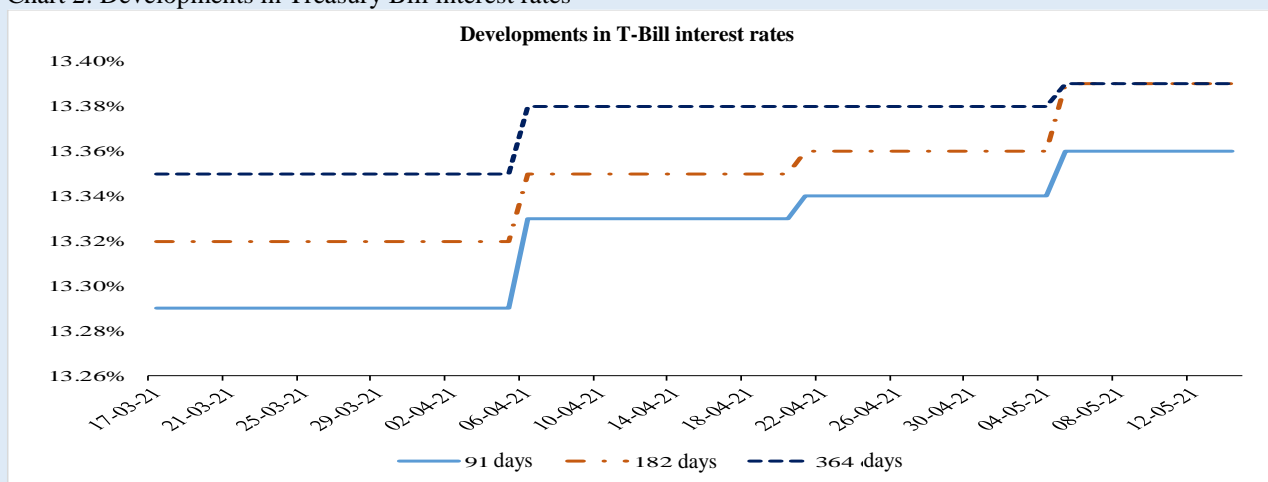


Source: BM

a) Treasury Bill Interest Rates' Developments

In the period under review, interest rates on Treasury Bills (T-Bills), which are the BM's deepest intervention instrument, continued to increase as they did in the previous period and are above the MIMO rate. Indeed, T-Bill interest rates for the reference periods increased between 4 and 7 bps, respectively. At the last T-Bill auction, interest rates stood at 13.36%, 13.39%, and 13.39%, for the 91, 182 and 364-day terms, respectively (Chart 2).

Chart 2: Developments in Treasury Bill interest rates

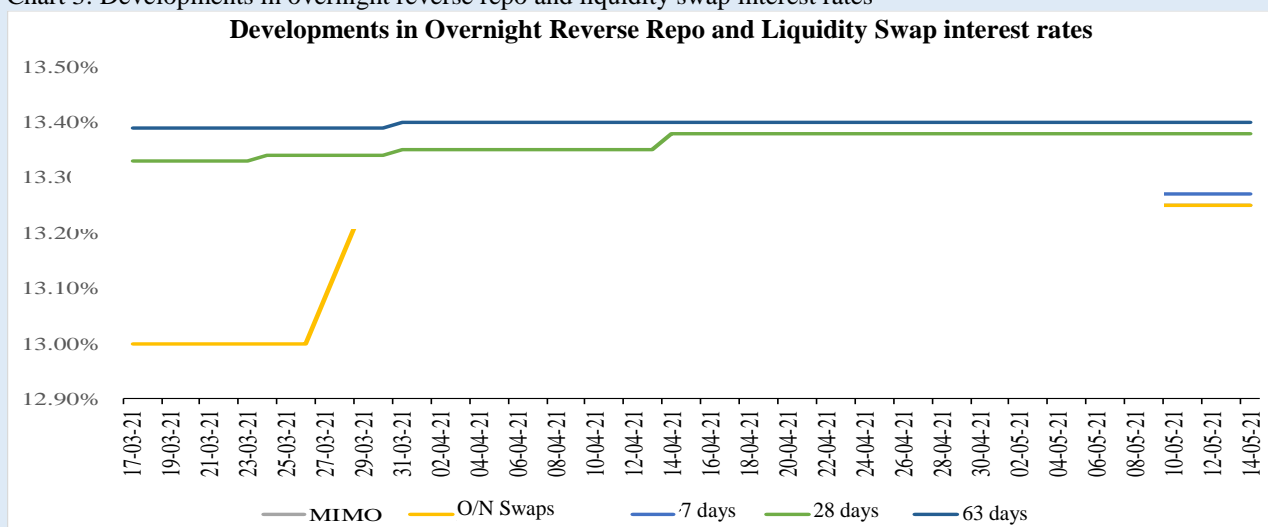


Source: BM

b) Overnight Reverse Repo and Liquidity Swap interest rates

Interest rates on operations for shorter terms also increased slightly. Thus, the 7-day T-Bill reverse repo transactions the BM by recorded an increase of 2 bp to 13.27% and, for the 28-day maturity, there was an increase of 5bp to 13.38. Finally, the 63-day reverse repo observed stability by only growing 1 bp. In turn, the interest rate on liquidity swaps between banks, without collateral, for overnight maturity increased by 25 bp, and was fixed at the level of the monetary policy interest rate, MIMO rate, at 13.25%. Chart 3 below illustrates the developments in reverse repo and liquidity swaps interest rates for the overnight term (1 day).

Chart 3: Developments in overnight reverse repo and liquidity swap interest rates

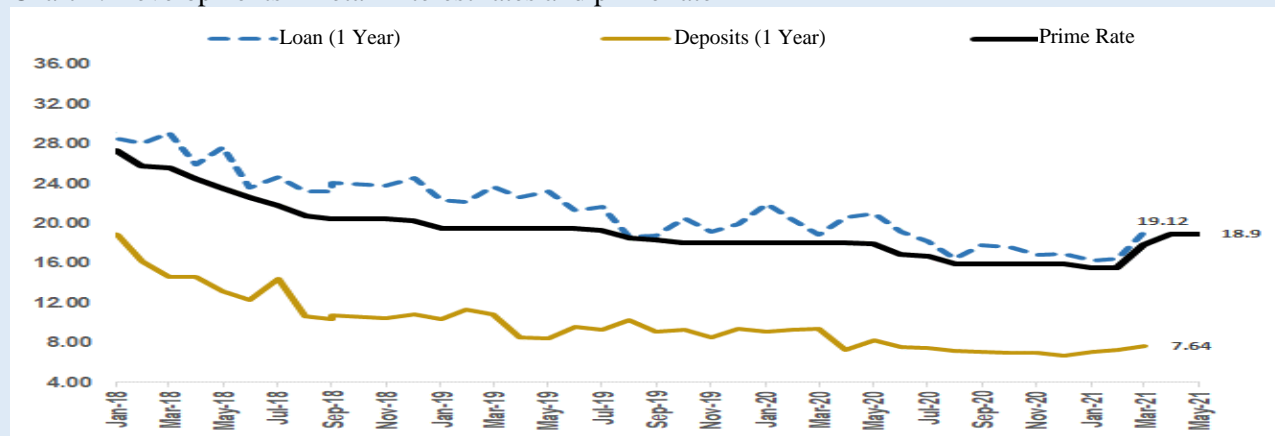


Source: BM

II. Retail interest rate

The Prime Rate and retail interest rates increased in line with the upward adjustment of the MIMO rate. In fact, from February to March 2021, the interest rate on one-year loans increased by 269 bps to 19.12%, while the interest rate on deposits increased by 39 bps to 7.64%. The spread between the two rates was 11.48% in March, against 9.18% observed in February. In April, the prime rate increased to 18.90% and remained unchanged in May, after 17.80% and 15.50% in March and February, respectively (Chart 4).

Chart 4: Developments in retail interest rates and prime rate

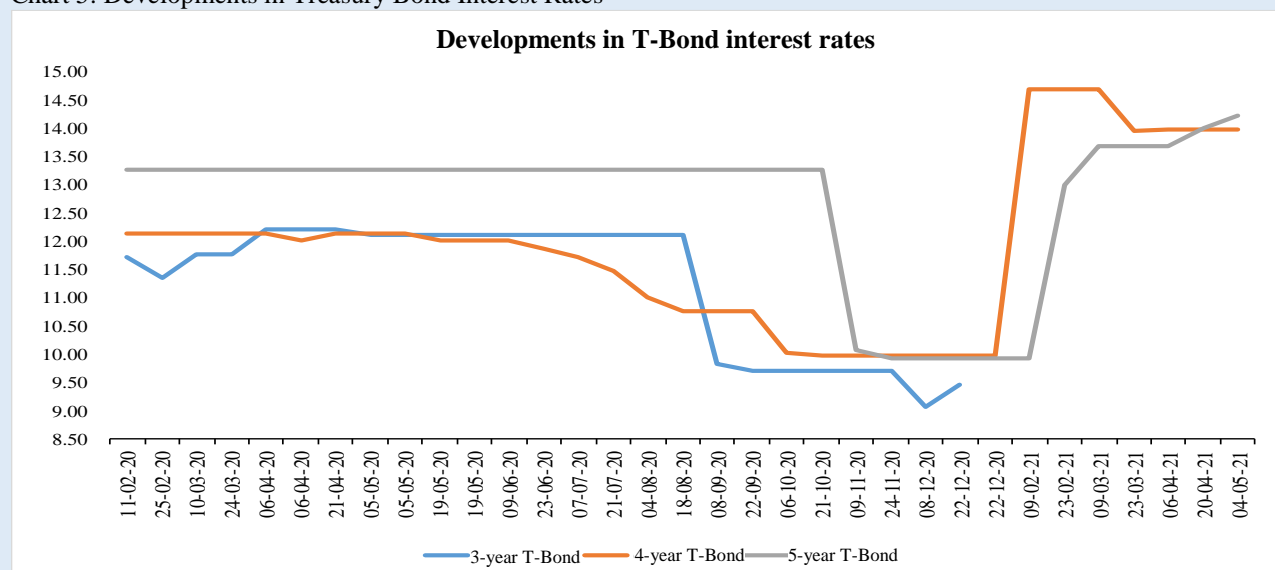


Source: BM

III. Developments in Treasury Bond Interest Rates

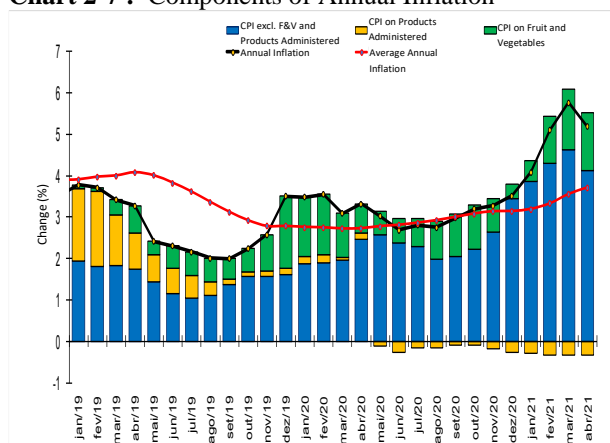
Treasury bond interest rates (T-Bonds), observed a mixed behavior. Indeed, in the interval between the two MPC Sessions (March and April), four Treasury Bond sessions were held, two for the 4-year term and two for the 5-year maturity. The 4-year interest rate decreased by 72 bp to 13.97% while the 5-year interest rate increased by 54 bp to 14.23% (Chart 5).

Chart 5: Developments in Treasury Bond Interest Rates



Source: BM

Chart 2-7 : Components of Annual Inflation



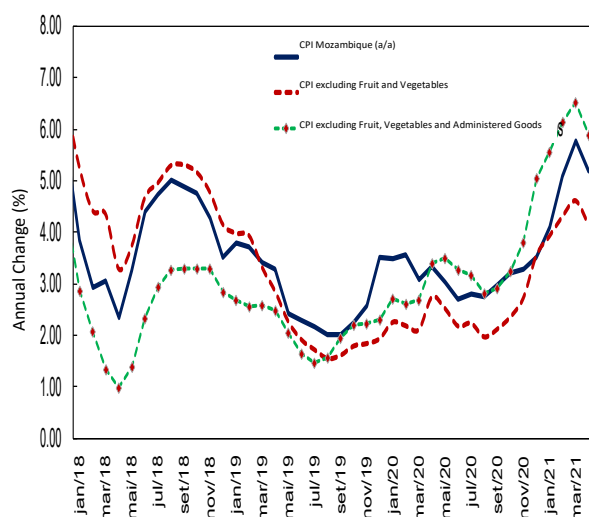
Source: INE / BM

Table 2-6: Core Inflation - Mozambique (Annual Change %)

	dec/20	jan/21	feb/21	mar/21	apr/21
CPI	3.52	4.09	5.10	5.76	5.19
Food	8.03	9.14	11.51	12.65	11.23
Cereals and derivatives	5.92	7.52	7.75	7.99	8.27
Fruit and vegetables	3.31	5.83	13.57	18.22	16.67
Administered	-1.18	-1.25	-1.47	-1.47	-1.47
Liquid Fuels	-6.36	-6.36	-6.36	-6.36	-6.36
CPI x F&V	3.54	3.91	4.30	4.60	4.14
CPI x Admin.	4.87	5.59	6.95	7.80	7.05
CPI x Comb.	4.41	4.94	5.69	6.38	5.74
CPI x F&V and Admin	5.05	5.55	6.13	6.53	5.90

Source: INE

Chart 2-8: Annual Inflation and Core Inflation (Annual Change %)



Source: INE

II.2. Recent Inflation Developments and Short-Term Prospects

The dissipation of the effect of the weather shocks recorded at the beginning of the year in the country and the recent appreciation of the Metical led to the slowdown in inflation in April.

Mozambique's annual inflation slowed from 5.76% in March to 5.19% in April.² Still, annual average inflation maintained its upward trend, rising to 3.71% in April, after 3.55% in the previous month (Chart 2-7).

In terms of components, the slowdown in annual inflation is mainly explained by the slowdown in food class prices, with the reduction in fruit and vegetable prices standing out, reflecting the dissipation of the impact of the weather that affected the country at the beginning of the year, combined with the recently observed appreciation of the national currency against the currencies of the main trading partners (Table 2-6).

In turn, the maintenance of prices of administered products and the stability of liquid fuel prices in the country (Table 2-6 and Chart 2-7) favored the trend of slowing inflation.

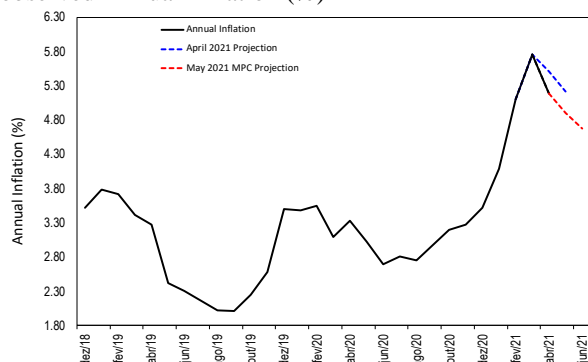
Meanwhile, underlying inflation has slowed, after seven consecutive months of acceleration. Indeed, excluding the fruit and vegetable subgroup (the most volatile component of the CPI basket) and the administratively priced subgroup of products, underlying annual inflation decreased from 6.53% in March to 5.90% last April (Table 2-6 and Chart 2-8).

Short-term prospects point to a deceleration of inflation in the coming months. This forecast is supported (i) by the higher domestic supply of fruits and vegetables, in the face of the fresh season, and the relative stability of the price of managed goods and services (Chart 2-9), in addition to the recent dynamics of the exchange rate.

For the same period, forward indicators of price developments, such as the Diffusion Index and the Purchasing Managers Index (PMI), confirm the

²Reported inflation refers to the change in Mozambique's Consumer Price Index (CPI).

Chart 2-9: Short-term Annual Inflation Projections and observed Annual Inflation (%)

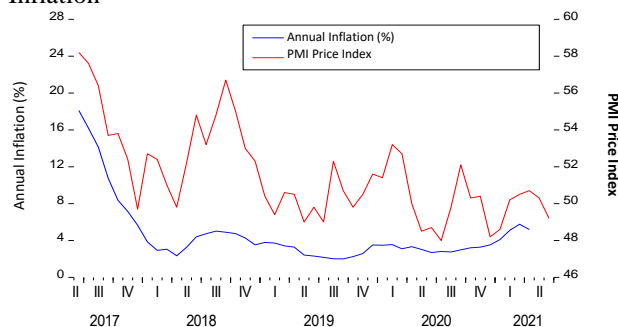


Source: BM

trend of slowing inflation in the coming months (Charts 2-10 and 2-11).

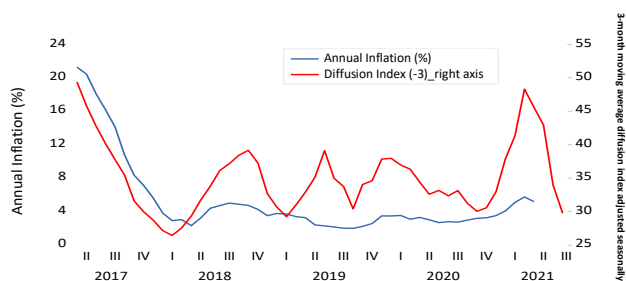
Meanwhile, economic agents expect inflation to accelerate towards the end of the year. The BM's May macroeconomic expectations survey, administered to domestic economic agents by the BM, shows that annual inflation could be around 5.56% by the end of the year, after 5.06% from April's survey. (Chart 2-12)

Chart 2-10: Price Index in Production and Annual Inflation



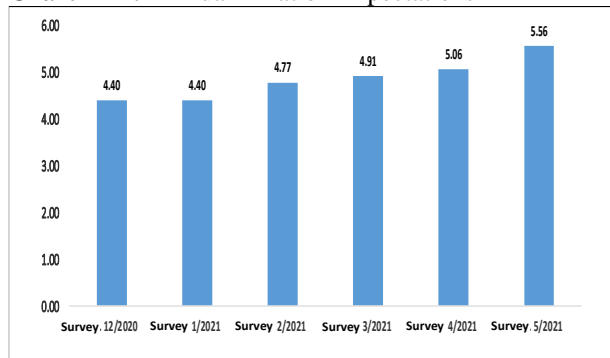
Source: BM/ HIS, Markit and INE

Chart 2-11: Diffusion Index and Annual Inflation



Source: BM/INE

Chart 2-12: Annual Inflation Expectations

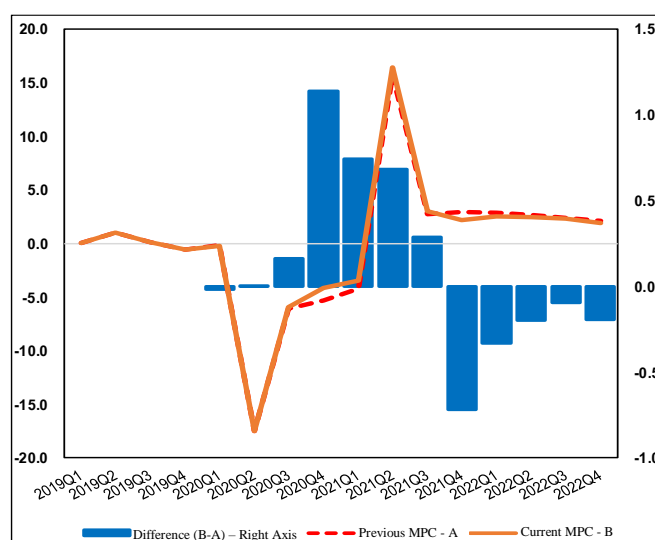


Source: BM

Chapter III: Medium-Term Inflation and Economic Activity Forecasts

Inflation forecasts were revised downwards. In the short and medium term, a slower pace of acceleration in inflation is anticipated mainly due to recent dynamics in exchange rate, against a backdrop of still subdued domestic demand. Regarding economic activity, an even more restrained performance is expected in 2021, supported by weak domestic demand, combined with the suspension of the Mozambique LNG project, despite the forecast of a gradual resumption of external demand and the expected containment of the COVID-19 spread. In view of the worsening of the risks and uncertainties, despite the downward revision of inflation forecasts, the MPC has decided to keep the MIMO rate unchanged at 13.25%.

Chart 3-1: South Africa Annual GDP Growth Forecast (%)



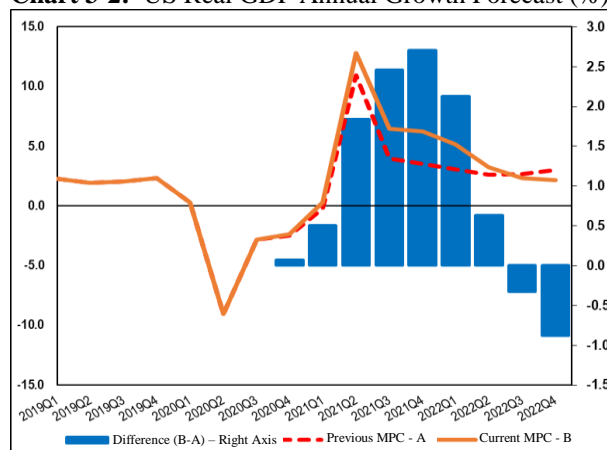
Source: GPMN (Global Projection Model Network) / BM

3.1. External Assumptions for Inflation Projections³

Upward revision of economic growth prospects in South Africa and the US in 2021. Regarding the March 2021 MPC, the Global Projection Model Network (GPMN) projections indicate an upward revision in the growth of economic activity in South Africa and the US, from 4.3% to 4.6% and from 4.6% to 6.5%, respectively (Charts 3-1 and 3-2).

Upward revision of the inflation forecasts for South Africa and the US in 2021 and 2022. Compared to the March MPC, the most recent inflation projections for South Africa point to an acceleration of 3.9% (within the target of 3-6%) against the previous 3.7%, reflecting increased pressure on the price of fuels, against a background of gradual recovery in the price of oil on the international market. For the US, the fiscal stimulus packages are expected to strengthen domestic demand, leading to a further acceleration in inflation from 2.5% to 3.1%, against a target of 2%. For 2022, inflation is expected to be 4.1% and 3.1% for South Africa and the USA, respectively. (Charts 3-3 and 3-4).

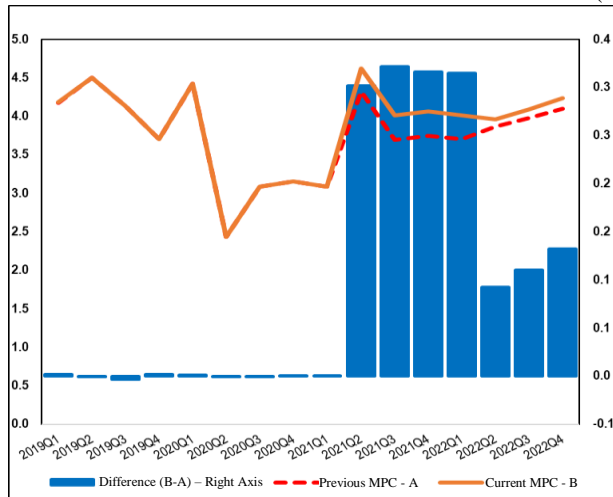
Chart 3-2: US Real GDP Annual Growth Forecast (%)



Source: GPMN / BM

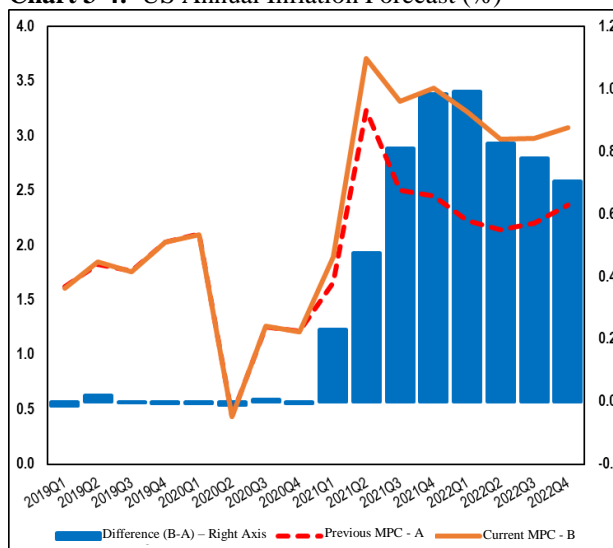
³Source: Global Projection Model Network (GPMN)

Chart 3-3: Annual inflation Forecast in South Africa (%)



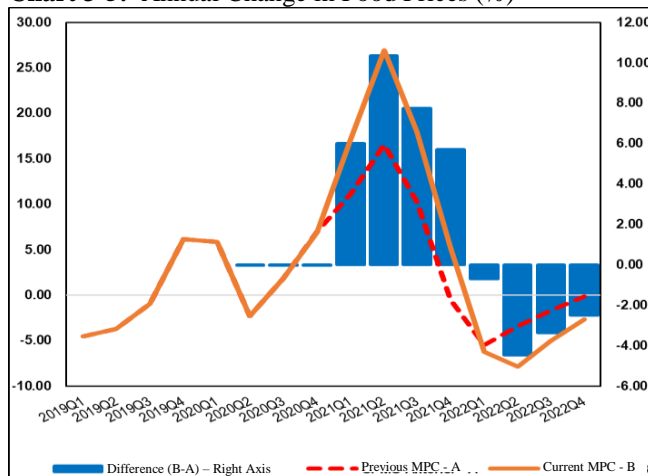
Source: GPMN / BM

Chart 3-4: US Annual Inflation Forecast (%)



Source: GPMN / BM

Chart 3-5: Annual Change in Food Prices (%)



Source: GPMN / BM

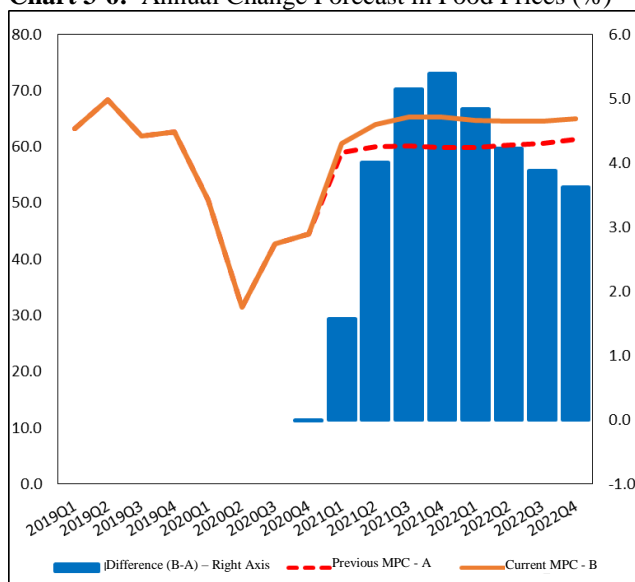
Upward revision of food price forecasts in the international market for 2021 and 2022. The projections of food prices in the international market, as measured by the GPMN price index, were again revised upwards for 2021, going from an annual change of 9.4% to 16.8%, reflecting climate shocks in the main production regions and supply chain disruptions. For the year 2022, a slowdown is expected from -2.7% to -5.4% (Chart 3-5).

Upward revision of oil barrel price forecasts for 2021 and 2022. Oil price projections were revised upward to 63.8 USD/barrel from the previous 59.7 USD/barrel, reflecting the gradual recovery in global demand, against a backdrop of relief from restrictive measures imposed to contain COVID-19 and fiscal stimulus packages in the US. For 2022, an average price of 64.7 USD/barrel is expected against the previous forecast of 60.5 USD / barrel (Chart 3-6).

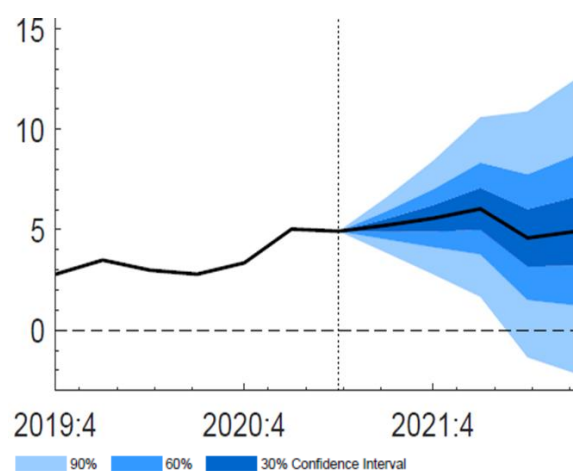
3.1. Internal Assumptions

Pressure on the prices of administered goods is expected to continue in 2021. For 2021, we continue to anticipate a decompression of some measures adopted by the government to mitigate the effects of COVID-19, which combined with the recovery in the price of oil in the international market, may generate pressure on the overall price level. However, the recent exchange rate gains of the Metical against its main counterparties, coupled with the extension of the VAT exemption on essential goods until 2023, may help to smooth the administratively set price adjustments.

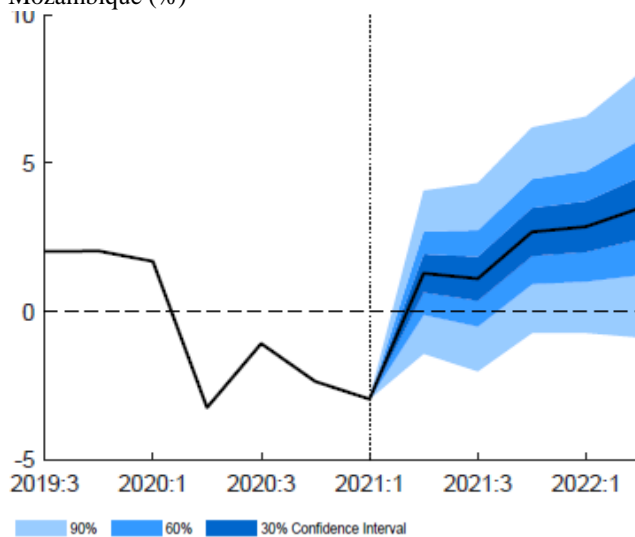
Prospects of lower exchange rate pressure in the medium term. The recent dynamic of the exchange rate has changed the basis of the projections for the medium term. However, we anticipate a slight exchange rate pressure in line with the prospects of a gradual reopening of the

Chart 3-6: Annual Change Forecast in Food Prices (%)

Source: GPMN / BM

Chart 3-7: Mozambique Annual Inflation Projection (%)

Source: BM

Chart 3-8: Projection of Annual Real GDP growth for Mozambique (%)

Source: BM

economy, in a context of maintaining the trade deficit.

Prospects of greater pressure on public spending remain. The military instability in the northern region associated with the logistical needs for the administration of the vaccine against COVID-19 will continue to pressure public spending leading to the maintenance of a worsening of the budget deficit.

3.2. Projection Results

Inflation forecasts were revised downward, despite the worsening risks. A slower acceleration in inflation is expected for the short and medium term (Chart 3-7), mainly reflecting the recent dynamic of the exchange rate in a context of weak domestic demand that outweighs the effect of the prospects of rising food and oil prices on the international market. However, the risks and uncertainties associated with to the projections have worsened.

A slower recovery of the economy is anticipated for 2021. This prospect is supported by weak domestic demand and the suspension of the gas exploration project by Total. However, a gradual recovery in external demand is expected, as a result of the gradual easing of restrictive measures associated with the trend of containing COVID-19 spread and the adoption of fiscal stimulus packages in advanced economies, in particular in the US, with positive effects on economic activity (Chart 3-8).

3.3. Monetary Policy Decision

The Monetary Policy Committee (MPC) of the Banco de Moçambique decided to keep unchanged the monetary policy rate, MIMO rate, at 13.25%. The decision is based on the worsening of the risks and uncertainties, notwithstanding the downward revision of the

inflation forecasts for the short and medium term, reflecting mainly the recent appreciation of the Metical.

Among the main risks and uncertainties linked to the projections, the intensification of military instability in the northern zone of the country and the greater volatility of the exchange rate stand out, domestically. In the external environment, there is a greater fluctuation in the prices of financial assets and commodities, as well as the emergence of new strains of the coronavirus.

The MPC will continue to monitor the domestic and international macroeconomic environment, as well as the prevailing risks, and will not hesitate to take the necessary corrective measures before the next ordinary meeting scheduled for July 21, 2021.

