MONETARY POLICY COMMITEE

COMMUNIQUÉ N. º 04/2018

Maputo, 30 August 2018

The Monetary Policy Committee (MPC) of the Bank of Mozambique, gathered today, has decided to cut the key lending rate, MIMO rate, by 75 basis points to 15,00 per cent.

Additionally, in view of the volatility observed in the foreign exchange market, it increased the Reserve Requirement ratio for liabilities expressed in foreign currency by 500 basis points to 27.00% while keeping the liabilities expressed in domestic currency at 14.00% as well as the Standing Lending Facility (SLF) rate at 18.00%, and the Standing Deposit Facility at 12.00 per cent.

The assessment of the short- and medium-term outlook indicates the maintenance of single-digit inflation in a context where there is no evidence that the current level of aggregate demand could create significant price pressures, thus justifying a reduction in the MIMO rate. The MPC considers that the current stance of monetary policy is appropriate in its contribution to the preservation of macroeconomic stability.

Despite the slight acceleration verified in July, annual inflation remains low. Information related to July 2018 indicates that annual inflation, as measured by the variation of the Consumer Price Index (CPI) of Mozambique, stood at 4.73%, after 4.40% in the previous month, and 16.17%, in July 2017. This trend reflects the increases in administered prices in a scenario in which the less pronounced increase in food prices contributes to slow down inflation

GDP continues to grow in a diversified and moderate manner. In the second quarter of 2018, Gross Domestic Product (GDP) grew 3.4% year-on-year, against 3.2% in the previous quarter and 3.8% in the same period of 2017. The sectors of agriculture, mining industry, social services and public administration were decisive for the performance of economic activity in the period under review. However, the decline in electricity and water services, construction, hotels and restaurants have all contributed to curbing economic growth.

Businessmen expectations remain positive. The economic climate index, leading indicator of economic activity, rose favorably for the third consecutive quarter to reflect the increased confidence of businessmen in transport and trade sectors, supplanting the pessimism of industrial and construction businessmen.

Domestic public debt declined slightly in view of the stagnation of credit to the private sector. In August, the balance of domestic public debt incurred with recourse to

Treasury Bills, Treasury Bonds and advances from Bank of Mozambique totaled MZN 105,267 million (equivalent to 12.0% of GDP), a slight decrease when compared to the balance registered in June of MZN 105,931 million (12,1% of GDP). The above amounts do not take into account other amounts of domestic public debt, such as mutual and leasing contracts, as well as past due liabilities. On the other hand, taking as reference July data, credit to the private sector remains stagnant

Metical shows a strong volatility vis-a-vis the main currencies in the Mozambican exchange market, tending to weaken against the US dollar in recent weeks. After recording an average quotation of MZN 59,38 on 15 June, the average exchange rate applied by commercial banks to the public appreciated to MZN 58,07, on 10 August, and then depreciated to MZN 60,05 at the close of business on 29 August. Meanwhile, during the same period, the South African Rand quotation reduced from MZN 4,49 to MZN 4,24.

Payment of specialized services abroad for natural gas project has led to a worsening of the current account deficit. Provisional data for the first half of 2018 indicate that the current account deficit increased by USD 414 million to USD 1,596 million when compared to the same period of 2017. This was mainly a result of the increase in the import of specialized and financial services within the scope of implementation of the Rovuma basin natural gas project, in view of a slight deterioration of the trade balance resulting from increased imports of machinery and intermediate consumer goods.

Payment of the external public debt contributed to the use of international reserves. Up to 24 August, the service of the external public debt paid ascended to USD 220 million, thus contributing for the use of Net International Reserves (NIR) reduced by USD 67 million. Nevertheless, the balance of the Gross International Reserves (GIR) is at comfortable levels (USD 3,156 million), allowing for the coverage of about 7.0 months of imports of goods and services, excluding major projects transactions.

Economic conditions continue to favor the projection of low and stable inflation in the short and medium term, but several risks remain that require prudence in the conduct of monetary policy.

After considering the direct and indirect effects of the recent upward revision of prices of administered goods and services, particularly for electricity and water, MPC projections continue to point to one-digit inflation over the next eight quarters, composing the current projection horizon.

Among the risks associated with these projections, it remains, internally, those associated to the domestic debt sustainability as well as the uncertainties regarding the evolution of the prices of administered goods. The external component highlights the risks associated with the commercial and geopolitical tension between the major economies, as well as the volatility of the US dollar and international commodity prices, with an emphasis on the price of oil.

Considering the short and medium-term inflation outlook and the underlying risks, the MPC has decided to:

- ✓ Cut, with immediate effect, the monetary policy interest rate, MIMO rate, by 75 basis points, to 15,00 %;
- ✓ Keep the Standing Lending Facility (SLF) at 18,00%;
- ✓ Keep the interest rate for the Standing Deposit Facility (SDF) at 12,00 %;
- ✓ Keep the reserve requirement for liabilities in domestic currency at 14.0%;
- ✓ Increase, with effect from the date of buildup starting on September 7, the reserve requirement for liabilities in foreign currency by 500 basis points to 27,00%.

The MPC will continue to monitor economic and financial indicators and risk factors and may take the necessary corrective measures before the next meeting, scheduled for 22 October 2018.

Rogério Lucas Zandamela
Governor