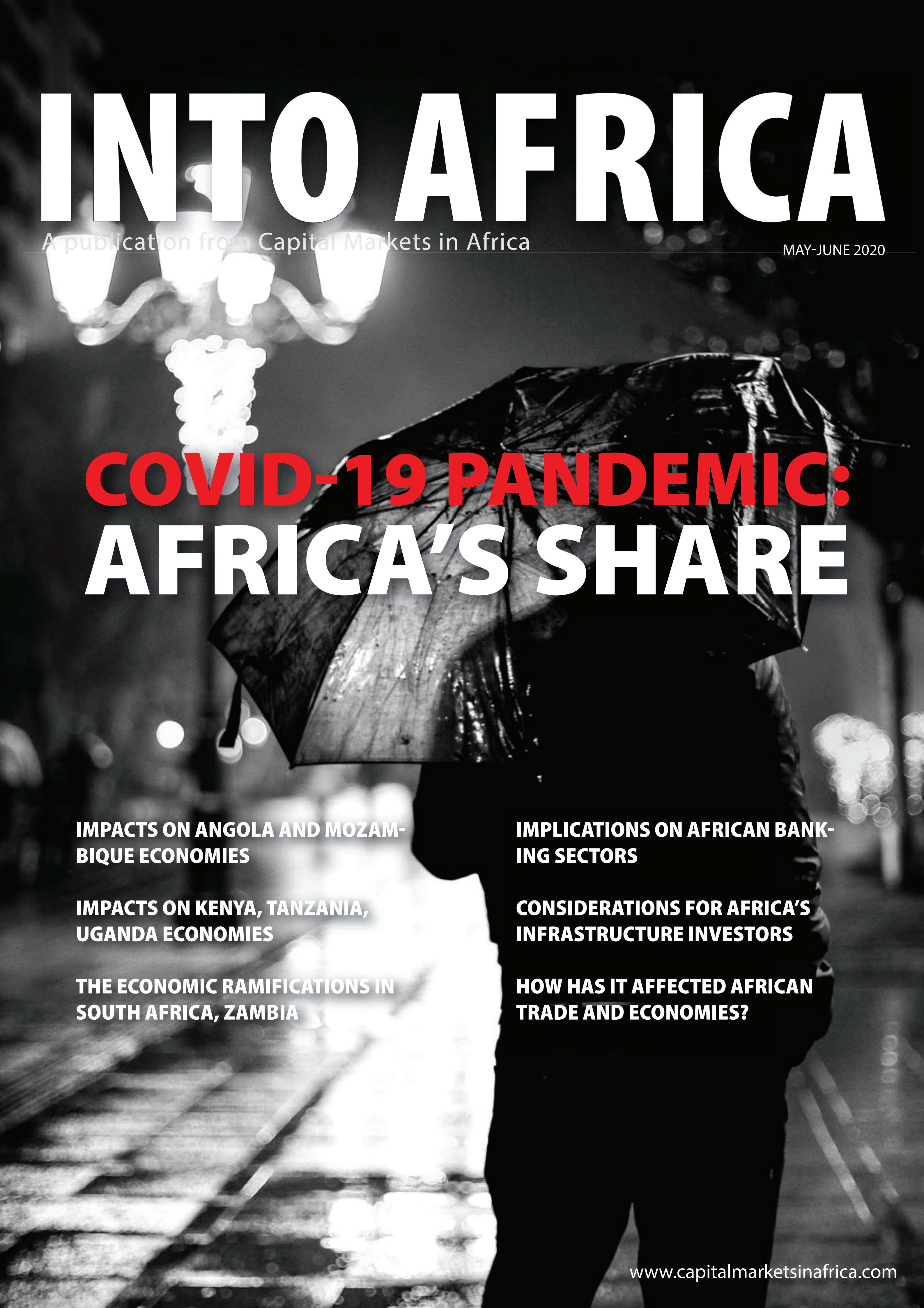

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COVID-19 PANDEMIC

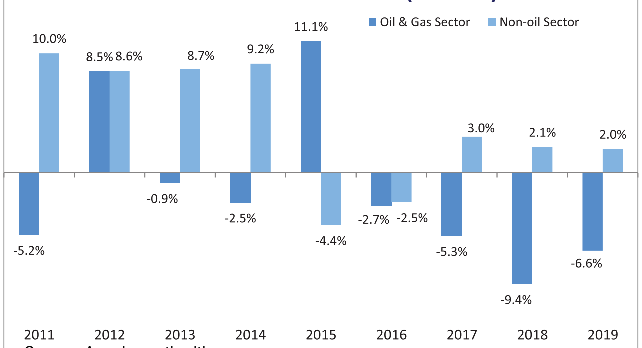
IMPACTS ON ANGOLA AND MOZAMBIQUE ECONOMIES

By **Tiago Dionisio,** Chief Economist, Eaglestone Advisory Portugal

ANGOLA: DOUBLE WHAMMY OF LOW OIL PRICES AND COVID-19

Economic activity in Angola contracted for a fourth straight year in 2019 mainly due to a marked decline in oil and gas production that reflects recent under-investment in the sector following the sharp fall in oil prices at the end of 2014. Current estimates indicate that real GDP contracted 0.9% in 2019 after falling 2% in the previous year. In particular, activity in the oil and gas sector continued to see a material decline (estimated at 6.6% YoY after already tumbling 9.4% in 2018) while growth in the non-oil sector remained quite modest (forecast of 2% vs. 2.1% in the previous year).

REAL GDP GROWTH (2011-19)

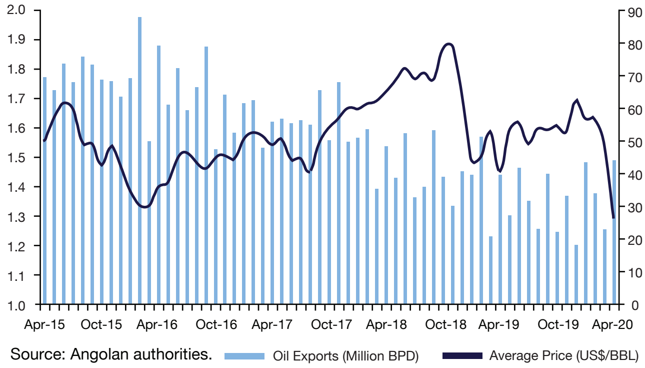


Source: Angolan authorities.

Angola remains highly dependent on the oil sector, as efforts to improve economic diversification are taking time to show a more significant impact. The latest figures show that the oil sector still accounted for more than 30% of the country's GDP, 96% of its exports (two-thirds of these going to China) and 60% of government proceeds last year. As a result, the return of a lower crude price environment in recent months, if prolonged, will have huge implications for public receipts, external accounts and the Angolan economy in general. On top of this, the oil production cut agreement signed by OPEC and its partners in April 2020 means that Angola will have to reduce its supply until April 2022 from already relatively low levels.

Meanwhile, the Covid-19 pandemic poses yet another major threat to Angola. Although the country faces relatively low infection rates, the pandemic could aggravate its tight situation in terms of public finances and put additional strain on its rather poor health infrastructures. Angola's high poverty levels

ANGOLAN OIL EXPORTS AND AVERAGE CRUDE PRICE



Source: Angolan authorities.

(estimated at 40.6% of the population) and unemployment rate (31.8% in Q4 2019) are also at risk of deteriorating further, putting more pressure on household disposable income and affecting consumer spending while widening inequality.

Overall, a double whammy of low oil prices and Covid-19 means that Angola will (almost) certainly remain in a recession this year, with the risk of real GDP contracting another 3-4%. As pressure on the country's fiscal and external accounts persist, the central bank is unlikely to be able to lower interest rates anytime soon, even if this was a key measure adopted by most central banks to attenuate the impact from the pandemic.

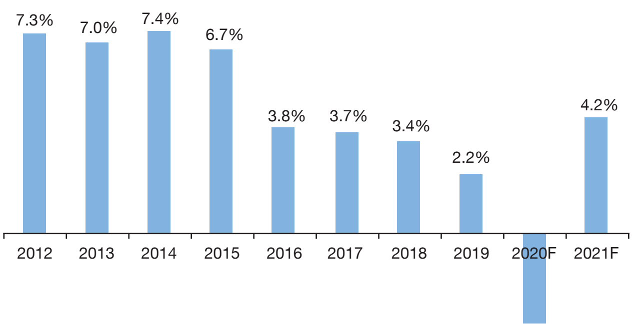
The government is expected to announce a revised budget for 2020 in the next few weeks where it is anticipated to lower its oil price assumption to a level no greater than US$ 35 per barrel (vs. US$ 55 per barrel in the initial budget). Nevertheless, and despite the efforts to cut (and reprioritize) expenditures and the already announced utilization of US$ 1.5 billion from the Sovereign Wealth Fund to help finance the budget, the government is likely to record a fiscal deficit in 2020. This compares with a fiscal surplus of 1.2% of GDP initially targeted for this year and the positive performance recorded in 2018-19.

Angola's long-term growth outlook will depend on the implementation of structural reforms that remain critical to reduce the country's dependency on the oil sector and the size of the public sector. These reforms, which have the backing of the IMF and also include greater exchange rate liberalization, will be crucial to accelerate growth in the non-oil sector as well as improve governance and the business environment in order to attract more foreign direct investment to the country.

MOZAMBIQUE: RECESSION DUE TO PANDEMIC SHOULD BE SHORT-LIVED

Mozambique is expected to enter a recession in 2020, with the government estimating real GDP to contract 3.3% this year (vs. a previous growth forecast of 2.2%) as a result of the impact that Covid-19 will have on the local economy. Significant disruptions are already impacting the services, transport, agriculture, manufacturing and communications sectors while a much worse external environment is affecting export-oriented sectors, such as mining. Although Mozambique performed relatively well in the last global crisis a decade ago (growing at 6-7% annually), it looks like this time it will be different. The country's main trading partners (South Africa, India, China and the Euro area) are all being severely affected by the pandemic while the prices of its main exports (aluminium and coal) have plummeted, putting additional pressure on already fragile external accounts.

REAL GDP GROWTH (2012-21F)



Source: Mozambican authorities and Eaglestone Securities.

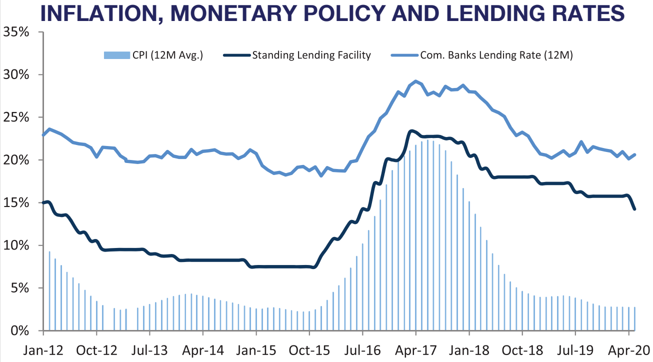
The announcement by US oil major ExxonMobil that it was postponing (without deadline) the final investment decision on its LNG project in the Rovuma Basin (in the north of the country) due to the latest crash in energy prices is also likely to affect economic activity while the escalation of military tensions in the northern and central parts of the country could also limit its growth trajectory in 2020.

The 2020 budget figures also reflect the impact of Covid-19 in the country's public accounts. In particular, the government projects a double-digit decline in public revenues this year (mostly from much lower tax receipts), which, coupled with another strong increase in expenditures (related to higher spending on goods and services and debt payments), will translate into a wider fiscal gap. The budget deficit is expected to reach 7.7% of GDP (vs. 2.1% in 2019) even after including a significant improvement in grants following an abnormally low contribution in recent years.

The local authorities have taken several measures to try to mitigate the impact of Covid-19, including increasing health spending, strengthen social protection to the most vulnerable and support micro-businesses and SMEs. Mozambique will see the return of direct budget support after this type of financial assistance was interrupted in the last three years (2017-19) in the aftermath of the revelation of previously undisclosed debts in April 2016. The IMF has already injected US$ 309 million in direct financial support to the budget to help mitigate the impact of Covid-19. In total, the country asked for US$ 700 million from international partners to cover the budget deficit, with US$ 400 million going to the social area. Several other partners have also expressed their intention to support the country, including the World Bank, African Development Bank and the European Union.

The Bank of Mozambique also lowered its main policy interest rates and provided additional liquidity in both local and foreign currencies to market participants. Specifically, the central bank (1) reduced reserve requirements in local and foreign currencies, (2) announced a credit line of US$ 500 million in foreign currency for the banking sector and (3) waived the requirement for local banks to build extra provisions in case customers affected by the pandemic need to restructure their loans.

INFLATION, MONETARY POLICY AND LENDING RATES



Source: Mozambican authorities.

In conclusion, Mozambique is expected to see some debt service relief from multilaterals and private creditors in the next few months. These are positive news, as it will provide a short-term safety net and allow the local authorities to allocate much-needed funds to combat several areas of the economy more affected by Covid-19. However, these challenging times must not put in jeopardy the progress that the country has recently made in restoring macroeconomic stability and, more importantly, they must not deviate attentions from the need to bring public debt (already exceeding 100% of GDP) to more sustainable levels over the medium-term.