March 2021
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ECONOMIC OUTLOOK AND INFLATION FORECASTS

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March 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. At the same time, the BM is 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 the 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 17 April 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 forecasts, 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 its policy rate, MIMO rate, at 13.25%. The decision is justified by the prevalence of high risks and uncertainties, despite the downward revision in the inflation forecasts for the short and medium term, largely reflecting the effects of the January's MPC meeting decisions.

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

Inflation forecasts have been revised downward, to a single digit. Annual inflation trended upward, rising from 3.52% in December 2020 to 5.10% last February, due to the impact of climate shocks and the pass-through of the Metical depreciation to domestic prices. Meanwhile, core inflation, which excludes goods and services with administered prices and fruits and vegetables, accelerated at a slower pace when compared to headline inflation, as expected. For the short and medium-term, it is expected a lower price increase, mainly reflecting the current Metical appreciation trend, resulting from the measures taken in the last MPC meeting, in a context of weak economic activity.

Risks and uncertainties associated with inflation projections remain high. At domestic level, it stands out the uncertainty regarding the spread of COVID-19, the impact of natural disasters and the prevalence of military instability, particularly in the northern part of the country. In the external environment, the main source of uncertainty is the volatility in the price of the country's main import and export commodities and the strengthening of the US dollar.

Prospects for a sluggish recovery in economic activity in 2021 remain. Following a contraction of the Gross Domestic Product by 1.3%, in 2020, a slight growth is expected in 2021, supported by the likely recovery of external demand, due to the progress in the vaccination, adoption of fiscal stimulus packages, and the progressive easing of measures imposed under COVID-19. At domestic level, a gradual recovery in the economy is expected, as a result of the progress in containing the spread of COVID-19, in a context of implementation of projects in the Rovuma Basin. In this regard, the MPC continues to consider relevant, the deepening of structural reforms aimed at strengthening institutions, improving the business environment, attracting investment and creating jobs.

Pressure on public finances persists. The prospects of an increase in the public spending to cope with the country's challenges continues to justify the worsening of the budget deficit. Among the factors for a higher fiscal pressure, the key are the acquisition and logistics for the administration of the vaccine against COVID-19, the mitigation of the socio-economic impact of climate shocks, as well as the spending on the military instability, particularly in northern areas of the country. In fact, since the last MPC, domestic public debt, excluding loan and lease contracts and overdue liabilities, has increased from 183.8 billion meticais to 189.0 billion meticais.

Exchange pressure reduces significantly and the Metical appreciates against the US Dollar. Since the beginning of March, demand for foreign currency has been completely satisfied, as a result of a greater fluidity in the foreign exchange market, in contrast with the trend observed at the beginning of the year. As such, the Metical has appreciated, standing at 73.35 MZN/USD, after 75.11 MZN/USD at the end of last January. In parallel, gross international reserves remain at comfortable levels, standing at USD 3 987 million, sufficient to cover more than six 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 take the necessary corrective measures before the next ordinary meeting scheduled for May 19, 2021.

Chapter I. Recent Developments in International Economy

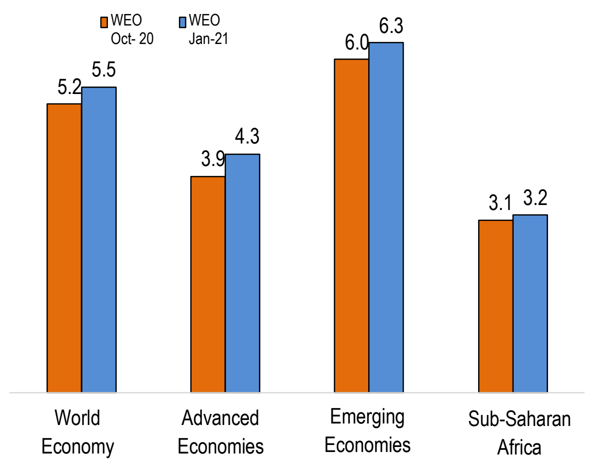
The re-imposition of containment measures to curb the spread of COVID-19 in the last months of 2020, conditioned the growth of advanced economies in the fourth quarter of 2020 and first quarter of 2021. However, their contribution to the current trend of containment of the pandemic, coupled with progress in vaccination programs and additional stimulus packages to economies, renew optimism about the growth of the world economy in 2021. Meanwhile, inflation has accelerated in most countries against a backdrop of recovery in the prices of major export commodities and oil in the international market.

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

Region	Achieved	Projection		
	2019	2020	2021	2022
World Economy	**2.8**	**-3.5**	**5.5**	**4.2**
Advanced	**1.6**	**-4.9**	**4.3**	**3.1**
U.S.	2.2	-3.4	5.1	2.5
Euro Area	1.3	-7.2	4.2	3.6
Germany	0.6	-5.4	3.5	3.1
Japan	0.3	-5.1	3.1	2.4
United Kingdom	1.4	-10.0	4.5	5.0
Emerging and Developing	**3.6**	**-2.4**	**6.3**	**5.0**
Brazil	1.4	-4.5	3.6	2.6
India	4.2	-8.0	11.5	6.8
China	6.0	2.3	8.1	5.6
Sub-Saharan Africa	**3.2**	**-2.6**	**3.2**	**3.9**
South Africa	0.2	-7.5	2.8	1.4

Source: IMF, WEO (January 2021)

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



Source: IMF

1.1. Recent Economic Activity and Forecasts

Better global economic performance is expected in 2021.

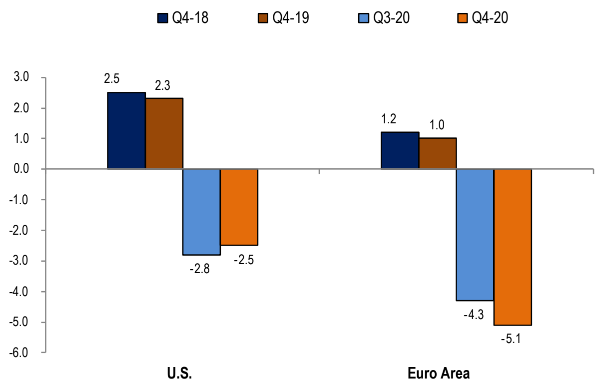
In the January's edition of the World Economic Outlook (WEO), the International Monetary Fund (IMF) updated the growth forecasts of the world economy for 2021 to 5.5%, from5.2% in October 2020 (Table 1-1 and Chart 1-1).

The greatest optimism stems mainly from: (i) the start of vaccination programs in several countries, and (ii) the approval of additional stimulus packages by the US and Japan. However, the IMF warns that the projected recovery may differ according to the difficulties in accessing the vaccines, the effectiveness of policies to support the economy and the structural characteristics of economies in the pre-pandemic period.

In the fourth quarter of 2020, there was a mixed performance of economic activity in the country's main trading partners.

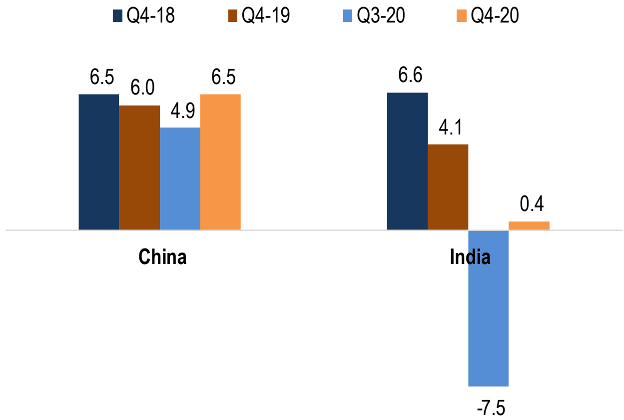
In the US and Euro Area, economic activity remained subdued. The emergence of new waves and strains of COVID-19 led to the re-imposition of containment measures, and contributed to the maintenance of negative growth in these economies (Chart 1-2).

Chart 1-2: U.S. and Euro Area Real GDP (%)



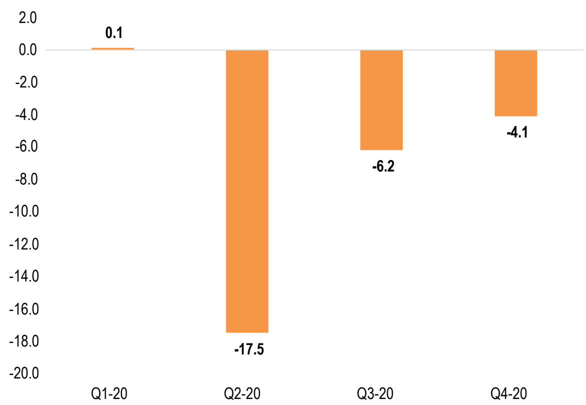
Source*:* Reuters and Trading Economics

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



Source*:* Reuters and Trading Economics

Chart 1-4: Real GDP of South Africa (%)



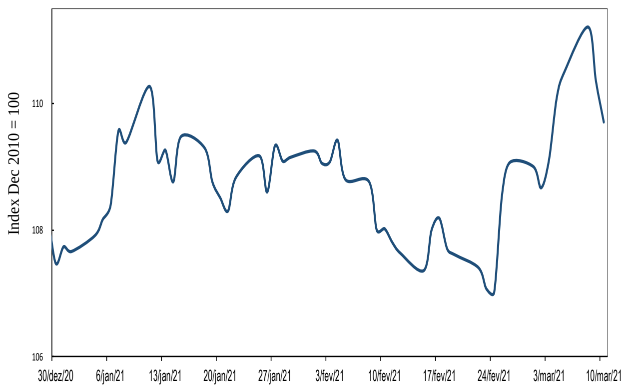
Source*:* Reuters and Trading Economics

In China and India, the performance of economic activity was positive, reflecting the relative control of the pandemic. In the fourth quarter of 2020, the Chinese economy registered a growth of 6.5%, standing out as the only largest economy with a positive performance in the year.

In the same vein, the gradual relaxation of restrictive measures in India resulted in an increase in public and private investment, and consequently an expansion of 0.4% in the last quarter of the year, after a contraction of 7.5% in the third quarter of 2020 (Chart 1-3).

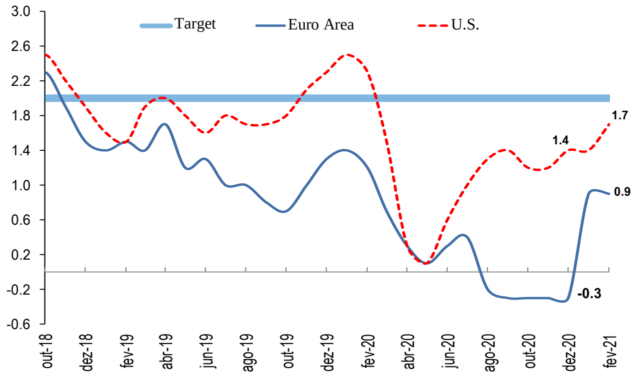
The South African economy contracted by 4.1% in the last quarter of 2020. In essence, the smaller contraction in GDP compared to the previous quarter, reflects the gradual reopening of the economy, after the relaxation of restrictive measures, to the state of public calamity, which prevailed in the first two months of the fourth quarter of 2020 (Chart 1-4).

Chart 1-5: Composite Index of USD against Currencies of Major Trading Partners



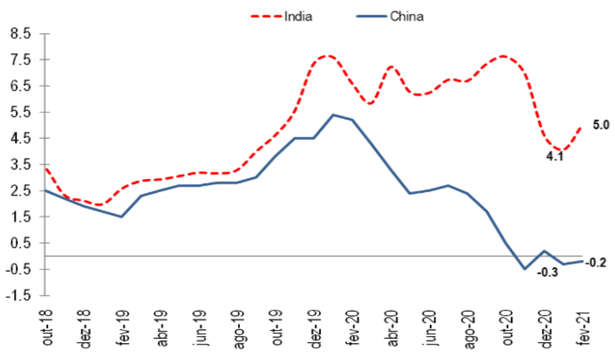
Source: Reuters

Chart 1-6: Inflation in US and Euro Area inflation(%)



Source: Reuters and Trading Economics

Chart 1-7: Inflation in China and India (%)



Source: Reuters and Trading Economics

The US dollar (USD) strengthens against major currencies.

The increased optimism around the recovery of the US economy in the face of progress in vaccination programs and the approval of the additional fiscal stimulus package (of USD 1.9 trillion) favored the recovery of the dollar. Indeed, from the last MPC (January/2021) to the first week of March, the USD Composite Index against the main trading currencies (Euro, Rand, Pound and Yen) recorded cumulative gains of 1.01% (Chart 1-5).

Annual inflation has accelerated for Mozambique's main partners, , but remains within its medium-term targets.

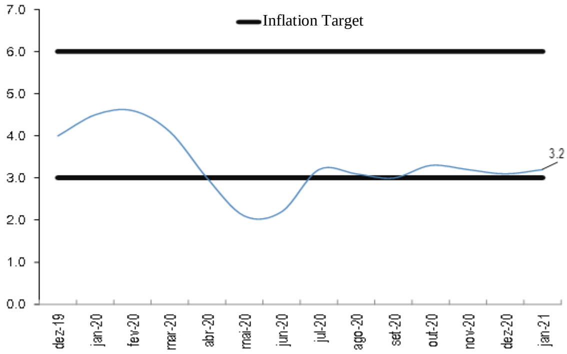
In advanced economies, annual U.S. inflation rose to 1.7% in February, mainly reflecting the rising cost of liquid fuels and electricity. Meanwhile, in the Euro Area, inflation remained at 0.9% (Chart 1-6).

In the emerging economies group, in the same period, China's annual inflation recorded lower deflation (-0.2%), and in India, it accelerated by 90 basis points (bp) to 5.0% in the face of rising food prices (Chart 1-7).

In South Africa, annual inflation accelerated by 10 bp to 3.2% in January. The upward price pressure stems from the education, health and catering classes, which have been partially dampened by lower fuel prices (Chart 1-8).

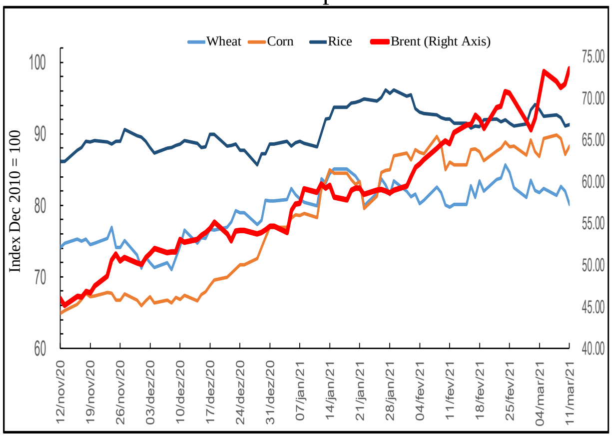
In most countries, central banks have kept monetary policy interest rates. This stance is justified by the expectation of maintaining the inflation rate within its targets, despite said acceleration.

Chart 1-8: Inflation in South Africa (%)



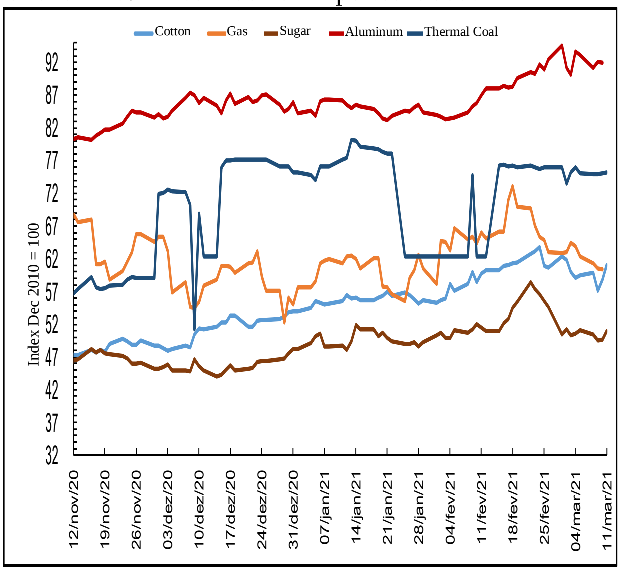
Source*:* Reuters and Trading Economics

Chart 1-9: Price Index of Imported Goods



Source: Reuters

Chart 1-10: Price Index of Exported Goods



Source: *Reuters*

1.2. Prices of Main Goods

Progress in vaccination programs, coupled with the approval of additional stimulus packages to economies, reinforce optimism about the faster recovery in global demand, with an impact on the prices of major export and import goods, especially oil.

From 27 January to the second week of March, the price of brent recorded cumulative gains of 24.8%, raising its international market price to 69.63 USD/barrel on the day (chart 1-9), which raises concerns about its impact on domestic inflation, given the high weight of liquid fuel prices in the Consumer Price Index. The rise in the price of brent is essentially explained by OPEC's continued production cuts and the recent approval of the US stimulus package.

The upward trend was also observed in the prices of some Mozambican export products, such as aluminum and coal (Chart 1-10), which may favor the country's export revenues, starting in the third quarter of 2020, with an impact on Mozambique's economic growth.

Chapter II. Recent Developments in Domestic Economy

In the fourth quarter of 2020, GDP contracted by 2.4%, resulting in negative growth of 1.3% in the year. The significant deterioration in economic activity in 2020 reflected, essentially, the adverse effects of the COVID-19 pandemic at a global level, in a context in which the maintenance of military instability, especially in the northern region of the country, also conditioned the normal course of implementation of hydrocarbon exploration projects in the Rovuma Basin. From the second quarter of 2021, a sluggish recovery in economic activity is expected, mainly justified by likely recovery of external demand and the gradual resumption of the functioning of the domestic economy, in the face of the reduction of daily infections and possible progressive relief of restrictions. On the price side, a smaller pressure is expected in the short term, mainly reflecting the current trend towards Metical appreciation, despite the effect of the recent climate shocks.

II.1. Economic Activity

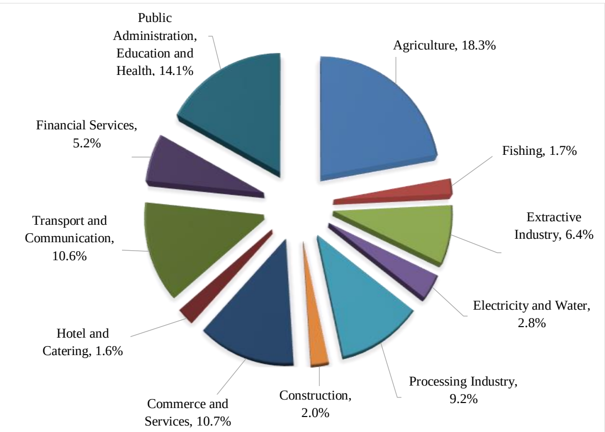
Table 2-1: Real GDP by Sectors - Annual Change (%)

Activity Sectors	2019		2020			
	IV	Year	III	IV	Year	Against pp
Primary Sector	**-0.5**	**0.0**	**-1.9**	**-2.7**	**-1.9**	**-0.6**
Agriculture	6.6	1.1	3.2	1.1	2.8	0.6
Fishing	6.5	2.3	-2.8	1.6	-0.4	0.0
Extractive Industry	-15.7	-3.7	-16.2	-13.1	-16.8	-1.2
Secondary Sector	**11.8**	**1.0**	**0.6**	**-2.3**	**-0.3**	**0.0**
Electricity and Water	5.3	-1.1	4.1	-5.2	2.7	0.1
Processing Industry	13.6	1.4	-0.9	-1.1	-1.2	-0.1
Construction	13.7	2.8	-0.2	-3.5	-0.6	0.0
Tertiary Sector	**2.9**	**2.7**	**-2.4**	**-4.1**	**-2.4**	**-1.1**
Commerce and Services	6.1	0.0	0.2	-1.8	-1.2	-0.1
Hotel and Catering	-3.6	1.0	-31.4	-22.5	-23.1	-0.4
Transport and Communication	0.3	4.2	-1.2	-7.5	-2.2	-0.2
Financial Services	1.7	4.0	-1.9	-2.1	-1.1	-0.1
Public Administration, Education and Health	3.7	2.7	-1.8	-3.1	-2.6	-0.4
Other Sectors	3.6	4.3	0.1	0.2	1.3	0.1
GDP at factor cost	**3.1**	**1.6**	**-1.9**	**-3.4**	**-1.9**	**-1.7**
Tax on products	-11.2	8.3	4.5	6.4	3.7	0.4
GDP	**1.4**	**2.3**	**-1.1**	**-2.4**	**-1.3**	**-1.3**

Source: INE

Economic activity deteriorated in the fourth quarter of 2020, reflecting the adverse impact of COVID-19 on the economy. Preliminary data from the National Statistics Institute (INE), indicate that, in annual terms, GDP contracted 2.4% in the fourth quarter of 2020, having contributed to a negative growth of 1.3% in the year, after a positive growth of 2.3% in 2019 (Table 2-1).

Chart 2-1: Sectoral Structure of GDP in the Third Quarter of 2020 (%)



Source: INE

Compared to the performance observed in the third quarter, the recent dynamic of the economy is explained by the slowdown in agriculture and contraction in the electricity and water sector, which were dampening the contraction in GDP in the sectors most affected by the pandemic.

In fact, the weight of aggregate, agricultural, and electricity, and the water has dropped by 4.6 percentage points (pp to 21.1% of the GDP, and that is also seen in the deterioration of the contribution of trade and services, as well as transport and communications, in the face of weak domestic and external demand , the latter, which influenced greatly on the performance of the export sector, despite the improvement observed in the extractive industry in the fourth quarter (see Table 2-1 and Chart 2-1).

The contraction of GDP in the fourth quarter of 2020 led to the aggravation of the output gap, despite the optimistic expectations expressed by economic agents, , especially by the improvement of the Economic Climate Index (ECI) in the face

Chart 2-2: Output Gap and ECI Developments

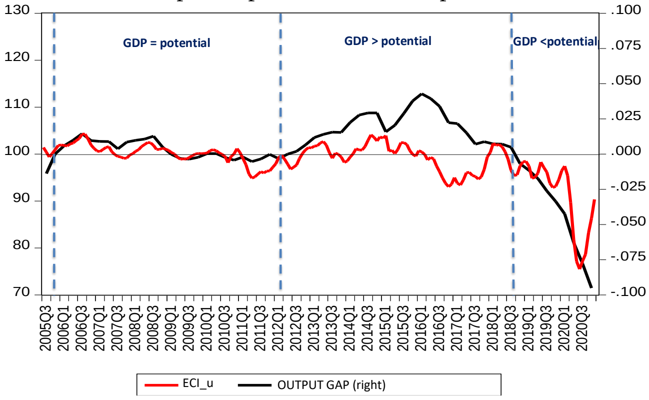
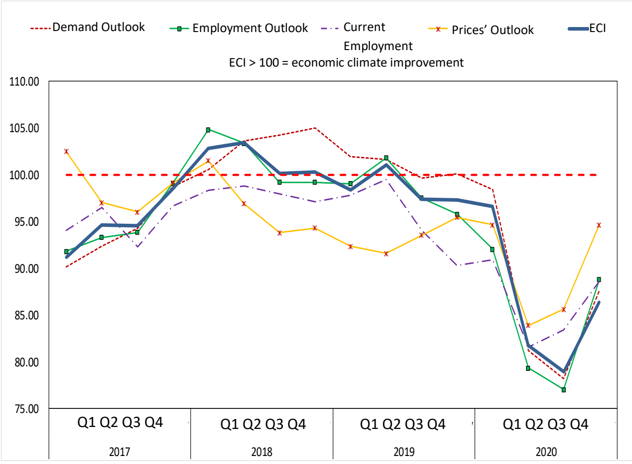


Chart 2-3: Economic Climate Indicator by Activity Sectors



Source: INE

Table 2-2: Balance of Payments (million USD)

	Incl. GP (million USD)					
	Q1	**Q2**	**Q3**	**Q4**	**Accrued (Year)**	**Annual Rate**
Current Account	**-1,205**	**-1,041**	**-835**	**-731**	**-3,813**	**-790**
Balance of Goods	-890	-544	-432	-427	-2,294	-211
Exports	893	725	929	1,041	3,588	-1,080
Imports	1,784	1,269	1,361	1,469	5,883	-870
Balance of Services	-299	-480	-506	-449	-1,733	154
Balance of Primary Income	-114	-85.7	-74	-189	-463	-167
Balance of Secondary Income	98	68	177	334	678	-567
Capital Account	46	20	29	41	135	29
Financial Account	**962**	**887**	**731**	**649**	**3,230**	**-172**
comprising						
FDI	714	44	786	794	2,337	126
Other investments	247	838	-61	-140	884	-292

Source: BM

of the relief of restrictive measures in the country (Charts 2-2 and 2-3).

By breakdown of the components of the aggregate demand, GDP contraction is justified by the restrictions imposed by COVID-19, which resulted in:

(i) **Deterioration of the current account balance as a result of weak external demand.** In fact, in 2020 exports decreased due to the combined effect of the reduction in volume and prices, in a context of a decreasing economic activity worldwide, particularly for the country's main trading partners. Meanwhile, the reduction in imports was less significant (Chart 2-2).

Table 2-3: Goods exported in 2020 (million USD)

	Q1	Q2	Q3	Q4	Accrued
Mineral Coal	195	140	156	178	668
Aluminum Bars	229	212	220	250	911
Heavy Sands	51	66	30	100	247
Tobacco	31	2	58	86	177
Aluminum Cables	22	11	18	21	73
Sugar	6	2	17	17	42
Cotton	6	1	4	4	16
Electric Power	121	101	126	117	465

Source: BM

Table 2-4: Goods imported in 2020 (million USD)

	Q1	Q2	Q3	Q4	Accrued
Machinery	314	209	237	262	1,023
Fuels	213	139	104	86	543
Raw aluminum	95	62	79	13	249
Construction Material	145	122	131	201	600
Cars	76	49	67	62	254
Fertilizers	9	15	14	22	61

Source: BM

Table 2-5: Public Expenditure in 2020 (10^6 MT)

(million meticais)	2019 Paid-in	Q32020 Paid-in	Revised Budget	2020 Paid-in	Change% 2020/2019
Total Revenue	**276,788**	**171,049**	**214,142**	**236,322**	**-14.62%**
Net expenditure and loans	**313,622**	**265,727**	**333,603**	**340,223**	**8.48%**
Current Expenditure	**195,802**	**161,963**	**231,046**	**225,946**	**15.40%**
Staff Expenditure	112,837	91,807	124217,1	124,444	10.29%
Goods and Services	25,735	22,366	40,308	40,308	56.63%
Debt Service	29,703	22,165	28,675	29,908	0.69%
Current Transfers	25,620	23,087	31,466	32,328	26.18%
Investment Expenditure	**72,053**	**43,530**	**90,571**	**68,564**	**-4.84%**
Deficit before donations	(36,833)	(94,678)	(119,461)	(103,902)	……
Donations	11,106	16,130	39,273	35,208	……
Loans	36,891	17,143	51,037	36,200	(0.02)
Balance after donations	**(25,727)**	**(78,548)**	**(80,188)**	**(68,694)**	**……**
Domestic Financing	28,545	44,775	53,013	54,068	89.41%
Use for Added Value	5,274	14,274	16,631	17,541	……
Total Resources	**358,605**	**…..**	**374,096**	**379,338**	5.78%

**revenue+donations+foreign loans+domestic loans+added value*

Source: Ministry of Economy and Finance (MEF)

(ii) **Continued reduction of capital expenditure at the expense of increased current expenditure.** In 2020, pressure on public spending and domestic funding increased, in the face of military instability in the central and northern regions of the country, and the increased need for funds to mitigate the impacts of COVID-19 on the economy. In fact, current expenditure absorbed the most resources, increasing by 15%, in contrast to the reduction in public investment, a component with a significant impact on GDP (Table 2-5).

Since January's MPC meeting, by mid-March, the state increased its domestic debt in 6338 million Meticais, as a result of the issuance of Treasury Bonds in February and March. (Table 2-6).

Economic activity is expected to deteriorate in the first quarter of 2021. This perspective stems from the impact of the following factors: (i) the climate shocks that affected the country at the beginning of the year, (ii) the re-imposition of restrictive measures at the domestic level and in some trading partners, in the face of the increase in the number of COVID-19 infections at the beginning of the year and (iii) the slowdown in the implementation of the onshore activities of the Rovuma natural gas projects.

For the second quarter of 2021, a sluggish growth of the domestic economy is expected. The weak performance of economic activity could be supported mainly (i) by external demand and the maintenance of the trend of recovery in the prices of the main exported goods, in a context of reduction of daily COVID-19 infections in the face of progress in vaccination programs in most of Mozambique's trading partners, combined with (ii) the likely gradual resumption of the functioning of the economy as a result of the trend to contain the spread of the pandemic.

This optimism is in line with the favorable development of the Purchasing Managers' Index (PMI) in February 2021 (Chart 2-4).

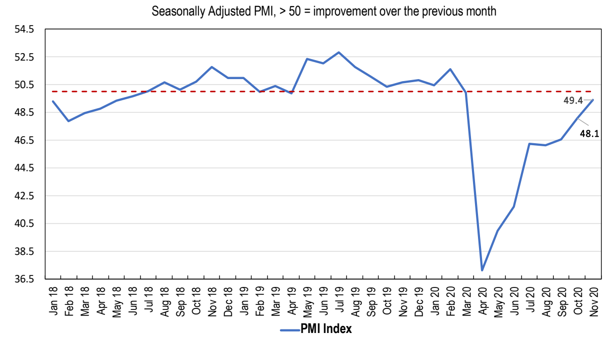
Table 2-6: Domestic Public Debt in the form of Treasury Bills and Bonds and BM advances (million MT)

Domestic Public Debt in the form of T-Bills, T-Bonds and BM advances (million MT)					
	Use of T-Bills	Treasury Bonds	In the BM	Total Debt	Debt as GDP%
Dec - 2018	20,957	50,986	40,978	112,921	12.6%
Dec - 2019	29,671	61,817	48,067	139,555	14.6%
Dec – 2020	44,220	88,100	46,369	178,689	20.0%
Jan – 2021	44,220	88,100	50,369	182,689	16.1%
Feb – 2021	44,220	92,238	50,369	186,827	16.5%
Mar – 2021	44,220	94,438	50,369	189,027	16.7%
Flow (Jan and Mar)	0	6,338	-	6,338	

*The deb-to-GDP ratio increase in 2020 is due to the GDP reduction.

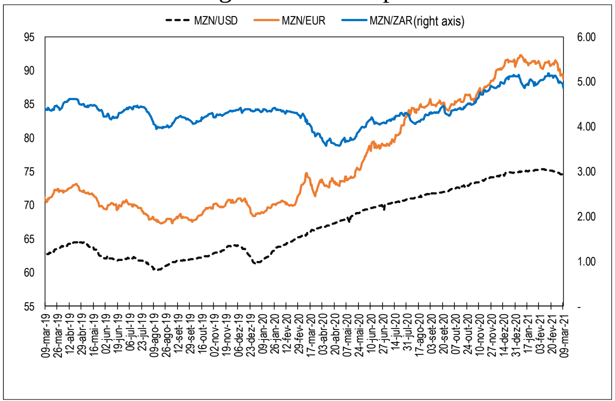
Source: BM

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



Source: HIS, Markit

Chart 2-5: Exchange Rate Developments



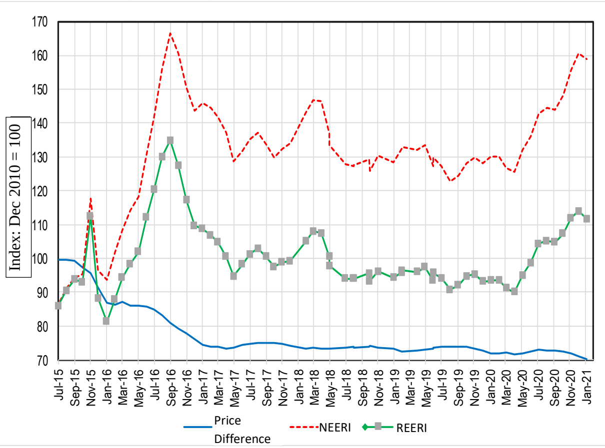
Source: BM

The country's external position, as measured by gross international reserves (GIR), remains at comfortable levels. In the second week of March, the GIR balance was USD 3,987 million, enough to cover more than 6.0 months of imports of goods and services, excluding imports from major projects.

Exchange pressure reduces significantly and the Metical appreciates against the US Dollar. Since the beginning of March, demand for foreign currency has been completely satisfied, as a result of a greater fluidity in the foreign exchange market, in contrast with the trend observed at the beginning of the year. Indeed, Metical appreciated against the Dollar (0.95%), the Euro (4.82) and the Rand by 1.22%, contributing to cumulative nominal gains of 0.61%, 5.09% and 2.02%, respectively (Chart 2-5). The trend towards appreciation of the Metical is mainly due to the policy measures taken by the MPC last January, including the upward adjustment of the MIMO rate to 13.25%.

The developments of the Real Effective Exchange Rate Index (REER) in the period under review shows, that Mozambique recorded annual gains in the competitiveness of its exports, as a result of the depreciation of the Nominal Effective Exchange Rate Index (19.45%), in a context of continued stability of the difference between domestic prices and those of the country's main trading partners (Chart 2-6).

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



Source: BM

Box 1 : Monetary and Financial Developments

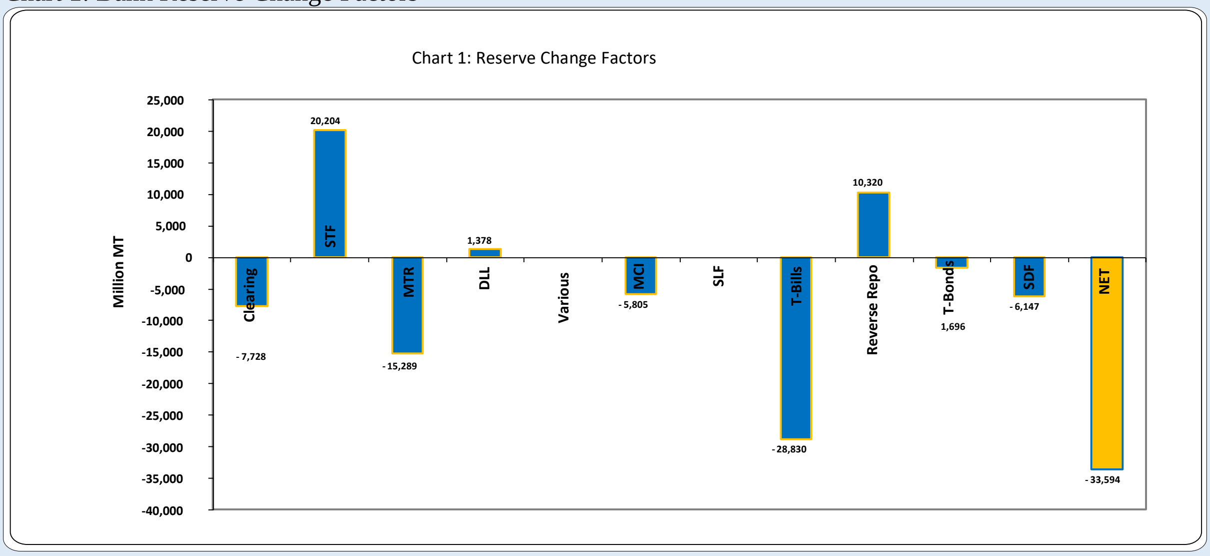
I. Contextualization

At the first session of the BM's MPC, held on January 27, 2021, the committee decided to increase the policy interest rate (the MIMO rate) by 300 bp to 13.25%. The decision to increase the MIMO rate was justified by the upward revision of the inflation outlook for the medium term, reflecting the continued depreciation of Metical, in an environment of worsening risks and uncertainties, with emphasis on the negative impact of (I) the accelerated spread of the COVID-19 pandemic, (ii) the occurrence of natural disasters and (iii) military instability. The MPC also decided to increase the Standing Deposit Facility (SDF) and the Standing Lending Facility (SLF) interest rates by 300 bp, to 16.25% and 10.25%, respectively, and maintain the Reserve Requirement ratios for liabilities in domestic and foreign currency at 11.50% and 34.0%, respectively. It was in this context that monetary policy was conducted in the interval between the last two sessions of MPC.

II. Liquidity developments

The MMI continues to be characterized by excess liquidity, but with a downward trend. Indeed, in the interval between the two MPC sessions (January and March 2021), bank reserves in national currency reduced by 33,594.0 million meticais, - Chart 1.

Chart 1: Bank Reserve Change Factors



Source: BM

The depletion of bank reserves was mainly justified by the following factors:

- ✓ Negative net effect of the issuance and repayment of Treasure Bills in about 28,830.0 million meticais;
- ✓ Net negative impact of electronic transfers between banks in real time (MTR) in the order of 15,289. 0 million meticais;
- ✓ Losses from commercial banks in clearing, of about 7,728.0 million meticais;
- ✓ Negative net impact of Standing Deposit Facility (SDF) operations of 6,147.0 million meticais.
- ✓ Debit resulting from net foreign exchange sales to commercial banks by the BM on the Interbank Foreign Exchange Market (MCI) of 5,805.0 million meticais; and
- ✓ Debt to credit institutions resulting from the issuance of Treasury bonds (T-Bonds) of about 1,696.0 million meticais.

This fall in reserves was restrained by the following factors:

- ✓ Transfers from the State to the economy via the Electronic Funds Transfer System (STF) of 20,204.0 million meticais;
- ✓ Positive net impact of reverse repo operations of approximately 10,320.0 million meticais; and
- ✓ Net cash withdrawals (DLL) of 1,378.0 million meticais;

III. Reserve Requirements and Liquidity

In the reserve requirement establishment periods, from 7 January to 6 February and from 7 February to 6 March 2021, Credit Institutions complied with the reserve requirements. In fact, bank liquidity (bank reserves minus reserve requirements) stood, on average, at 1,186.0 and 3,530. 0 million meticais, respectively, over the above periods. The extended liquidity, which includes overnight maturity transactions carried out by commercial banks with the BM, moved to 12,908.0 million meticais, after 131,819. 0 million verified in the previous establishment period, reflecting the new intervention stance of the BM in the market.

In turn, the potential liquidity, which incorporates Treasury securities (Treasury Bills and Treasury Bonds) and long-term Reserve Repo, observed a reduction, on average, to 250,663.0 million meticais in the period of establishment of reserve requirements from 7 February to 6 March 2020, as a reflection of the measures taken by the BM in the January 2021 MPC (Table 1).

Table 1: Distribution of Bank Liquidity (million MT)[2]

Description	Jan 6 - Feb 7	Feb 7 – Mar 6
a) Restricted Liquidity = Bank Reserves - Reserve Requirements (Average Basis)	**1,186**	**3,530**
SDF	866	9,378
Overnight Reverse Repo	129,767	0
SLF	0	0
Repo	0	0
b) Broad Liquidity = (a) + SDF + R. Repo – SLF - Repo	**131,819**	**12,908**
Treasury Bills (T-Bills)	72,019	82,909
Long term reverse repo	0	63,872
Treasury Bonds (T-Bonds)	88,414	90,974
(c) Potential Liquidity = (b) + T-Bills + T-Bonds	**292,252**	**250,663**

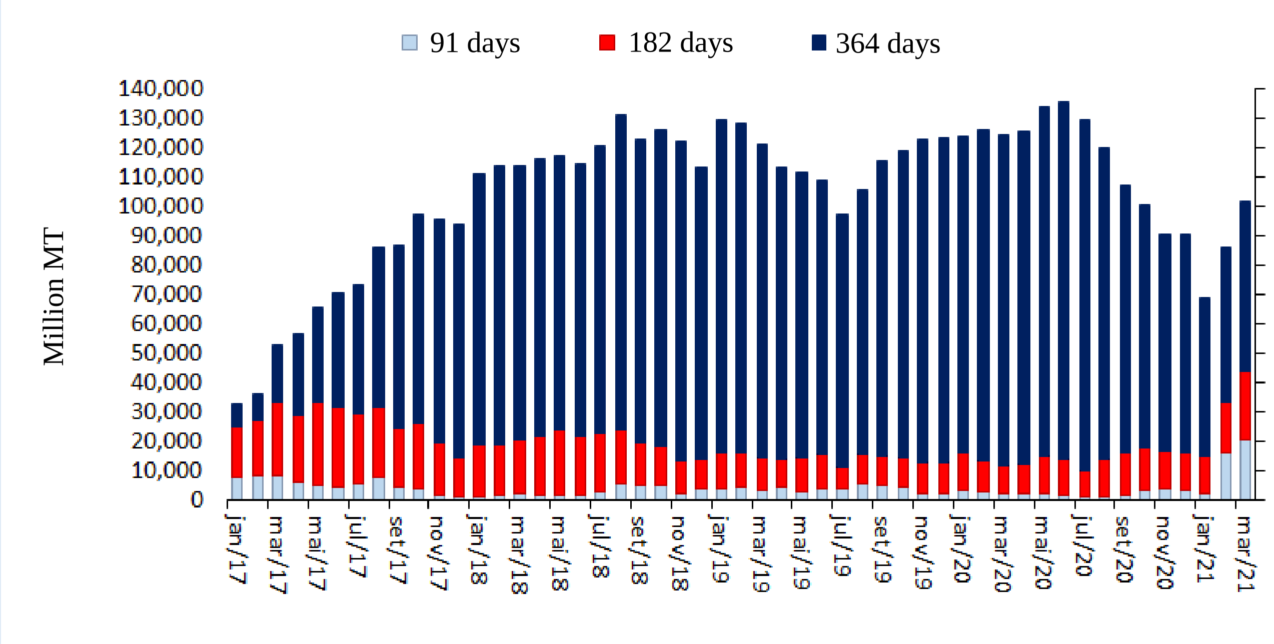
Source: BM

IV. Portfolio Balance of Treasury Bills

Thus, derived from the net issuance of Treasury Bills, its portfolio balance increased to 101,393.0 million meticais (Chart 2), divided by the following maturities: (I) 91 days: 20,423. 0 million meticais; (ii) 182 days: 23,125. 0 million meticais; and (iii) 364 days: 57,845. 0 million meticais. In terms of concentration, although the 364-day period remains the most preferred by commercial banks with 57% of the overall value, there is an upward trend in terms of preference for other maturities, rising to 23% (182 days) and 20% (91 days), respectively.

[2] Taking into account the change in the regime for constituting reserve requirements (daily to medium), with effect from July 7, 2017, the bank's liquidity is reported in terms of average in the period of constitution, as well as the position on the day of holding the MPC.

Chart 2: Portfolio Balance of Treasury Bills

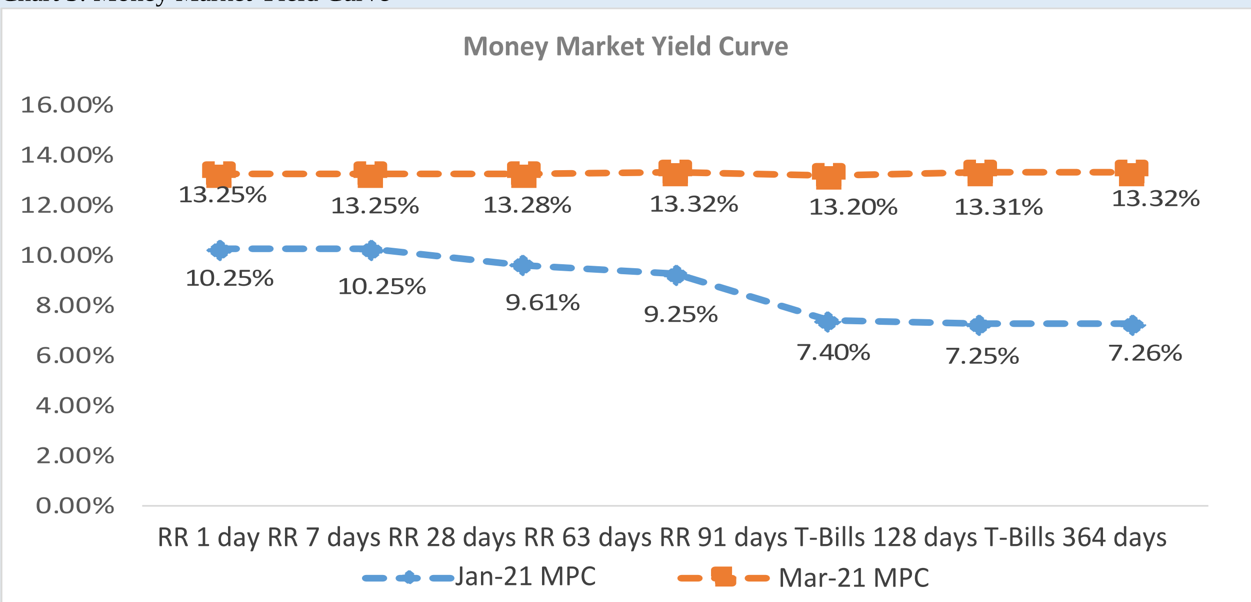


Source: BM

V. MMI Interest Rates' Developments

MMI interest rates increased in line with the upward adjustment of the monetary policy interest rate, MIMO rate, by 300 bp. Indeed, the results of the last auction of the reverse repo and primary issuance of Treasury Bills, carried out before the March 2021 MPC, show that the interest rates of the BM intervention instruments in the MMI increased between 300 and 606 bp for maturities of 1 to 364 days. The money market yield curve tends to be positive compared to the January MPC, showing a substantial change in Market Operator expectations.

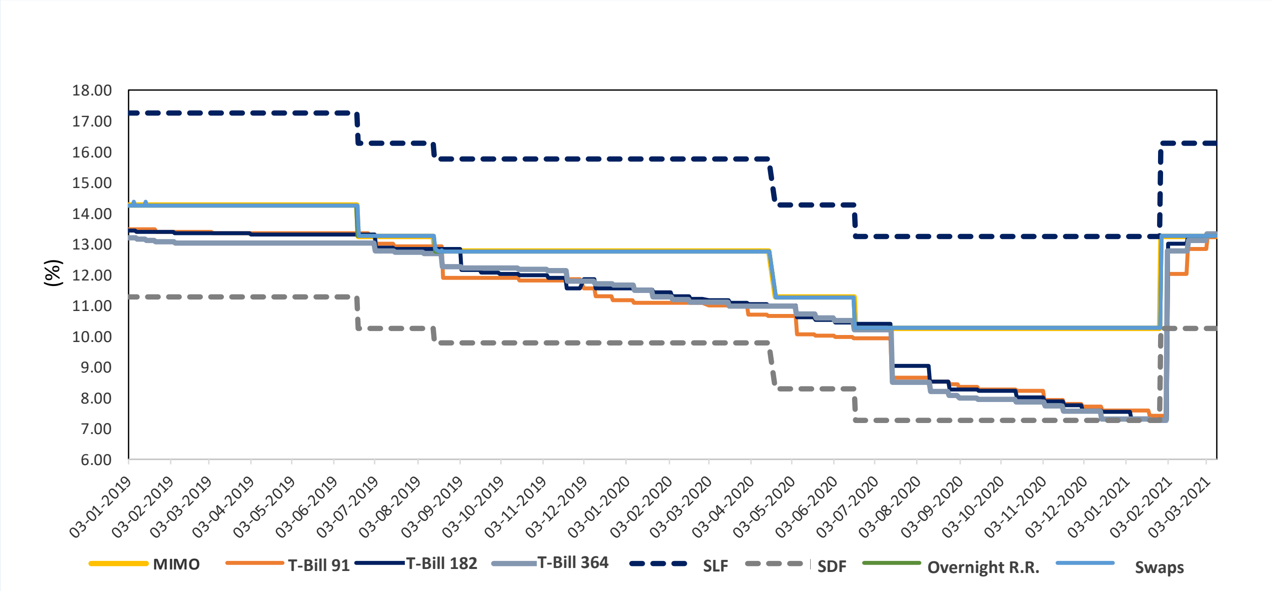
Chart 3: Money Market Yield Curve



Source: BM

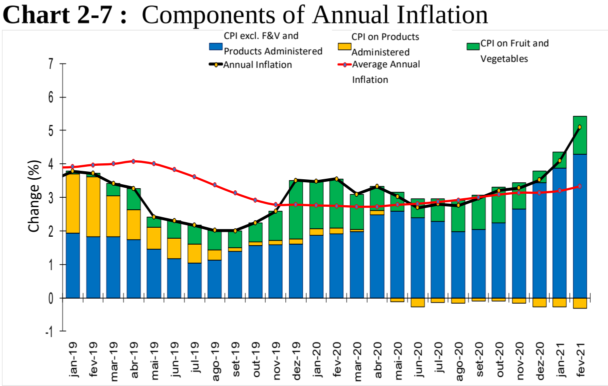
Interest rates in the interbank segment also showed an upward movement, in line with the MIMO rate rise. In fact, the interest rate on liquidity exchange operations between banks increased by 300 bp, remaining within the corridor of the SLF and SDF rates - Chart 4.

Chart 4: Interbank Money Market Interest Rates.



Source: BM

Chart 2-7 : Components of Annual Inflation



Source: INE / BM

Table 2-7 : Core Inflation - Mozambique (Annual Change %)

	oct-20	nov-20	dec-20	jan-21	feb-21
CPI	**3.20**	**3.27**	**3.52**	**4.09**	**5.10**
Food	**8.10**	**8.18**	**8.03**	**9.14**	**11.51**
Cereals and derivatives	4.19	4.68	5.92	7.52	7.75
Fruit and Vegetables	15.19	10.61	3.31	5.83	13.57
Administered	**-0.43**	**-0.76**	**-1.18**	**-1.25**	**-1.47**
Liquid Fuels	-4.04	-5.06	-6.36	-6.36	-6.36
CPI x F&V	**2.34**	**2.71**	**3.54**	**3.91**	**4.30**
CPI x Admin.	**4.26**	**4.44**	**4.87**	**5.59**	**6.95**
CPI x Comb.	**3.91**	**4.03**	**4.41**	**4.94**	**5.69**
CPI x F&V and Admin.	**3.23**	**3.81**	**5.05**	**5.55**	**6.13**

Source: INE

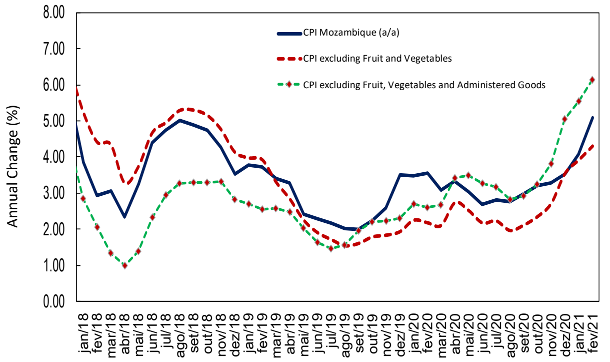
II.2. Recent Developments in Inflation

The effect of weather shocks and the depreciation of Metical led to a noticeable increase in prices in February. However, in the short term less aggravation is expected.

Mozambique's annual inflation, measured by the change in Mozambique's Consumer Price Index (CPI), accelerated from 4.09% in January to 5.10% in February. Also, annual average inflation maintained its upward trend, rising to 3.33% in February, after 3.19% in the previous month (Chart 2-7).

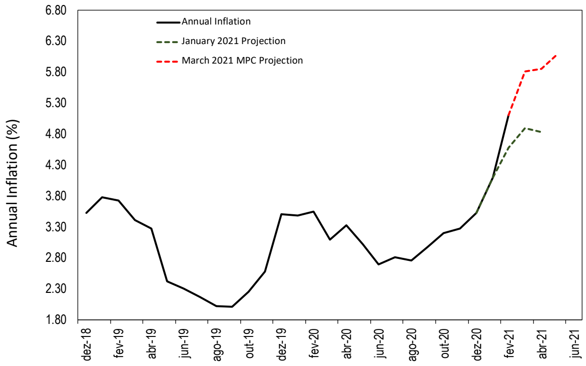
In terms of components, the acceleration of annual inflation is mainly explained by the increase in prices of the food class, highlighting the increase in the cost of fruit and vegetables and cereals and derivatives, reflecting the loss of domestic production of these products, due to the effect of cyclones and intense rains (central and southern regions) that flooded the production fields and hindered the movement of people and goods (Table 2-7).

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



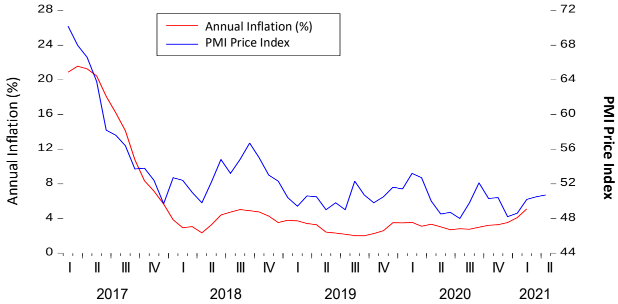
Source: INE

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



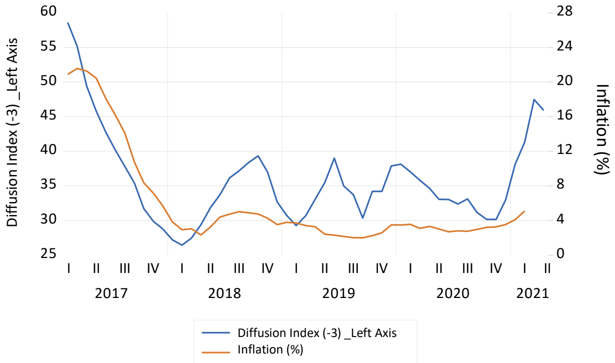
Source: BM

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



Source: BM/ HIS, Markit and INE

Chart 2-11: Diffusion Index and Annual Inflation



The accelerating trend in food inflation was mitigated by the reduction in the prices of products administered, favored by the stability of the prices of liquid fuels in the country (Table 2-7, Chart 2-7).

Meanwhile, core inflation accelerated to a lesser extent. Core inflation, which excludes the prices of goods and services administered and fruit and vegetables, also accelerated, but to a lesser extent compared to the general inflation dynamics between December/2020 and February, in line with what was expected (Table 2-7 and Chart 2-8).

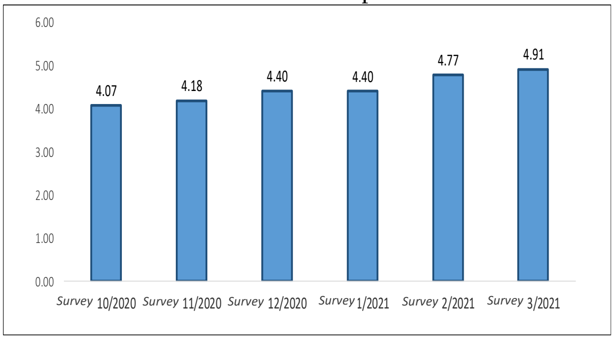
The outlook for the short-term points to a lower acceleration in inflation. The forecast of price increases, although at a slower pace, is supported by the following factors: (i) lower domestic supply of food products; (ii) acceleration of the cost of transportation/freight of goods and the prices of imported food goods; and (iii) possible adjustment of school fees in the face of the return of hands-on classes, mitigated by the trend towards appreciation of the Metical against the US Dollar (Chart 2-9).

For the same period, forward indicators of price developments, such as the Diffusion Index and the Purchasing Managers Index (PMI), confirm the trend of accelerating inflation in the coming months (Chart 2-10 and 2-11).

By the end of the current year, economic agents surveyed in March expect inflation to be 4.91% in December/2021, which means a slight acceleration compared to that observed in 2020 (Chart 2-12).

Source: BM/INE

Chart 2-12: Annual Inflation Expectations

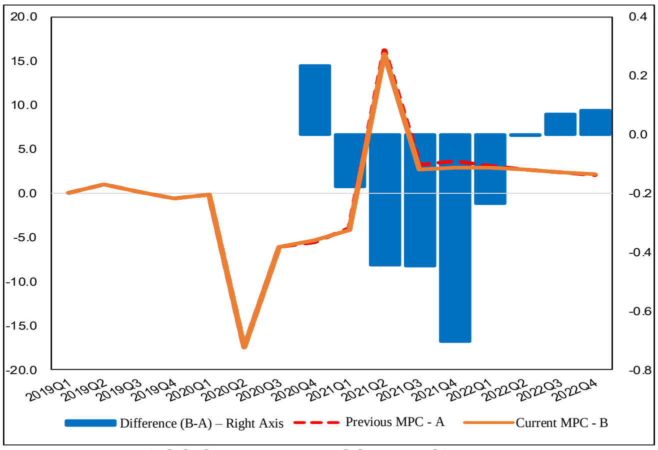


Source: BM

Chapter III: Medium-Term Inflation and Economic Activity Forecasts

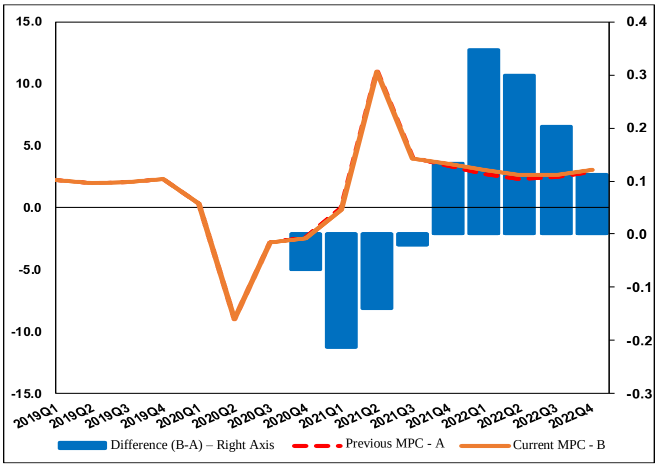
Inflation forecasts have been revised downward, to a single digit. For the short and medium term, a smaller acceleration in general inflation is expected, mainly reflecting the current Metical trend appreciation as a result of the measures taken at the last MPC meeting, in a context of weak economic activity. Regarding economic activity, prospects for a sluggish recovery in 2021 remain, supported by the likely recovery of external demand, due to the progress in vaccinations, the adoption of fiscal stimulus packages and the progressive easing of the measures imposed under COVID-19. At the domestic level, the gradual recovery in the economy is expected in the face of the progress in containing the spread of COVID-19, in a context of implementation of projects in the Rovuma Basin. Given this macroeconomic framework and the risks and uncertainties associated with the inflation projections, the MPC decided to maintain the MIMO rate at 13.25%.

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



Source: GPMN (Global Projection Model Network) / BM

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



Source: GPMN / BM

3.1. External Assumptions for Inflation Projections[3]

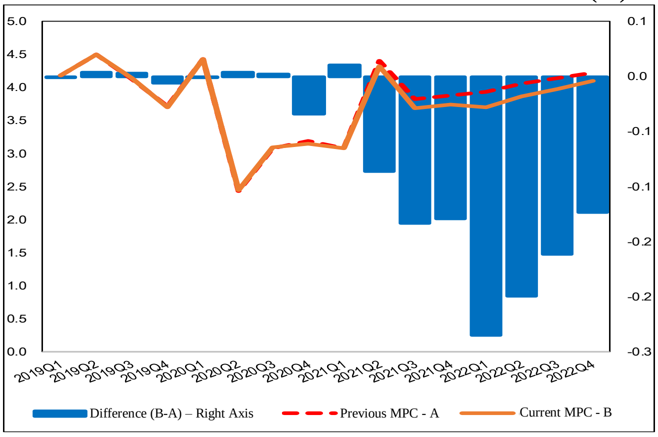
Downward revision of South Africa's growth forecasts and maintenance of US GDP growth forecasts in 2021. Regarding the January 2021 MPC, the projections indicate a downward revision in South Africa's economic activity growth from 4.8% to 4.3%, and the maintenance of the US GDP growth prospects at 4.6% (Charts 3-1 and 3-2).

Slight downward revision of the inflation outlook for South Africa and upward revision for the US, for 2021. When compared to the January MPC, the inflation outlook for South Africa was revised slightly down from 3.8% to 3.7% (within the 3-6% target), while for the US, the inflation outlook was revised up from 2.4% to 2.5%, against the 2.0% target. For the year 2022, the inflation projections were revised downwards, from 4.1% to 3.9%, and from 2.3% to 2.2%, for South Africa and the USA, respectively (Charts 3-3 and 3-4).

Upward revision of the outlook for food prices in the international market in 2021. Food price projections in the international market, as

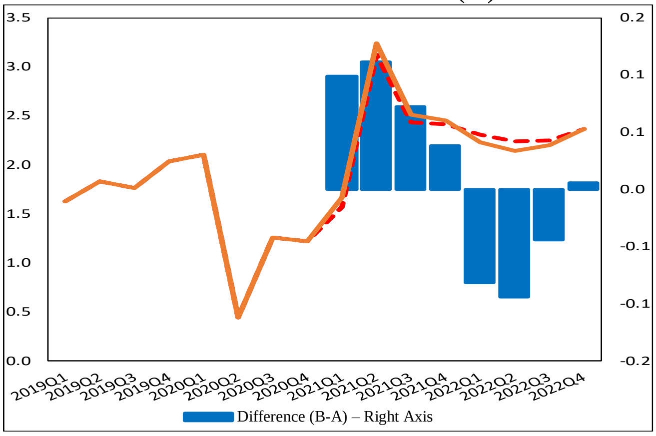
[3]Source: Global Projection Model Network (GPMN)

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



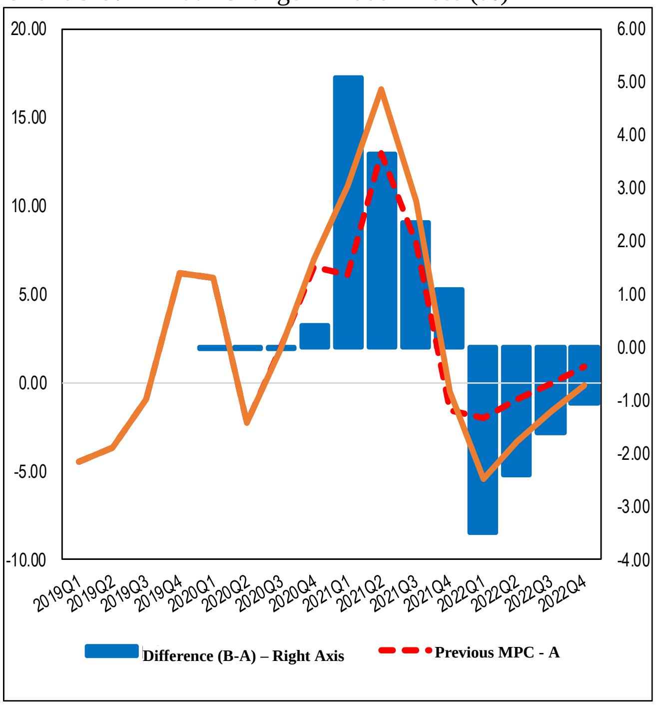
Source: GPMN / BM

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



Source: GPMN / BM

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



Source: GPMN / BM

measured by the Global Projection Model Network (GPMN) price index, were revised upwards for 2021, from an annual change of 6.3% to 9.4%, and downwards for 2022, from -0.5% to -2.7% (Chart 3-5). The upward revision of the projections of food prices on the international market in 2021, reflects high demand from China, supply shocks due to drought in South America and increased tariff on the export of wheat by Russia.

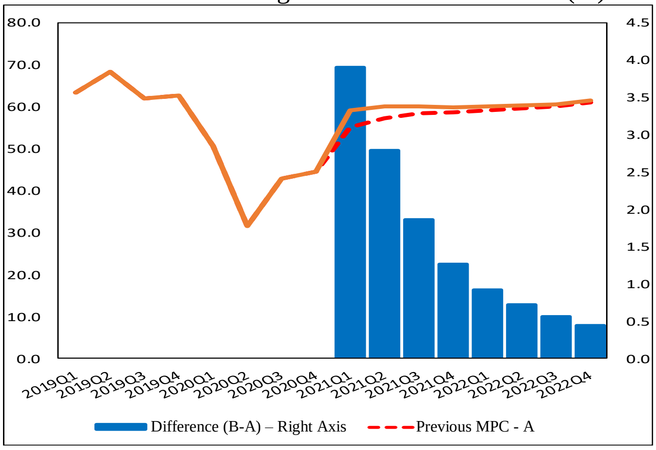
Slight upward revision of the oil barrel price in the international market in 2021 and 2022. In the latest GPMN projections, the oil price was revised higher, reflecting production cuts by OPEC+, added to an optimism in the recovery of global demand for oil, associated with the approval of the fiscal stimulus package in the US (Chart 3-6).

3.1. Internal Assumptions

Outlook for administered goods prices adjustments in 2021 remain. For 2021, the prospects of lifting some measures adopted by the government to mitigate the effects of COVID-19 and its consequent decompression remain, in a context of recovery in the price of oil in the international market. Meanwhile, extended VAT exemption on essential goods until 2023 could help to smooth out administratively defined price adjustments.

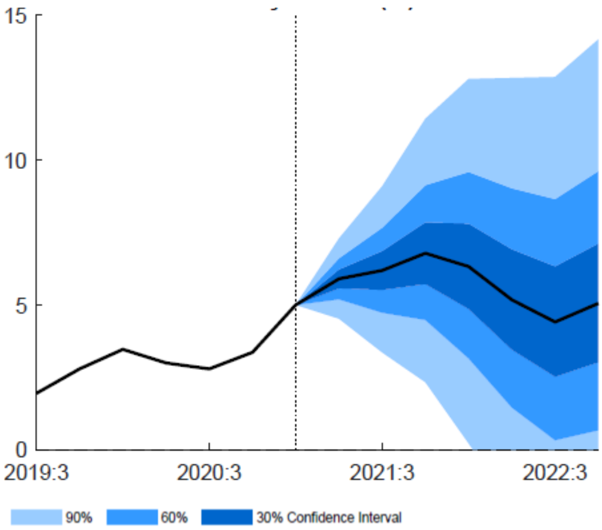
Prospects for slowdown exchange rate pressure in the medium term. Since the beginning of March, the demand for foreign exchange has been fully satisfied as a result of a greater fluidity in the foreign exchange market, with Metical registering a trend towards appreciation against the US Dollar. For the medium term, a lower exchange rate pressure is expected to reflect the recent exchange rate dynamics as well as the prospects for investment

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



Source: GPMN / BM

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



Source: BM

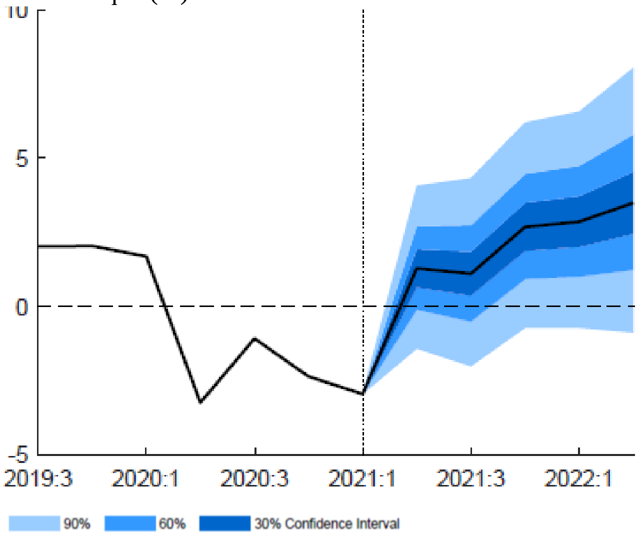
inflows associated with natural gas exploration projects.

The prospects for greater pressure on public spending remain. The prospects of an increase in the public spending to cope with the country's challenges continues to justify the worsening of the budget deficit. Among the factors for a higher fiscal pressure, the key are the acquisition and logistics for the administration of the vaccine against COVID-19, the mitigation of the socio-economic impact of climate shocks, as well as the expenses arising from the situation of military instability in the central and northern areas of the country..

3.2. Forecast Results

Inflation forecasts have been revised downward, to a single digit. For the short and medium term, it is expected a lower price increase (Chart 3-7), mainly reflecting the current Metical appreciation trend, in a context of weak domestic demand.

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



Source: BM

Forecasts of a timid recovery in economic activity in 2021 remain. Following a contraction of Gross Domestic Product by 1.3%, in 2020, a slight growth is expected in 2021, supported by the likely recovery of external demand, as a result of the progress in the vaccinations, the adoption of fiscal stimulus packages and the progressive easing of the measures imposed under COVID-19. At the domestic level, a gradual recovery in the economy is expected in the face of the progress in containing the spread of COVID-19, in a context of implementation of projects in the Rovuma Basin. (Chart 3-8).

3.3. Monetary Policy Decision

The Monetary Policy Committee (MPC) of the Banco de Moçambique decided to keep unchanged its policy rate, MIMO rate, at 13.25%. The decision is justified by the prevalence of high risks and uncertainties, despite the downward revision in the inflation forecasts for the short and medium term, largely reflecting the effects of the January 2021's MPC meeting decisions.

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

The MPC will continue to monitor the domestic and international macroeconomic environment, as well as the prevailing risks, and will not hesitate take the necessary corrective measures before the next ordinary meeting scheduled for May 19, 2021.