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REPUBLIC OF MOZAMBIQUE

July 2013

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION, SIXTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT, REQUEST FOR A THREE-YEAR POLICY SUPPORT INSTRUMENT AND CANCELLATION OF CURRENT POLICY SUPPORT INSTRUMENT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2013 Article IV consultation with Mozambique, the following documents have been released and are included in this package:

- **Staff Report** for the 2013 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 8, 2013, with the officials of Mozambique on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 10, 2013. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- **Informational Annex** prepared by the IMF.
- **Public Information Notice** (PIN) and **Press Release** summarizing the views of the Executive Board as expressed during its June 24, 2013 discussion of the staff report that concluded the Article IV consultation/Review.
- **Statement by the Executive Director** for the Republic of Mozambique.

The documents listed below have been or will be separately released.

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

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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KEY ISSUES

Context, outlook, and risks. Macroeconomic performance remains strong and program implementation satisfactory. Economic growth continues to be broad-based, with a boom in mining due to the start-up of coal production and exports.

Fiscal policy and debt sustainability. The revised budget is in line with the medium-term fiscal strategy, while addressing the impact of severe floods in early 2013. The authorities' fiscal strategy envisages a gradual move to domestic primary surpluses while keeping external borrowing within the bounds of debt sustainability against the backdrop of an increasing contribution of mineral resources to the economy.

External sustainability. The external current account deficit is and will remain wide in the medium term, funded by large FDI and privately-financed mining operations. International reserves are adequate though need to keep up with the steady growth in the economy and imports beyond mining activities. The DSA update moves Mozambique from low to moderate risk of debt distress, reflecting the new potential and risks implied by the exploration and prospective liquefaction of natural gas.

Program issues. Staff recommends waivers for nonobservance of the end-December 2012 assessment criteria on net credit to the government and reserve money, and completion of the sixth PSI review. Staff supports the authorities' request for a new three-year PSI to maintain macroeconomic stability and target poverty reduction through: (i) capacity building in economic management; (ii) more focused priority spending; (iii) enhanced debt management; (iv) financial sector efficiency; and (v) improvements in the business climate and competitiveness.

Article IV. Discussions focused on ensuring sustainable macroeconomic policies and inclusive growth over the medium term, while strengthening natural resource management. The last Article IV consultation was completed in June 2011.

Approved By
David Robinson and Vivek Arora

A staff team comprising Ms. Ross (head), Messrs. Gitton, Xiao, Xiong (all AFR), Perone (SPR), and Melina (RES), visited Maputo during April 24–May 8, 2013. The mission met with Minister Chang (Finance), Cuereneia (Planning and Development), and other line ministers (Energy, Agriculture, Natural Resources, Industry and Trade, Women and Social Action), Bank of Mozambique Governor Gove, and other senior government officials. The mission also met with development partners, civil society, academia, and the private sector. It was assisted by Mr. Lledo (resident representative), Mr. Simione, and Ms. Palacio (resident representative office). Messrs. Conceição (OED), Revilla and Blanco Armas (World Bank) participated in some of the policy discussions.

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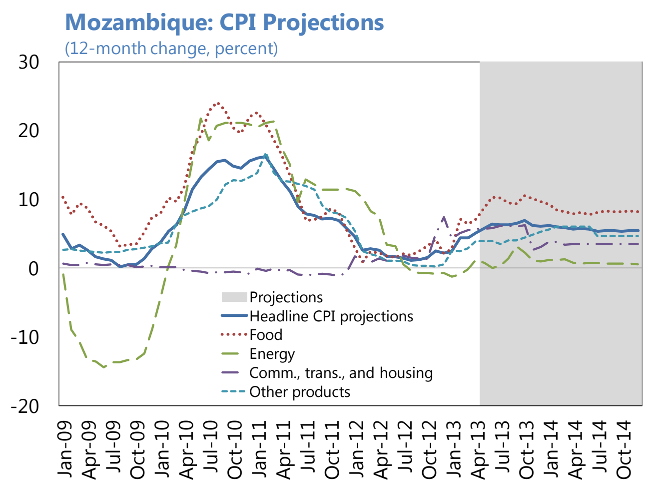
RECENT DEVELOPMENTS AND PROGRAM PERFORMANCE

A. Macroeconomic Developments

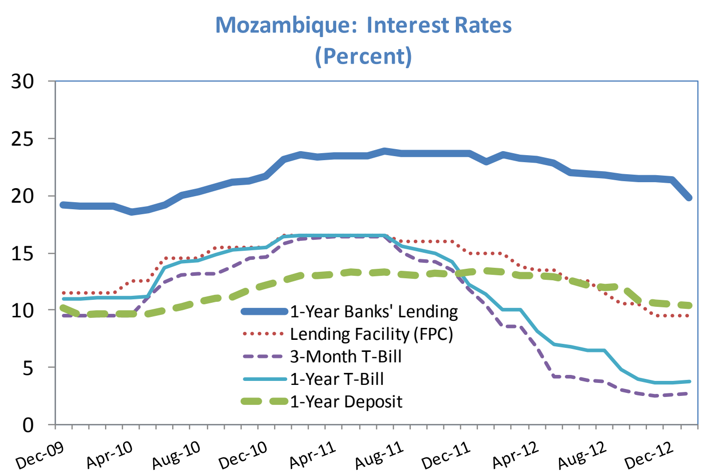
MEFP ¶2

1. **The Mozambican economy registered strong growth in 2012, but floods in early 2013 have diminished prospects slightly.** Preliminary data suggest that real GDP rose by 7.4 percent in 2012. This was broad-based and led by the start-up of coal production and exports, agriculture, construction and financial services. In early 2013, severe floods destroyed agricultural crops in the South and severely damaged infrastructure (roads, railways and the power transmission line to South Africa). Real GDP is nevertheless projected to grow by 7 percent in 2013 reflecting a further boost in coal exports with improvements in rail transport capacity and the implementation of other large infrastructure projects.

2. **Inflation remains moderate but food prices have risen recently due to the flood impact.** Inflation had come down rapidly in 2012, supported by lower-than-expected prices of imported food and stable administered prices (fuels, public transport, utilities). Year-on-year inflation fell to 2.2 percent in 2012, the lowest rate in SADC, but rose to 5.1 percent in April 2013 reflecting flood-related food price increases. Combined with the monetary easing since 2012, CPI inflation is projected to rise to about 6 percent by end-2013, in line with the authorities' medium-term objective.



3. **Mining operations dominate external sector developments.** The significant weakening of the external current account in 2012 was caused by a spike in imports of services, reflecting large investments in gas exploration, that were only partly compensated by the start-up of coal exports and a significant increase in traditional exports (by 16 percent). Foreign direct investment doubled in 2012 and related imports of services resulted in a current account deficit of 36 percent of GDP. While this reduced the import cover of international reserves, the authorities continued to accumulate reserves on the back of strong exports and capital inflows (FDI and foreign borrowing).



Source: Mozambican authorities

B. Monetary response

4. The growth of broad money and credit to the economy accelerated in 2012, though commercial banks' lending rates remain high. The Bank of Mozambique (BM) adopted a looser policy stance, lowering its policy lending rate eight times by a cumulative 6.5 percentage points since late 2011. M3 growth reached 29 percent while credit to the economy accelerated to 18 percent at end-2012, led by credit to households for consumer durables. Growth in lending to small and medium-sized enterprises (SMEs) is limited by banks' perception of a paucity of safe lending opportunities in the private sector. Despite some mopping up of liquidity in late 2012, the BM could not fully neutralize the effect of higher-than-programmed bank deposits at the central bank on reserve money. The assessment criterion was missed by Mt 1 billion or 3 percent of reserve money, which is a minor deviation relative to the large uncertainties affecting money demand. The corresponding indicative target for March 2013 was also exceeded (by Mt 1.6 billion or 4 percent of reserve money) against the backdrop of a weak cash return to the banking system in the post-flood period, and large accumulation of government deposits in commercial banks.

Program Performance

	Dec 2012 AC	Mar 2013 IT
Assessment Criteria		
Net credit to the government	not met	met
Stock of reserve money	not met	not met
Stock of net international reserves	met	not met
Nonconcessional external debt	met	met
Stock of short-term external public debt	met	met
External payments arrears	met	met
Indicative Targets		
Government revenue	not met	met
Priority spending	met	met

● met ▲ not met

5. Net international reserves (NIR) exceeded program targets in 2012, but fell back in early 2013. Reserve accumulation in 2012 exceeded the end-year target slightly and gross reserves reached $2.8 billion. However, in early 2013 flood-related lower exports and higher imports and delays in aid disbursements ($45 million against $194 million) resulted in a drawdown of NIR by about $0.3 billion to 3.8 months coverage of 2013 non-megaproject imports, below the end-March indicative target.

C. Fiscal response

6. Fiscal performance was largely consistent with the program in 2012, notwithstanding higher capital spending and some overrun in bank credit to the government late in the year. Revenue was slightly below the indicative target as one-off capital gains tax receipts offset therevenue impact of lower-than-expected inflation and transition problems in customs with the introduction of a single trade window in the second quarter. However, an overrun in grant-financed investment and spending on special programs late in the year led the overall deficit and government domestic borrowing (NCG) to exceed their end-year targets. The authorities took some corrective action to tighten expenditure control. Priority spending exceeded its indicative target at end-2012, reflecting the authorities' continued efforts to implement their poverty reduction strategy.

7. Fiscal performance in early 2013 reflected a number of different factors. The government restrained other current expenditure in favor of emergency spending on flood mitigation, but protected priority spending (March indicative target was met). It limited externally-financed capital spending when some donor budget support was delayed over governance concern[1] (generating a $150 million shortfall). Donor support should resume with the remedial actions being taken by the authorities. Fiscal revenue, boosted by large capital gains windfall receipts ($224 million), significantly exceeded the March indicative target. These factors combined to a much lower-than-programmed flow of NCG in the first quarter (target met).

D. Structural Reforms

8. The authorities continued their structural reform agenda and focused on debt management and financial stability and development (see Table 9). The structural benchmark on adopting an Annual Domestic Borrowing Plan was met on time in January. The submission to the Council of Ministers of the draft Financial Sector Development Strategy (FSDS) was delayed to March and swiftly approved thereafter. The Financial Sector Contingency Plan was approved by the BM in early April and implementation is starting.

OUTLOOK AND RISKS

9. Mozambique's medium-term growth outlook remains strong. Growth across sectors is projected to remain vigorous at 8.5 percent in 2014, with strong medium-term stimuli provided by a rebound in agriculture (reflecting both productivity increases and an expansion of arable land under cultivation) and infrastructure investments and the start of construction of a gas liquefaction plant (LNG). Inflation is expected to remain contained in the absence of major food or fuel price shocks and continued prudent monetary policy.

MEFP ¶5

10. The external outlook reflects the need for massive investments in the next few years to commercialize natural gas reserves. The external current account deficit is projected at around 40 percent of GDP during the initial 4-5 year construction phase of the LNG plant starting in 2014, financed largely by FDI and private commercial borrowing. As improvements in rail transport capacity allow more coal exports over time, and once LNG exports start around 2020, exports would rise sharply and the current account deficit would decline. With the completion of the LNG plant likely by 2023, imports should also see a steep decline, further lowering the external current account deficit to more sustainable levels.

11. Risks to this outlook stem from both the global and domestic environments (see Box 1). Mozambique has been relatively isolated from the global recession as its interconnections with neighboring countries are mainly of a logistical nature for hinterland countries. Its trade with the

[1] Investigations are underway into suspected timber smuggling from Mozambique to China, and (limited) fraudulent salary payments in the Ministry of Education.

region is centered on South Africa, and exports (mainly electricity) and imports (food and manufactured goods) have been fairly steady and not shown significant spillovers. While Portuguese banks dominate the Mozambican banking sector, they are funded locally and operations are largely separated from developments in Portugal. Nonetheless, Mozambique is exposed to risks of climate disasters, commodity price shocks for its major export or import commodities (coal, gas, fuel), and the impact of a decline in donor funding. Domestic risks include delays in upgrading transport infrastructure, especially railways and ports, electricity supply constraints, and policy slippages in the context of the November 2013 municipal and October 2014 presidential elections. Nevertheless, there are strong mitigating factors: financial support from BRICs is increasing, prospects for coal production and exports are bright, as well as for continued strong FDI inflows in several megaprojects, including LNG development.

12. The authorities broadly agreed with the staff's assessment of the outlook and associated risks and policy options. While acknowledging that the impact of high economic growth on poverty reduction had been limited in recent years, they emphasized that poverty reduction and more inclusive growth were the main pillars of their economic strategy. Their strategy includes: continued macroeconomic stability; faster progress in reforms to enhance competitiveness and improve the business environment; and continued high investment in social sectors (health, education and job training) and infrastructure (transport, water and electricity).

Box 1. Mozambique: Risk Assessment Matrix[1]

Nature/Source of Risk	Likelihood in the next three years (L, M, H)	Expected impact on the economy (L, M, H)	Policy Response
Protracted period of slower European growth	M	L	Accelerate policies to diversify exports and structural reforms to boost competitiveness
Global commodity price weakening for Mozambican exports (especially coal and gas)	L	M	Exchange rate flexibility as first line of defense, coupled with monetary easing (while being vigilant to second round effects), and automatic stabilizers
Significant aid decline	M	H	Continue to seek donor support and maintain consistent policies
Climate disasters	M	H	Accelerate prevention and risk management policies. Automatic stabilizers and targeted spending initiatives. Supportive monetary and exchange rate policies
Financial crisis stemming from a weakening of dominant Portuguese-owned banks	L	H	Strengthen financial supervision, including stress-testing, and implement the financial contingency plan
Policy slippages in run-up to elections	M	M	Maintain macroeconomic stability and accelerate structural reforms (business climate, financial development)
Social unrest in connection with lower than expected benefits from natural resource management	M	M	Foster inclusive growth and intensify public communication on the long term social benefits of natural resources
Infrastructure bottlenecks hampering exports and economic growth	H	H	Maintain high public investment and enhance project selection and financing consistent with debt sustainability
Excessive borrowing leading to unsustainable external public debt	M	H	Enhance debt management, project selection and assessment process

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline. The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with authorities.

ARTICLE IV DISCUSSIONS

13. *Discussions centered on the appropriate fiscal and monetary policies for 2013 and the medium term,* given *the strong foreign-financed investment stream and the need to facilitate credit to the economy in the context of emerging moderate inflationary pressures. Optimizing the benefits from the increasing contribution of the extractive industry to the economy was also at the core of discussions.*

14. The government's economic policies have been implemented in line with its medium-term agenda and were broadly consistent with Fund advice during the 2011 Article IV consultation. The authorities and the staff generally agreed on the appropriate macroeconomic policy stance and the focus of the structural reform agenda. These were consistent with the government's 2010–13 PSI-supported economic program focused on maintaining macroeconomic stability, promoting infrastructure investment, capacity building, and fostering inclusive growth. Progress toward these objectives has been good regarding macro-economic performance and the PSI-supported program is on track with all reviews completed on schedule. Mozambique has been declared compliant with the Extractive Industry Transparency Initiative (EITI) in October 2012. Capacity building is ongoing thanks to an extensive technical assistance program involving IFIs and donors.

15. The 2013 Article IV discussions focused on the development agenda and appropriate policy priorities to successfully transition to a resource-rich era. These include skillful medium-term management of the impact of developing coal and gas resources and high public investment spending on growth, external competitiveness and, through increased commercial borrowing, on debt sustainability and investment planning. These priorities are consistent with the government's 2010-2014 plan (*Plano Quinquenal do Governo*), its long-term vision described in the *Agenda 2025*, and are supporting the 2011-14 Poverty Reduction Strategy (*PARP*). All aim at maintaining macroeconomic stability, investing in infrastructure and social sectors, fostering inclusive growth, and building capacity in various areas.

A. Preparing for Natural Resource Management

16. *The authorities and staff discussed how to adapt macroeconomic management to the demands of a resource rich economy. Preliminary estimates suggest that coal and natural gas production could potentially boost growth by 2 percentage points annually during 2013-23. While fiscal revenues from megaprojects will remain moderate in the short and medium term, revenues could reach a quarter of total fiscal revenues in the longer run, mostly from the natural gas sector.*[2]

[2] See Appendix III.

MEFP ¶6, 24-29

17. The authorities and staff shared the view that while major public and private investment is necessary to realize the extractive industry's potential, related fiscal revenues are expected to remain modest for a decade. Confirmed coal deposits and natural gas reserves make the country a potential leading exporter, and hydropower potential is vast. The investments required to fully exploit this potential are very large relative to the size of the economy, either for LNG (about $40 billion or 2.7 times 2012 GDP) or for other large projects, including railroads, ports, power generation and transmission. As regular resource revenue will grow only gradually, exceeding current aid flows ($1.2 billion in 2012) only in a decade, staff advised the authorities to continue to prudently manage public expectations.

Mozambique: Contributions to Tax Revenues

	2010	2011	2012	2013	2014	2015	2016	2017	2018
	Act.	Act.	Est.	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
	(Percent of GDP)								
Total revenues	19.6	20.7	23.5	24.5	23.5	24.1	24.7	25.3	25.4
Tax revenues	17.0	18.1	20.0	20.4	19.4	20.0	20.6	21.2	21.3
Coal revenues	0.0	0.0	0.1	0.3	0.5	0.9	1.3	1.7	1.6
Non-coal tax revenues	17.0	18.1	19.9	20.2	18.9	19.1	19.3	19.5	19.7
Of which capital gains	0.0	0.0	1.2	1.5	-	-	-	-	-
Of which other tax revenues	17.0	18.1	18.7	18.7	18.9	19.1	19.3	19.5	19.7
	(Percent of non-coal GDP)								
Non-coal revenues	19.8	20.9	23.9	25.2	24.0	24.4	24.8	25.2	25.3
Non-coal tax revenues	17.3	18.2	20.4	20.9	19.7	20.1	20.5	20.8	21.0
Non-coal, non-capital gains tax revenues	17.3	18.2	19.1	19.4	19.7	20.1	20.5	20.8	21.0
	(Billions of MT)								
Coal GDP	4.1	2.5	9.8	15.9	20.7	30.8	39.6	50.5	52.7
Non-coal GDP	310.8	362.8	394.3	438.0	499.4	565.1	640.1	724.7	831.4

Sources: Mozambican authorities and IMF staff estimates and projections.

18. Strengthening revenue forecasting in the context of a natural resource rich environment would help to guide the formulation of a fiscal policy strategy. While the revenues stemming from gas production and exports will be generated only in a decade, coal revenues have started to make a contribution to the country's tax revenue/GDP ratio. Tax policy should evolve in line with the changing structure of the economy. Combined revenue from coal and LNG is projected to reach 9 percent of non-coal, non-LNG GDP by 2030, or about a quarter of all government revenue. The medium-term fiscal strategy should evolve to distinguish "core revenues" from resource revenue (e.g. royalties) and other one-off receipts (e.g. capital gains taxes).

19. The authorities concurred that continued capacity building will enable the country to reap the benefits from the mining and hydrocarbon activities. Staff encouraged the authorities to continue strengthening internal proficiency in regulatory and fiscal frameworks, macroeconomic and fiscal projections, as well as assessing and optimizing the impact of megaprojects and any financial government participation in them. This is all the more critical at the present juncture: the new mining and petroleum legislation, which is before Parliament**,** will need to be transposed into regulations and implemented, and a revision of the fiscal regimes of the mining and hydrocarbon sectors is underway with technical assistance from the IMF and others.

20. Ensuring high transparency in all aspects of the resource sector is essential. Mozambique has gained international recognition in complying with the EITI; the coverage of its reports on extractive industry payments and government receipts has been expanded from 6 to 46 enterprises, and payments reported by mining companies correspond very closely to receipts recorded by the government. Staff noted that transparency of contracts, regulation, taxation and revenues builds confidence and allows for checks and balances to secure a fair share of resource wealth for corporate partners, the government and the population at large.

21. The authorities agreed with the staff's analysis and are determined to further enhance macro-management capacity. Improvements in statistics on production and economic sectors are ongoing. Inter-institutional coordination is being strengthened to deepen economic analysis and the basis for policy formulation.

B. Fiscal Policy

MEFP ¶15-20

22. The government's objective to maintain elevated spending on public investment and social development, while maintaining macroeconomic stability, is appropriate. The authorities' fiscal anchor implies a gradual improvement in the domestic primary balance from a deficit of 2¾ percent of GDP in 2013 to a small surplus in 2017, while keeping borrowing, particularly externally on commercial terms, within the bounds of debt sustainability (see IMF-World Bank Debt Sustainability Analysis). Even with an expected gradual decline in external concessional funding as a share of GDP, the overall deficit after grants would remain at 5–8 percent of GDP per year, underpinned by a revenue objective, and could be financed by modest commercial foreign borrowing (1-2 percent of GDP) and some domestic borrowing (up to about 1 percent of GDP).

MEFP ¶17

23. A rule for the use of revenue windfalls should be established. Fiscal risks are currently on the upside; a capital gains tax revenue stemming from the sale of stakes among investors received in early 2013 ($224 million; 1.5 percent of GDP) is funding the supplementary budget for 2013. It allows mostly for investment spending in post-flood reconstruction and resettlements in the context of infrastructure projects. More such windfalls could materialize in 2013, and the authorities may consider establishing an explicit rule for spending these on infrastructure, either directly or through state-owned enterprises, and debt reduction, including accelerating the clearing of VAT refund arrears.[3]

24. The VAT administration and refund process needs to be reformed. The budget records VAT on a gross basis and includes an allowance for VAT refunds as an expenditure item. Staff

[3] Existing legislation allows the use of actual revenue in excess of budgeted amounts for debt reduction or investment.

emphasized that a true VAT is inherently net of refunds, and adjusted its analytical presentation accordingly in line with best practice.

- **The budget should record VAT revenue on a net basis, ensuring timely payment of VAT refunds**. The authorities agreed to devise a comprehensive action plan to modernize the VAT administration and overall refund process by October, drawing on IMF technical assistance. They thought that they could only gradually move to net VAT budgeting and envisaged it for the 2015 budget.

MEFP ¶23

- **Unsettled VAT refund requests have accumulated** and at end-2012 reached 1.3 percent of 2013 GDP, representing a cost to the private sector. Staff urged the authorities to settle this backlog. The authorities agreed that possible additional windfall revenue in 2013 could be applied towards clearing this.

MEFP ¶17

25. Consistent with their poverty reduction strategy, the authorities continue to prioritize spending towards infrastructure and social development while limiting fiscal risks. Two thirds of budgetary spending is in priority sectors.

- **Containing the public wage bill.** The lion share of the wage bill goes to education and its increase reflects significant new hiring in priority sectors in recent years, including education and health, and efforts to decompress wage scales in the civil service. The wage bill in the 2013 revised budget (10.8 percent of GDP) absorbs ½ of current spending. The government recognizes the need to slow down the decompression of the salary scales and the pace of recruitment in non-priority areas and aims to contain the wage bill at around 8.5 percent of GDP in the medium term. It continues to align the multiple payroll systems used and move forward the rollout of the electronic payroll system (e-Folha) and the integrated civil service database (e-CAF). Staff suggested also to develop a system to link compensation to results.

MEFP ¶18, 21

- **Prioritizing public investments.** Mozambique has a high rate of public investment (nearly 15 percent of GDP) of which more than half is financed domestically. The authorities are working to strengthen their project selection and economic profitability analysis capacity, and to assess the impact of related borrowing on public debt. The Ministry of Planning of Development is preparing an Integrated Investment Program in this perspective, and is working with line ministries to apply the new manual for the appraisal and evaluation of public investments projects.

MEFP ¶22

- **Managing public enterprises.** Following the adoption of the Public Enterprises Act (Law 6/2012 of February 2012), state-owned enterprises' investment and borrowing plans need to be approved by the sector ministry and the Ministry of Finance. The government will also enforce the publication of the annual reports of large state-owned companies. Staff suggested to improve transparency of the government's financial relations (including transfers and debt forgiveness) with public

MEFP ¶30-32

enterprises. It should limit subsidies to state enterprises, and monitor closely their financial participation in large infrastructure projects to contain fiscal risks.

MEFP ¶20

- **Transparency of energy subsidies.** *Electricity tariffs* are below cost-recovery levels and the financial situation of the electricity company (EDM) is deteriorating. The government has provided transfers through cancellation of on-lent loans and a new management contract is under negotiation. However, a tariff study has suggested a restructuring of and increases in tariffs, keeping costs to low-income consumers low. The proposals are expected to be presented to the Council of Ministers soon. Staff suggested that the government should cover investment costs of the rural electrification program and its own use of electricity (e.g. municipal street lighting), and gradually adjust tariffs to cost recovery levels. A sound financial footing for EDM would help attract investors to the sector's massive expansion plans and improve access to electricity, which currently reaches only 38 percent of the population and hinders business development. The government maintains *administered prices for fuels*, cross-*subsidizing the c*onsumption of fuel outside the megaprojects. It determines compensation payments to fuel importers based on a market-linked pricing formula. The 2013 budget includes 0.3 percent of GDP in payments to importers. Staff noted that differentiated pricing for diesel provides incentives for corruption and distorts price signals; the price-setting formula should be applied to the retail prices of all petroleum products.

MEFP ¶19

- **Social protection.** The government has substantially increased the budget for social protection (0.4 percent of GDP in the budget for 2013). It plans to increase the allocation further over the medium term, while better targeting beneficiaries, including establishing a consolidated electronic registry, and coordinating the allocation system.

26. The authorities generally concurred with staff's analysis, but pointed to political economy constraints. They noted that reform efforts are under way in many areas and need time to show results. Staff encouraged the authorities to communicate more publicly about the need for reforms, and the government's plans to address the challenges, especially with respect to civil service compensation and energy pricing.

Box 2. Social Protection Floor in Mozambique

Social protection is an essential ingredient in Mozambique's *poverty reduction strat*egy (PARP). The scheme is designed to address both the sheer level of poverty (over half of the population live below the poverty line), and the country's exposure to economic and climatic shocks that undermine and often reverse efforts to enhance skills and enable the poor to move out of low-productivity sectors, especially subsistence agriculture. Social protection can mitigate these risks, further social and human development and thus allow for more inclusive growth.

The government has made significant progress in establishing the legal and institutional framework for a national social protection floor. A 2007 Social Protection Law set the legal and institutional framework with broad components (social transfers, health, education, and social inclusion through work) defined in the 2010 National Strategy for Basic Social Security (ENSBB). New social protection programs created in 2011 expanded the ENSSB into a comprehensive social safety net consisting of a cash transfer program, targeting extremely poor households with no able-bodied income earner and a direct employment program in public works projects.

Spending on social protection has increased significantly in recent years. It has risen from around $13 million in 2008 to $57 million under the 2013 budget (0.4 percent of GDP). The government intends to increase budgetary appropriations to 0.8 percent of GDP over the medium term, reach around 0.9 million beneficiaries, and raise the level of cash transfers to bring recipients to the poverty line.

Work is on-going to address numerous implementation challenges. With the support of the World Bank, the UN system, and other development partners, the government is developing a common targeting system that combines geographical identification with community targeting to minimize exclusion errors and a proxy means-test instrument to minimize inclusion errors; a single registry of beneficiaries, and an information management system. Payment procedures are to be outsourced to commercial banks and mobile operators. Most systems are expected to be operational by 2014. Capacity is also being built at the district level. The creation of a common fund to secure further donor resources is under discussion.

C. Debt Management and Borrowing Strategy

27. External borrowing has risen significantly since 2012, especially on commercial terms. The government has increased its use of external non-concessional financing to fund several infrastructure investments. Combined with the major structural changes in the BOP due largely to the recent gas exploration and LNG investments, the current debt sustainability analysis (DSA) is moving the country from an outlook of low to moderate risk of debt distress. The authorities plan to continue public infrastructure investment at a high level, and have requested a new NCB ceiling based on the prospective contracting of new loans and the DSA outlook. Staff estimates that, at the current 3 percent discount rate, a new ceiling of $2 billion over the next 3 years is consistent with maintaining debt sustainability.

28. Staff modeled alternative approaches to public investment scaling up. Applying a new quantitative tool designed to analyze the effects of alternative paths of public investment scaling-up in resource-abundant developing countries[4], shows that a gradual scaling up that anticipates some future LNG revenue would be appropriate in the case of Mozambique, and is consistent with the assumptions in the DSA. An aggressive scaling up approach is not likely to yield better growth outcomes than a more gradual approach due to absorptive capacity constraints, and could put debt sustainability at risk (see Appendix V).

MEFP ¶22

29. Strengthening debt management and project selection is a strategic priority. The authorities have made some progress in making debt management more forward-looking. Yet various economic planning tools (Integrated Investment Plan, DSA, medium-term budget and debt strategy) are still to be linked and used as inputs to the annual budget preparation. Staff emphasized the urgent need to strengthen project analysis, selection and monitoring capacity and to anticipate the related financing in the DSA.

30. The authorities stressed their priority for continued high public investments and concurred with the staff's analysis. They agreed to moderate the pace of new borrowing over the medium term until the coming on stream of revenues from the coal and natural gas sectors, while strengthening the absorption capacity and effectiveness of investment. The authorities noted that this was consistent with maintaining sustainable debt ratios, and these were expected to fall sharply when exports and GDP rise sharply in the LNG production phase.

D. Monetary Policy and Financial Sector Issues

MEFP ¶10-14

31. Monetary policy was loosened in 2012, and is geared towards containing inflationary pressures while supporting economic activity. The BM aims to keep reserve money growth slightly above nominal GDP growth to support financial deepening and the provision of credit to the economy, while maintaining inflation at 5-6 percent in the medium term.

32. Inflationary pressures should be closely monitored and controlled within the overall macroeconomic policy mix. Staff suggested that the BM remain vigilant of possible lagged effects of monetary loosening, and monitor any second-round pass-through effects from the flood-related food prices increase. The impact of recent wage increases in the public sector and adjustments to some administered prices also need to be factored in. The authorities expressed their readiness to tighten monetary conditions if inflation accelerates beyond their current projections.[5]

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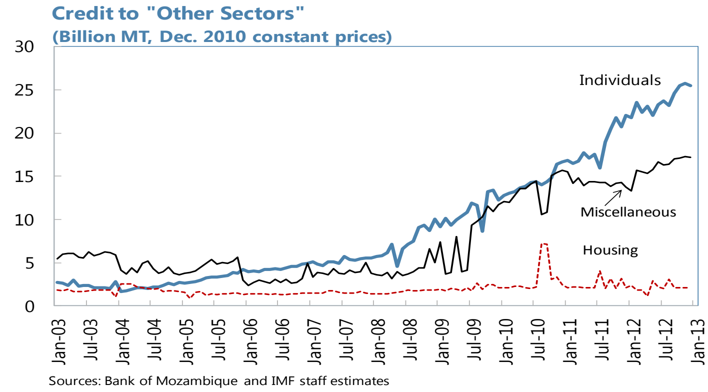
[4] DIGNAR (Debt, Investment, Growth and Natural Resources).

[5] The BM forecasts somewhat higher inflation than staff for 2013 based on its internal model, which the staff considers to reflect an upward bias due to its historic base period.

33. The transmission of monetary policy to private-sector financing is relatively weak. The banking system is very liquid and monetary aggregates have recently grown significantly faster than credit. The latter is increasingly allocated to household consumption of durable goods. While bank lending rates have fallen somewhat, they remain high. Staff suggested that strong monetary easing had one little to increase credit to the productive sector, especially SMEs, and that the authorities should focus instead on structural policies, including enhancing the creditworthiness of borrowers. Also, developments in credit to households and non-performing loans need to be closely monitored. The authorities acknowledged the concentration of credit in few large companies and underscored that diversifying SME's sources of financing is a critical pillar of the Financial Sector's Development Strategy. They also pointed to the steady and low level of non-performing loans.



34. The BM continues to modernize its monetary policy operations framework. They are strengthening coordination on cash flow planning with the Ministry of Finance, which is essential to better control base money developments and manage liquidity, and enhancing monetary policy instruments while contributing to developing the domestic securities market. Primary government bond dealers have been accredited for the first time recently, and the first-ever auction of treasury bonds (TB) was held that was significantly oversubscribed (market-clearing interest rate was 7.5 percent for 4-year TBs). To help develop capital markets, TBs will be auctioned in several smaller batches during the year, against a single annual placement in the past.

MEFP ¶11

MEFP ¶22

35. The authorities are enhancing their financial stability framework. Prudential indicators of the predominantly Portuguese-owned banking sector remain sound. Updated stress-tests conducted by an IMF TA mission in December 2012 suggest that the overall system may be fairly resilient to both solvency and liquidity shocks, and that contagion risks may be limited because of low interbank exposures. The fast expansion of the banking sector (18 banks compared to 12 in 2007) nevertheless calls for vigilance. The BM is developing its own stress-testing exercise, revising the regulation on the definition of nonperforming loans to make it internationally comparable, and planning a revision of regulations on concentration limits. Risk management guidelines and a legal and analytical framework for risk-based surveillance were adopted in March 2013, moving closer to the adoption of the Basel II Capital Accord in 2014. Moreover, the financial sector contingency plan has been completed and simulation exercises will be conducted with the support of the World Bank, while a deposit insurance fund will soon become operational upon release of donor funding.

MEFP ¶38-39

Also, a draft AML/CFT law incorporating comments from the IMF Legal Department is expected to be approved by Parliament soon.

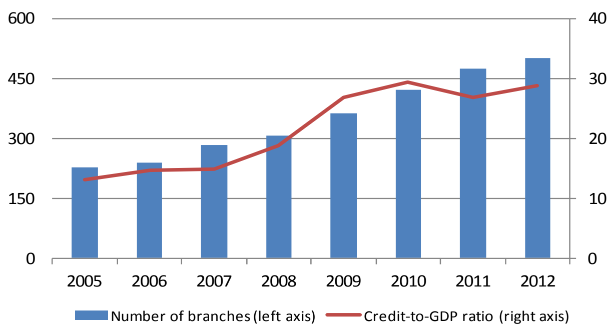
36. The authorities have adopted a Financial Sector Development Strategy aimed at deepening financial inclusion (Box 3). The financial strategy for 2013-2022 was subject to a comprehensive consultation process. It aims at strengthening financial stability and facilitating long-term financing of the private sector, and includes a broad range of targeted measures to enhance financial inclusion and deepening, competition, consumer protection and financial literacy.

37. The authorities are concerned about the supply and high cost of credit to the economy and agree with the need to focus on structural reforms. They acknowledged the need to deepen the analysis of monetary policy transmission mechanisms. The draft law on the creation of private credit registry bureaus is expected to be submitted to the Council of Ministers by June 2013 (structural benchmark), and should facilitate access to finance for SMEs; the deepening of domestic capital markets will also contribute to the financing of the economy.

Box 3. Financial Inclusion in Mozambique

Financial deepening in Mozambique is increasing amid banks' fast expansion. The number of branches of credit institutions rose from 228 in 2005 to 502 in 2012, and the credit-to-GDP ratio rose from 13.2 percent to 28.8 percent (Figure 1).[1] The share of the adult population that has a bank account increased to 20 percent in 2012.[2] By end-2012, the sector consisted of 18 banks, 8 microbanks, 7 credit unions, 11 savings and loans organizations, 202 microcredit operators, 1 electronic money institution and 3,051 agents of mobile banking.[3]

Figure 1: Banking Expansion and Financial Deepening (2005-12)



Yet, the sector remains concentrated and uncompetitive. Around 85 percent of the system assets are held by the 3 largest banks. Almost 80 percent of bank agencies and ATMs are located in urban areas, around half in Maputo.

There is evidence of increased financial inclusion in recent years, as documented by a BM study. Reflecting in part the expansion of the branch network and improvements in access to telecommunications and electricity, the number of branches per 10,000 km^2 increased by 4 between 2005 and 2012, and the number of ATMs and POSs in 10,000 km^2 increased by 8 and 58, respectively.

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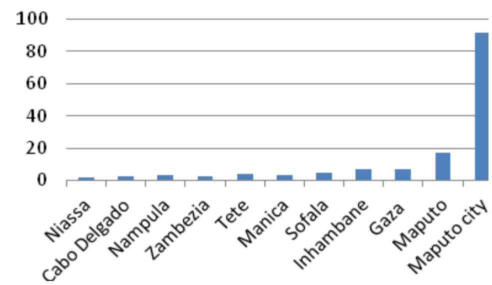
[1] Despite lying below the average of SADC region (40.6 percent).
[2] Although it is below the average for SADC (39 percent).
[3] Bank of Mozambique (2013).

The BM has constructed an index of financial inclusion (IFI)[4] showing an upward trend overall, but with regional asymmetries. The index rose from 9.2 in 2005 to 13.1 in 2012, with the jump in 2011 explained mainly by the emergence of mobile banking services. However, while Maputo city had a very high IFI at end-2012 (91.8), other provinces remained with very low access to financial services (Figure 2).

Figure 2: Index of Financial Inclusion by Province (2012)



Despite higher financial inclusion, access to credit continues to be a major concern, particularly for SMEs. Interest rates on loans have been declining gradually, but remain high, and credit remains biased towards middle-income households at the exclusion of productive sectors such as agriculture and industry.

Looking forward, it is necessary to address the challenges to financial inclusion, both on the supply and demand sides. The authorities have reached a key milestone with the approval of the Financial Sector Development Strategy in March 2013, which appropriately lays out a number of policies to improve access to financial services.

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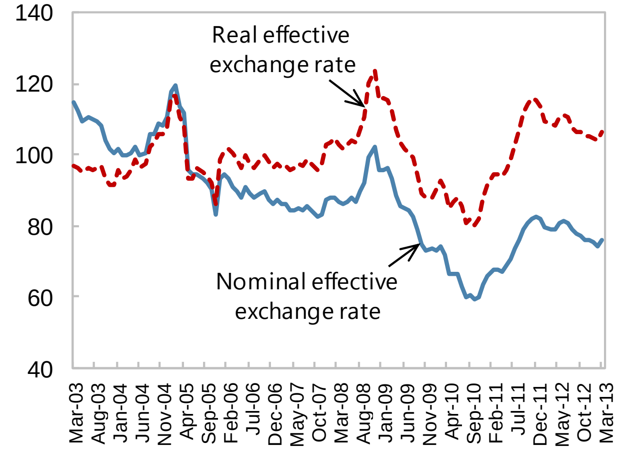
[4] The index of financial inclusion, as defined in the BM study, measures the level of access to and use of formal financial services on a 0-100 scale.

E. External Sector Stability[6]

38. *The real effective* exchange rate (REER) fluctuated somewhat in recent years. The REER reached a peak in early 2009, then depreciated through late 2010,as a result of the Bank of Mozambique loosening monetary policy in response to the world economic crisis. It recovered in 2011 as the authorities tightened monetary policy, and depreciated slightly in 2012 and early 2013 following the monetary easing. Since 2011 the REER has remained above its average level in previous years, which is likely to be related partly to the start up of coal exports in 2011, and thus could signal future further appreciation.

Nominal and Real Effective Exchange Rates
(Index, Average 2005=100)



39. On balance, staff views the real effective exchange rate (REER) as broadly in line with fundamentals. Standard CGER calculations suggest a large overvaluation, but this can be misleading as the calculated current account norm is based on economic parameters derived from historical values. Applying the CGER methodology to the non-LNG current account suggests that the REER is relatively close to its equilibrium rate. Staff considers that developments in the coal and natural gas sectors will likely cause the exchange rate to appreciate.

Mozambique: Exchange Rate Misalignments (Excluding LNG)

Method	**2018**
Macro balance	-3.2
Equilibrium Real Exchange Rate	-7.9
External Sustainability	10.1
Purchasing Power Parity	1.7
Average	**0.2**

40. The current reserve coverage appears adequate to withstand external shocks and is projected to remain so over the medium term. Mozambique's current reserve coverage of about 4 months of projected non-megaproject imports of goods and services appears adequate considering various measures of reserve adequacy. The relevant measure of reserve cover in Mozambique is imports of goods and services excluding megaprojects because the megaproject imports are financed by FDI and are, in effect, self-financing. Moreover, a one standard deviation shock to the current account or exports in terms of GDP reveals that the impact on Mozambique—between one and two months of imports—could be weathered.

41. Mozambique's doing business indicators suggest that the economy's competitiveness can be improved through structural reforms. The country is lagging behind its peers in the region and has shown little progress under various survey-based indicators. It is ranked near the bottom of

[6] See Appendix IV.

the World Bank's latest Doing Business ratings, having dropped from 139 in 2012 to 146 in 2013. More needs to be done to improve external competitiveness, including enhancing institutions, infrastructure (such as transportation systems), the provision of health and education services, and further steps to enhance the business climate, such as simplifying the procedures for starting and operating a business.

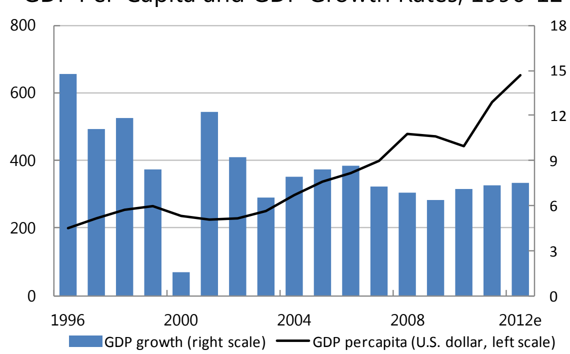
42. The authorities agreed with the medium-term reserve adequacy level and with the need to focus on structural reforms to enhance competitiveness. In 2012 Parliament authorized the government to establish bankruptcy rules for insolvent companies, and a simplified licensing regime was adopted for a range of commercial activities, while regulations are being streamlined for others.

F. Inclusive Growth

43. Despite Mozambique's 20 years of high growth, substantial development challenges remain. Record growth since the end of the Civil War in 1992 reflected sound macro-economic management, a number of large-scale foreign investment projects ("megaprojects"), and strong donor support. Yet Mozambique started from a very low base and remains among the world's poorer countries with a per capita GDP of $650 in 2012. While poverty has been reduced, more than half of the population still lives below the national poverty line according to the latest data available (for 2009). Improvements have been most pronounced in the already more affluent Southern regions and in urban centers, especially the Maputo area, while nationwide rural poverty continues to be severe.

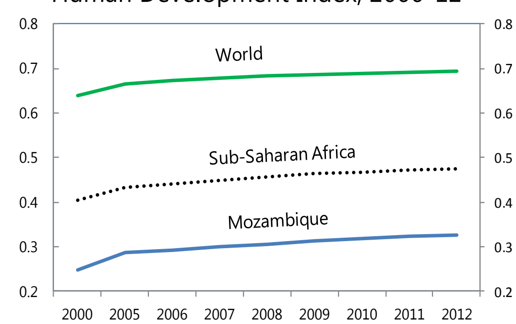
Mozambique: Development Indicators

GDP Per-Capita and GDP Growth Rates, 1996-12



Sources: World Bank, *World Development Indicators* and INE.

Human Development Index, 2000-12



Source: UNDP, Human Development Indicators.

44. Making growth more inclusive is the authorities' guiding priority—and an immense long-term challenge. The correlation between economic growth and the poverty rate has weakened in recent years. While agriculture played an important role in the post-crisis reconstruction period, growth is increasingly driven more by extractive industries, which are highly capital-intensive and create (directly) few jobs for nationals. Employment remains dominated by agriculture (78 percent of the economically active population), mostly in subsistence activities and with very low productivity. Average skill levels in the labor force are low and will take time to improve. The population is relatively young and growing at about 3 percent a year, with the labor force growing rapidly. Responding to these long-term challenges is at the core of the poverty reduction strategy (PARP 2011–14) and of priority spending in the budget, and measurable progress is likely to be gradual (see Appendix VI).

Mozambique: Millenium Development Goals

	1995	2005	2011	SSA 2011
Population (millions)	16	21	24	875
National household survey poverty incidence	69.0	54.1 [1]	54.7 [2]	...
GDP per capita (2000 US$)	233	308	402	648
Primary school enrollment ratio (percent of net)	56	76	90	76
Ratio: girls to boys in primary/secondary education (percen	75	84	90	90
Under 5 mortality rate (per 1000)	183	162	103	108
Prevalence of HIV, total (percent of population aged 15-49)	10	12	11	5
Access to improved water sources (percent of population)	42	45	47	61 [2]

[1] Refers to the 2003 and 2008 household survey results. [2] 2010.

45. Making growth more inclusive requires a decisive multidimensional strategy centered on job creation and economic transformation. Staff agreed with the authorities that the priorities continue to include addressing the large infrastructure gaps, strengthening productivity in agriculture, investing in health, education and vocational training to provide a qualified workforce and innovators to take advantage of the emerging opportunities, supporting access to credit including for smaller or newer enterprises, facilitating the creation of markets with supporting market infrastructure (such as transportation networks) both locally and within the region to create demand for new products, and continued efforts to strengthen the basic social protection system to help the most vulnerable.

46. The authorities noted the significant progress made in improving social-development indicators, and acknowledged the need for further reforms to expand economic diversification and improve the business environment. They noted that these issues remain at the core of the current PARP and its successor planned for early 2015, and the government's overall economic strategy.

NEW PSI AND PROGRAM ISSUES

47. The authorities requested (i) waivers for breaches of the end-December net credit to government and reserve money targets considering the corrective action taken and the minor size of the deviation, respectively, and the strong ownership and overall good performance of the Fund-supported program that they have demonstrated; **and (ii) the completion of the sixth review under the PSI.**

48. The authorities requested continued Fund support through a new three-year PSI. They noted that the PSI has served them well in building capacity in a broad spectrum of areas, strengthening the monitoring and implementation of their economic and social development strategy, and had a positive signaling effect for donor support. They appreciated the Fund's flexibility in responding to shocks and addressing infrastructure gaps.

49. In the staff's view, the PSI remains an appropriate instrument for Mozambique. The current PSI allowed for a close policy dialogue between the Fund and the authorities. Economic policies established a commendable track-record of domestic and external stability that is necessary to support strong and durable poverty reduction and growth. The macroeconomic position of the country is broadly stable and sustainable and therefore does not require Fund financing or significant macroeconomic policy adjustments.

50. Staff proposes to maintain the program conditionality largely unchanged as it adequately reflects policy priorities. The indicators relative to the quantitative assessment variables (ACs) and indicative targets would remain the same, though the definition of government revenue will now reflect VAT on a net basis. With respect to external borrowing limits, the PSI maintains limits on the contracting of commercial borrowing with limits set consistent with maintaining debt sustainability. The proposed structural conditionality (SBMs) draws on TA recommendations from the Fund, in the areas of PFM, tax administration, investment planning, monetary and financial sector management, and real and external sector statistics, and will be conducive to achieving the program objectives (see paragraphs 13 and 14). The emphasis on capacity building in macro-management will support the country's transition to a resource-rich economy. In the short run, structural conditionality will focus on public financial management, investment planning, business environment and financial sector development (see Table 4 of the MEFP). The authorities will cancel the existing PSI at the time of approval of a successor. Reviews and ACs will be semi-annual, with the first review by end-December 2013 based on end-June 2013 ACs and SBMs.

STAFF APPRAISAL

51. Mozambique's economic growth performance has been remarkable and the outlook remains strong. Economic growth was buoyant in 2012 and inflation fell sharply. Economic growth was broad-based and led by the start-up of coal production and exports. Performance in 2013 is expected to remain strong with growth at 7 percent and low inflation, despite the adverse impact of floods early this year.

52. Several factors mitigate the identified vulnerabilities. Prospects for coal production and exports are good, and further tax windfalls from sales of shares in gas operations could materialize this year. Strong FDI inflows in several megaprojects, including LNG development, are ongoing and the related widening of the external current account deficit does not signal fundamental external imbalances.

53. Monetary and financial policies remain broadly appropriate. The authorities' objective of strengthening the BM's monetary policy framework should help improve the weak transmission mechanisms. Monetary conditions should be tightened if inflation accelerates beyond the authorities' current projections. Ongoing reforms of financial and prudential regulations aiming at strengthening the soundness and supervision of the banking system and financial deepening should be swiftly implemented along the lines of the Financial Sector Development Strategy. Staff views the real effective exchange rate as broadly in line with fundamentals and reserve coverage as adequate.

54. Fiscal policy remains prudent, but over the medium term should be adapted to the new natural resource-rich environment. As revenues stemming from the extractive industry will remain modest for a number of years, continued donor support is essential to help address Mozambique's significant remaining development challenges. Reforms to modernize revenue administration and PFM need to continue across the board, and steps taken to ensure timely settlement of VAT refunds. The authorities should focus on the results of spending and base project selection on economic profitability The current high level of public investment can make an important contribution to closing infrastructure gaps and enabling Mozambique to access its natural resource wealth, but the pace of investment needs to be monitored carefully to avoid hitting absorptive capacity constraints and to preserve debt sustainability. Thus the authorities should strengthen their medium-term debt strategy and remain in line with the gradual borrowing approach underlying the DSA. They also need to continue to analyze the risks to domestic and external debt outlook on the basis of periodic DSA updates.

55. The authorities should persist in their broad structural reform agenda. Monetary policy and financial sector development, business environment reforms and policies to strengthen agricultural productivity are essential to support growth in the private sector outside the megaprojects, and advance the implementation of the poverty reduction strategy. Prompt adoption by Parliament of the draft AML/CFT law would contribute to further support anti-corruption efforts. Infrastructure investments and measures to build human capital through improved education, job training and health services are also crucial, thought the latter tend to have long lead times before showing results. Statistics are broadly adequate for surveillance purposes, and reforms to broaden coverage and improve compilation should continue in all areas.

56. Based on the satisfactory program performance to date, staff recommends completion of the sixth review under the PSI. It also recommends waivers for the non-observance of the end-December 2012 ACs on reserve money and net credit to the government, since the deviations from the targets were minor and corrective action was taken since then to strengthen expenditure control, and did not undermine the program objectives.

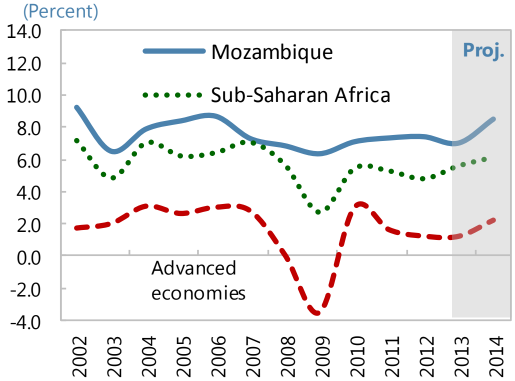
57. Staff recommends approval of the proposed successor three-year PSI. The country has a policy framework focused on consolidating macroeconomic stability and debt sustainability, while deepening structural reforms in key areas that currently constrain growth and poverty reduction; the authorities demonstrated their openness to a close policy dialogue with the Fund, through the Fund's endorsement and assessment of their economic and financial policies under a PSI. Such support would be helpful as the country enters a transition period marked by massive investments planned largely by the private sector to bring Mozambique's gas reserves to the market.

58. It is proposed that the next Article IV consultation take place within 24 months subject to the provisions of the decision on consultation cycles in program countries.

Figure 1. Mozambique: Impact of Global Developments

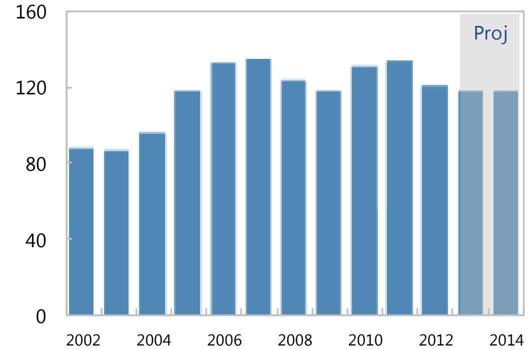
Despite the global weakness, Mozambique's growth outlook is robust, although slowed by the flooding in 2013.

Real GDP Growth
(Percent)



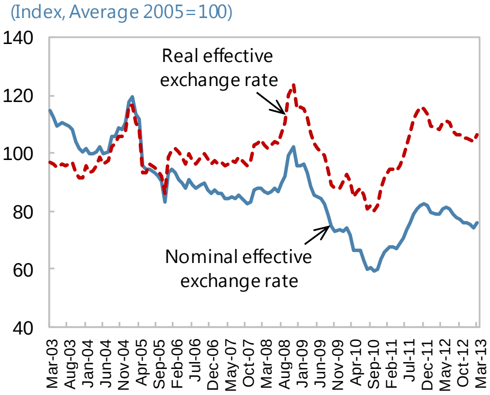
Terms of trade gains recently reversed due to weakening international commodity prices…

Terms of Trade Index
(2005=100)



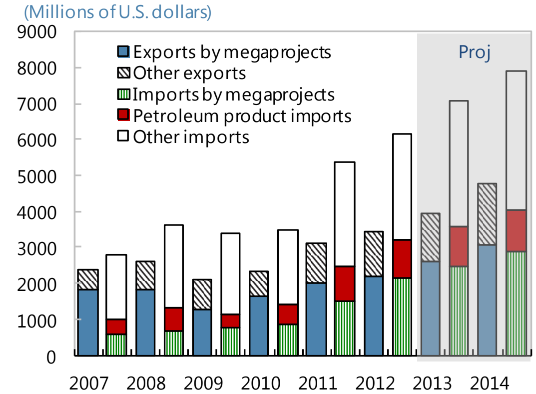
…while the metical has depreciated somewhat following the recent monetary easing.

Nominal and Real Effective Exchange Rates
(Index, Average 2005=100)



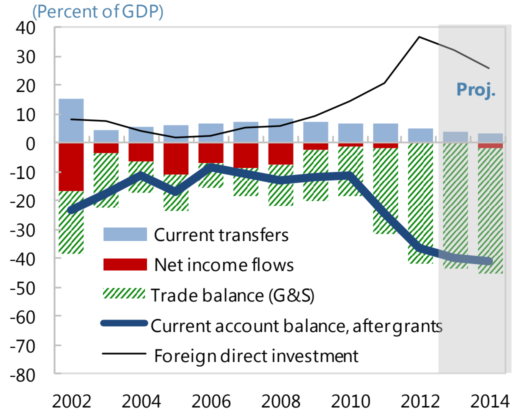
Megaprojects' strong export growth was counterbalanced by investment-related and fuel imports.

Merchandise Trade
(Millions of U.S. dollars)



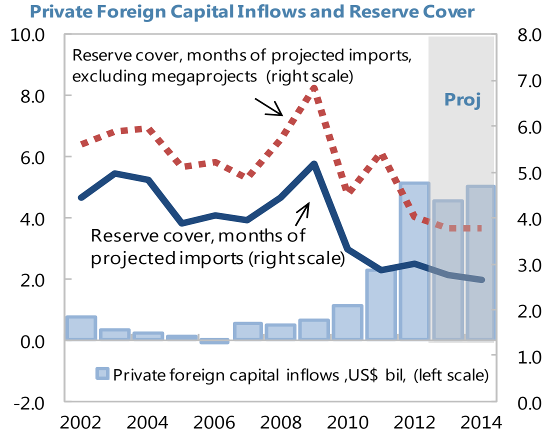
The current account deficit has widened, reflecting sizeable investment imports by the natural resource sector.

Current Account Balance and Foreign Direct Investment
(Percent of GDP)



Despite strong private capital inflows, the reserve cover declined owing to rapid import growth related to investment.

Private Foreign Capital Inflows and Reserve Cover

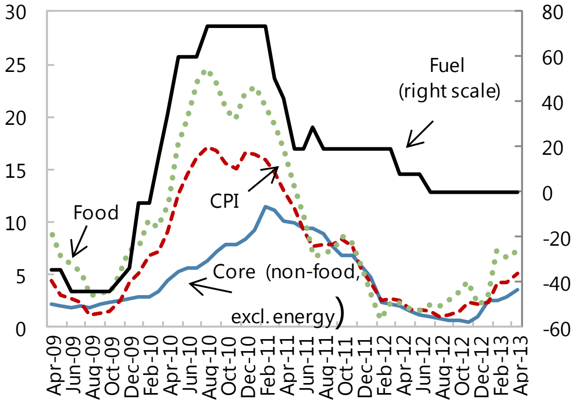


Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 2. Mozambique: Inflation and Monetary Developments

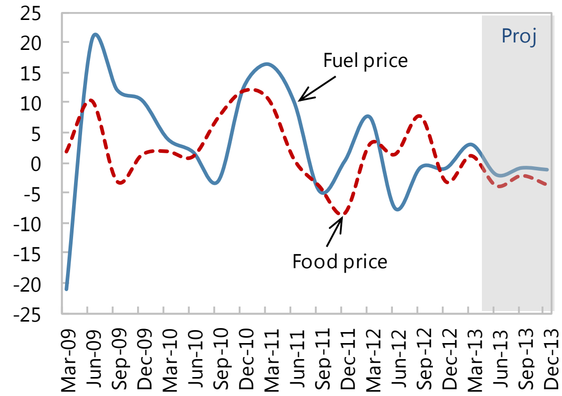
Inflation remained low in 2012 but began to rise after the floods in early 2013.

CPI and Components
(Percent change, year-on-year)



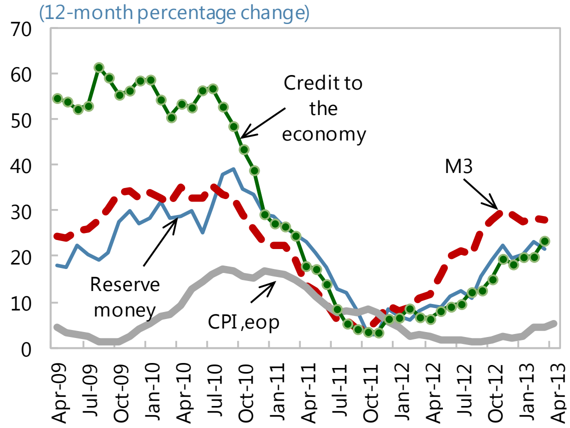
Low inflation was helped by favorable developments in international prices and...

International Food and Fuel Price Change
(Percent over previous quarter)



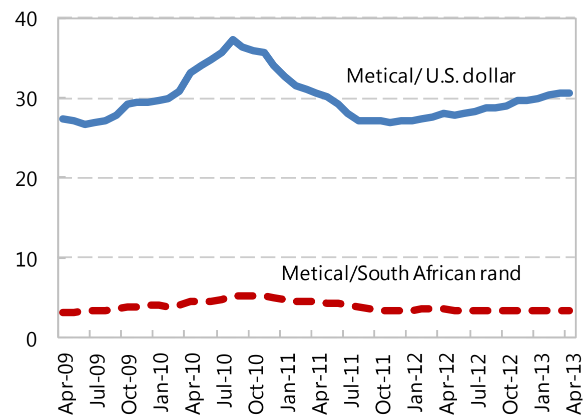
...determined monetary tightening during 2010-11. Looser broad money in 2012 helped push up private sector credit growth and may generate some inflationary pressures.

Money, Credit and Inflation
(12-month percentage change)



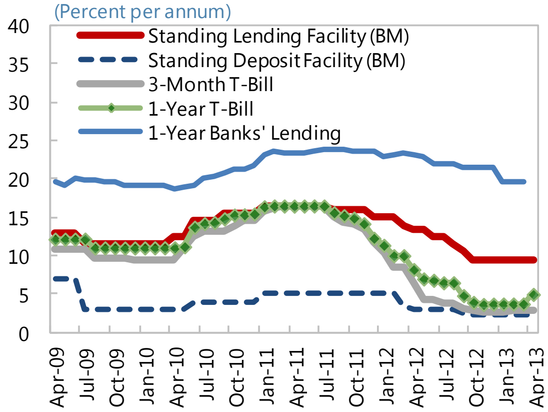
The Mt/$ exchange rate appreciated during the monetary tightening 2010-11, and has depreciated somewhat since. The rate against the rand has been more stable.

Bilateral Exchange Rates



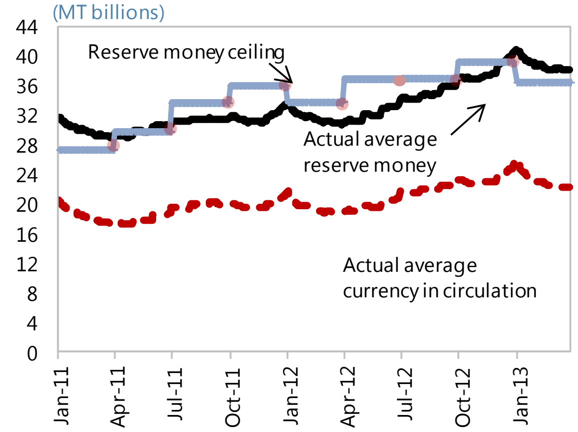
The BM's policy rates and the T-bill rates are coming down, although banks' lending rate remains sticky.

Interest Rates
(Percent per annum)



Reserve money was broadly in line with program targets, helping to maintain a low inflation environment.

Reserve Money
(MT billions)

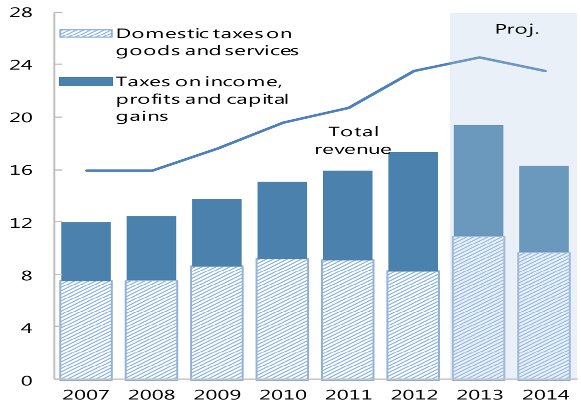


Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 3. Mozambique: Fiscal Developments

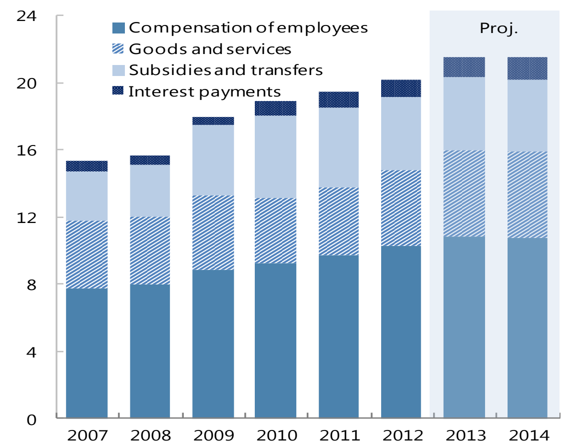
As the result of recent tax administration reforms, revenue collections continue to be buoyant but are expected to slow down…

Revenue Collections
(Percent of GDP)



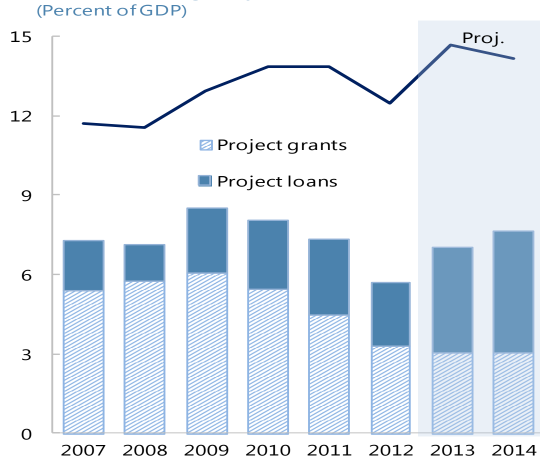
… while spending on subsidies, especially the fuel subsidy, was contained, providing room for other spending.

Domestic Current Expenditures
(Percent of GDP)



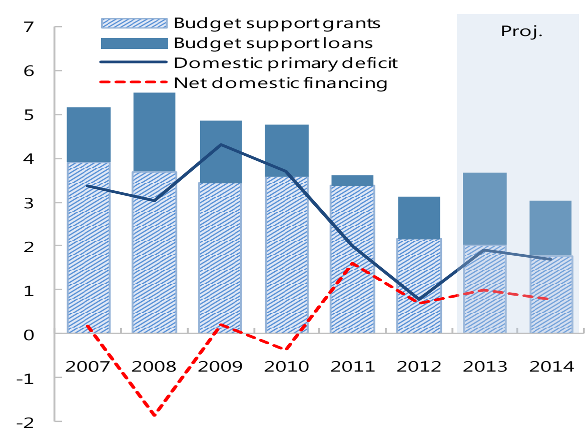
External borrowing is gradually replacing budget support for the financing of capital spending…

Capital Spending, Project Grants and Loans
(Percent of GDP)



…while the domestic primary deficit has been contained, keeping recourse to domestic financing down despite the decline in external budget support.

Budget Financing
(Percent of GDP)



Sources: Mozambican authorities and IMF staff estimates and projections.

Table 1. Mozambique: Selected Economic and Financial Indicators, 2010-18

	2010	2011	2012		2013		2014	2015	2016	2017	2018
	Act.	Act.	CR 13/1	Est.	CR 13/1	Proj.			Proj.		
(Annual percentage change, unless otherwise indicated)											
National income and prices											
Nominal GDP (MT billion)	315	365	414	404	483	454	520	596	680	775	884
Nominal GDP growth	18.3	16.0	13.4	10.6	16.5	12.3	14.6	14.6	14.0	14.0	14.1
Real GDP growth	7.1	7.3	7.5	7.4	8.4	7.0	8.5	8.5	8.0	8.0	8.0
GDP per capita (US$)	442	571	650	634	688	640	684	753	826	904	990
GDP deflator	10.5	8.1	5.5	3.0	7.5	5.0	5.6	5.6	5.6	5.6	5.6
Consumer price index (annual average)	12.7	10.4	2.4	2.1	7.0	5.5	5.6	5.6	5.6	5.6	5.6
Consumer price index (end of period)	16.6	5.5	4.1	2.2	6.5	6.1	5.4	5.6	5.6	5.6	5.6
Exchange rate, MT per US dollar, eop	32.8	27.1	...	29.7	...	...	...	...	...	...	...
Exchange rate, MT per US dollar, per.avg.	33.0	29.1	...	28.4	...	...	...	...	...	...	...
External sector											
Merchandise exports	8.7	33.6	16.9	11.3	16.1	13.8	20.9	25.0	13.1	14.0	21.4
Merchandise exports, excluding megaprojects	-20.5	65.8	19.3	15.6	9.1	4.0	26.2	29.8	9.8	10.8	10.1
Merchandise imports	2.6	52.8	9.9	14.9	7.4	15.3	11.3	19.3	4.0	24.2	4.8
Merchandise imports, excluding megaprojects	-0.7	46.2	-0.2	4.9	11.3	15.2	8.4	7.8	10.2	9.8	9.1
Terms of trade	10.5	2.5	-9.8	-10.0	-2.9	-1.9	-0.1	0.4	0.4	-0.1	-0.3
Nominal effective exchange rate (annual average)	-22.4	12.4	...	7.4	...	...	...	...	...	...	...
Real effective exchange rate (annual average)	-15.1	19.7	...	5.4	...	...	...	...	...	...	...
(Annual percentage change, unless otherwise indicated)											
Money and credit											
Reserve money	29.2	8.5	18.0	19.7	18.4	17.9	15.0	15.3	14.8	14.8	14.8
M3 (Broad Money)	22.8	9.4	18.6	29.4	19.3	19.0	15.5	15.6	15.1	15.1	15.1
Credit to the economy	29.3	6.4	17.9	18.3	18.9	21.5	19.1	16.4	15.9	15.8	15.8
(Percent of GDP)	29.3	26.9	28.0	28.8	28.5	31.1	32.3	32.9	33.4	33.9	34.4
(Percent of GDP)											
Investment and saving											
Gross domestic investment	19.5	36.7	37.2	48.3	39.0	49.4	51.8	54.4	55.8	59.0	57.2
Government	14.5	14.9	12.9	13.6	14.6	16.2	17.2	16.7	16.5	16.2	15.9
Other sectors	5.0	21.9	24.3	34.7	24.3	33.2	34.6	37.7	39.3	42.8	41.3
Gross domestic savings (excluding grants)	0.9	5.5	6.0	8.0	9.0	6.0	7.0	10.1	13.7	9.1	16.0
Government	1.2	2.0	3.5	4.1	3.0	3.8	3.6	4.5	5.3	6.1	6.4
Other sectors	-0.2	3.6	2.5	3.9	6.0	2.2	3.4	5.7	8.3	3.0	9.6
External current account, before grants	-18.5	-31.2	-31.2	-40.3	-30.0	-43.4	-44.8	-44.3	-42.2	-49.9	-41.2
External current account, after grants	-11.7	-24.3	-26.9	-36.5	-26.3	-39.9	-41.3	-41.4	-39.8	-47.9	-39.5
Government budget											
Total revenue [1]	19.6	20.7	23.9	23.5	23.1	24.5	23.5	24.1	24.7	25.3	25.4
Total expenditure and net lending	32.9	33.6	33.3	32.9	34.0	36.3	35.5	34.8	34.4	33.8	32.6
Overall balance, before grants	-13.2	-13.1	-9.3	-9.6	-10.9	-11.8	-12.0	-10.7	-9.7	-8.6	-7.2
Total grants	9.0	7.8	5.8	5.4	5.4	5.1	4.8	4.0	3.3	2.8	2.3
Overall balance, after grants	-4.3	-5.3	-3.6	-4.2	-5.5	-6.7	-7.2	-6.7	-6.4	-5.8	-4.8
Domestic primary balance, before grants	-4.1	-2.9	-1.3	-1.0	-2.3	-2.7	-1.7	-0.9	-0.2	0.1	1.0
External financing (incl. debt relief)	4.2	3.7	3.6	4.2	4.9	5.7	6.4	6.1	6.0	5.1	4.4
Net domestic financing	0.0	1.6	0.0	0.7	0.6	1.0	0.8	0.6	0.4	0.7	0.4
Privatization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total public debt [2]	46.1	39.3	48.1	42.2	50.7	47.8	50.9	51.9	53.0	53.4	52.5
Of which: external	40.2	32.6	39.1	36.3	42.3	41.6	44.7	45.9	47.4	47.7	47.2
Of which: domestic	6.0	6.7	9.1	5.9	8.3	6.2	6.2	6.0	5.6	5.7	5.4
(Millions of U.S. dollars, unless otherwise indicated)											
External current account, before grants	-1,770	-3,922	-4,558	-5,737	-4,726	-6,373	-7,158	-7,947	-8,466	-11,176	-10,312
External current account, after grants	-1,113	-3,059	-3,924	-5,198	-4,153	-5,854	-6,608	-7,433	-7,988	-10,731	-9,890
Overall balance of payments	608	323	246	373	155	100	320	805	636	187	660
Net international reserves (end of period) [3]	1,908	2,239	2,530	2,605	2,685	2,704	3,023	3,828	4,463	4,651	5,311
Gross international reserves (end of period) [3]	2,099	2,428	2,723	2,799	2,874	2,894	3,211	3,980	4,580	4,732	5,358
Months of projected imports of goods and nonfactor services	3.3	2.9	3.4	3.0	2.7	2.8	2.6	3.1	3.0	3.0	3.5
Months of imports of goods and nonfactor services, excl. megaprojects	4.2	3.7	5.1	3.8	5.1	3.7	3.7	4.2	4.3	4.1	4.2

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

[1] Net of verified VAT refund requests.

[2] Consistent with DSA definition, the nonconcessional Portuguese credit line is included under the external debt.

[3] Includes disbursements of IMF resources under the ESF and August 2009 SDR allocation.

Table 2. Mozambique: Government Finances, 2010-13

(Billions of Meticais)

	2010	2011	2012		2013	
	Act.	Est.	CR 13/1	Est.	CR 13/1	Proj.
Total revenue[1]	61.62	75.75	99.04	94.85	111.76	111.42
Tax revenue	53.69	66.17	87.33	80.88	97.08	92.82
Income and profits	18.48	24.89	35.21	36.77	31.58	38.35
Of which: capital gain tax	…	…	5.03	5.03	…	6.80
Goods and services[1]	28.84	33.05	42.87	33.33	53.15	49.45
Of which: International trade	5.26	6.73	7.42	7.57	9.58	9.58
Other	1.10	1.51	1.83	3.20	2.77	5.02
Nontax revenue	7.94	9.58	11.71	13.97	14.68	18.60
Total expenditure and net lending	103.52	122.81	137.78	133.12	164.41	164.92
Current expenditure	57.89	68.55	84.46	78.30	97.26	94.31
Compensation to employees	29.11	35.66	41.35	41.53	48.81	49.21
Goods and services[1]	10.69	12.09	18.84	15.13	23.56	19.96
Interest on public debt	2.67	3.58	4.63	4.13	5.62	5.62
Domestic	1.86	2.59	3.55	2.89	3.56	3.56
External	0.81	0.99	1.07	1.24	2.06	2.06
Transfer payments	15.42	17.21	19.64	17.51	19.28	19.53
Of which: fuel subsidy (old stock)	4.69	4.09	2.68	2.47	1.33	1.24
basic social protection floor	0.73	0.75	1.01	1.01	1.68	1.68
Domestic current primary balance	6.41	10.78	19.21	20.68	20.12	22.73
Capital expenditure	43.70	50.60	46.99	50.36	57.65	66.54
Domestically financed	20.03	20.32	24.26	24.74	30.78	34.71
Externally financed	23.67	30.28	22.73	25.62	26.87	31.83
Net lending	1.93	3.66	6.34	4.47	9.49	4.06
Domestically financed	-0.40	0.39	0.40	-0.38	0.33	0.33
Externally financed loans to public enterprises	2.33	3.26	5.94	4.85	9.17	3.74
of which: nonconcessional net lending	0.00	0.00	4.24	1.90	8.28	1.26
Unallocated revenue (+)/expenditure (-) [2]	0.36	-0.78	0.00	-0.47	0.00	0.00
Domestic primary balance, before grants, above the line [3]	-12.86	-10.70	-5.45	-4.14	-10.98	-12.30
Overall balance, before grants	-41.53	-47.83	-38.74	-38.74	-52.65	-53.50
Grants received	28.34	28.63	23.87	21.94	26.23	22.94
Project support	17.11	16.37	15.60	13.27	17.65	13.81
Investment projects	7.19	6.70	7.56	7.30	8.80	7.00
Special programs	9.92	9.68	8.05	5.96	8.86	6.81
Budget support	11.24	12.26	8.26	8.67	8.58	9.12
Overall balance, after grants	-13.19	-19.20	-14.87	-16.80	-26.42	-30.56
Net external financing	13.25	13.48	14.82	13.83	23.65	26.01
Disbursements	14.28	14.60	16.97	15.45	25.73	29.22
Project	8.19	10.50	7.12	6.73	9.22	18.02
Nonproject support	6.09	4.10	9.85	8.72	16.51	11.20
Loans to public enterprises	2.33	3.26	5.94	4.85	9.17	3.74
of which: nonconcessional	0.00	1.50	4.24	2.25	8.28	1.26
Budget support	3.76	0.83	3.91	3.87	7.34	7.46
Cash amortization	-1.03	-1.12	-2.15	-1.61	-2.07	-3.21
Net domestic financing	-0.04	5.72	0.05	2.94	2.76	4.54
Net privatization	-0.01	0.00	0.00	0.03	0.00	0.00
Memorandum items:						
Gross aid flows	42.62	41.73	36.60	35.13	43.68	50.90
Budget support	14.99	13.09	12.17	12.54	15.92	16.59
Nonbudget support	27.63	28.64	24.43	22.59	27.76	34.31
Project support	25.30	26.88	22.73	20.00	26.87	31.83
Concessional loans to public enterprises	2.33	1.76	1.70	2.60	0.89	2.48

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

[1] VAT presentation was changed to a net basis (collection minus requested VAT refunds). CR 13/1 showed gross VAT revenues and refunds as an expenditure item.

[2] Residual discrepancy between identified sources and uses of funds.

[3] Revenue minus noninterest current expenditure minus locally financed capital expenditure and locally financed net lending.

Table 3. Mozambique: Government Finances, 2010-18

	2010	2011	2012		2013		2014	2015	2016	2017	2018
	Act.	Est.	CR 13/1	Est.	CR 13/1	Proj.	Proj.				
	Percent of GDP										
Total revenue [1]	19.6	20.7	23.9	23.5	23.1	24.5	23.5	24.1	24.7	25.3	25.4
Tax revenue	17.0	18.1	21.1	20.0	20.1	20.4	19.4	20.0	20.6	21.2	21.3
Taxes on income and profits	5.9	6.8	8.5	9.1	6.5	8.4	6.6	6.8	7.4	8.3	9.0
Taxes on goods and services [1]	9.2	9.0	10.3	8.2	11.0	10.9	9.7	10.0	9.9	9.6	9.0
Taxes on international trade	1.7	1.8	1.8	1.9	2.0	2.1	2.1	2.2	2.2	2.3	2.3
Other taxes	0.4	0.4	0.4	0.8	0.6	1.1	1.0	1.0	1.0	1.0	1.0
Nontax revenue	2.5	2.6	2.8	3.5	3.0	4.1	4.1	4.1	4.1	4.1	4.1
Total expenditure and net lending	32.9	33.6	33.3	32.9	34.0	36.3	35.5	34.8	34.4	33.8	32.6
Current expenditure	18.4	18.8	20.4	19.4	20.1	20.8	19.9	19.7	19.4	19.2	19.0
Compensation to employees	9.2	9.8	10.0	10.3	10.1	10.8	10.7	10.5	10.2	9.8	9.5
Goods and services [1]	3.4	3.3	4.5	3.7	4.9	4.4	3.6	3.4	3.3	3.3	3.3
Interest on public debt	0.8	1.0	1.1	1.0	1.2	1.2	1.3	1.4	1.5	1.7	1.8
Transfer payments	4.9	4.7	4.7	4.3	4.0	4.3	4.3	4.4	4.4	4.4	4.4
Of which: fuel subsidy (old stock)	1.5	1.1	0.6	0.6	0.3	0.3	...	...	...	...	...
basic social protection floor	0.2	0.2	0.2	0.2	0.3	0.4	0.4	0.6	0.8	0.8	0.8
Capital expenditure	13.9	13.9	11.3	12.5	11.9	14.7	14.2	13.4	13.0	12.3	11.2
Domestically financed	6.4	5.6	5.9	6.1	6.4	7.6	6.5	6.7	7.0	7.6	7.2
Externally financed	7.5	8.3	5.5	6.3	5.6	7.0	7.6	6.7	6.1	4.7	4.1
Net lending	1.0	1.0	1.5	1.1	2.0	0.9	1.4	1.7	1.9	2.4	2.4
Domestically financed	-0.1	0.1	0.1	-0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Externally financed loans to public enterprises	0.7	0.9	1.4	1.2	1.9	0.8	1.3	1.6	1.9	2.3	2.3
Of which: nonconcessional net lending	0.0	0.0	1.0	0.5	1.7	0.3	0.9	1.3	1.6	2.1	2.1
Unallocated revenue (+)/expenditure (-) [2]	0.1	-0.2	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Domestic primary balance, before grants [3]	-4.1	-2.9	-1.3	-1.0	-2.3	-2.7	-1.7	-0.9	-0.2	0.1	1.0
Overall balance, before grants	-13.2	-13.1	-9.3	-9.6	-10.9	-11.8	-12.0	-10.7	-9.7	-8.6	-7.2
Grants received	9.0	7.8	5.8	5.4	5.4	5.1	4.8	4.0	3.3	2.8	2.3
Project	5.4	4.5	3.8	3.3	3.7	3.0	3.0	2.5	2.1	1.7	1.5
Investment projects	2.3	1.8	1.8	1.8	1.8	1.5	1.3	1.1	0.9	0.8	0.7
Special programs	3.1	2.6	1.9	1.5	1.8	1.5	1.7	1.4	1.2	1.0	0.8
Budget support	3.6	3.4	2.0	2.1	1.8	2.0	1.8	1.5	1.2	1.0	0.9
Overall balance, after grants	-4.3	-5.3	-3.6	-4.2	-5.5	-6.7	-7.2	-6.7	-6.4	-5.8	-4.8
Net external financing	4.2	3.7	3.6	3.4	4.9	5.7	6.4	6.1	6.0	5.1	4.4
Disbursements	4.5	4.0	4.1	3.8	5.3	6.4	7.2	6.9	6.7	6.0	5.5
Project	2.6	2.9	1.7	1.7	1.9	4.0	4.6	4.2	4.0	2.9	2.6
Nonproject support	1.9	1.1	2.4	2.2	3.4	2.5	2.5	2.6	2.7	3.0	2.9
Loans to public enterprises	0.7	0.9	1.4	1.2	1.9	0.8	1.3	1.6	1.9	2.3	2.3
of which: nonconcessional	0.0	0.4	1.0	0.6	1.7	0.3	0.9	1.3	1.6	2.1	2.1
Budget support	1.2	0.2	0.9	1.0	1.5	1.6	1.2	1.0	0.9	0.7	0.6
Cash amortization	-0.3	-0.3	-0.5	-0.4	-0.4	-0.7	-0.8	-0.7	-0.7	-0.9	-1.1
Net domestic financing	0.0	1.6	0.0	0.7	0.6	1.0	0.8	0.6	0.4	0.7	0.4
Net privatization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Budgeted VAT refund (Actual till 2012)	0.5	0.8	...	0.8	...	0.8	...	...	...	...	...
Gross aid flows	13.5	11.8	8.8	8.8	9.0	11.2	11.0	9.6	8.4	6.6	5.7
Budget support	4.8	3.6	2.9	3.1	3.3	3.7	3.0	2.5	2.1	1.7	1.5
Nonbudget support	8.8	8.3	5.9	5.7	5.7	7.6	8.0	7.1	6.3	4.9	4.2
Project support	8.0	7.4	5.5	4.9	5.6	7.0	7.6	6.7	6.1	4.7	4.1
Concessional loans to public enterprises	0.7	0.9	0.4	0.7	0.2	0.5	0.4	0.3	0.3	0.2	0.2

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

[1] VAT presentation was changed to a net basis (collection minus requested VAT refunds). CR 13/1 showed gross VAT revenues and refunds as an expenditure item.

[2] Residual discrepancy between identified sources and uses of funds.

[3] Revenue minus noninterest current expenditure minus locally financed capital expenditure and locally financed net lending.

Table 4. Mozambique: Monetary Survey, 2010-13

	2010	2011	2012					2013				
			Q1	Q2	Q3	Q4		Q1		Q2	Q3	Q4
	Act.	Act.	Act.	Act.	Act.	CR/13/1	Act.	CR/13/1	Act.	Proj.	Proj.	Proj.
Bank of Mozambique												
Net foreign assets	56.9	56.9	55.4	60.0	72.9	75.9	73.1	77.3	64.9	68.3	77.7	81.9
(US$ billions)	1.7	2.1	2.0	2.1	2.5	2.4	2.5	2.4	2.1	2.2	2.5	2.6
Net international reserves	62.2	61.1	59.5	64.2	77.4	80.9	77.5	81.8	69.4	72.8	82.4	86.6
(US$ billions)	1.9	2.2	2.2	2.3	2.7	2.5	2.6	2.5	2.3	2.4	2.6	2.7
Net domestic assets	-25.2	-22.6	-24.5	-25.9	-36.2	-35.4	-32.0	-40.6	-27.2	-26.7	-33.0	-33.4
Credit to government (net)	-20.6	-26.8	-26.2	-28.6	-27.6	-26.7	-27.6	-27.9	-26.8	-29.1	-25.8	-38.5
Credit to banks (net)	0.4	-3.8	-4.7	-6.5	-16.3	-6.0	-12.7	-13.8	-1.6	-1.0	-8.3	2.6
Credit to the economy	0.5	0.9	1.0	1.0	1.1	0.9	1.3	1.0	1.2	1.2	1.2	1.2
Other items (net; assets +)	-5.6	7.1	5.5	8.1	6.7	-3.6	6.9	0.1	-0.1	2.3	-0.1	1.2
Reserve money	31.6	34.3	31.0	34.1	36.7	40.5	41.1	36.7	37.7	41.6	44.7	48.4
Currency in circulation	20.4	21.9	18.7	21.6	23.1	27.7	26.2	23.6	22.3	25.9	27.7	30.7
Currency outside banks	17.4	17.5	15.3	17.5	18.2	20.6	19.7	12.0	17.5	20.9	23.5	25.5
Currency in Banks (Cash in Vault)	3.1	4.4	3.5	4.1	4.8	7.1	6.6	11.6	4.8	5.0	4.3	5.3
Bank deposits in BM	11.2	12.4	12.2	12.5	13.6	12.8	14.8	13.1	15.4	15.8	17.0	17.7
Required reserves	10.8	11.4	11.4	11.7	12.2	...	13.6	...	14.6	15.1	15.7	16.5
Free reserves	0.4	1.0	0.8	0.7	1.4	...	1.2	...	0.8	0.7	1.3	1.2
Commercial Banks												
Net foreign assets	22.8	16.1	16.6	17.8	19.8	22.2	22.6	18.4	29.3	25.2	25.6	30.5
(Millions of U.S. dollars)	0.7	0.6	0.6	0.6	0.7	0.7	0.8	0.6	1.0	0.8	0.8	1.0
Net domestic assets	92.5	109.1	110.3	119.7	127.7	127.7	142.6	136.2	135.6	144.1	155.3	165.5
Banks' reserves	14.3	16.8	15.5	16.8	19.5	19.9	22.2	24.7	21.5	20.8	21.3	23.0
Credit to BM (net)	-0.3	4.0	6.2	6.2	16.6	6.0	12.3	13.8	8.4	1.0	8.3	-2.6
Credit to government (net)	8.4	21.1	22.2	26.0	17.9	21.9	27.5	23.0	19.8	18.0	21.9	33.9
Credit to the economy	91.9	97.3	98.1	101.9	105.8	114.9	114.9	115.1	121.1	128.9	131.2	140.0
Other items (net; assets +)	-21.8	-30.1	-30.0	-31.2	-32.1	-35.0	-34.3	-40.4	-35.3	-24.6	-27.4	-28.9
Deposits	115.3	125.3	126.9	137.5	147.5	150.0	165.3	154.6	164.9	169.3	180.9	196.0
Demand and savings deposits	73.0	79.1	79.3	86.8	94.9	94.7	108.4	97.7	103.3	104.7	113.2	123.8
Time deposits	42.3	46.2	47.7	50.7	52.6	55.3	56.8	56.9	61.6	64.6	67.7	72.2
Monetary Survey												
Net foreign assets	79.6	73.0	72.0	77.7	92.7	98.1	95.7	95.7	94.2	93.6	103.3	112.3
(US$ billions)	2.4	2.7	2.6	2.8	3.2	3.1	3.2	3.0	3.1	3.0	3.3	3.5
Net domestic assets	51.8	70.8	71.1	78.2	74.1	72.4	90.3	70.8	89.0	96.6	101.1	109.1
Domestic credit	80.2	92.6	116.2	100.4	97.2	111.0	116.2	111.0	115.4	119.0	128.5	136.7
Credit to government (net)	-12.2	-5.7	-4.0	-2.6	-9.7	-4.8	-0.1	-5.0	-6.9	-11.1	-3.9	-4.5
Credit to the economy	92.4	98.3	99.1	102.9	106.9	115.9	116.2	116.0	122.3	130.1	132.4	141.3
Cred. economy in foreign currency	-21.8	21.8	22.4	24.4	25.2	24.8	28.8	26.0	29.1	28.8	29.3	29.7
Other items (net; assets +)	-28.3	-21.8	-24.0	-22.2	-23.0	-38.6	-25.9	-40.2	-26.4	-22.3	-27.4	-27.7
Money and quasi money (M3)	131.5	143.8	143.1	155.9	166.8	170.5	186.0	166.6	183.2	190.2	204.4	221.4
Foreign currency deposits	46.2	38.1	39.6	42.7	47.2	45.0	53.3	45.4	55.0	52.6	55.5	63.5
(US$ billions)	1.4	1.4	1.5	1.5	1.6	1.4	1.8	1.4	1.8	1.7	1.8	2.0
M2	85.3	105.7	103.5	113.2	119.6	125.5	132.7	121.1	128.2	137.6	148.8	157.9
Memorandum Items												
Avg daily reserve money in 3rd month of quarter	31.8	33.3	30.8	33.4	36.0	39.3	40.3	36.5	38.0	40.8	43.8	47.5
12-month percent change	35.0	4.5	6.2	8.5	14.4	18.0	21.1	18.6	23.6	22.3	21.8	17.9
Avg daily currency in 3rd month of quarter	20.4	21.2	18.6	20.8	22.4	26.7	25.0	23.4	22.1	24.8	27.0	29.3
12-month percent change	30.1	3.7	7.6	10.9	13.3	26.3	18.0	25.6	18.8	19.7	20.2	17.1
NCG stock (prog def.)	-15.8	-12.5	-11.8	-10.6	-18.4	-9.0	-9.8	-9.4	-17.3	-15.7	-8.3	-8.9
NCG flow (prog def.) cum from end-year	-1.2	3.3	0.8	1.9	-5.8	0.1	2.9	0.5	-7.5	-5.9	1.5	0.9
12-month percent change												
Reserve money	29.2	8.5	8.1	11.2	15.6	18.0	19.7	18.6	21.7	22.3	21.8	17.9
M2	17.6	23.9	23.1	24.9	24.8	18.7	25.6	17.0	23.9	21.6	24.4	19.0
M3	22.8	9.4	10.7	20.1	25.5	18.6	29.4	16.4	28.0	22.0	22.5	19.0
Credit to the economy	29.3	6.4	6.7	9.0	12.6	17.9	18.3	17.1	23.5	26.4	23.9	21.5
Money multiplier (M2/reserve money)	2.70	3.08	3.34	3.32	3.26	3.10	3.23	3.30	3.40	3.30	3.33	3.26
Velocity (GDP/M2)	3.69	3.46	3.90	3.57	3.38	3.30	3.05	3.99	3.54	3.30	3.05	2.87
Nominal GDP	315	365	...	...	...	414	404	...	...	...	...	454
Nominal GDP growth	18.3	16.0	...	...	...	13.4	10.6	...	...	...	...	12.3
Policy lending rate (end-of-period)	15.5	15.0	13.75	12.50	10.50	...	9.50	...	...	...	...	...
T-bill 91 days rate	14.7	11.8	8.6	4.2	3.0	...	2.6	...	...	...	...	...

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

Table 5. Mozambique-Balance of Payments, 2010-18

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

	2010	2011	2012		2013		2014	2015	2016	2017	2018
	Act.	Act.	CR/13/1	Est.	CR/13/1	Proj.			Projections		
Current account balance	-1,113	-3,059	-3,924	-5,189	-4,153	-5,854	-6,608	-7,433	-7,988	-10,731	-9,890
Trade balance for goods	-1,179	-2,249	-3,140	-2,698	-3,055	-3,163	-3,140	-3,478	-3,073	-4,506	-3,447
Of which: Megaprojects	768	468	-641	34	-243	129	194	-253	489	-619	768
Exports, f.o.b.	2,333	3,118	3,644	3,470	4,229	3,950	4,774	5,966	6,750	7,695	9,342
Megaprojects	1,668	2,015	2,328	2,195	2,794	2,623	3,101	3,794	4,365	5,054	6,433
Other	665	1,103	1,316	1,275	1,435	1,326	1,673	2,172	2,384	2,641	2,909
Imports, f.o.b.	-3,512	-5,368	-6,784	-6,168	-7,284	-7,112	-7,914	-9,444	-9,823	-12,201	-12,789
Megaprojects	-900	-1,547	-2,969	-2,161	-3,037	-2,494	-2,906	-4,046	-3,877	-5,673	-5,665
Other	-2,613	-3,820	-3,815	-4,007	-4,248	-4,618	-5,008	-5,398	-5,946	-6,528	-7,125
Trade balance for services	-506	-1,482	-1,405	-3,210	-1,470	-3,225	-3,779	-4,092	-4,427	-4,956	-4,517
Income balance	-85	-190	-108	-40	-94	-23	-267	-404	-1,007	-1,770	-2,410
Of which: Dividend payments by megaprojects	0	-157	-10	0	-21	-17	-241	-304	-771	-1,384	-1,768
Current transfers balance	657	863	729	760	467	557	578	541	519	500	484
Of which: External grants	605	785	634	538	573	520	550	514	478	445	422
Capital and financial account balance	1,663	3,364	4,131	5,471	4,307	5,954	6,928	8,238	8,624	10,918	10,550
Capital account balance	346	432	401	426	434	384	387	394	403	415	435
Financial account balance	1,318	2,933	3,730	5,044	3,874	5,571	6,542	7,844	8,221	10,503	10,115
Net foreign direct investment	1,340	2,599	3,090	5,210	3,261	4,719	4,120	4,143	4,179	4,227	4,267
Net foreign borrowing by the general government	468	531	603	501	892	961	1,149	1,142	1,199	1,120	1,004
Net foreign borrowing by the nonfin private sector	-348	-39	-173	188	-384	-43	1,350	2,654	2,956	5,290	4,994
Other [1]	-142	-159	210	-854	105	-66	-78	-95	-114	-134	-150
Net errors and omissions	58	17	39	91	0	0	0	0	0	0	0
Overall balance	608	323	246	373	155	100	320	805	636	187	660
External financing	-58	-323	-246	-373	-155	-100	-320	-805	-636	-187	-660
Reserve assets [1]	-87	-321	-242	-369	-152	-97	-317	-770	-600	-152	-626
Net use of credit	18	-2	-4	-4	-3	-3	-3	-35	-36	-35	-34
Of which: Net use of Fund credit	20	-2	-2	-2	-3	-3	-3	-35	-36	-35	-34
Exceptional financing	10	0	0	0	0	0	0	0	0	0	0
Memorandum items:											
Current account balance (percent of GDP)	-11.7	-24.3	-26.9	-36.4	-26.3	-39.9	-41.3	-41.4	-39.8	-47.9	-39.5
Excluding external grants	-18.5	-31.2	-31.9	-41.8	-30.0	-43.4	-44.8	-44.3	-42.2	-49.9	-41.2
Net foreign assets	1,745	2,082	2,324	2,451	2,479	2,551	1,205	2,010	2,646	2,833	3,493
Net international reserves [1]	1,908	2,239	2,530	2,605	2,685	2,704	3,023	3,828	4,463	4,651	5,311
Gross international reserves [1, 2]	2,099	2,428	2,723	2,799	2,874	2,894	3,211	3,980	4,580	4,732	5,358
Months of projected imports of goods and nonfactor services	3.3	2.9	3.4	3.0	2.7	2.8	2.6	3.1	3.0	3.0	3.5
Months of projected G&S imports (excl. megaproject imports)	4.2	3.7	5.1	3.8	5.1	3.7	3.7	4.2	4.3	4.1	4.2
Percent of broad money (M2)	80.8	62.3	…	62.5	…	58.7	57.5	61.6	62.9	57.4	57.4

Sources: Data from Government of Mozambique and projections by IMF staff.

[1] Includes net portfolio investment and other investment assets.

[2] The ratio to short term debt is not presented due to availability of the data.

Table 6. Mozambique: Financial Soundness Indicators for Banking Sector, 2003–12

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Capital adequacy										
Regulatory capital to risk-weighted assets	16.5	18.0	13.4	12.5	14.2	13.9	15.1	14.4	17.1	17.9
Regulatory Tier I capital to risk-weighted assets	14.7	16.0	13.6	10.7	12.1	12.4	13.0	13.7	16.1	16.9
Capital (net worth) to assets	7.4	7.4	6.6	6.3	7.2	7.5	7.7	8.0	9.0	9.5
Asset composition and quality										
Foreign exchange loans to total loans	60.8	62.0	51.4	33.2	28.5	32.8	32.4	29.5	25.1	28.1
Nonperforming loans to gross loans [1]	13.8	5.9	3.5	3.1	2.6	1.9	1.8	1.9	2.6	3.2
Nonperforming loans net of provisions to capital [1]	8.8	3.8	1.9	3.6	0.5	2.5	5.9	5.6	6.6	6.8
Earnings and profitability										
Return on assets	1.4	1.5	1.9	4.0	3.8	3.5	3.0	2.6	2.5	1.9
Return on equity	18.6	20.6	26.9	60.8	50.7	44.7	36.6	32.9	26.5	19,.6
Interest margin to gross income	62.1	65.8	63.6	67.4	70.2	58.8	55.7	59.4	64.9	58.9
Noninterest expenses to gross income	81.9	81.6	75.2	60.2	60.8	58.7	58.4	59.7	61.3	66.1
Personnel expenses to noninterest expenses	42.4	43.1	43.5	42.6	46.3	45.1	45.9	45.5	47.1	49.1
Trading and fee income to gross income	37.9	34.2	36.4	32.6	29.5	40.5	44.3	23.8	17.2	19.5
Spread between reference loan and deposit rates (90 days, local currency)	17.4	14.9	13.8	14.6	11.1	10.7	11.1	10.3	11.4	…
Funding and liquidity										
Liquid assets to total assets [2]	45.2	38.3	31.1	33.9	36.0	36.2	27.9	22.4	27.8	33.4
Customer deposits to total (non-interbank) loans	193.6	205.0	177.6	169.5	184.9	165.7	138.2	131.2	131.6	143.8

Source: Bank of Mozambique (BM).

[1] Nonperforming loans are defined according to Mozambican accounting standards (they include only part of the past-due loans).

[2] Includes deposits at parent banks.

Table 7. Mozambique: Quantitative Assessment Criteria and Indicative Targets under the 2010-13 PSI 1

(Millions of meticais, unless otherwise specified)

	2012								2013			
	End-Sept Indicative Target			Status	End-Dec Assessment Criteria			Status	End-March Indicative Target			Status
	Prog.	Adj.	Act.		Prog.	Adj.	Act.		Prog.	Adj.	Act.	
Assessment Criteria for end-June/December												
Net credit to the central government (cumulative ceiling)	-745	-745	-5,823	M	52	52	2,707	NM	517	3,534	-7,488	M
Stock of reserve money (ceiling)	37,031	36,676	35,975	M	39,264	39,264	40,283	NM	36,495	36,495	38,048	NM
Stock of net international reserves of the BM (floor, US$ millions)	2,323	2,323	2,693	M	2,530	2,530	2,604	M	2,544	2,444	2,278	NM
New nonconcessional external debt contracted or guaranteed by the central government or the BM or selected state-owned enterprises with maturity of one year or more (cumulative ceiling over the duration of the program, US$ millions)[2]	1,500	1,500	1,379	M	1,600	1,600	1,387	M	1,600	1,600	1,387	M
Stock of short-term external debt contracted or guaranteed by the central government (ceiling)	0	0	0	M	0	0	0	M	0	0	0	M
External payments arrears of the central government (ceiling, US$ millions)[2]	0	0	0	M	0	0	0	M	0	0	0	M
Indicative targets												
Government revenue (cumulative floor)	69,687	69,687	73,619	M	99,043	99,043	98,615	NM	23,656	23,656	30,022	M
Priority spending (cumulative floor)	35,934	35,934	42,269	M	72,563	72,563	81,400	M	10,797	10,797	17,979	M

Sources: Mozambican authorities and IMF staff estimates.

[1] For definition and adjustors, see the Program Monitoring Section of the Memorandum of Economic and Financial Policies and the Technical Memorandum of Understanding.

Table 8. Mozambique: Proposed Quantitative Assessment Criteria and Indicative Targets under the Proposed 2013-16 PSI [1]

(Millions of meticais, unless otherwise specified)

	2013		
	End-June Assessment Criteria	End-Sept Indicative Target	End-Dec Assessment Criteria
	Proposed	Proposed	Proposed
Assessment Criteria for end-June/December			
Net credit to the central government (cumulative ceiling)	-5,858	1,504	895
Stock of reserve money (ceiling)	40,787	43,817	47,493
Stock of net international reserves of the BM (floor, US$ millions)	2,360	2,621	2,704
New nonconcessional external debt contracted or guaranteed by the central government or the BM or selected state-owned enterprises with maturity of one year or more (cumulative ceiling over the duration of the program, US$ millions) [2]	1,200	1,200	1,200
Stock of short-term external debt contracted or guaranteed by the central government (ceiling)	0	0	0
External payments arrears of the central government (ceiling, US$ millions)	0	0	0
Indicative targets			
Government revenue (cumulative floor) [3]	55,760	81,891	111,419
Priority spending (cumulative floor)	43,748	76,041	119,025

Sources: Mozambican authorities and IMF staff estimates.

[1] For definition and adjustors, see the Program Monitoring Section of the Memorandum of Economic and Financial Policies and the Technical Memorandum of Understanding.

[2] Net of verified VAT refund requests.

Table 9. Mozambique: Structural Benchmarks Under the Current PSI 2010-13

Structural Benchmarks	Expected Date of Implementation	Status
The Ministry of Finance will submit to the Council of Ministers the draft Financial Sector Development Strategy (FSDS), as described in ¶26 of the MEFP dated December 7, 2012.	End-December 2012	Delayed. Completed in March 2013.
The Bank of Mozambique will finalize the draft financial sector contingency plan, as described in ¶26 of the MEFP dated December 7, 2012.	End-March 2013	Delayed. Completed in early April.
The Government will adopt an Annual Borrowing Plan for 2013, as described in ¶20 of the MEFP dated May 10, 2012.	End-January 2013	Met.

REPÚBLICA DE MOÇAMBIQUE

Appendix I—Letter of Intent

Maputo, Mozambique
June 7, 2013

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

Dear Ms. Lagarde:

The Government of Mozambique requests the completion of the sixth review under the Policy Support Instrument (PSI) and approval of a successor PSI for 2013-16. We plan to cancel the current PSI at the time of the approval of the successor PSI. In support of this request we are transmitting the attached Memorandum of Economic and Financial Policies (MEFP), which reviews implementation of the current PSI and establishes policy objectives and indicator targets for the short and medium term to be adopted under the next program.

The new PSI will be based on the following four pillars:

(i) Consolidating macroeconomic stability in the context of natural resource exploration;
(ii) Attaining robust and more-inclusive growth;
(iii) Continuing institutional capacity-building in macroeconomic policy formulation and implementation; and
(iv) Strengthening governance and public sector transparency

The program is in line with our Poverty Reduction Strategy Paper (PARP) for 2011-14 and with our plans regarding its successor strategy.

The Government is of the view that the policies outlined in the MEFP are adequate to achieve the objectives of the PSI-supported program. We stand ready to take any additional measures necessary to achieve our policy objectives.

The Government will consult with the IMF on the adoption of these measures, and—at its own initiative or whenever the Managing Director requests such a consultation—in advance of any revision to the policies contained in the MEFP, in accordance with the Fund's policies on such consultation. The Government will provide the IMF with such information as the IMF may request to be able to assess the progress made in implementing the economic and financial policies and achieving the objectives of the program.

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

Sincerely yours,

/s/

Manuel Chang
Minister of Finance

/s/

Ernesto Gouveia Gove
Governor
Bank of Mozambique

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

Attachment 1—Memorandum of Economic and Financial Policies

June 7, 2013

1. This MEFP (i) describes recent developments and performance of the Government's economic program under the three-year PSI to date, and (ii) elaborates on economic and structural policy intentions for a new program under the PSI for 2013-16. It builds on the MEFPs underlying the initial PSI request of May 2010 and those for its five reviews, the last of which was completed in December 2012.

Recent Economic Developments and Performance under the Program

2. Mozambique's economy remains robust, despite a still-fragile world economic environment resulting from the financial crisis that shook the international economy and was exacerbated by the Euro zone sovereign debt crisis**.**

- **Economic performance.** Preliminary data for 2012 indicate that economic activity grew by 7.4 percent, in line with the growth forecast. This performance is explained by the expansion and rapid rise in coal production as well as in financial services, transport and communications, and agriculture, the last making a major contribution to GDP. Having said that, despite no preliminary estimates as yet for economic activity in the early months of the year, economic performance in the first quarter of 2013 is expected to be lower than the same period in 2012 due to the negative impact of floods in early 2013, which mainly affected the agriculture, electricity, mining, and transport and communications sectors.

- **Inflation** The annual inflation rate slowed from 5.5 percent at end-2011 to 2.2 percent at end-2012. However, the trend is expected to reverse in 2013, given the 5.1 percent rate posted in April. The 2012 deceleration in inflation was the result of the good harvest and attendant increase in food supply, the relative stability of the metical in relation to the leading currencies, favorable developments in international prices, and stable administered prices. Inflation is expected to increase mainly because of the rise in the prices of food, as result of the floods, and school fees in January-April 2013.

- **BOP developments in 2012 were dominated by operations related to the development of the LNG sector.** FDI jumped from \$2.6 billion in 2011 to \$5.2 billion in 2012 primarily as a result of the exploratory operations in the Indian Ocean in the north of the country where massive reserves of natural gas have been identified. Related imports of goods and services pushed the current account deficit from 24 percent of GDP in 2011 to 36 percent of GDP in 2012. Donor disbursements fell somewhat in terms of GDP from 10 to 7 percent. Traditional exports, mainly agricultural products, continued their strong performance increasing by almost 16 percent over 2011.

- **Net international reserves.** Due to these BOP developments, the country had a stock of reserves of \$2.6 billion at end-December 2012, equivalent to approximately to 3.8 months of projected imports of non-megaproject imports for 2013 compared to 3.7 months at the end of 2011. However, as of end-March 2013, weak foreign assistance disbursement (\$45 million against the $194 million expected) coupled with an increase in imports to make up the food shortages created by the floods and emergency infrastructure replacements, net international reserves (NIR) were down to $2.3 billion, around 3.1 months coverage of 2013 imports of goods and non-factor services.

3. Performance under the program has been broadly satisfactory, and the authorities largely complied with the quantitative goals for the period.

- **Four of the six end-December 2012 quantitative assessment criteria were met**, but not those for net credit to the Government (NCG) and reserve money (RM). The end-December 2012 average RM balance was Mt 40.3 billion, around Mt 1 billion above the target, a shift caused by higher than projected demand for money at the end of the year. For its part, in 2012, the overall flow of NCG was Mt 2.7 billion—above the programmed target of Mt 52 million—on account of a shortfall in revenue compared to the program target, and higher than planned investment spending, which is hard to predict.

- **Among the indicative targets for March 2013, the RM target was likewise** exceeded owing to continued high demand for broad money demand and limited scope for monetary intervention in the short term (including an increase in required reserves associated with higher government deposits, and a weak cash return to the banking system in the post-flood period). In contrast, NCG for March 2013 was within projections.

- **Nonconcessional borrowing.** The Government's total external non-concessional borrowing for 2012 was $1.2 billion, increasing the cumulative amount under the PSI to $1.4 billion, staying below the program's ceiling of $1.6 billion through end-June 2013. There was no additional non-concessional borrowing in the first four months of 2013. These loans are intended to finance only infrastructure projects with their own debt-servicing capacity.

- **All structural benchmarks were met, but with some delays.** The Annual Domestic Borrowing Plan for 2013 was approved on schedule in January 2013. The Financial Sector Contingency Plan was approved on April 2, 2013, two days later than planned. The Financial Sector Development Strategy, which was submitted to the Cabinet in March 2013 and was approved on April 9, 2013.

Implementation of the Poverty Reduction Strategy

4. We are committed to sustain our pursuit of more inclusive growth during and beyond the current Poverty Reduction Strategy (PARP 2011-14). The PARP aims to induce patterns of inclusive growth by increasing the allocation of funds for investment under the following pillars: (i) enhancing production and productivity in agriculture and fishing; (ii) creating employment; and (iii) enhancing social and human development. A review of its quantified indicators is underway to refine them, make them more relevant for assessing progress toward strategic aims, and ensure that they are all measurable and adequate for the new development challenges.

- **Enhancing production and productivity in agriculture.** Agriculture employs 78 percent of the economically active population and contributes 23 percent to GDP. Thus productivity increases and the expansion of areas under cultivation are key to improvements in the livelihood of the population. To this end, we have adopted an agricultural sector development strategy (PEDSA) for 2011-20 and just launched an agricultural investment plan (PNISA) 2013-17 that will help to gradually shift production from subsistence to commercial farming.

In 2012, there was progress in several areas:

- *Land use titles.* Land rights to 108 community areas were delimited, covering a total area of 1.6 million ha, mainly in the provinces of Niassa (48 communities with 1.2 million ha), Zambézia, (27), Gaza (16) and Nampula (6). Also, 56 communities were certified with and area of 0.1 million ha. This has allowed us to enforce community land use rights, reducing land conflicts and ensuring land use for agriculture and other productive purposes.

- *Productivity increases.* Soybean productivity increased by near 40 percent (1.17 tons per hectare against 0.85 ton per hectare programmed for the year). Twenty five percent of farmers had adopted new technologies, according to the 2012 agrarian Survey (TIA). The adopted technologies included the use of improved inputs (improved seed and mechanization) and vaccination of livestock.

- *Strengthening monitoring systems*. The Agrarian Statistics Master Plan, which was approved in 2012, combined with the Early Warning System and the TIA, provide a "statistical framework" to measure production and productivity more accurately and better assess progress under the PEDSA.

- **Creating employment.** In all, 270,267 formal sector jobs were created: 92,140 in the public sector and 178,127 in the private sector, of which more than half were for Mozambican miners to work in South Africa in line with bilateral agreements. While this figure exceeded the goal by 6 percent, it was 14 percent lower than in 2011 reflecting mainly the contraction in the South African mining sector affected by domestic events and the global financial crisis.

- **Establishment of the Labor Market Monitoring Group** (*Observatório do Mercado de Trabalho*). This forum of stakeholders on labor market issues will deepen interactions on the linkages between the demand and supply of jobs, and help improve employment policies and statistics. Views are being sought from other ministries and the regulations for its creation are expected to be approved in April 2013.

- **Improvement of the business climate will be crucial to attract more investors and enhance employment creation.** We have been working in partnership with the IFC since 2010 to assess and streamline business licensing requirements and procedures, and this work will continue. Milestones reached in 2012 included:

    - Parliamentary adopted a resolution authorizing the Government to establish bankruptcy rules for insolvent companies;

    - Cabinet Decree No. 5/2012 established simplified rules for licensing of companies in more than two hundred types of activities in one day;

    - The Integrated Citizen Services Platform (*e-BAU*) was launched. It will reduce the number of procedures, time, and costs involved in licensing and registering companies;

- The Decree 49/2004 on normal corporate licensing procedures, including a standard form to simplify the procedure for starting a business was amended by Council of Minister on May 21, 2013;

- The 2nd Strategic Plan to Improve the Business Environment was drafted and provides, among others, for the simplification of forms for starting and registering companies, and procedures for construction licensing. It is currently being aligned in discussions with the relevant line ministries, provincial governments, and the private sector and is expected to be submitted to the Council of Minister in June 2013 for approval in August 2013 (**structural benchmark**).

- **Enhancing social and human development.** Efforts to boost primary school enrolment continued. The school enrollment rate at age 6 in first grade increased by two percentage points relative to 2011, and net enrollment at age 7 is close to 100 percent. Significant strides in this regard have been the creation of an increasingly gender-equitable system, particularly in secondary schools, and progress in monitoring and evaluating student performance in primary schools. Also notable is the significant increase in age-appropriate enrollment at different levels.

- **Health sector**. The 2012-16 Health Strategy and the Monitoring and Evaluation plans were adopted recently that aim to push forward improvements in the still relatively weak public health system. We launched the Action Plan for Pharmaceutical Logistics and finalized the Pharmaceutical Logistics Strategy as a means to deal with the drug logistics crisis and emergency that had arisen in 2011. PFM systems in the sector have also strengthened with bi-monthly monitoring of the sector accounts.

Macroeconomic Policy

A. Economic Objectives

5. We expect growth in the medium term to remain high and robust, reflecting the boom in the extractive industry and hydrocarbon sector. However, the still-fragile world economic environment will constitute a risk to growth in the short term.

- Over the next five years, the increased contribution of coal production and exports; the implementation of significant infrastructure projects, including the liquefied natural gas plant; greater dynamism in the construction and transport and communications sectors, and continuing growth in other sectors could accelerate economic growth to rates between 7½ and 9 percent per year, in line with our objectives.

- As a result of temporary shocks to our economy, we expect to see inflation accelerate in 2013. However, we maintain our medium-term inflation objective of 5 to 6 percent per year.

- Developments in the external sector over the coming years will continue to be influenced by the emergence and development of new companies involved in direct foreign investment in mineral exploration. Thus, the current account deficit excluding grants could be around 45 percent of GDP, basically reflecting the increase in imports of goods and services to supply the large investments made by such enterprises, funded largely by FDI and private borrowing. We expect the import cover of international reserve cover to remain around four months of projected imports of non-megaproject goods and non-factor services.

B. Macroeconomic Policy Mix

6. We will continue with our current combination of fiscal and monetary policies with a view to maintaining macroeconomic stability in the medium-term and promoting structural reforms. We will also strengthen our macroeconomic planning tools and economic policy coordination within the government and with the BM.

7. Monetary policy will remain oriented toward achieving the objectives of keeping inflation low and stable, safeguarding the financial system, and encouraging lending to the economy. We will continue reforms to improve operations of the banking system and broaden further access to financial services for depositors as well as borrowers.

8. The tax and budget policy will continue to meet the objectives in terms of natural resource taxation, priority spending on infrastructure investment, health and education, and income redistribution. The medium-term fiscal framework (CFMP) for 2013-15 envisages moderate fiscal deficits, continued strong external support, and modest domestic financing needs. It demonstrates the Government's efforts to increase internal revenue generation capacity and cover the outlays necessary to keep its administrative machinery running with self-generated funds. The CFMP provides for a decrease in the overall fiscal deficit after grants from 8.6 percent to 7 percent between 2013 and 2015, and the Government will continue to give priority to concessional borrowing to finance the budget deficit. However, any recourse to nonconcessional loans must be within the approved ceiling and the funds must be used for investment in public infrastructure projects with a proven ability to generate financial and debt-servicing capacity, as evidenced in the summary description of the project.

9. We will also move forward structural and governance reforms to improve the business climate and facilitate job creation by the private sector and encourage activity outside the megaprojects. These address, on the one hand, the need to raise average labor skills and narrow the infrastructure gap, and on the other the need to facilitate business operations through, among others, more client-oriented taxpayer services, streamlining of licensing requirements, and the availability of credit and debtor information.

C. Monetary and Exchange Rate Policies

10. In the short term, monetary policy will aim to sustain economic growth while maintaining macroeconomic stability. We will continue to aim for reserve money growth slightly above nominal GDP growth to support financial deepening and the provision of credit to the economy, while maintaining inflation at 5-6 percent in the medium term.

11. Enhancing the framework for monetary policy operations remains a priority. The BM will focus on the following areas:

- ***Strengthening coordination with the Ministry of Finance.*** The BM and MF will continue to strengthen their coordination and exchange of information as envisaged in the

Memorandum of Understanding signed on March 25, 2011, with a view to improving liquidity management in the economy.

- **Developing the domestic repo market to help improve money market management and the liquidity of government securities.** Following the July 2012 approval of the legal framework, which made all treasury bills (BT) eligible for repo transactions and permitted secondary trading in BTs, the electronic platform (Meticalnet Module) was modified, enabling the launch on March 13 this year of the first primary market operation with fungible BTs. Further improvements in the Maticalnet for the secondary market are in progress, and are envisaged to be completed by end-June 2013.

- ***Continued coordination with the MF with a view to using government bonds (OTs) as security in the Interbank Money Market (MMI).*** The inclusion of OTs in the MMI became an integral part of a broader project to develop the government securities market (public debt market), the first phase of which was a diagnostic assessment of the conditions for its implementation. This was completed in November 2012 and identified a number of technical and legal constraints that will have to be removed in the course of 2013 ahead of implementation scheduled for early 2014.

- ***Transformation of the standing deposit facility into repo operations.*** A set of transactions designed and tested for this purpose is currently undergoing improvements and is scheduled for implementation in June 2013.

12. We continue to improve monetary policy formulation and implementation, and to communicate this. The publication of the quarterly monetary policy report as part of efforts to enhance monetary policy communication and transparency is now an established consolidated process. The fifth edition was published in April 2013. In terms of monetary policy implementation, the BM will continue to improve data collection and refine its inflation and liquidity forecasting models, as well as the analytical contents of its publications.

13. We remain committed to a flexible exchange rate regime. The BM will allow the exchange rate to adjust freely to evolving patterns of trade and financial flows and closely monitor developments in the real effective exchange rate vis-à-vis a broad basket of currencies, with a view to ensuring external competitiveness and a comfortable level of international reserves.

14. The Mozambican authorities remain committed to their obligations under Article VIII, sections 2, 3, and 4 of the Fund's Articles of Agreement. The BM will continue to monitor the implementation of the new foreign exchange regulations, its implementation norms, as well as the functioning of the foreign exchange market, with a view to avoiding practices that could be inconsistent with Article VIII principles. We will keep IMF staff informed of any developments that could potentially run against those principles.

D. Fiscal Policy

15. Fiscal policy aims at the creation of productive capacity in the country, reducing the vulnerability to external shocks, and fostering sustainable and inclusive economic growth and development. The 2013 Budget Law envisages an increase in the revenue ratio of 23.6 percent of GDP through continued improvements in revenue administration. The level of spending is budgeted at around 35.4 percent of GDP. The resulting deficit would be financed by external funds and domestic borrowing to the tune of 11.8 percent and 0.6 percent of GDP, respectively.

16. 2013 Budget Revision. In response to the floods in early 2013 that devastated a number of provinces in the southern, central, and northern regions of the country, leading to a slowdown in economic growth, the Government intends to submit a revised budget to the National Assembly in August 2013. This revision increases spending to mitigate the vulnerability of those affected and rebuild destroyed infrastructure. This will be funded by already realized windfall revenue on capital gains tax from sales of shares in hydrocarbon companies.

17. Use of potential further windfall revenue. Depending on activity between private parties involving the sale of shares in mineral/hydrocarbon projects, the government could receive further windfall revenue in 2013. The government intends to use such windfalls to advance the socio-economic development of the country. Existing budget rules allow the use of such fiscal space (i) to increase investment, including the contribution of public enterprises to complex PPP investments such as envisaged in the electricity sector, railway projects, and LNG, or (ii) to reduce government debt, e.g. reducing the stock of VAT refunds arrears.

18. Continuation of the wage policy. In 2013 the Government's wage bill is projected at about 10.4 percent of GDP to sustain the existing payroll, new hiring, and promotions and progressions with a major impact on the education, health, and justice sectors, notwithstanding the impact of other sectors. In the medium term wage policy reforms will continue to (i) advance the decompression of the salary structure and address equity issues through differentiated adjustments in minimum wage across sectors; (ii) strengthen the link between remuneration and productivity in various sectors; and (iii) slow down recruitment in non-priority sectors to create room for the needs of the priority sectors. These measures are intended to reduce the wage bill as a share of GDP to around 8.5 percent in the medium term**.**

19. Spending for priority sectors. The Government has given priority to significant spending on priority sectors, amounting to 72.3 percent of total expenditure, excluding interest on government debt and government financial operations, compared with 66.9 percent in 2012, in order to ensure the implementation of measures aimed at reducing rural and urban poverty rates through investments to boost national output capacity, productivity, and the competitiveness of domestic inputs. In recent years, the Government has given substantial attention to social protection, in particular measures to protect the most vulnerable. In this regard:

- **Enhancing social protection.** Earmarked government spending on social protection in the 2013 budget increased to Mt 1.7 billion (0.4 percent of GDP).[1] We expect to draw on additional World Bank financing for public works programs, for which pilot schemes have been under way. The Government has renewed its commitment to increasing budget appropriations to 0.8 percent of GDP over the medium term with the aim of reaching around 900,000 beneficiaries and raising the level of cash transfers to meet the poverty line over the coming years.

[1] Of particular note in this area is the increase in the monthly minimum basic welfare allowance from Mt 130 to Mt 253 per beneficiary.

- **Developing a more effective programmatic targeting system.** The government has begun to develop and test a set of operational tools to improve beneficiary selection and enhance the implementation of social-protection programs with the support of development partners. These include a common targeting system, a consolidated registry of beneficiaries, an information-management system, and a mechanism to redress complaints and grievances. The government has designed an innovative targeting system that combines geographical identification with community targeting to minimize exclusion errors and a proxy means-test instrument to minimize inclusion errors. The system will be tested in 2013 and will be used to select the beneficiaries of the PASP beginning in 2014.

- **Relief for the early-2013 floods.** To alleviate the impact of the natural disasters on the populations concerned, the Government will approve a Post-Flood Reconstruction Plan, which includes the following measures to be implemented over the next three budgets: actions on mitigation, resettlement and reconstruction of infrastructure (emergency and permanent replacement of infrastructures, roads, bridges, water and sanitation, railways, public administration buildings, enhancing flood resistance). We foresee the rehabilitation and construction of affected infrastructure in education and health; replacement of damaged furniture and equipment; and for the specific case of health, the replenishment of medical drug stocks.

- **Improving Infrastructure.** The Government is committed to spatial planning in rural areas and towns, and to regulate urban and peri-urban land use, with a target to demarcate 70,000 plots across the country. Major transport investments in the coming years include the ring road around Maputo; Beira – Machipanda road; the railway line from Moatize via Malawi to Nacala, the deep water port in Nacala, and the Nacala international airport. In the area of water and sanitation, we will focus on promoting sustainable water supply systems in rural areas, expansion of systems in all cities, and rehabilitation and construction of dispersed sources of water supply. The Government will also establish arrangements to monitor water entering Mozambique, and to rehabilitate levees defense platforms and strengthen areas prone to flooding and mitigation of floods and droughts.

- **In the area of education**, the Government's effort will be focused on building educational infrastructure and improving the quality of education by increasing financial resources, human and material, directly benefiting schools and improving student learning. Continued priority to universalization of Primary education, with a focus on learning and developing basic skills in reading, writing and numeracy.

- **In the health sector**, the government will improve the health network through the rehabilitation and expansion of primary, secondary, tertiary and quaternary networks. We will promote equal access to health care focusing on health of women and children and other vulnerable groups. Furthermore, we will improve the management of human resources, raising the level of humanization of services, control the impact of endemic diseases, and reduce malnutrition rates.

20. Energy subsidies.

- **Subsidies on petroleum products**. The Government will continue to monitor fuel prices in the international market and their appropriate framework in the domestic market. To ensure the sustainability of fuel provision activities, including the remuneration of providers, the Government aims to gradually eliminate blanket subsidies over the medium term, and target subsidies exclusively at vulnerable social segments.

- **Compensation to fuel importers.** The Government allocated around Mt 1.3 billion in the 2013 budget (0.3 percent of GDP) to pay fuel importers in compensation for fuel losses incurred in 2012.

- **Electricity tariffs.** The challenges facing the electricity sector include carrying out investments to develop energy production, transmission, and distribution infrastructure; advancing rural electrification to meet demand, which has been steadily rising in recent years as a result of the increasingly dynamic domestic economy; and re-establishing the financial sustainability of EDM, Mozambique's public electricity company. A tariff study has been prepared and proposed a tariff adjustment mechanism in each consumer segment. A proposal building on this is expected to be presented to the Council of Ministers in the first half of 2013. Other elements such as government transfers to EDM for investments in rural electrification are also under consideration.

Structural Reforms

A. Public Financial Management and Reporting

21. Public financial management remains a priority.

- ***Streamlining wage bill administration (expanding coverage of e-Folha and e-CAF).*** By end-June 2013, the Government will approve the action plan for the expansion of the electronic payroll system (including e-Folha) and of the integrated civil service database (e-CAF) **(structural benchmark)**. The e-CAF will enable the Government to make salary payments to civil servants and government agents by direct bank transfer, in particular those that do not meet the requirements for inclusion in e-Folha. The expansion of direct salary payments will include all institutions covered by e-CAF and with direct access to e-SISTAFE by end-December 2013 **(structural benchmark).**

- ***Strengthening expenditure execution processes.*** The electronic expenditure system (e-SISTAFE) is currently used largely for payment purposes. However, it is capable of handling the three separate phases of expenditure execution: *commitment* when an order for goods or services is made; *verification* when the delivery of goods and services received is confirmed and their value accepted as payment obligation; and *payment* when the payment obligation to the supplier is met. A pilot for the 3-step expenditure chain has been implemented for public debt servicing, and we plan to expand this practice to other expenditure areas/units starting in January 2014.

  Migrating to IPSAS-compatible reporting. Under the action plan to reform the public accounting system approved in October 2012, a proposal for new Accrual Accounting Rules in line with International Public Accounting Standards (IPSAS) will be elaborated by July 2013. The proposal will be open to public consultation in August; the Council of Ministers will consider it thereafter, and then submit it to Parliament for approval.

- ***Improving budget classification.*** We are working on the mapping of priority spending according to the PARP pillars through a more detailed budget classification by spending programs, and expect this to be completed by mid-2013 for the 2014 budget. In addition we have started to structure the presentation of spending according to programmatic classifiers to align it with the program structure of the Government's next Five Year Plan (Plano Quinquenal do Governo). As an intermediate step, we have updated the economic and the organic classification of expenditure for 2013 to allow a more detailed classification by expenditure units in our accounting system.

- ***Preparation of the new economic revenue classifier (CER).*** Preparation of the CER is underway and scheduled for conclusion by end-2013 for application in the next budgets. While the current CER aims to identify the nature of the revenue, the new classifier will identify the origin of funds according to the economic nature of the underlying activity, thereby affording greater precision, transparency, and consistency.

B. Investment Planning and Debt Management

22. The Government will continue to give priority to modernizing its debt management and investment planning procedures.

- ***Strengthening investment planning.*** The Ministry of Planning and Development (MPD) will submit by June 2013 the Integrated Investment Program (IIP) for Cabinet approval. The document will present a list of priority projects together with sufficiently specific information to analyze the impact of related borrowing on debt sustainability. (**structural benchmark**)

- ***Strengthening project selection tools.*** In February 2013, the MPD completed the Project Preparation Manual and template along with a form for a summary description of individual projects. The Project Management and Selection Committee will start using the Manual in July 2013 to analyze projects and, once Cabinet approved a particular project, will publish the template and summary description on the website with relevant information on that project. The Debt Management and Project Selection Committees will continue to provide training to key line ministries in the use of the new project selection tools and criteria.

- ***Enhancing debt management.*** The preparation of a Debt Sustainability Analysis is underway to serve as an input for the 2014 State Budget. The DSA is scheduled for completion by end-June 2013. The Government intends to incorporate the analysis of costs and risks associated with the public debt portfolio and borrowing plans over the medium term in the quarterly debt report, ensuring linkages with the State Budget and the Integrated Investment Program, as well as enhancing debt monitoring in line with the medium-term debt strategy (MTDS). The latter was last completed at end-2012 and is forward-looking policy tool to inform the selection of investment projects in light of the volume and composition of public debt, using cost-risk analysis consistent with the macroeconomic projections and the DSA.

- ***Advancing development of capital markets and first Annual Domestic Borrowing Plan for 2013.*** In order to promote public savings and stimulate domestic capital market development, a domestic borrowing plan will be prepared annually after the budget has been approved. The first such plan was approved and published in January 2013. Consistent with World Bank/IMF technical assistance recommendations for an auction strategy and determination of a yield curve for the state, as of 2013, Treasury bonds (T bonds) will be issued in several tranches per year and interest rates will be determined at auctions held at the stock exchange. Decree 5/2013 of March 2013 paved the way for the introduction of specialized Treasury bond dealers (OEOT). About ¾ of the total of 20 financial institutions invited to become OEOTs have accepted, facilitating the creation of a secondary market. The first primary T bond auction took place in April 2013 and was substantially oversubscribed.

C. Tax Policy and Administration

23. The modernization of tax administration will continue. The implementation of measures aimed at the widespread adoption of information and communication technologies for managing tax processes will remain a priority, both in customs and inland revenue, enabling increased coverage of potential taxpayers and broadening the tax base. It will also pay particular attention to taxation of the mining and hydrocarbon sectors as well as megaprojects more generally by building up institutional capacities to conduct dedicated monitoring and audits.

- **VAT administration and refunds.** The Government will follow up on April 2013 IMF technical assistance that studied VAT budgeting and proposed steps to resolve problems with VAT refunds. We are analyzing the recommendations as part of the overall budget planning process, and expect to devise a plan by October 2013 (**structural benchmark**) to gradually reduce the stock of pending refunds, avoid accumulating new ones, optimize the VAT administration and refund process. We expect to increase the budget allocation for VAT refunds in 2014 to avoid a further accumulation of pending refunds. We intend to submit any changes to the VAT law that may be needed to Parliament in time for application of VAT on a net basis beginning from the 2015 budget.

- **Implementing the single taxpayer database (NUIT) in the e-Tax Project.** The NUIT database in the framework of the e-Tax project is already available and the process of updating information on large taxpayers in all Unidades de Grandes Contribuintes (Large Tax Payer Units) is currently underway. The process is expected to be completed by end-June 2013. Expansion of the NUIT system to all computerized regional tax collection offices (DAFs) is underway on the same schedule. Information on all other taxpayers, whether individuals or legal entities, is being updated and should be completed in 2014.

- **Implementing tax payments through banks (e-Tax) for VAT and the simplified small taxpayer regime (ISPC).** Preparation of the business model for applying e-Tax to VAT/ISPC was completed in terms of legislative amendment, and IT adjustment is ongoing.[2] Its implementation is now being prepared with a view to launch a pilot in the first quarter of 2014. Actual tax payments through banks will only begin in a second phase that fully

[2]This involves changes to the Enterprise Tax and Policy management System (ETPM).

develops the VAT/ISPC module and a corresponding pilot is planned for the second half of 2014.

- **Simplifying the small taxpayers regime**. General ISPC regime provisions currently are rivaled in provisions for simplified regimes in the specific tax legislation for VAT, corporate and personal income taxes (IRPC and IRPS). A study on the overlaps and possible inconsistencies will be concluded by December 2013. The results of those studies will determine the next steps in order to streamline the system for taxpayers and the tax authority alike.

- **Strengthening the large taxpayers units (UGCs and DCAT).** The pilot scheme phase for the large taxpayers database installed in the Maputo UGC and the General Tax Directorate's (DGI) Technical Support and Coordination Department (DCAT) is currently underway. Installation in the remaining UGCs (cities of Beira and Nampula) is scheduled for Q4, 2013. The database will improve handling of information on the economic activities of large taxpayers and allow better monitoring.

- **Mitigating transfer pricing.** To mitigate transfer pricing, the government, with technical assistance from the IMF, is working on draft regulations which are expected to be completed in Q4, 2013. We also intend to adopt an action plan to implement the regulations and strengthen capacity building.

- **Revisiting bilateral double taxation agreements** (DTAs)**.** The Government is analyzing existing DTAs in order to identify possible weaknesses or areas that could lead to an unfair loss of revenues for Mozambique. We intend to negotiate the necessary adjustments with our partners.

D. Improving Earnings from Natural Resource Exploration

24. The Government will continue to strengthen its capacity to manage the country's rich natural resources and channel its benefits to the whole population. This involves improvements in several areas, including analytical tools, sector legislation and taxation, transparency, and the optimization of government participation in the mining and hydrocarbon sectors. The Government is receiving technical assistance in these areas from various development partners, and will supplement this with hiring specialized expertise where needed.

25. The Government is strengthening the statistical tools to help analyze developments and inform economic and social policy making and planning. This involves production statistics, national accounts, fiscal data, balance of payments and financial sector statistics, where INE, BM, MF, MIREM and other government bodies are working together.

26. Extractive Industry Transparency Initiative (EITI) and Transparency. Mozambique has now published three EITI reports in keeping with the country's laws, which reconcile payments made by previously selected companies in the mining and hydrocarbons sectors with the revenues reported by the government agencies in charge of their collection. The 2nd EITI report rated the country as compliant with the Initiative's rules. The inclusion of more enterprises in reconciliation reports is a reflection of growth in the country's extractive industry: the 1st first report covered only six enterprises, the 2nd and 3rd reports encompassed 36 and 46 enterprises, respectively. The 4th EITI reconciliation report on extractive industry payments and government receipts covers the financial year 2011 is currently under preparation and expected to be published by end-2013.

27. Mining and Petroleum Legislation. The Government approved the draft revisions to the mining and hydrocarbon laws in April 2013; the latter of which includes legal provisions for infrastructure concessions to allow for LNG development. Public consultations were held, including through web-posting of the draft laws. This legislation is going to be submitted to Parliament shortly. The existing legislation on public-private partnerships (PPPs) envisages the publication of PPP contract, and this will also be applied to mining and hydrocarbon contracts. Once the new laws are approved, the Government will update the related regulations within 6 months. The government expects to issue tenders for new hydrocarbon exploration areas only after the approval of the revisions to the hydrocarbon law.

28. Enhancing the mining and hydrocarbon fiscal regime. We continue to work on revisions to the fiscal regimes applicable to the mining and hydrocarbon sectors with technical assistance from the IMF and other donors. We have launched the public consultation process in May 2013, and are confident of submitting both bills to Parliament in August 2013. We are also requesting further technical assistance on constructing revenue forecasting tools and administrative capacity.

29. Participation of public enterprises in mining and hydrocarbon development. In the case of oil and gas the state hydrocarbon company ENH participates in PPPs. While this participation is typically on a full carry basis during the exploration period, we are still considering the type of involvement of ENH in the development and production phases with a view to maintaining debt sustainability and managing risks.

E. Management of Public Enterprises

30. Strengthening supervision of public enterprises. Following the adoption of the Public Enterprises Act (Law 6/2012 of February 2012), the Government has enhanced its monitoring of the activities of public enterprises in order to reduce fiscal risk and integrate it in the MTDS. The aim is improving governance and strengthening accountability, as well as ensuring that investment and borrowing plans are assessed and approved in advance by the sector ministry and financial oversight unit in the MF.

31. Ensuring transparency in public enterprise management. With a view to increasing transparency in the management of public companies in line with the Public Enterprises Act, the Government will ensure that the 2012 reports and accounts (including audit reports) of four large state-owned companies are published in 2013, and annual publication is continued in the future.

32. The Government's strategy with respect to the participation of large public enterprises in large infrastructure investments is under elaboration. Such companies/projects include the railway CFM in the construction of new railroads and ports (Nacala line, Nacala and Techobanine ports), ENH in hydrocarbon projects as discussed above, and EDM in electricity generation, transmission and distribution (Mphanda Nkuwa hydropower station and backbone transmission line, Ressano Garcia gas-fired power station with Sasol), and many potential others. The government will carefully manage the participation of state enterprises in order to mitigate risks and keep public debt sustainable.

F. Good Governance Framework

33. The Government continues its efforts toward good governance and fighting corruption. The issues are complex and have been at the center of our dialogue with development partners, involving legislation (anti-corruption package) and its implementation as well as reforms of the justice system and law-enforcement. The Judiciary continues to investigate all allegations of corruption received.

34. In 2012 the Government submitted to Parliament the remaining two laws of the anti-corruption package, which are awaiting approval, namely (i) the revised and consolidated Criminal Code and (ii) the revised Criminal Procedure Code. To guide implementation of the package, a costed action plan is being prepared with a first draft expected in June 2013.

35. The three other elements of the anti-corruption package already adopted are (i) the Public Probity Law, (ii) the law on Whistleblowers and witness protection, and (iii) changes to the organic laws of the prosecution service and Judiciary. These came into effect in November 2012 and advances have been made to address conflicts of interest and enforce mandatory asset declarations for those holding public office. Ethics Commissions in each public agency are tasked with the internal follow-up, and a Central Public Ethics Commission was set up in February 2013.

Financial Sector Policies

A. Financial Sector Surveillance

36. The BM will continue reforms aimed at enhancing financial sector surveillance despite the difficult global environment. It remains focused on:

- ***Strengthening banking supervision with a view to mitigating and preventing systemic risk:*** A sample of lending institutions' data was collected for conducting the first stress tests, with the expectation that this exercise will be performed by a designated team as part of the quarterly surveillance process from July 2013 on, including with the respective report on stress tests results. In this context, the regulation pertaining to nonperforming loan accounting will be revised in June 2013 to make it internationally comparable, followed by the revision of the regulation on concentration limits before September 2013, including banks' placements abroad, and modified reporting requirements. Likewise with a view to strengthening surveillance, the risk management guidelines and the legal and analytical framework for risk-based surveillance were adopted on March 14, 2013, and will be put into practice in the course of 2013, on track for the adoption of Basel II Capital Accord in 2014.

- ***Completion of the financial sector contingency plan.*** The package of rules governing the Contingency Plan and Emergency Liquidity Assistance was completed and approved in early April 2013 (**existing structural benchmark**) with a short delay. The underlying legal provisions were published in April 2013. Implementation will start in June, including the preparatory work to conduct simulation exercises with the help of the World Bank.

- ***Making the Deposit Insurance Fund (DIF) operational.*** The DIF's social capital has been approved and fully constituted and the members of the DIF's Executive Board have been appointed in April 2013. The DIF will become operational once the funding from KfW is disbursed, and this process was completed with the appointment of the Executive Board in May 2013.

B. Financial Sector Development

37. We will step up our efforts to improve financial inclusion as part of Mozambique's Financial Sector Development Strategy (FSDS) for 2013-2022. In April 2013, the Cabinet approved the FSDS. Its main objectives are to (i) maintain financial sector stability through improving the fiscal and monetary policies and deepening the government debt market, strengthening the bank supervision and regulation and the financial sector safety nets, and developing the insurance and pension sectors; (ii) increase access to financial services by eliminating structural impediments in the economy in general, and specifically in financial intermediation, particularly those that limit access to credit and increase the costs and risks of providing credit and financial services; and (iii) increase the supply of private capital to support private sector development by improving the mobilization and investment of long-term funds, including PPPs, and supporting the development of the domestic capital market, and the role and capacity of the Mozambique Stock Exchange (BVM). A dissemination plan on the FSDS was approved by the Minister of Finance in May 2013, including workshops and seminars planned for June 2013. Key priorities include:

- ***Establishing private credit registry bureaus***. A law on the creation of private credit registry bureaus was drafted in November 2012 and is expected to be submitted to the Parliament by November 2013. **(structural benchmark)**

- ***Promoting mobile banking.*** Specific regulations governing mobile banking services are under preparation by a task force at the BM and expected to be completed by end-September 2013. Given the dynamic nature of these particular services, an operator has already been licensed, with the licensing of a second operator in progress.

- ***Encouraging banking competition.*** We will foster competition in the banking sector by (i) introducing laws and regulations that address anti-competitive practices, (ii) fostering transparent pricing for financial services to allow consumers to compare costs, and (iii) introducing low-cost online access to credit files. A consumer protection framework will be designed and outreach will promote financial awareness so as to allow consumers (including SMEs) to make better use of available financial services; to encourage competition and innovation amongst financial services providers; and to provide consumers with reasonable protections against unfair business practices, while ensuring financial institutions' soundness.

- ***Strengthening the insolvency framework***. An Insolvency Bill was prepared, and Parliament authorized the government to develop the legal basis for insolvency proceedings. It is expected that this legislation will be adopted in 2013.

- ***Collateral framework***. We will work on a Collateral Bill with an eye to establishing a moveable collateral registry.

C. Money Laundering and Terrorism Financing

38. The AML/CFT framework continues to be improved. A draft AML/CFT law was approved by Parliament on May 16, 2013. Under the new law the financing of terrorism is considered a crime.

39. Progress in developing the AML/CFT legal framework. The government is pursuing a plan for implementing the FATF standards approved by the FATF-style regional body (ESAAMLG). It will build on the recommendations of an IMF Legal Department mission of April 2013 and the technical assistance action plan for eliminating shortcomings identified in the legal system; supervision of financial institutions and Designated Non-Financial Business Professions (DNFBP), Legal Persons and Arrangements; and international cooperation matters. The mission also provided introductory training on surveillance under a risk-based approach for staff from the various institutions involved in combating money laundering.

D. Payment System

40. The BM will further enhance financial stability and promote market development through reforms in the national payment system. In pursuing this objective, the BM will continue to focus mainly on oversight practices and development of the retail payment systems:

- ***Enhancing oversight practices.*** The BM approved a payment systems oversight policy strategy in March 2012 and will finalize and implement and oversight function by end-November 2013 (**structural benchmark**). Key actions would include (i) the implementation of an oversight manual, and (ii) the start of the operations of an oversight unit. The revised regulation of the electronic clearing system (CEL) for checks will also be approved and published by end-June 2013.

- ***Developing the retail payments network shared by the BM and commercial banks.*** The interbank retail payments network (SIMO) has been developed and successfully tested. Two banks are currently linked to the network and expanding their services, while the remaining banks are either conducting tests or adjusting their systems with a view to linking to the SIMO network. We expect the platform to cover the major banks operating in the market and handle domestic retail transactions by end-November 2013.

Program Monitoring

41. The proposed assessment criteria and indicative targets up to December 2013 are shown in Table 1. Table 2 provides a list of the proposed structural benchmarks. The first PSI review is expected to be completed in December 2013, and the second PSI review by end-June 2014.

Table 1. Mozambique: Quantitative Assessment Criteria and Indicative Targets under the 2010-13 PSI [1]

(Millions of meticais, unless otherwise specified)

	2012								2013			
	End-Sept Indicative Target			Status	End-Dec Assessment Criteria			Status	End-March Indicative Target			Status
	Prog.	Adj.	Act.		Prog.	Adj.	Act.		Prog.	Adj.	Act.	
Assessment Criteria for end-June/December												
Net credit to the central government (cumulative ceiling)	-745	-745	-5,823	M	52	52	2,707	NM	517	3,534	-7,488	M
Stock of reserve money (ceiling)	37,031	36,676	35,975	M	39,264	39,264	40,283	NM	36,495	36,495	38,048	NM
Stock of net international reserves of the BM (floor, US$ millions)	2,323	2,323	2,693	M	2,530	2,530	2,604	M	2,544	2,444	2,278	NM
New nonconcessional external debt contracted or guaranteed by the central government or the BM or selected state-owned enterprises with maturity of one year or more (cumulative ceiling over the duration of the program, US$ millions) [2]	1,500	1,500	1,379	M	1,600	1,600	1,387	M	1,600	1,600	1,387	M
Stock of short-term external debt contracted or guaranteed by the central government (ceiling) [2]	0	0	0	M	0	0	0	M	0	0	0	M
External payments arrears of the central government (ceiling, US$ millions) [2]	0	0	0	M	0	0	0	M	0	0	0	M
Indicative targets												
Government revenue (cumulative floor)	69,687	69,687	73,619	M	99,043	99,043	98,615	NM	23,656	23,656	30,022	M
Priority spending (cumulative floor)	35,934	35,934	42,269	M	72,563	72,563	81,400	M	10,797	10,797	17,979	M

Sources: Mozambican authorities and IMF staff estimates.

[1] For definition and adjustors, see the Program Monitoring Section of the Memorandum of Economic and Financial Policies and the Technical Memorandum of Understanding.

[2] Assessed on a continuous basis.

Table 2. Mozambique: Proposed Quantitative Assessment Criteria and Indicative Targets under the Proposed 2013-16 PSI [1]
(Millions of meticais, unless otherwise specified)

	2013		
	End-June Assessment Criteria	End-Sept Indicative Target	End-Dec Assessment Criteria
	Proposed	Proposed	Proposed
Assessment Criteria for end-June/December			
Net credit to the central government (cumulative ceiling)	-5,858	1,504	895
Stock of reserve money (ceiling)	40,787	43,817	47,493
Stock of net international reserves of the BM (floor, US$ millions)	2,360	2,621	2,704
New nonconcessional external debt contracted or guaranteed by the central government or the BM or selected state-owned enterprises with maturity of one year or more (cumulative ceiling over the duration of the program, US$ millions)[2]	1,200	1,200	1,200
Stock of short-term external debt contracted or guaranteed by the central government (ceiling)[2]	0	0	0
External payments arrears of the central government (ceiling, US$ millions)[2]	0	0	0
Indicative targets			
Government revenue (cumulative floor)[3]	55,760	81,891	111,419
Priority spending (cumulative floor)	43,748	76,041	119,025

Sources: Mozambican authorities and IMF staff estimates.
[1] For definition and adjustors, see the Program Monitoring Section of the Memorandum of Economic and Financial Policies and the Technical Memorandum of Understanding.
[2] Assessed on a continuous basis.
[3] Net of verified VAT refund requests.

Table 3. Mozambique: Structural Benchmarks Under the Current PSI 2010-13		
Structural Benchmarks	**Expected Date of Implementation**	**Status**
The Ministry of Finance will submit to the Council of Ministers the draft Financial Sector Development Strategy (FSDS), as described in ¶26 of the MEFP dated December 7, 2012.	End-December 2012	Delayed. Completed in March 2013.
The Bank of Mozambique will finalize the draft financial sector contingency plan, as described in ¶26 of the MEFP dated December 7, 2012.	End-March 2013	Delayed. Completed in early April.
The Government will adopt an Annual Borrowing Plan for 2013, as described in ¶20 of the MEFP dated May 10, 2012.	End-January 2013	Met.

Table 4. Mozambique: Structural Benchmarks Under the Proposed PSI 2013-16

	Structural Benchmarks	Expected Date of Implementation
1.	Government approval of the action plan for the expansion of the electronic payroll system (including e-Folha) and of the integrated civil service database (e-CAF). (¶21)	End-June 2013
2.	Completion of the expansion of salary payments by direct bank transfer to all institutions covered by e-CAF and with direct access to e-SISTAFE. (¶21)	End-December 2013
3.	Submission of Integrated Investment Plan to the Council of Ministers with sufficient specific information to analyze the impact of the related borrowing on debt sustainability. (¶22)	End-June 2013
4.	Submission of the 2nd Strategic Plan to Improve the Business Environment to the Council of Ministers (¶4)	End-August 2013
5.	Submission to Parliament of draft law on the creation of private credit registry bureaus. (¶37)	End-November 2013
6.	Staffing a payment systems oversight unit in the BM and begin operations by end-November 2013. (¶40)	End-November 2013
7.	Preparation of a plan to gradually reduce the stock of pending VAT arrears, avoid accumulation of new arrears, and optimize the administration and refund process. (¶23)	End-October 2013

Attachment 2—Technical Memorandum of Understanding

June 7, 2013

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

Definitions

A. Net credit to the central government

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

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

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

B. Government revenue and financing

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

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

C. Priority social spending

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

D. Reserve money

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

E. Net international reserves

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

F. New nonconcessional external debt contracted or guaranteed by the central government, the BM, and selected state-owned enterprises, with maturity of more than one year

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

11. The ceiling applies to external debt with original maturity of one year or more and with a grant element below 35 percent. The grant element is calculated using currency-specific discount rates based on the Organization for Economic Cooperation and Development (OECD) commercial interest reference rates in accordance with the annual Budget Law.

12. The term 'debt' will have the meaning set forth in Point 9 of the Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements adopted on August 3, 1979, as amended August 31, 2009, effective December 1, 2009. The concept of external debt is defined on the basis of the residency of the creditor. This assessment criterion is defined cumulatively from the beginning of the program and will be assessed on a continuous basis.

G. Stock of short-term external debt contracted or guaranteed by the central government

13. The central government will not contract or guarantee external debt with original maturity of less than one year. This assessment criterion applies to debt as defined in Point 9 of the Guidelines on Performance Criteria with Respect to External Debt in Fund Arrangements adopted on August 3, 1979, as amended August 31, 2009, effective December 1, 2009. The concept of external debt is defined on the basis of the residency of the creditor. Excluded from this assessment criterion are short-term, import-related trade credits. This assessment criterion will be assessed on a continuous basis.

H. External payments arrears of the central government

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

I. Foreign program assistance

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

J. Actual external debt service payments

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

Adjusters

A. Net international reserves

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

- downward by the shortfall in external program aid less debt service payments (up to US$100 million), compared to the program baseline (Table 1);
- downward/upward for any revision made to the end-year figures corresponding to the previous year; and

- downward to accommodate higher external outlays because of natural disasters, up to US$20 million.

B. Net credit to central government

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

- upward by the shortfall in the MT value of external program aid receipts less debt service payments (up to the MT equivalent of US$100 million at exchange rates prevailing at the respective test dates), compared to the program baseline (Table 1);
- downward by privatization proceeds in excess of those envisaged in the program, unless these proceeds are deposited in the government's savings accounts abroad;
- downward (upward) for any increase (decrease) in domestic financing from the nonfinancial private sector; and
- upward to accommodate the higher locally-financed outlays because of natural disasters, up to the MT equivalent of US$20 million at exchange rates prevailing at the respective test dates.

C. Reserve money

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

Data and Other Reporting

20. The Government will provide Fund staff with:

- monthly and quarterly data needed to monitor program implementation in relation to the program's quantitative targets and broader economic developments;
- weekly updates of the daily data set out in Table 1;
- weekly data set out in Table 4 of the TMU dated May 26, 2005;
- monthly updates of the foreign exchange cash flow of the BM;
- monthly data on government revenues (in detail according to the fiscal table) with a lag not exceeding one month;
- monthly data on verified VAT refund requests;
- monthly information on the balance of government savings accounts abroad;
- monthly data on domestic arrears;
- monthly data on external arrears;

- monthly budget execution reports (that will also be published) with a time lag not exceeding 45 days;
- the "mapa fiscal" with a time lag not exceeding 60 days;
- monthly monetary survey data with a time lag not exceeding 30 days;
- monthly data on gross international reserves, with the composition by original currencies and converted to US dollars at the actual exchange rates; and
- quarterly balance-of-payments data with a time lag not exceeding 65 days;
- monthly disbursements on the nonconcessional Portuguese credit line with a time lag not exceeding 30 days.

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

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

TMU Table 1. Mozambique: Net Foreign Assistance, 2012-13

	2012				2013			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Act.	Act.	Act.	Act.	Prel.	Proj.	Proj.	Proj.
Net foreign program assistance (US$ mn)	91	114	128	-5	-5	230	102	45
Gross foreign program assistance	118	141	155	21	37	271	144	86
Program grants	118	32	125	21	37	191	34	36
Program loans	0	109	30	0	0	80	110	50
External debt service	27	27	27	27	41	41	41	41
Cumulative net foreign program assistance in US dollars	91	205	334	328	-5	225	328	373
Gross foreign program assistance	118	259	414	435	37	307	451	537
External debt service	27	53	80	107	41	82	124	165
Net foreign program assistance (MT mn)	2,578	3,274	3,767	-64	-59	6,848	3,169	1,366
Gross foreign program assistance	3,221	3,946	4,432	627	1,105	8,274	4,472	2,737
Program grants	3,221	900	3,569	627	1,105	5,823	1,047	1,150
Program loans	0	3,046	863	0	0	2,451	3,426	1,587
External debt service	643	672	666	691	1,164	1,426	1,303	1,371
Cumulative Net foreign program assistance in MTN millions	2,578	5,852	9,619	9,555	-59	6,789	9,959	11,324
Gross foreign program assistance	3,221	7,167	11,599	12,225	1,105	9,379	13,851	16,588
External debt service	643	1,314	1,980	2,670	1,164	2,590	3,893	5,264

Source: Mozambican authorities and IMF staff estimates.

Appendix II—Mozambique: The Impact of Megaprojects on Growth and fiscal Revenue

Along with agriculture, "megaprojects" have played an important role in the postwar development of the Mozambican economy. With the start of operations of coal mining in Tete in 2011 and the upcoming expansion of natural gas production, they bear the potential to radically transform the structure of the Mozambican economy within a decade. Preliminary estimates suggest that coal and natural gas production could potentially boost growth by 2 percentage points annually during 2013-23. While fiscal revenues from megaprojects will remain moderate in the medium term, revenues could reach a quarter of total fiscal revenues in the long term, mostly from the natural gas sector.

Overview of Megaprojects

1. Starting with Cahora Bassa and Mozal, megaprojects have made an important contribution to Mozambique's economic success over the past two decades. Megaprojects are large, generally foreign-owned, and capital-intensive enclave activities that rely on extracted resources and/or imported intermediate goods, and export almost all of their production. Currently six megaprojects operate in Mozambique (Table 1 and Figure 1): (i) the hydro-power station Cahora Bassa; (ii) the Mozal aluminum smelter; (iii) the Sasol on-shore natural gas extraction; (iv) the Kenmare heavy sands project; (v) the Vale coal mine; and (vi) the RioTinto coal mine. Several potential new megaprojects are currently in the exploration or development stage, including : (i) off-shore oil and gas exploration by Anadarko, ENI, Statoil and Petronas; (ii) the hydro-power dam Mphanda Nkuwa 60 km downstream from Cahora Bassa, and "backbone" transmission lines to South Africa, neighboring countries and for domestic distribution; (iii) JSPL and Beacon Hill coal exploration; and (iv) exploration of heavy sands in the South of Mozambique.

2. Most of the current and planned megaprojects are in the extractive industries. Mozambique is rich in a variety of mineral resources, and the country has been extracting natural gas and heavy sands since the mid-2000s. However, it is the discovery of large coal deposits in Tete, the Central-Western region of the country, and the recent discovery of enormous off-shore gas fields in the Rovuma Basin, South of the border with Tanzania, that has put Mozambique on the world stage for mineral and hydrocarbon-fuel production and has the potential to radically transform the structure of the Mozambican economy. There are over 32 billion tons of confirmed *coal deposits* in Mozambique; full exploitation of these resources could make the country one of the world's leading coal exporters.[1] Confirmed *gas reserves* in the Rovuma Basin currently amount to 130 trillion cubic feet (comparable with Norway), and further discoveries of substantial commercial value are expected in the near future. Thus Mozambique could become a major exporter of natural gas over the medium term.

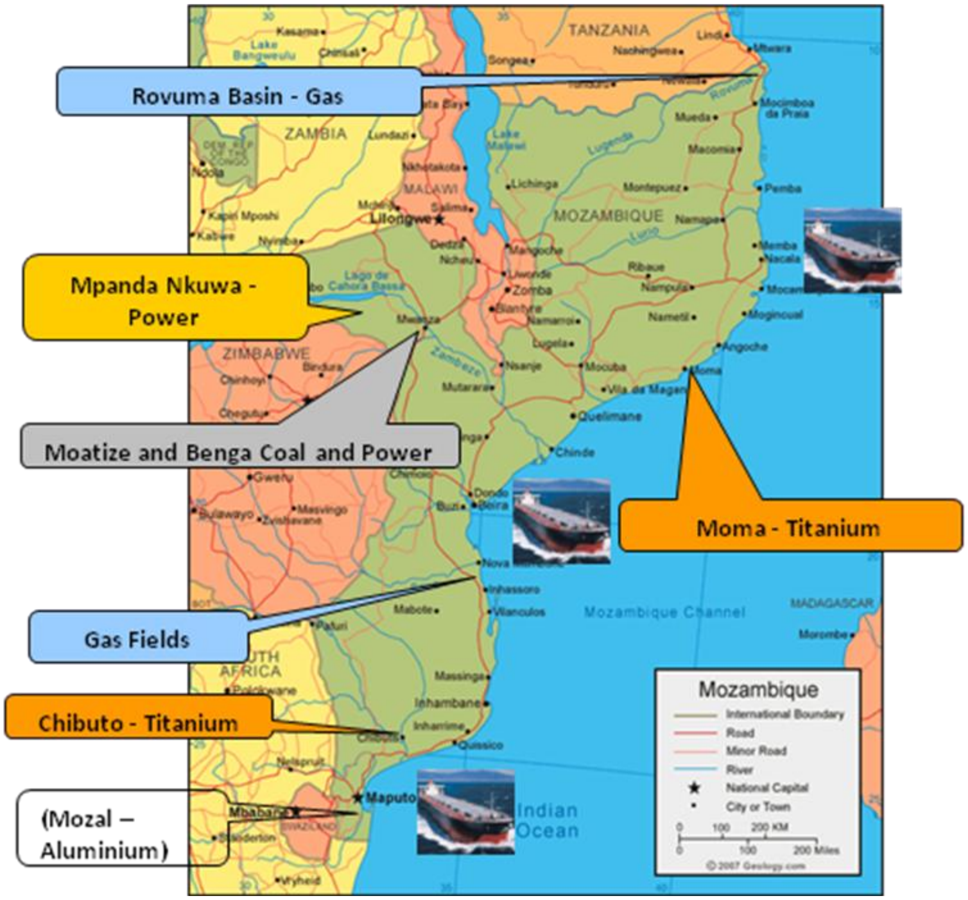
[1] Global coal production was 7.7 billion tons in 2011, about half of which was consumed by China.

Table 3.1: Mozambique: List of Megaprojects

	Company name	Sector	Location (city, province)	Capacity/reserves	Construction	Production
Current and extensions under consideration						
1	Hydroelectrica Cahora Bassa (HCB)	electricity generation	Cahora Bassa, Tete			
	HCB			2,075 MW	1995-97	1998
	HCB_North			1,240 MW		
2	Mozal	aluminium smelter	Beluluale Industrial Park, Maputo			
	Mozal I			245 thousand tons	1998-2000	2000
	Mozal II			245 thousand tons	2001-2003	2003
	Mozal III					
3	Sasol	natural gas	Pande and Temane gas fields, Inhambane	154 GJ	2002-2004	2004
	50% expansion			183 GJ	2011	ramp up by 2016
4	Kenmare	heavy sands	Moma, Nampula	600 thousand tons	2004	2007
	50% expansion			300 thousand tons	2011-2012	2013
5	Vale (CVRD)	coal	Moatize mine, Tete	25 million tons per year	2007-2011	2011
6	Rio Tinto	coal	Benga mine, Tete	45 million tons per year	Acquisition in 2011	2012
7	JSPL	coal	Changara district, Tete	10 million tons		2012-2016 ramp up
8	Beacon Hill	coal	Moatize, Tete	87 million tons of reserve	Acquisition in 2010	2013
Under consideration						
1	Mphanda Nkuwa	electricity	Zambesi river, Tete	1500 MW	2014-18	2018
2	Anadarko (US)	natural gas	Rovuma basin	10 million tons per year	2014-19	2020
3	ENI (Italy)	natural gas	Rovuma basin	10 million tons per year	2014-19	2020
4	Statoil (Norway)	natural gas	Rovuma basin			
5	Petronas (Malaysia)	natural gas	Rovuma basin			
6	Minas de Revuboè	Coal	Revuboe, Tete	5 million tons per year	2013-2015	2016
7	Ncondezi (integrated mine and power plant)	Coal and thermal power	Tete	1.2 million tons per year / 300 MW	2015	2016 (mine), 2017
8	Baobab Resources	Iron ore	Tenge/Ruoni deposit, Tete	725 million tons		
9	ENRC					
	Coal transport logistics	Rail line	Tete	40 million tons per year	2014-2015	2016
	Coal mines	Coal	Tete	20 million tons per year	2014-2015	2016
10	Corridor Sands	heavy sands	Chibuto, Gaza province			

Source: Mozambican authorities, and project operators.

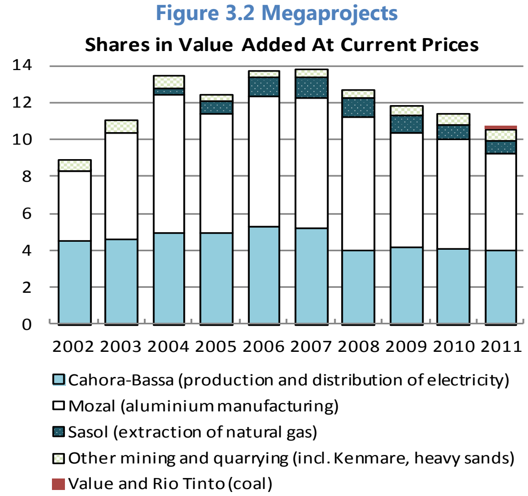
Figure 3.1: Mozambique: Megaprojects



Source: The World Bank (2013).

3. Historically, a 2-4 percentage point p.a. boost to economic growth was observed in the years when a major megaproject started production.[2] These include the period 1998-99 (the re-launching of power generation at Cahora Bassa) and the period 2001-03 (the launch of Mozal). After Sasol in March 2004, no major megaproject was launched until 2011, and the share of megaprojects in value added was relatively stable (Figure3.2).

Figure 3.2 Megaprojects



Contribution to Nominal GDP, 2002-2011

4. Megaprojects' contribution to fiscal revenues has been low in the past. The tax regime for megaprojects and the extractive industries has evolved over time. The authorities' primary motive for the first megaprojects was to

[2] See IMF Country Report No. 11/350, Appendix II: "The Impact of Megaprojects on Growth in Mozambique", http://www.imf.org/external/pubs/ft/scr/2011/cr11350.pdf.

establish Mozambique as an attractive destination for foreign investment after a long civil war, and therefore the fiscal terms of those contracts were very favorable to the foreign companies. On average, megaprojects have contributed less than ½ percent of total fiscal revenues during 2007-11. Tax terms were brought closer in line with international norms with the revision of fiscal legislation for mining and petroleum in 2007 and have applied to contracts signed since then. The government is also planning to re-discuss the tax treatment for older megaprojects when the initial terms expire (typically after 20 years). The tax treatment of the mining and hydrocarbon sectors is currently being revised, with technical assistance from the Fund and others, to adapt it to current international standards.

Key Megaprojects Going Forward: Coal and Natural Gas

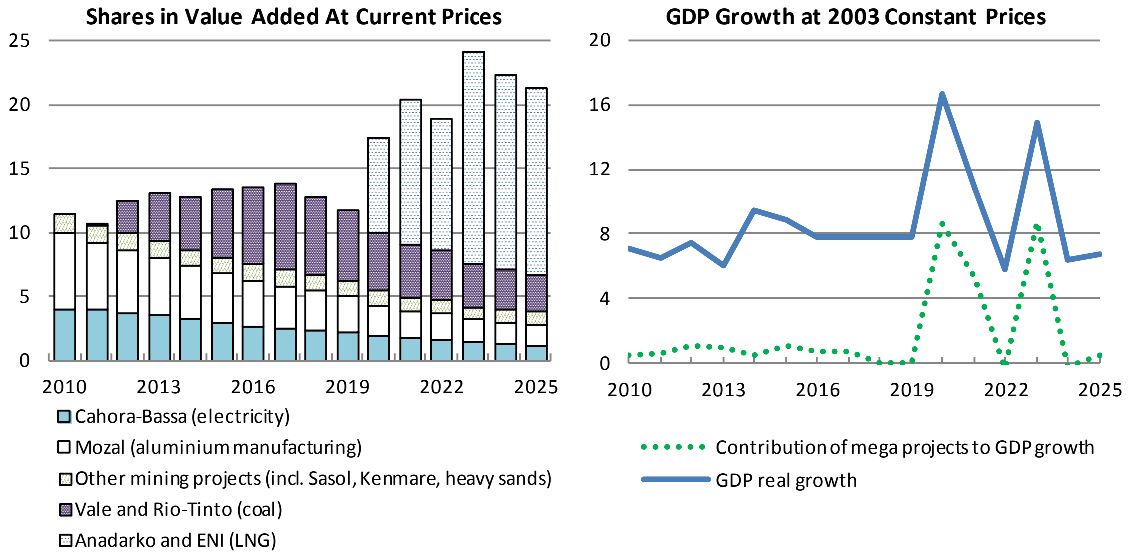
5. Looking forward, megaprojects in two emerging natural resources sectors, coal and natural gas, are set to contribute significantly to economic growth, exports, and fiscal revenue. Coal operations in Tete Province are led by two major operators, Vale and Rio Tinto. Coal production reached 5 million tons in 2012 constrained mainly by railway and port capacity. Abundant and high-quality natural gas reserves have been discovered off-shore in the Rovuma basin. The natural gas operators (Anadarko and ENI) plan to start construction of LNG extraction, manufacturing and transport facilities by 2014, and start exporting LNG by 2020.

6. Staff estimated the impact of LNG sector on GDP and fiscal revenue using the Fiscal Analysis of Resource Industries (FARI) model. The FARI model is a project-by-project model initially developed by the IMF's Fiscal Affairs Department that enables detailed design, modeling, and comparison of fiscal regimes across the entire lifecycle of petroleum or mining projects. Output from the model depends on a series of assumptions about production, investment, cost structure, prices, and fiscal regime. The results presented here are very preliminary, but reflect staff's best estimate based on latest information from the authorities and the coal and gas companies.

- **Coal**: coal is currently exported through the Sena line (some 500 km), the only railway that connects the coal mines to a port (Beira). With the ongoing rehabilitation of the Sena line, coal production is expected to reach 9 million tons by 2014 (of which 6 million tons of coking coal). The construction/rehabilitation of a second rail line through Malawi by Vale that will connect to a new deep water port at Nacala (800 km) is expected to become operational in 2015, allowing coal production and exports to be scaled up. Production is projected to reach 22 million tons per year from 2017. Tentative plans for another southern railway and a new deep water port near Quelimane would further increase export volumes, but are not projected here.

  Natural gas: construction of an LNG plant that consists of four LNG production units ("trains") is expected to start in 2014. Each train has a capacity of manufacturing 5 million tons of LNG per year. LNG production would start gradually between 2020 and 2023; the first train is projected to become operational by end-2019, the second by end-2020, and the last two trains by end-2022. The total project costs of about $40 billion (2.7 times 2012 GDP) cover all upstream (natural gas exploration, drilling, and pipelines) and midstream (LNG plant) investments. Eventual downstream projects (domestic distribution) are not included here.

Figure 3.3: Mozambique: Projected Megaprojects Contribution to Value Added, 2010-2023



Sources: Mozambican authorities, and IMF staff estimates.

7. The value added from coal and LNG production is projected to exceed by far that from existing megaprojects over the next decade. The value added share of coal and LNG sectors is expected at about 20 percent of GDP by 2023, while the share of existing megaprojects will decline to less than 5 percent (Figure 3.3, left panel). Coal and gas contributions to GDP growth will average 2 percentage points per year between 2013 and 2023. GDP growth will reach double digits in the years when some LNG trains become operational (Figure3.3, right panel). The FARI model includes only those projects planned by the government and operating companies.[3] Current reserve estimates suggest that both coal and natural gas reserves could support a much larger production capacity than currently planned.

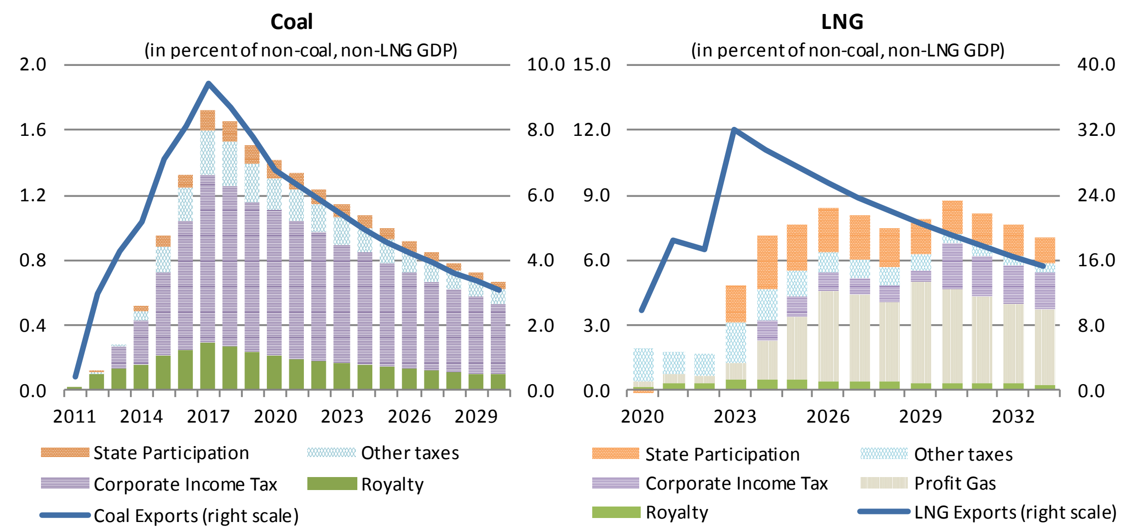
8. In addition, coal and LNG-related investments will boost medium-term growth. The coal sector will bring in more than $3 billion in investments in railways and ports in the next five years. Gas investments so far are largely in exploration activities with very limited domestic content. Domestic value added will increase in the LNG plant construction stage, employing local construction workers and utilizing local construction materials and services. The exact contributions to growth from these investments are hard to project, and they are assumed to be included in the projected rapid GDP growth of 8 percent each year.

9. Government revenue from coal and gas is expected to be small over the medium term (Figure 3.4). Revenue from the coal sector will increase proportionally to coal exports.

[3] By law the government enters into Public Private Partnerships with private operators in the natural resource sector, with a government share in gas operations of 10-15 percent.

About half of the revenue will be corporate income taxes; the rest is mostly royalties and other taxes. Total revenue from coal will not exceed 2 percent of GDP. The LNG sector will not generate any fiscal revenue before it starts production in 2020, other than possible windfall capital gain taxes from the sale of stakes among investors.

Figure 3.4: Mozambique: Coal and LNG Contribution to Fiscal Revenue



Sources: Mozambican authorities, coal and gas companies, and IMF staff estimates.

10. Resource revenue is projected to become an important source of government revenue in a decade. The bulk of the revenue will come from the LNG sector. While LNG production would reach full capacity in 2023, fiscal revenue will increase only gradually over course of the 2020s. This is because (i) gas companies pay lower corporate income tax in the first 8-10 years of production, and (ii) the government's share in profit gas will increase only gradually due to cost-recovery provisions. The combined revenue from coal and LNG is projected to reach 9 percent of non-coal, non-LNG GDP by 2030, or about a quarter of all government revenue.[4]

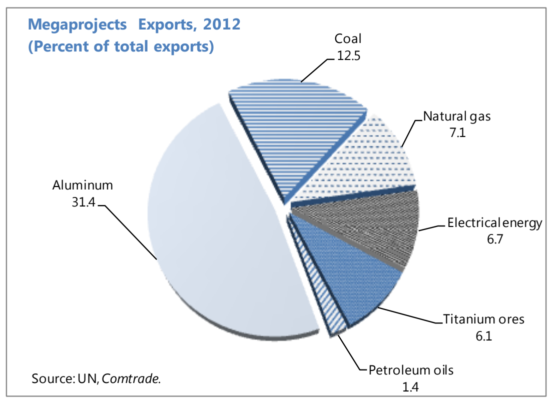
[4]This assumes that other government revenue will be about 27 percent of non-coal, non-LNG GDP in 2026, slightly higher than the fiscal revenue to GDP ratio in 2012 (25 percent).

Appendix III—Mozambique: External Balance and Reserve Adequacy Assessment[1]

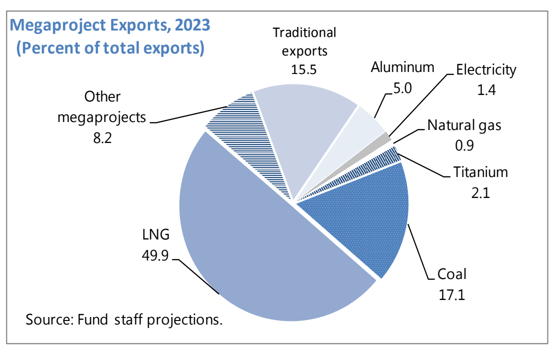
Trade and Exchange Rate Developments

1. **Mozambique's trade balance and current account have undergone major shifts in with the onset of coal exports in 2011 and natural gas exploration activities.** About 2/3 of exports are from megaprojects, though traditional exports, especially from new large-scale farms, have doubled between 2010 and 2012. Reflecting the fact that the older megaprojects have reached their production phase, the megaprojects accounted only for about ¼ of imports in 2010. However, with the onset of large-scale new investments, megaproject imports constituted over 1/3 of the total in 2012, and contributed to a sharp rise in service imports (largely for off-shore exploration) since 2010. As a result, the current account deficit widened from 12 to 36 per-cent of GDP between 2010 and 2012.

2. **Exports are dominated by mega-projects (which account for over 60 percent of total exports) and will continue so for the foreseeable future.** Exports of aluminum and coal currently account for most of current mega-project exports. The aluminum smelter operation in Mozambique has reached a mature stage and is now operating at full capacity so it is not expected that the volume of aluminum exports will increase unless further investment in the operation is undertaken. Coal exports are expected to scale up as land and sea transportation capacity expands. Electrical energy exports are also likely to increase as more hydro power is tapped.



3. **Beginning in 2020, exports of liquid natural gas (LNG) will transform the composition of trade and the economy.** When LNG production reaches full capacity (projected to be in 2023), LNG exports are projected to amount to almost 30 percent of GDP and 50 percent of total exports. Mozambique would become one of the top 5 LNG exporters worldwide.

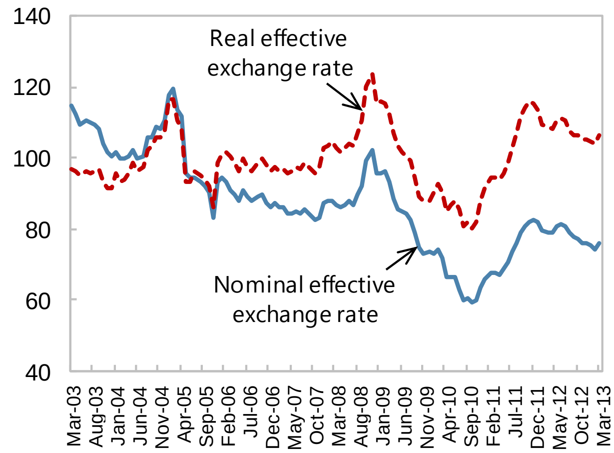


[1]Prepared by Perry Perone (SPR) and Yi Xiong (AFR) with RO support from Naly Carvalho (AFR).

4. **Imports have increased rapidly recently because of new megaproject investments.** Services imports almost doubled in 2012 as LNG exploration expenditures increase. Goods imports also increased by 15 percent in 2012, driven by investments of coal mining companies.

5. **The real effective exchange rate (REER) fluctuated somewhat in recent years.** The REER reached a peak in early 2009, then depreciated through late 2010,as a result of the Bank of Mozambique loosening monetary policy in response to the global financial crisis. It recovered in 2011 as the authorities tightened monetary policy, and depreciated slightly in 2012 and early 2013 following the monetary easing, Since 2011 the REER has remained above its average level in previous years, which is likely to be related partly to the start up of coal exports in 2011, and thus could signal future further appreciation.

Nominal and Real Effective Exchange Rates
(Index, Average 2005=100)

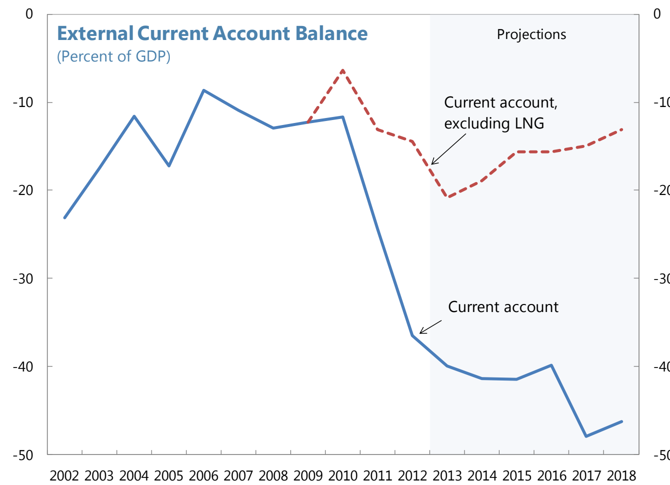


6. **Traditional exports have performed well.** Between 2006 and 2012 traditional exports grew almost 19 percent per year on average, led by sugar, tobacco, and lumber exports. Even more impressive, they grew at an average of 40 percent per year since 2010 as the REER appreciated. Traditional exports are expected to continue strong growth as output increases and productivity improves with continued investments in agriculture and infrastructure, and improvements in the business climate.

Assessing the Exchange Rate

7. **The standard CGER calculations do not provide an accurate picture on the valuation of the metical.** Both the macro balance and external stability assessments show a large overvaluation as they derive a current account norm based on econometric derivation of parameters based on historical values. As noted above, however, the current account deficit has more than tripled recently as a result of imports of goods and services related to the exploitation of large, recently discovered natural gas reserves. Thus the standard CGER methodology needs to be adapted to the Mozambican reality.

8. It is important to take into account the dominance of mega-projects (especially natural gas) when assessing the exchange rate. Megaproject exports are virtually inelastic to movements in the exchange rate. Moreover, the magnitude of the operations in the gas sector will cause drastic shifts in the current account balance. Currently, gas operations are in the exploration stage and will soon go into construction of liquefaction plants ("trains") that will produce liquid natural gas (LNG) for export. This has and will result in large imports of goods and services and large current account deficits financed by FDI until recently and in the future increasingly by private debt. Once the LNG trains are completed and exports come on line, LNG-related imports will be reduced sharply and exports will boom, resulting in an abrupt reduction in the current account deficit.



9. Applying the CGER methodology excluding LNG from the current account shows mixed results but suggests that the REER is relatively close to its equilibrium rate. The deviation from the non-LNG current account norm is about 2 or 5 percentage points of GDP over the medium term (in the macro balance and external sustainability calculations respectively).[2] The exchange rate adjustment needed to bring the current account to its calculated norm depends on the elasticity of the trade balance to changes in the exchange rate. For this calculation a trade balance elasticity derived in Tokarik (2010) for Mozambique under the small-country assumption was used instead of the standard CGER elasticity.[3] This yields a requisite depreciation of the exchange rate on the order of between -3 and 10 percent. Conversely, the equilibrium exchange rate calculation indicates an undervaluation close to 8 percent primarily as a result of an increase in productivity in Mozambique relative to trade partners

Mozambique: Exchange Rate Misalignments (Excluding LNG)

Method	**2018**
Macro balance	-3.2
Equilibrium Real Exchange Rate	-7.9
External Sustainability	10.1
Purchasing Power Parity	1.7
Average	**0.2**

[2] The Macro balance approach suggests a current account norm of –15 percent in 2018, compared to an underlying non-LNG current balance of about –13 percent.

[3] This assumes that the volume of exports and imports of the country cannot affect world prices (IMF Working Paper WP/10/180).

10. On balance staff views the exchange rate as broadly in line with fundamentals. Developments in the coal and natural gas sectors will likely to cause the equilibrium exchange rate to appreciate. The fact that traditional exports have grown at a strong pace points to productivity gains.

Assessing Reserve Adequacy

11. Mozambique's reserve coverage compares reasonably well with other PSI countries. Low-income countries hold reserves primarily to smooth consumption/absorption in the event of external shocks and, to a lesser degree, to cover against episodes of capital flight. For the former the standard measure of reserve adequacy is reserves in terms of months of imports. For the latter the standard measure is reserves in terms of broad money. Compared with other PSI countries, Mozambique's reserve cover is a bit below the PSI average in terms of months of projected imports of non-megaproject goods and services but is still close to 4 months and is at about 44 percent of broad money which is close to the 46 percent average of PSI countries. Mozambique's reserves in terms of GDP (20 percent) are higher than the PSI average (14 percent).

Comparison of Reserve Adequacy in PSI Countries

	2008	2009	2010	2011	2012
Months of imports					
PSI average	4.7	5.1	4.3	4.3	4.5
Mozambique	**4.4**	**5.2**	**4.2**	**3.7**	**3.8**
Percent of broad money					
PSI average	53.3	51.8	48.9	48.8	46.2
Mozambique	**49.7**	**50.2**	**52.7**	**49.1**	**43.5**
Percent of GDP					
PSI average	12.9	14.2	14.5	14.0	13.7
Mozambique	**16.7**	**20.2**	**22.0**	**19.3**	**19.5**

12. Moreover, the reserve cover appears adequate to withstand a one standard deviation external shock. A one standard deviation shock to the current account or total exports in terms of GDP reveals that the impact on Mozambique could be between one and two months of imports, which could be weathered given the current reserve coverage.

Reserve Coverage Impact on Mozambique and PSI Countries

	Current Account/GDP		Exports/GDP		
	Std. Dev.	Reserve Coverage Impact	Std. Dev.	Reserve Coverage Impact	Actual Reserve Coverage
	(1990-2012)		(1990-2012)		(2012)
Rwanda	3.5	1.1	2.9	1.0	5.2
Tanzania	4.0	1.2	5.6	1.7	4.4
Uganda	3.5	2.9	5.0	4.1	4.2
Mozambique	3.5	0.7	8.2	1.7	3.8

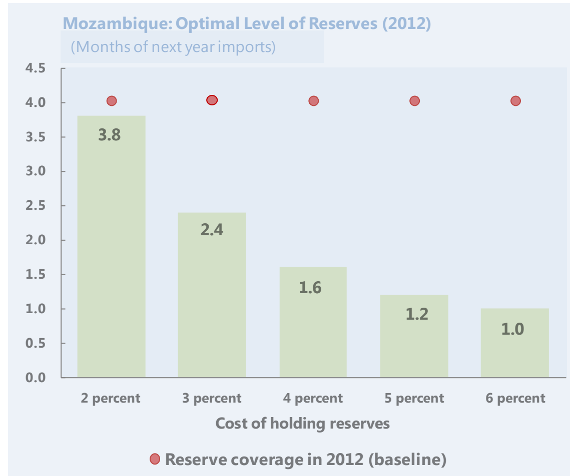
13. A cost-benefit analysis of reserve adequacy also shows that Mozambique's reserves are close to optimal. Using a model developed by IMF staff (Dabla-Norris et al 2011 and www.imf.org), a crisis is defined as a sharp drop in domestic absorption. The optimal level of reserves is determined when the crisis

Variables for Mozambique [1]

2012 Government balance (% of GDP)	-4.16
2011 CPIA	3.68
External demand growth, 10th percentile 2001-12	-2.08
Terms of trade growth, 10th percentile 2006-12	-8.80
Change in FDI to GDP, 10th percentile 2001-12	-2.66
Change in Aid to GDP, 10th percentile 2001-2012	-9.68

[1] External demand 10th percentile 2001-12, TOT average 2006-12, FDI 10th percentile 2001-12. Aid 10th percentile Aid to GDP change, 2001-12.

prevention and mitigation benefits of holding reserves are balanced against the net financial cost of holding reserves as defined by the foregone investment opportunities measured by the marginal product of capital.[4] Using Mozambique-specific variables at their tail values to simulate a shock and assuming various costs of holding reserves, the model shows optimal reserves ranging from 4 months of imports (when the cost of holding reserves is relatively low) to about 1 month of imports (when the cost of holding reserves is relatively high). Given the large infrastructure investment needs in Mozambique, the opportunity cost of holding reserves is likely to be relatively high. Therefore, the projected reserve cover over the medium term of 4 months of imports of non-megaproject goods and services looks comfortable. The relevant measure of reserve cover in Mozambique is imports of goods and services excluding megaprojects because the megaproject imports are financed by FDI and are, in effect, self-financing.



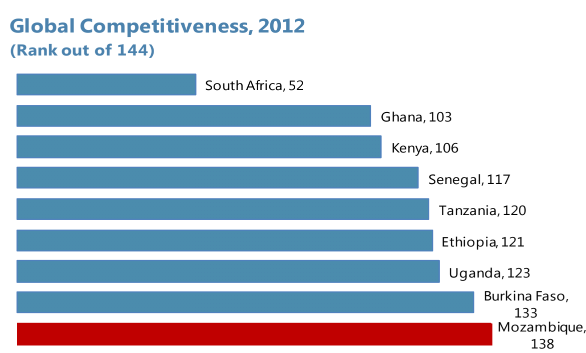
External Competitiveness

14. Even though the exchange rate appears broadly in line with the fundamentals, Mozambique's doing business indicators suggest there is a need for improvement in non-price areas. It is lagging behind its peers in the region and has shown little progress under various survey-based indicators, such as the Global Competitive Index and the World Bank's Doing Business ratings. In 2012 Mozambique was ranked 139 out of 144 countries in terms of competitiveness. It was also ranked near the bottom of the World Bank's latest Doing Business rankings having dropped from 139 in 2012 to 146 in 2013.

Mozambique: Doing Business Rankings

	2013	2012	Change
Overall Ranking	146	139	-7
Starting a Business	96	82	-14
Dealing with Construction Permits	135	135	0
Getting Electricity	174	174	0
Registering Property	155	160	5
Getting Credit	129	127	-2
Protecting Investors	49	46	-3
Paying Taxes	105	103	-2
Trading Across Borders	134	135	1
Enforcing Contracts	132	132	0
Resolving Insolvency	147	146	-1

Source: *Doing Business Database.*



Source: *Global Competitivess Indicators.*

[4]Dabla-Norris et al. (IMF Working Paper WP/11/249) and "Assessing Reserve Adequacy" (IMF Staff Paper www.imf.org).

15. These results suggest that improving external competitiveness will depend on implementation of structural reforms. Several measures were implemented in 2012 to facilitate doing business in Mozambique, such as Parliament authorizing the Government to establish bankruptcy rules for insolvent companies and the simplification of rules and procedures for licensing companies. More needs to be done, however, to improve external competitiveness, including enhancement of institutions, infrastructure (such as transportation systems), the provision of health and education services, and further steps to improve the business climate (such as simplifying the procedure for starting a business). Mozambique is benefiting from advice from the IFC in this area.

Appendix IV—Natural Gas, Public Investment and Debt Sustainability[1]

1. Coal mining and natural gas developments are likely to transform the Mozambican economy over the next decades. In particular, in a decade, government revenues from liquefied natural gas (LNG) could be substantial (up to 40 percent of total revenues). This represents an opportunity to make growth-enhancing public investment but also a challenge to assure macroeconomic stability and debt sustainability.

2. Staff applied DIGNAR (*Debt, Investment, Growth and Natural Resources*) to the Mozambican economy. [2] DIGNAR is a quantitative tool (developed by the Research Department of the IMF) for analyzing the effects of public investment scaling-up in resource-abundant developing countries and debt sustainability. The tool is based on a dynamic macroeconomic model that captures the investment-growth nexus, as well as investment inefficiencies and absorptive capacity constraints encountered in low-income countries.

3. Given the uncertainty that typically surrounds LNG markets, two scenarios are analyzed:

a. a ***baseline scenario*** in which the LNG production is the same as that used for the revenue projections obtained from the FARI model (developed by the Fiscal Affairs Department of the IMF) and a price path observable in normal times. In particular, production starts in 2020 and reaches a level of 1019 millions of cubic feet by 2023. In this scenario LNG revenue rises to a peak of 40 percent of total revenues.

b. an ***adverse scenario*** in which average LNG production is smaller (80 percent of the level in the baseline scenario), there are negative LNG price shocks of size typically observable in oil and gas market crises as well as an earlier exhaustion of gas reserves. In this scenario LNG revenues reach a peak of 20 percent of total revenues.

4. Public investment, if properly planned and executed, has the potential to significantly augment the stock of Mozambican public capital, positively impacting productivity and hence non-LNG production and growth. However, it has to be stressed that public investment does not automatically translate into productive public capital.

[1] Prepared by Giovanni Melina (RES) and Yi Xiong (AFR).

[2] For the technical details of DIGNAR see Melina G., Yang S., and Zanna F. (2013) Debt Sustainability, Public Investment and Natural Resources in Developing Countries, *IMF Working Paper* (forthcoming), Washington DC: International Monetary Fund. The framework combines a debt sustainability analysis model (Buffie E., Berg A., Pattillo C., Portillo R., and Zanna L.F. (2012) Public Investment, Growth and Debt Sustainability: Putting Together the Pieces, *IMF Working Paper*, 12/144, Washington DC: International Monetary Fund) and a natural resource model (Berg A., Portillo R., Yang S., Zanna L.F. (forthcoming) Public Investment In Resource-Abundant Developing Countries, *IMF Economic Review*).

5. Empirical studies suggest that investment inefficiencies (poor planning, higher-than-expected costs, bad governance, corruption, supply bottlenecks, lack of complementary infrastructure, etc.) are pervasive in developing countries. On average only around half of public investment expenditure translates into effective public investment (i.e. investment that enhances the public capital stock).

6. If public investment is scaled up too quickly, the degree of inefficiency is likely to increase, i.e. it is more likely to bump into absorptive capacity constraints. These are limits on the level of public investment that the economy is able to retain. If the pace of the investment scaling-up is too quick, these constraints are more likely to bind, investment efficiency is likely drop further and hence a bigger part of investment expenditures will be wasted.

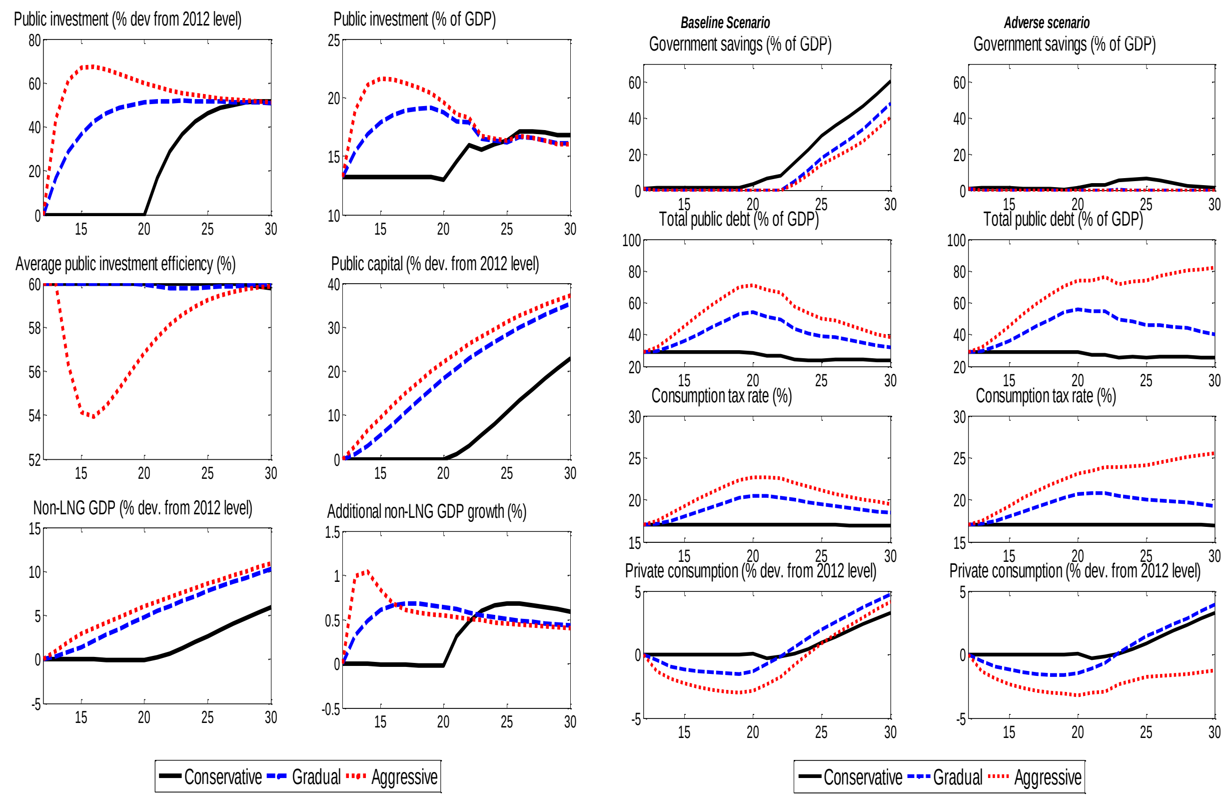
7. Three alternative approaches to the public investment scaling up are explored (Figure V.1).

a. **A *conservative approach* would await the LNG revenues.** Spending on growth-enhancing investment projects (e.g. up a level 50 percent higher than 2012 in real terms) would increase only in the years when LNG production starts. Public debt does not rise as a share of GDP and declines over the longer term, thus no fiscal adjustment is required. The start of LNG production would allow building strong fiscal buffers in the form of government savings.

b. **Under a *gradual approach* public investment is gradually increased in anticipation of LNG production and it reaches its new level by the time production is in place.** This approach allows anticipating some of the LNG revenue. Public debt rises gradually to a peak of 50 percent of GDP in 2019-20, then declines over the longer term to more sustainable levels, thus the required fiscal adjustment (e.g. in terms of tax increases) is small. The full roll-out of LNG production would allow building fiscal buffers in the form of government savings from 2023 on.

c. **An *aggressive approach* would fully anticipate future LNG revenues and increase public investment spending massively early on** (up to 8 percentage points of GDP). However, due to absorptive capacity constraints, the higher investment spending delivers a similar build-up in the public capital stock as under the gradual approach. The effect on the additional non-LNG growth generated is dampened similarly. An aggressive approach implies a much bigger build-up of public debt to 70 % of GDP in 2019-20, and would require a painful fiscal adjustment in order to service the accumulated debt.

Figure V.1. Mozambique: Effects of Alternative Public Investment Scaling-ups, 2013–30



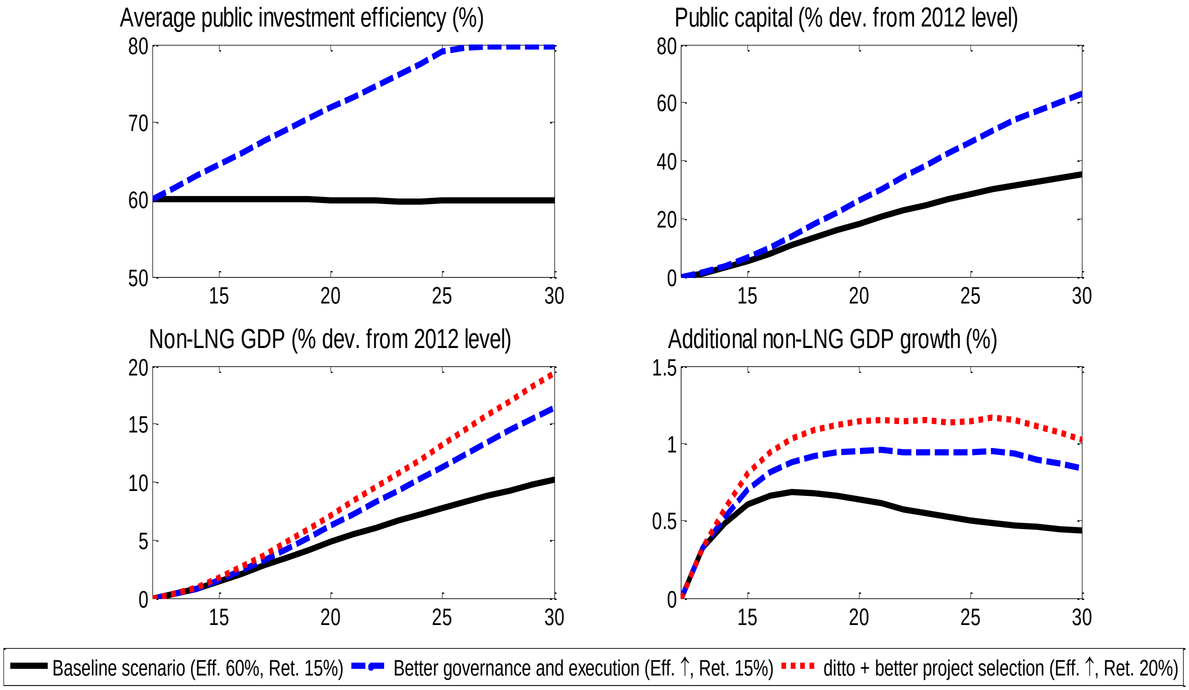
Source: IMF staff simulations.

8. **In an *adverse scenario* with lower LNG production, lower LNG prices and an earlier exhaustion of gas reserves, there would be no room to build up significant fiscal buffers.** Public debt would (i) not rise under the *conservative approach*, (ii) rise faster under a *gradual approach* than in the baseline; (iii) rise explosively under an *aggressive approach*, requiring painful and sustained fiscal adjustment without stopping the accumulation of debt. Simulations assume that at least half of recurrent infrastructure costs are covered by user fees. Failure in collecting fees exacerbates debt sustainability risks.

9. If, over time, institutions, governance, manage*ment* practices are *im*proved, public investment becomes, on average, more efficient and absorptive capacity constraints become less binding. If investment projects are better designed, selected, and implemented, the average real return of investment increases (Figure V.2). This will increase productivity of private factors for production with a more positive impact on capital stock accumulation, growth and incomes. For instance, a increase of average public investment efficiency from 60 to 80 per-cent over ten years,[3] combined with a better project selection that brings the average annual net economic return on investment from 15 to 20 percent, deliver an increase in the additional non-LNG GDP growth rate of more than half percentage point over a period of more than 15 years.

[3]Such an increase in efficiency has to be taken just as an example. In fact it can be very challenging for a developing country to achieve such an efficiency improvement over ten years. This ultimately depends on policy choices and individual country experiences.

Figure V.2. Mozambique: Effects of Improvements in Governance and Project Selection, 2013–30



Source: IMF staff simulations.

10. In sum, a gradual public investment scaling-up anticipating some but not all future LNG revenue would be appropriate given Mozambique's infrastructure investment needs and the uncertainty regarding LNG production/revenue. Due to absorptive capacity constraints, an aggressive approach is not likely to yield tangibly better growth outcomes and poses threats to debt sustainability.

11. Good governance and careful project selection and execution are key determinants of the impact public investment has on growth. Optimizing the effectiveness of investment is crucial to maximize its positive effects and limit the build-up of debt funding such investment.

Appendix V—Implementation of the Poverty Reduction Strategy

Mozambique's progress in implementing the Poverty Reduction Strategy (PARP 2011-14) has been broadly satisfactory. Several key quantitative indicators of development—especially school enrolment ratios and infant/maternal mortality rates—have shown clear improvements, but reflecting the broad scope and long-term nature of the challenges, progress has been uneven.

1. **The PARP aims to induce patterns of inclusive growth by increasing the allocation of funds for investment** under the following pillars: (i) enhancing production and productivity in agriculture and fishing; (ii) creating employment; and (iii) enhancing social and human development.

2. **Annual reports on progress under the PARP are produced by the government in its report on economic developments (PES) as well as in a joint review by the government and a core group of donors.**

- The *annual PES* provides a tabulation of detailed indicators of progress. While the 2013 report continues to highlight significant improvements in a broad range of social indicators, progress has been uneven both across indicators and between different regions (see MEFP ¶4). Progress has been strongest on improvements in school enrollment and infant/maternal mortality rates, with less progress seen on access to medical staff, water and sanitation. The government plans to undertake the next household expenditure survey in 2014/15 that will provide a comprehensive view on social conditions. A more frequent survey using a much smaller sample is also under preparation to enable higher frequency monitoring of progress.

- The *annual reviews with donors/development partners* undertaken in May 2013concluded that progress under the PARP has been sufficient to allow for the continuation of donor budget support. The review highlighted important legal and institutional advances, including: (i) the improvement of the legal framework for combating corruption (with the partial approval by Parliament of the anti-corruption packge); (ii) the approval of the National Investment Plan for the Agriculture Sector (PNISA), and (iii) the approval of simplified rules for the licensing of companies. These and other legal and institutional advances have not yet, however, translated into a clear increase in the production and productivity of small-scale agriculture or inmeeting the increasing demand for technical and vocational skills. Additional steps discussed included the need for: (i) a strong monitoring system with results-based indicators that can be measured more frequently; (ii) more determined progress on reforms to business environment reforms that has just started to build momentum, and (ii) a clear and unified vision on how to leverage the largely unexplored resource wealth to transform and diversify Mozambique's economy.

3. **Budgetary spending/allocations in support of the PARP have increased.** Key programs for the period ahead to meet the PARP objectives are identified in the MEFP ¶19. Spending on priority sectors has increased from just under half of spending in 2011 to almost ¾ in the 2013 budget, or from 15.9 percent of GDP in 2011 to 20.2 percent in 2012 and 26.2 percent in 2013. The PFM reforms under way should allow a more detailed expenditure breakdown by function in coming years.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

June 10, 2013

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION, SIXTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT, REQUEST FOR A THREE-YEAR POLICY SUPPORT INSTRUMENT AND CANCELLATION OF CURRENT POLICY SUPPORT INSTRUMENT—DEBT SUSTAINABILITY ANALYSIS (DSA)

Approved By
David Robinson and Vivek Arora (IMF) and Marcelo Giugale and Jeff Lewis (World Bank)

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

This debt sustainability analysis (DSA) updates the joint IMF/IDA DSA from May 2012. Mozambique moves from low to moderate risk of debt distress as the result of (i) a lower discount rate, (ii) a significant increase in debt contracted in the last two years related to an ambitious public investment program aimed at narrowing the infrastructure gap, and facilitating the development of natural resources , and (iii) large movements in the underlying balance of payments with the onset of coal exports and significant commercial investments in natural gas exploration and liquefaction. Staffs agree with the authorities on the importance of the public investment program for development. The increased risks to debt sustainability, however, should be contained by moderating public external borrowing compared to its current accelerated pace. The DSA highlights that further improvements in debt management and investment planning capacity are important for continued debt sustainability, notably in the case of commercial borrowing.[1] *As public debt is largely external, the evolution of total public debt indicators mirrors that of public external debt. Private external debt is expected to increase rapidly in importance, mainly driven by investment in the natural gas sector, and to comprise the majority of external debt by the end of this decade.*

[1]The DSA presented in this document is based on the standard low-income countries (LIC) DSA framework. See "Debt Sustainability in Low-Income Countries: Further Considerations on an Operational Framework, Policy Implications" (IMF/SM/05/109 and IDA/SECM2004/0629, 9/10/04). Under the Country Policy and Institutional Assessment (CPIA), Mozambique is rated as a medium performer, albeit close to the threshold of 3.75 for strong performers, with an average rating of 3.71 during 2009–11; the DSA uses the indicative threshold for medium performers.

UNDERLYING DSA ASSUMPTIONS

1. **This DSA is consistent with the macroeconomic framework outlined in the Staff Report for the Sixth Review under the PSI** (Box 1). Compared to the previous DSA,[1] the main changes in this DSA are as follows:

a. **The medium-term macroeconomic framework has been revised** (Text Table 1). In particular, economic growth slows in 2013 as a result of widespread flooding early in the year that damaged agricultural output and transport infrastructure. Growth is projected to bounce back quickly and accelerate over the medium term as agriculture recovers, extractive industries boom, and infrastructure investments materialize. The fiscal deficit was lower in 2012, among other factors because of windfall capital gain tax revenues received. Significant revisions have been made to the balance of payments that result in larger current account deficits and larger FDI inflows—both historically and in the projections. The bulk of the revision is related to megaprojects, particularly the inclusion of imports of goods and services related to exploration in the natural gas sector; the counterpart of these imports is a large increase in recorded inward FDI.

Text Table 1: Evolution of Selected Macroeconomic Indicators between DSA Updates

	2011	2012	2013	2014	2015
		Est.	Projections		
Real GDP growth (%)					
Previous DSA	7.1	6.7	7.2	7.8	7.8
Current DSA	7.3	7.4	7.0	8.5	8.5
Nominal GDP (US$ million)					
Previous DSA	12.8	14.2	15.5	17.3	19.4
Current DSA	12.6	14.2	14.7	16.0	17.9
Overall fiscal deficit (% of GDP)					
Previous DSA	5.2	6.4	6.6	6.6	6.6
Current DSA	5.3	4.2	6.7	7.2	6.7
Current account deficit (% of GDP)					
Previous DSA	13.1	12.7	12.4	11.9	11.3
Current DSA	24.3	36.5	39.9	41.3	41.4
FDI (% of GDP)					
Previous DSA	16.4	11.2	10.2	10.1	9.7
Current DSA	20.7	36.6	32.2	25.8	20.8
Use of NCB ceiling (% of GDP) 1/					
Previous DSA	1.5	2.5	3.2	3.4	0.0
Current DSA	0.6	0.8	2.4	2.5	1.6
Disbursements under PTL (% of GDP) 2/					
Previous DSA	1.8	0.9	0.9	0.5	0.0
Current DSA	1.0	0.4	0.2	0.3	0.2
Grant financing (% of GDP) 3/					
Previous DSA	9.2	8.7	8.1	8.0	8.0
Current DSA	9.2	6.6	7.5	7.6	7.4

1/ The disbursement pace is not faster as in the previous DSA, because implementation of some projects has been slower than previously expected and the large prospective new loan for the Moamba Major Dam is currently expected to start disbursing only in 2015.
2/ Portuguese credit line.
3/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new disbursements).

[1] See IMF Country Report No. 12/148.

Box 1. Macroeconomic Assumptions 2013–33

The medium-term assumptions in the baseline scenario for 2013-33 are consistent with the medium-term macroeconomic framework underlying the Staff Report for the Sixth Review under the Policy Support Instrument.

Non-LNG Real GDP growth is projected to be around 8 percent on average in the next few years and 7½ percent in the longer term. Growth will slow down in 2013 due to the impact of floods, but is expected to accelerate over the medium term, supported by recovery in agricultural production, expansion in coal mining, and infrastructure investments in the pipeline, including to support coal exports and LNG manufacturing. Growth is sustained in the long term by strong population/labor force growth, continued infrastructure investment, and related productivity gains. Risks to growth include public investment not achieving expected payoffs and thus limiting productivity gains, and the possibility of Dutch disease effects. The government is aware of the risks, and is taking steps to strengthen project evaluation and selection, and is considering options such as fiscal rules and sovereign wealth funds to mitigate the risk of excessive real exchange rate appreciation.

LNG sector. LNG plants are assumed to be under construction during 2014–22. The projection assumes a moderate-sized plant consisting of four LNG manufacturing units ("trains"). One train is assumed to start production in 2020, followed by a second train in 2021, and the third and the fourth train will start production in 2023. Total investment is projected at $40 billion. The sector's contribution to GDP is expected to be small during the construction period due to a high import content. Annual LNG output will reach 20 million tons in 2023, contributing more than 20 percent of nominal GDP by then.

Consumer price inflation is projected to rise to 5–6 percent in 2013, owing to rising food prices and an increase in public transport fares in late 2012 and also reduced domestic food supply as a result of the floods. As per the Central Bank medium term target, inflation is assumed to stabilize at around 5½ percent over the forecast period beginning from 2014.

Growth of exports is projected to stabilize at around 5 percent a year in the longer term as coal and LNG exports stabilize. In the shorter term export growth rates show sharp changes as a result of coal and LNG operations. In particular the growth rate of exports would almost double in 2020-23 due to LNG exports coming on line.

Imports are projected to increase sharply in 2014 during the LNG plant construction phase and their growth would stabilize at around 9 percent a year in the long term.

The non-interest external current account deficit is projected to rise to over 40 percent of GDP in the medium term largely driven by LNG-related imports. The deficit will be primarily financed through FDI and private external borrowing. It would then stabilize at around 8 percent of GDP in the long term as coal exports increase with transport capacity and as LNG exports start.

The non-interest primary fiscal deficit is projected to widen in 2013 and 2014, reflecting high public investment in the pipeline to mitigate the infrastructure gap. The fiscal balance would improve in the medium to long term as public investment tapers off to more sustainable levels and non-interest spending falls in percent of GDP terms. The fiscal balance is expected to improve further from 2020 onwards once LNG revenue commences.

b. The natural gas sector. The baseline scenario in this DSA has incorporated the emerging gas sector in Mozambique. The basis for the development of the sector is one of the largest worldwide discoveries of gas. These developments result in: (i) higher foreign direct investment and private external borrowing for exploration (since 2010) and the construction of a 4-train gas liquefaction (LNG) plant (2014-2022); (ii) increased imports of goods and services related to LNG; and (iii) increased GDP and exports from 2020 onwards when the LNG plant becomes operational. Under baseline assumptions, the LNG sector will contribute 20 percent of GDP and half of exports by 2023. LNG-related fiscal revenue will be small in the beginning owing to cost recovery provisions. Revenue will gradually increase over the medium to long term.

c. The coal mining sector. Coal production is expected to expand rapidly over the medium term to 20 million tons (6 percent of GDP) in 2017 from about 5 million tons (2 percent of GDP) in 2012. Most of the coal produced will be for exports—high quality coking coal—while the abundant lower-value thermal coal is not currently marketed due to transport capacity constraints. Coal-related investments in mines, railways, ports, and a coal-fired power plant are conservatively expected to amount to $5 billion during 2013–17, financed by FDI inflows. Adverse world coal price movements constitute a risk to these expansion plans, which could result in delayed implementation or scaling back.

d. The related substantial BOP revisions show much larger changes in variables, especially FDI, and thus larger volatility than assumed in the last DSA. The related standard shocks in the DSA template produce larger deviations from the baseline scenario, and thus make breaches of the sustainability thresholds more likely and more prolonged than in the last DSA.

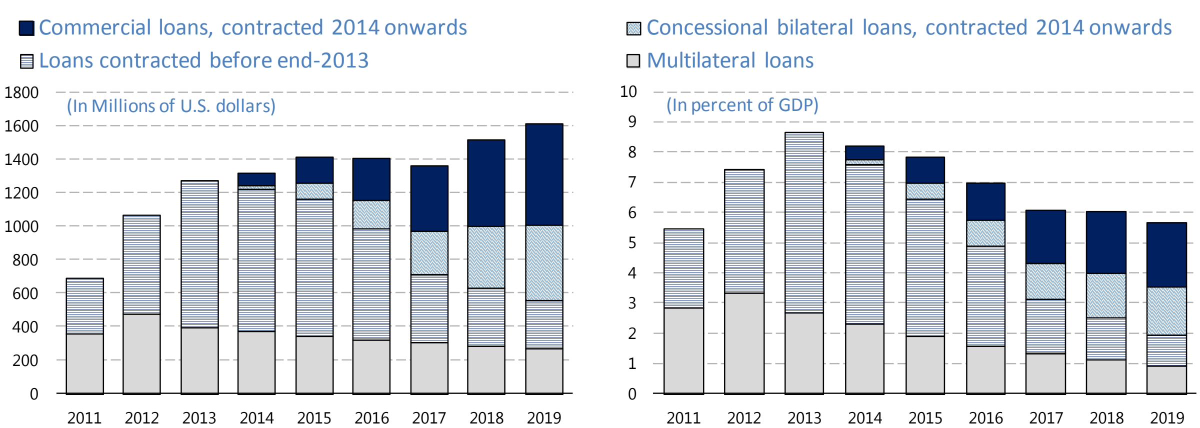
e. A revised public investment and external borrowing profile. Thus far, disbursements, particularly of nonconcessional loans, have been lower than expected in the previous DSA, mainly because of a somewhat slower start of projects. Disbursement are projected to increase in 2013–16, in line with the recent increase in the non-concessional borrowing ceiling to $1.6 billion under the current IMF-supported program and the proposed non-concessional borrowing ceiling under the successor program, but also through a notable increase in bilateral concessional loans (Text Table 2). Following the acceleration of external borrowing through end-2013, the authorities plan to moderate the pace of new borrowing over the medium term (Text Figure 1). Starting at the end of this decade, new public sector borrowing is expected to decline gradually relative to GDP in light of the coming on stream of natural resource-related revenue from the coal and natural gas sectors. Nominal disbursements, however, are projected to continue increasing throughout the projection period. Other large potential future investment projects, e.g. in railroads, the LNG and power sectors, are deemed commercially viable by the authorities and would be expected to be undertaken largely by the private sector, without substantial need for government financing or guarantees. However, these projects could constitute a risk for the public debt trajectory if significant government financing became necessary. Another risk is that pressures may emerge and make it difficult to slow the future pace of public loan contracting, particularly in light of the country’s vast infrastructure needs. Finally, project costs could be underestimated, as was the case for the Nacala airport.

Text Table 2. Non-concessional Loans Contracted and in the Pipeline

	Signed on	Loan amount (US$ millions)	Before 5th rev.	Between 5th and 6th rev.	After 6th rev.
Total non-concessional loans		**2,073**	**1,387**	**45**	**641**
Brazil					
Nacala Airport	Apr 28, 2011	80	80		
Study on Dam Moamba Major	Nov 22, 2012	9	9		
Nacala Airport (Augmentation)	Expect to sign by mid-2013	45		45	
Public Transport Maputo-Matola	Expect to sign by end-2013	135			135
Nacala Industrial Free Trade Zone	Expect to sign by end-2013	40			40
Dam Moamba Major	Expect to sign by end-2013	466			466
China					
Maputo Airport	Dec 16, 2010	67	67		
Ring Road *	Feb 17, 2012	300	300		
Katembe Bridge/Ponta D'Ouro Road	July 18, 2012	682	682		
India					
Maputo Power Supply *	Sep 20, 2012	250	250		
Large concessional loans in the pipeline		**946**			**946**
China					
Road Beira-Machipanda	Expect to sign by mid-2013	433			433
India					
Road Tica-Buzi-Nova Sofala	Expect to sign by mid-2013	150			150
400-1000 Basic Houses	Expect to sign by mid-2013	47			47
Agua Rural III	Expect to sign by mid-2013	20			20
KFW					
Mavuzi-Chicamba Rehabilitation	Expect to sign by mid-2013	24			24
Korea					
Nampula - Nametil Road	Expect to sign by end-2013	182			182
Maputo Sanitary Landfills	Expect to sign by mid-2013	25			25
250 Buses in Maputo and Matola	Expect to sign by mid-2013	30			30
Japan					
Chókwè City Dike	Expect to sign by end-2013	19			19
Dam Macarretane Rehabilitation	Expect to sign by end-2013	16			16

* 34 percent grant element.

Text Figure 1. Public Sector External Debt Disbursement Path



f. **A revised grant element in financing terms for future borrowing.** This DSA assumes that the grant element for new borrowing will experience a pronounced decline during the next two decades, contrary to the previous DSA that assumed a roughly constant 30-percent grant element. This reflects revised assumptions on the long-run availability of donor financing with government relying increasingly on commercial borrowing.

g. **The reduction of the DSA discount rate from 4 percent a year ago to 3 percent in this DSA** yields a higher present value of debt/borrowing in this DSA compared to the previous one.

EXTERNAL DEBT SUSTAINABILITY ANALYSIS

2. **External debt is projected to rise rapidly during this decade, reflecting mainly private sector investment in the natural gas sector.** External debt (both public and private) is expected to peak at about 128 percent of GDP in 2019, at which time private sector debt will constitute about two thirds of total external debt. With investment in the coal sector projected to be financed through foreign direct investment, this increase in private external debt is mostly driven by investments in the natural gas sector. Public sector debt is also expected to peak in 2018 at 45 percent of GDP (in PV terms) on the back of infrastructure investment. The significant buildup of private sector external debt needs to be monitored by the authorities to contain vulnerabilities. However, with renowned global companies leading investments in the natural resource sector, the risk for government contingent liabilities or other vulnerabilities beyond those specific to the natural resource operations is currently considered to be low.[3]

3. **All baseline public external debt indicators remain below their respective thresholds but now come closer to the thresholds than previously** (Figure 1).[4] While the indicators remain contained throughout the projection period, they are significantly higher than at the time of the last DSA, especially the PV of debt relative to GDP. It now peaks around 39 percent (in 2018), relative to a 28½ percent peak in the previous DSA. The beginning of LNG production, however, and the ensuing surge in GDP would drop the ratio safely back down to below 33 percent in the next decade (Table 1). The increase of debt ratios is partly due to the lowering of the discount rate from 4 to 3 percent, which contributed to about one third (3 percentage points) of the increase in the PV of debt to GDP ratio. PV of debt to GDP ratio would be about 6 percentage points lower throughout the DSA period if the discount rate were at the longer-term historical average benchmark rate of about 5 percent instead of the 3 percent assumed in this DSA (Figure 1 and Table 2).

[3] Likewise, the risk of BOP pressures emerging as a direct result of mega project-related investment activity is considered to be low. Care will have to be taken in the long term, however, once revenues from these ventures materialize, as these may be volatile reflecting world commodity prices and in relation to imports. Moreover, large natural resource exports then also hold competitiveness risks emerging from a possible exchange rate appreciation, which will have to be carefully managed.

[4] Compared to the DSA of Country Report 12/148 (May 2012).

4. External debt ratios remain vulnerable to FDI and exchange rate shocks. The threshold for the PV of debt to GDP ratio is breached under stress tests for a sustained period.[5] A sharp reduction in non-debt creating FDI in 2014-2015 would push the PV Debt/GDP ratio well above the 40 percent threshold during the second half of this decade, with a peak at more than 80 percent (Figure 1). Apart from the FDI shock, a sharp depreciation of the metical in 2014 also leads to breaches of this threshold (Table 2). Both shocks lead to a significant overshooting of the threshold for a sustained period: 13 years for the FDI shock and 19 years for the depreciation shock.[6] The impact of these two shocks is now much larger than in the previous DSA given revisions to historical BOP data to account for FDI-financed natural gas exploration.[7] The PV of debt will also breach two other thresholds: 150 percent of exports, and 250 percent of revenue under the FDI shock scenario.[8] The thresholds for the PV of debt to export ratio is breached by a number of indicators, particularly a shock to non-debt creating flows. In many countries with large natural resource sectors, price volatility adds another source of risks to external debt sustainability. Given the long-term nature of the contracts that usually govern LNG development – including buying prices – the risk of significant volatility for external debt sustainability seems relatively small.

5. Ensuring that LNG production materilizes is crucial for Mozambique's debt sustainability. The LNG sector will contribute significantly to GDP, exports and government revenue. A gradual public investment scaling-up under the baseline scenario anticipating some LNG revenue would be appropriate given Mozambique's infrastructure investment needs. If, however, LNG production or revenue is much lower than expected, the debt ratios would be higher over the medium to long term.[9]

PUBLIC SECTOR DEBT SUSTAINABILITY

6. The evolution of public debt indicators (including domestic debt) mirrors that of the external indicators because of the predominance of external debt (Table 3 and Figure 2)**.** The medium-term increase in public debt reflects the temporary surge in public investment financed in part by external borrowing on non-concessional terms. Under the baseline scenario, the PV of public

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

[6]The charts in Figure 1 display the stress test with the most adverse outcome in 2023.

[7]The BOP data revisions in 2010-2012 to account for natural gas exploration lead to a higher increase in FDI compared to previous years. As a result, the DSA's stress scenario for non-debt creating capital flows now assumes that these flows are subject to higher volatility than in the previous DSA.

[8]These breaches, however, should not be overemphasized as a fall in FDI would likely be linked to lower imports rather than higher borrowing as implicitly assumed in the standard shock scenario.

[9]See Staff Report for the 2013 Article IV Consultation, Appendix V "Natural Gas, Public Investment and Debt Sustainability" for discussions on public investment scaling up and risks to the debt sustainability from adverse LNG production and price shocks.

debt remains below 50 percent of GDP throughout, therefore remaining well contained below indicative benchmarks that research has linked to increased probability of debt distress.[10]

7. The public DSA illustrates that it is essential for debt sustainability to moderate the pace of new borrowing as is planned by the authorities. In other words, the fiscal primary balance will need to be reduced in the medium and long run. For illustrative purposes, the "Fix Primary Balance" scenario[11] shows the impact if the primary balance were fixed at values of its peak years 2013-15, i.e. if such a slowing in new borrowing would not take place.[12] Debt ratios would continue to rise throughout the projection period, quickly elevating risks to debt sustainability, no matter which assumptions are made on LNG production.

CONCLUSIONS

8. In staffs view, while the standard DSA shocks indicate that Mozambique would be in the moderate risk of debt distress category, the public investment program should continue to move forward but with a more moderate pace of public borrowing. Even against the background of a temporarily accelerated borrowing pace for infrastructure projects, the baseline debt trajectories remain below their respective thresholds throughout. Importantly, debt service indicators remain substantially below their thresholds, including under stress tests, and reflect conservative assumptions regarding the grant element for future borrowing.[13] The breaches under the stress tests are temporary, would be reversed by the coming on stream of LNG production, and seem manageable against the backdrop of the authorities' strong track record of prudent economic management.

9. This analysis highlights three important points for debt sustainability. First, it will be important to continue to improve debt management and investment planning capacity to ensure that the increasing share of non-concessional resources in the stock of debt is well managed and that the most deserving public investment projects are selected and yield their desired payoff. Second, it will be important for the authorities after 2013 to moderate the pace of new borrowing to maintain debt sustainability, in line with their commitments. Third, it is becoming more important—including from a debt sustainability perspective—to ensure that LNG production materializes in order to lock in the beneficial effects on GDP and fiscal revenue.

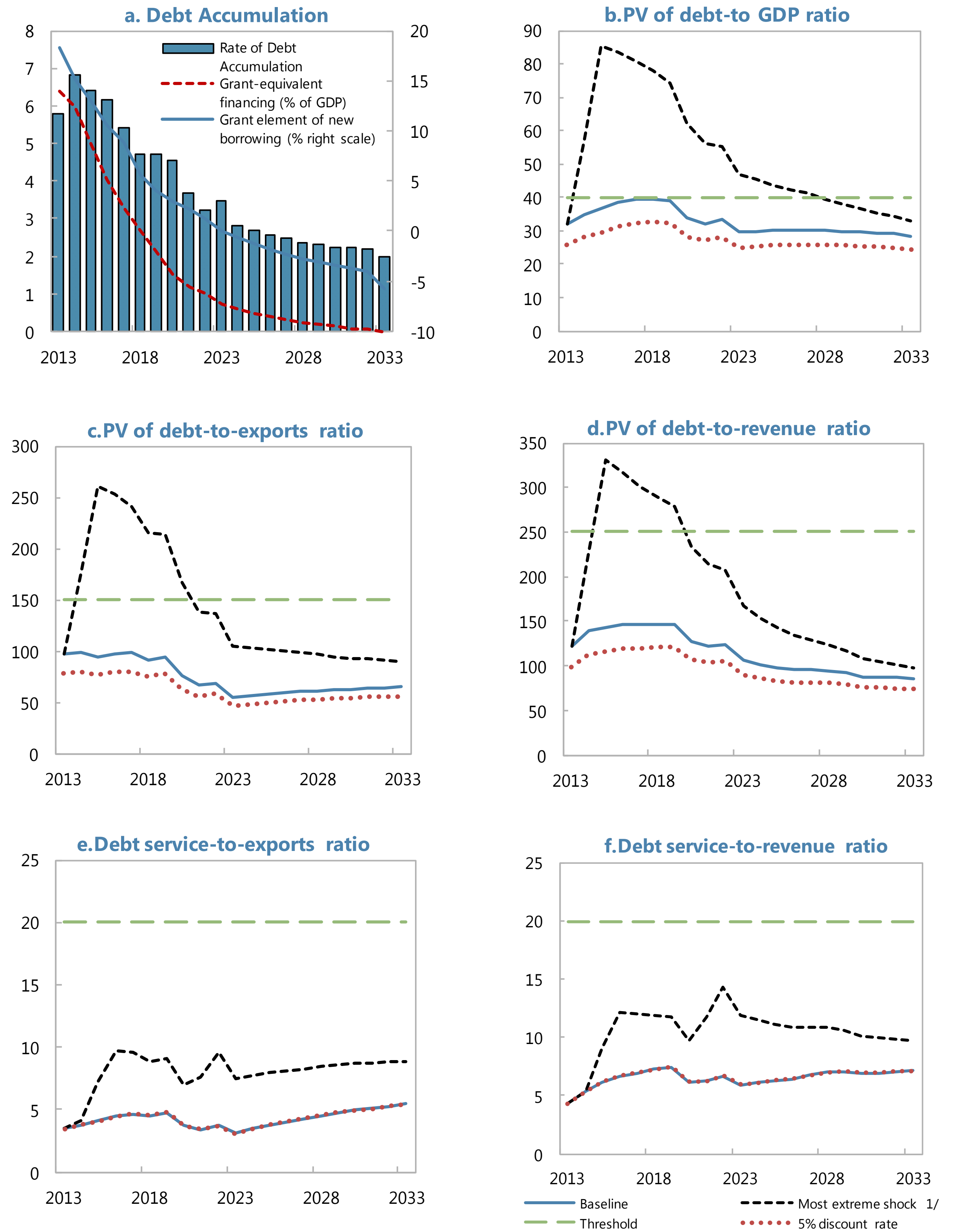
[10] At Mozambique's CPIA rating, the indicative public debt benchmark signaling higher risk of debt distress lies between 56 and 74 percent for the PV of debt-to-GDP ratio. See IMF, 2012, "Revisiting the Debt Sustainability Framework for Low-Income Countries."

[11] See Figure 2 and Table 4 (lines A2).

[12] To provide this illustration, the "Fix Primary Balance" scenario was adapted for this analysis from the standard of fixing the primary balance at 2012, instead fixing the primary balance at its 2013-15 average value in percent of GDP. This change was implemented, because the 2012 primary balance is low compared to those in the near future for two reasons: (i) because of windfall revenues in 2012, and (ii) because major investment projects are only starting.

[13] Moreover, these indicators do not account for other buffers, such as comfortable levels of international reserves relative to non-mega project imports.

Figure 1. Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2013-2033 1/



Sources: Country authorities and IMF staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2023. In each case it corresponds to a Combination shock.

Table 1.Mozambique: External Debt Sustainability Framework, Baseline Scenario, 2010-2033 1/

(Percent of GDP, unless otherwise indicated)

	Actual			Historical 6/	Standard 6/	Projections												
				Average	Deviation										2013-2018			2019-2033
	2010	2011	2012			2013	2014	2015	2016	2017	2018	2019	2020	2021	Average	2023	2033	Average
External debt (nominal) 1/	**63.8**	**48.3**	**50.7**			**54.9**	**64.8**	**78.0**	**89.9**	**109.0**	**122.5**	**127.6**	**106.9**	**99.2**		**76.6**	**55.4**	
of which: public and publicly guaranteed (PPG)	40.2	32.6	36.3			41.7	44.7	45.9	47.4	47.7	47.1	45.8	39.3	36.9		33.1	30.0	
Change in external debt	-1.9	-15.6	2.5			4.2	9.8	13.3	11.9	19.0	13.5	5.1	-20.7	-7.7		-17.1	-0.7	
Identified net debt-creating flows	0.5	-11.7	-5.8			4.3	11.3	13.5	13.4	22.6	14.7	7.1	-14.3	-10.8		-17.0	0.1	
Non-interest current account deficit	**10.0**	**22.8**	**35.4**	**14.2**	**8.9**	**38.4**	**39.7**	**39.3**	**36.7**	**44.0**	**34.2**	**26.3**	**15.7**	**7.1**		**4.0**	**8.7**	8.1
Deficit in balance of goods and services	17.7	29.7	41.5			43.5	43.3	42.2	37.4	42.2	31.8	24.0	9.3	2.0		-10.5	4.0	
Exports	31.2	30.7	29.8			32.7	35.7	39.0	39.4	40.1	43.4	41.4	44.5	48.7		53.7	44.1	
Imports	48.9	60.4	71.4			76.3	79.0	81.2	76.8	82.4	75.2	65.4	53.7	50.7		43.2	48.1	
Net current transfers (negative = inflow)	-6.9	-6.9	-5.3	-6.6	1.2	-3.8	-3.6	-3.0	-2.6	-2.2	-1.9	-1.6	-1.2	-1.0		-0.7	-0.3	-0.7
of which: official	-6.3	-6.3	-5.0			-3.5	-3.4	-2.9	-2.4	-2.0	-1.7	-1.4	-1.0	-0.8		-0.5	-0.1	
Other current account flows (negative = net inflow)	-0.7	0.0	-0.8			-1.4	0.0	0.1	1.9	4.1	4.4	3.9	7.7	6.1		15.2	5.0	
Net FDI (negative = inflow)	**-14.0**	**-20.7**	**-36.6**	**-10.7**	**10.8**	**-32.2**	**-25.8**	**-23.1**	**-20.8**	**-18.9**	**-17.0**	**-15.1**	**-11.8**	**-10.1**		**-8.0**	**-6.3**	-8.3
Endogenous debt dynamics 2/	**4.5**	**-13.9**	**-4.6**			**-1.9**	**-2.6**	**-2.7**	**-2.5**	**-2.6**	**-2.5**	**-4.2**	**-18.2**	**-7.9**		**-13.1**	**-2.4**	
Contribution from nominal interest rate	1.7	1.5	1.0			1.6	1.7	2.2	3.1	3.9	5.3	6.3	6.0	4.8		3.2	1.0	
Contribution from real GDP growth	-4.9	-3.5	-3.2			-3.4	-4.3	-4.9	-5.6	-6.4	-7.8	-10.5	-24.2	-12.7		-16.3	-3.4	
Contribution from price and exchange rate changes	7.7	-11.8	-2.5			...	...	...	...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**-2.4**	**-3.9**	**8.3**			**-0.2**	**-1.5**	**-0.2**	**-1.5**	**-3.6**	**-1.1**	**-2.0**	**-6.5**	**3.1**		**0.0**	**-0.8**	
of which: exceptional financing	-4.3	-5.5	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	41.4			45.0	54.9	68.7	81.0	100.6	114.9	120.7	101.5	94.5		73.1	53.7	
In percent of exports	...	...	138.9			137.6	154.0	175.9	205.4	250.6	264.4	291.6	228.1	194.2		136.1	121.9	
PV of PPG external debt	**...**	**...**	**27.0**			**31.8**	**34.9**	**36.6**	**38.4**	**39.3**	**39.4**	**39.0**	**33.8**	**32.2**		**29.5**	**28.4**	
In percent of exports	**...**	**...**	**90.6**			**97.1**	**97.9**	**93.7**	**97.5**	**97.9**	**90.8**	**94.1**	**76.1**	**66.2**		**54.9**	**64.4**	
In percent of government revenues	**...**	**...**	**110.7**			**121.6**	**138.9**	**142.2**	**146.3**	**146.4**	**146.0**	**146.5**	**127.5**	**122.7**		**105.7**	**84.9**	
Debt service-to-exports ratio (in percent)	**34.4**	**19.4**	**11.0**			**14.7**	**14.3**	**13.4**	**15.4**	**15.1**	**16.9**	**20.1**	**28.4**	**21.6**		**14.0**	**5.6**	
PPG debt service-to-exports ratio (in percent)	**1.9**	**2.0**	**0.0**			**3.4**	**3.8**	**4.1**	**4.4**	**4.7**	**4.5**	**4.8**	**3.7**	**3.4**		**3.1**	**5.4**	
PPG debt service-to-revenue ratio (in percent)	**2.9**	**2.8**	**0.0**			**4.3**	**5.3**	**6.2**	**6.7**	**7.0**	**7.2**	**7.4**	**6.2**	**6.3**		**5.9**	**7.1**	
Total gross financing need (Billions of U.S. dollars)	0.6	1.0	0.3			1.6	3.0	3.8	4.4	7.0	6.1	5.6	6.1	3.3		2.1	6.4	
Non-interest current account deficit that stabilizes debt ratio	11.9	38.4	32.9			34.2	29.9	26.0	24.8	25.0	20.7	21.2	36.4	14.8		21.1	9.4	
Key macroeconomic assumptions																		
Real GDP growth (in percent)	7.1	7.3	7.4	7.4	0.8	7.0	8.5	8.5	8.0	8.0	8.0	9.7	24.4	13.9	8.0	21.6	6.6	8.9
GDP deflator in US dollar terms (change in percent)	-10.5	22.7	5.5	5.6	9.7	-3.7	0.4	3.5	3.5	3.4	3.5	3.5	3.5	2.9	1.8	2.4	2.4	2.6
Effective interest rate (percent) 5/	2.4	3.0	2.4	3.1	1.0	3.2	3.4	3.8	4.4	4.8	5.4	5.9	6.1	5.3	4.2	4.2	1.9	3.5
Growth of exports of G&S (US dollar terms, in percent)	8.0	29.7	9.9	14.8	14.3	13.0	18.8	22.9	12.9	13.7	20.9	8.2	38.3	28.3	17.0	38.4	6.7	12.2
Growth of imports of G&S (US dollar terms, in percent)	3.9	62.8	33.8	18.6	19.1	10.1	12.8	15.5	5.7	19.7	2.1	-1.3	5.7	10.6	11.0	13.7	8.9	8.4
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	18.3	15.3	12.9	10.5	8.8	5.6	4.0	3.0	2.1	11.9	0.0	-5.8	-1.3
Government revenues (excluding grants, in percent of GDP)	20.5	22.2	24.4			26.1	25.1	25.7	26.3	26.9	27.0	26.6	26.5	26.2		27.9	33.5	30.4
Aid flows (in Billions of US dollars) 7/	0.9	1.0	0.8			1.1	1.1	1.0	1.0	0.9	0.8	0.8	0.7	0.7		0.6	0.3	
of which: Grants	0.9	1.0	0.8			0.7	0.8	0.7	0.7	0.6	0.6	0.5	0.5	0.5		0.4	0.2	
of which: Concessional loans	0.0	0.0	0.0			0.4	0.3	0.3	0.3	0.3	0.3	0.2	0.2	0.2		0.2	0.1	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			6.4	6.0	4.9	4.0	3.3	2.6	2.1	1.5	1.2		0.7	0.0	0.6
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			51.9	47.1	43.6	39.1	36.7	34.0	29.4	26.2	23.1		16.4	-1.0	11.7
Memorandum items:																		
Nominal GDP (Billions of US dollars)	9.5	12.6	14.2			14.7	16.0	17.9	20.1	22.4	25.0	28.4	36.6	42.9		57.1	129.6	
Nominal dollar GDP growth	-4.2	31.7	13.3			3.0	9.0	12.3	11.8	11.7	11.7	13.5	28.7	17.3	9.9	24.6	9.2	11.8
PV of PPG external debt (in Billions of US dollars)			3.7			4.5	5.5	6.5	7.6	8.7	9.8	11.0	12.3	13.6		16.6	36.3	
(PVt-PVt-1)/GDPt-1 (in percent)						5.8	6.8	6.4	6.2	5.4	4.7	4.7	4.6	3.7	5.9	3.4	2.0	2.9
Gross workers' remittances (Billions of US dollars)	...	...	...			...	...	...	...	...	...	...	...	...		...	...	
PV of PPG external debt (in percent of GDP + remittances)	...	...	27.0			31.8	34.9	36.6	38.4	39.3	39.4	39.0	33.8	32.2		29.5	28.4	
PV of PPG external debt (in percent of exports + remittances)	...	...	90.6			97.1	97.9	93.7	97.5	97.9	90.8	94.1	76.1	66.2		54.9	64.4	
Debt service of PPG external debt (in percent of exports + remittan	...	...	0.0			3.4	3.8	4.1	4.4	4.7	4.5	4.8	3.7	3.4		3.1	5.4	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2.Mozambique: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013-2033

(In percent)

	Projections											
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	**2023**	2033
PV of debt-to GDP ratio												
Baseline	32	35	37	38	39	39	39	34	32	33	**29**	28
A. Alternative Scenarios												
A1. 5 percent discount rate 1/	26	28	30	31	32	33	32	28	27	28	**25**	25
A2. New public sector loans on less favorable terms in 2013-2033 2/	32	37	40	44	46	47	47	41	40	42	**37**	40
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	32	35	38	39	40	40	40	35	33	34	**30**	29
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	32	40	54	54	54	53	51	43	40	40	**35**	29
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	32	36	41	43	44	44	43	38	36	37	**33**	31
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	32	59	81	79	77	74	70	59	53	52	**44**	31
B5. Combination of B1-B4 using one-half standard deviation shocks	32	57	85	83	81	78	74	62	56	55	**47**	33
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	32	49	52	54	55	56	55	48	45	46	**41**	40
PV of debt-to-exports ratio												
Baseline	97	98	94	97	98	91	94	76	66	69	**55**	64
A. Alternative Scenarios												
A1. 5 percent discount rate 1/	73	72	78	81	75	75	76	61	53	55	**45**	51
A2. New public sector loans on less favorable terms in 2013-2033 2/	97	103	103	111	114	108	113	93	82	86	**70**	92
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	97	96	93	96	97	90	93	75	65	67	**54**	63
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	97	133	200	199	194	176	178	141	120	121	**94**	96
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	97	96	93	96	97	90	93	75	65	67	**54**	63
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	97	166	207	200	191	170	169	132	109	108	**82**	70
B5. Combination of B1-B4 using one-half standard deviation shocks	97	175	261	253	241	215	214	167	138	137	**104**	89
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	97	96	93	96	97	90	93	75	65	67	**54**	63

Table 2.Mozambique: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2013-2033

(In percent)

	Projections											
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	**2023**	2033
Debt service-to-exports ratio												
Baseline	3	4	4	4	5	5	5	4	3	4	**3**	5
A. Alternative Scenarios												
A1. 5 percent discount rate 1/	3	4	4	4	5	5	5	4	3	4	**3**	5
A2. New public sector loans on less favorable terms in 2013-2033 2/	3	4	4	4	5	4	5	4	4	5	**4**	8
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	3	4	4	4	5	5	5	4	3	4	**3**	5
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	3	4	6	8	8	8	8	6	6	8	**6**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	3	4	4	4	5	5	5	4	3	4	**3**	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	3	4	6	8	8	7	7	5	6	8	**6**	7
B5. Combination of B1-B4 using one-half standard deviation shocks	3	4	7	10	10	9	9	7	8	10	**7**	9
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	3	4	4	4	5	5	5	4	3	4	**3**	5
Debt service-to-revenue ratio												
Baseline	4	5	6	7	7	7	7	6	6	7	**6**	7
A. Alternative Scenarios												
A1. 5 percent discount rate 1/	4	5	6	7	7	7	7	6	6	7	**6**	7
A2. New public sector loans on less favorable terms in 2013-2033 2/	4	5	6	7	7	7	7	6	7	8	**7**	10
B. Bound Tests												
B1. Real GDP growth at historical average minus one standard deviation in 2014-2015	4	5	6	7	7	7	8	6	6	7	**6**	7
B2. Export value growth at historical average minus one standard deviation in 2014-2015 3/	4	5	7	9	9	9	9	7	8	9	**8**	8
B3. US dollar GDP deflator at historical average minus one standard deviation in 2014-2015	4	6	7	8	8	8	8	7	7	8	**7**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2014-2015 4/	4	5	9	12	11	11	11	9	11	14	**11**	9
B5. Combination of B1-B4 using one-half standard deviation shocks	4	5	9	12	12	12	12	10	12	14	**12**	10
B6. One-time 30 percent nominal depreciation relative to the baseline in 2014 5/	4	8	9	10	10	10	11	9	9	9	**8**	10
Memorandum item:												
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	-4	-4	-4	-4	-4	-4	-4	-4	-4	-4	**-4**	-4

Sources: Country authorities; and staff estimates and projections.

1/ A discount rate of 5 percent is applied to the calcualtions of NPV of debt (discount rate is 3 percent in the baseline.)

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

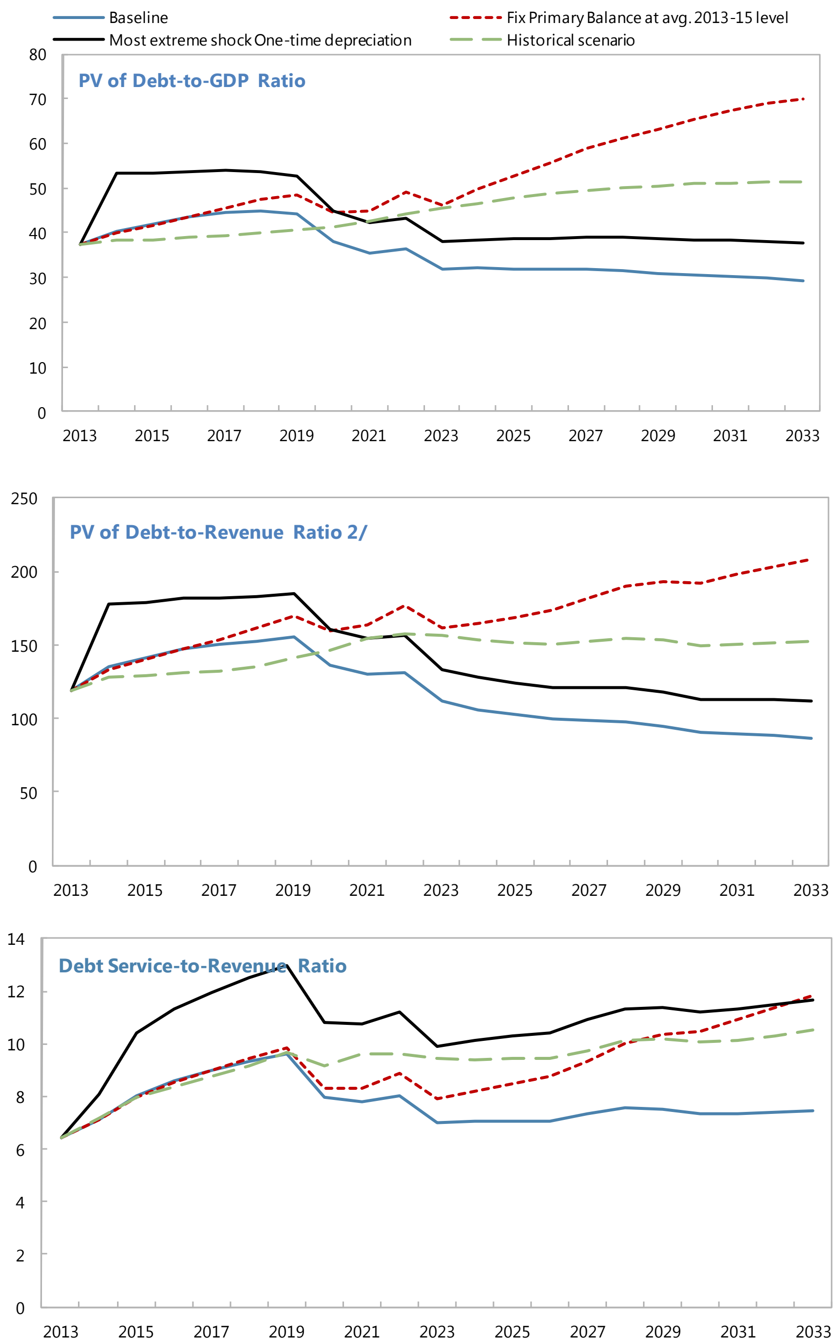
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Figure 2. Indicators of Public Debt Under Alternative Scenarios, 2013-2033 1/



Sources: Country authorities and IMF staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio in 2023.
2/ Revenues are defined inclusive of grants.

Table 3.Mozambique: Public Sector Debt Sustainability Framework, Baseline Scenario, 2010-2033

(Percent of GDP, unless otherwise indicated)

	Actual			Average 5/	Standard Deviation 5/	Projections													
	2010	2011	2012			2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2013-18 Average	2023	2033	2019-33 Average
Public sector debt 1/	46.1	39.3	42.2			47.1	50.2	51.3	52.5	52.9	52.4	51.2	43.3	40.3	40.7		35.4	30.8	
of which: foreign-currency denominated	40.2	32.6	36.3			41.7	44.7	45.9	47.4	47.7	47.1	45.8	39.3	36.9	37.6		33.1	30.0	
Change in public sector debt	0.5	-6.8	2.9			4.9	3.2	1.1	1.2	0.4	-0.5	-1.2	-7.8	-3.0	0.4		-5.3	-0.9	
Identified debt-creating flows	3.4	-8.1	3.5			3.9	2.3	0.8	1.1	0.2	-0.5	-1.3	-8.4	-3.7	-0.3		-6.0	-1.1	
Primary deficit	3.1	3.3	3.2	3.0	0.9	4.7	5.9	5.2	4.8	4.2	3.4	3.3	1.7	1.3	1.0	4.7	0.9	0.5	0.9
Revenue and grants	29.5	30.0	29.8			31.2	29.9	29.7	29.6	29.6	29.4	28.5	27.9	27.3	27.7		28.6	33.6	
Of which: grants	9.0	7.8	5.4			5.1	4.8	4.0	3.3	2.8	2.3	1.9	1.4	1.1	1.0		0.7	0.2	
Primary (noninterest) expenditure	32.5	33.4	33.0			35.9	35.8	34.9	34.4	33.8	32.8	31.8	29.6	28.6	28.7		29.5	34.1	
Automatic debt dynamics	0.5	-11.4	0.3			-0.8	-3.6	-4.5	-3.8	-4.0	-3.9	-4.6	-10.1	-5.0	-1.4		-6.9	-1.6	
Contribution from interest rate/growth differential	2.0	-9.5	-3.2			-0.5	-2.8	-4.1	-4.0	-3.9	-3.9	-4.6	-10.1	-5.1	-1.4		-6.9	-1.6	
Of which: contribution from average real interest rate	5.0	-6.3	-0.5			2.3	0.9	-0.2	-0.2	0.0	0.0	0.0	0.0	0.2	0.3		0.3	0.3	
Of which: contribution from real GDP growth	-3.0	-3.1	-2.7			-2.8	-3.7	-3.9	-3.8	-3.9	-3.9	-4.6	-10.0	-5.3	-1.7		-7.2	-2.0	
Contribution from real exchange rate depreciation	-1.5	-1.9	3.5			-0.3	-0.8	-0.3	0.2	0.0	0.0	0.0	0.0	0.2	0.0		...	...	
Other identified debt-creating flows	-0.2	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	-0.1	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	-0.1	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-2.9	1.3	-0.6			1.0	0.9	0.3	0.1	0.2	0.0	0.1	0.6	0.6	0.8		0.7	0.3	
Other Sustainability Indicators																			
PV of public sector debt	...	...	32.9			37.2	40.4	41.9	43.5	44.5	44.7	44.3	37.9	35.6	36.2		31.8	29.2	
Of which: foreign-currency denominated	...	...	27.0			31.8	34.9	36.6	38.4	39.3	39.4	39.0	33.8	32.2	33.2		29.5	28.4	
Of which: external	...	...	27.0			31.8	34.9	36.6	38.4	39.3	39.4	39.0	33.8	32.2	33.2		29.5	28.4	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...	...	...	...	...		...	...	
Gross financing need 2/	4.5	4.7	3.9			6.7	8.0	7.6	7.4	6.8	6.2	6.0	3.9	3.4	3.2		2.9	3.0	
PV of public sector debt-to-revenue and grants ratio (percent)	...	...	110.2			119.3	135.2	141.2	147.1	150.3	152.3	155.3	135.7	130.1	130.9		111.3	86.8	
PV of public sector debt-to-revenue ratio (percent)	...	...	134.8			142.3	160.8	163.1	165.6	165.7	165.5	166.5	142.8	135.5	135.6		114.2	87.2	
Of which: external 3/	...	...	110.7			121.6	138.9	142.2	146.3	146.4	146.0	146.5	127.5	122.7	124.2		105.7	84.9	
Debt service-to-revenue and grants ratio (percent) 4/	4.8	4.6	2.4			6.4	7.1	8.0	8.6	9.0	9.3	9.6	8.0	7.8	8.0		7.0	7.4	
Debt service-to-revenue ratio (percent) 4/	7.0	6.3	2.9			7.6	8.4	9.2	9.7	9.9	10.2	10.3	8.4	8.1	8.3		7.2	7.5	
Primary deficit that stabilizes the debt-to-GDP ratio	2.6	10.1	0.3			-0.1	2.7	4.2	3.7	3.8	3.9	4.5	9.5	4.3	0.6		6.2	1.4	
Key macroeconomic and fiscal assumptions																			
Real GDP growth (percent)	7.1	7.3	7.4	7.4	0.8	7.0	8.5	8.5	8.0	8.0	8.0	9.7	24.4	13.9	4.4	8.0	21.6	6.6	8.9
Average nominal interest rate on forex debt (percent)	0.6	0.9	0.0	0.6	0.4	1.2	1.5	1.7	1.9	2.0	2.1	2.3	2.4	2.5	2.6	1.7	2.7	3.4	2.9
Average real interest rate on domestic debt (percent)	4.6	5.3	8.6	6.1	7.6	9.5	10.4	10.1	10.5	11.3	11.0	10.8	8.4	8.4	8.4	10.5	8.4	8.4	8.6
Real exchange rate depreciation (percent, + indicates depreciatio	-3.4	-6.2	11.9	1.0	12.2	-1.0	...	...	...	...	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, percent)	10.5	8.1	3.0	7.2	2.4	5.0	5.6	5.6	5.6	5.6	5.6	5.6	5.6	5.6	5.6	5.5	5.6	5.6	5.6
Growth of real primary spending (deflated by GDP deflator, perc	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.0	0.1	0.2	0.1	0.0	0.1	0.3	0.1	0.1
Grant element of new external borrowing (percent)	...	...	...	...	...	18.3	15.3	12.9	10.5	8.8	5.6	4.0	3.0	2.1	1.2	11.9	0.0	-5.8	-1.3

Sources: Country authorities; and staff estimates and projections.

1/ Covers nonfinancial public sector. Gross debt is used.

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4.Mozambique: Sensitivity Analysis for Key Indicators of Public Debt 2013-2033

	Projections										
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2023	2033
PV of Debt-to-GDP Ratio											
Baseline	37	40	42	44	45	45	44	38	36	32	29
A. Alternative scenarios											
A1. Real GDP growth and primary balance are at historical averages	37	38	38	39	39	40	40	41	43	45	51
A2. Primary balance is unchanged from 2013-15 average	37	40	42	44	46	47	48	44	45	46	70
A3. Permanently lower GDP growth 1/	37	41	42	44	45	46	45	39	37	34	37
B. Bound tests											
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	37	42	45	47	49	50	50	43	41	38	41
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	37	39	39	41	42	43	42	36	34	31	29
B3. Combination of B1-B2 using one half standard deviation shocks	37	39	39	42	44	45	45	39	38	35	38
B4. One-time 30 percent real depreciation in 2014	37	53	53	54	54	54	53	45	42	38	38
B5. 10 percent of GDP increase in other debt-creating flows in 2014	37	49	50	51	51	51	50	42	40	35	31
PV of Debt-to-Revenue Ratio 2/											
Baseline	119	135	141	147	150	152	155	136	130	111	87
A. Alternative scenarios											
A1. Real GDP growth and primary balance are at historical averages	119	128	129	131	133	135	141	147	154	157	152
A2. Primary balance is unchanged from 2013-15 average	119	134	140	147	154	161	170	159	164	162	208
A3. Permanently lower GDP growth 1/	119	135	142	148	152	155	159	140	135	118	109
B. Bound tests											
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	119	138	150	158	164	168	174	154	150	132	122
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	119	129	132	139	142	145	148	130	125	108	85
B3. Combination of B1-B2 using one half standard deviation shocks	119	129	132	141	148	153	158	141	137	122	112
B4. One-time 30 percent real depreciation in 2014	119	178	179	182	182	183	185	161	155	133	112
B5. 10 percent of GDP increase in other debt-creating flows in 2014	119	165	168	172	173	174	175	152	145	122	92
Debt Service-to-Revenue Ratio 2/											
Baseline	6	7	8	9	9	9	10	8	8	7	7
A. Alternative scenarios											
A1. Real GDP growth and primary balance are at historical averages	6	7	8	8	9	9	10	9	10	9	11
A2. Primary balance is unchanged from 2013-15 average	6	7	8	9	9	9	10	8	8	8	12
A3. Permanently lower GDP growth 1/	6	7	8	9	9	9	10	8	8	7	8
B. Bound tests											
B1. Real GDP growth is at historical average minus one standard deviations in 2014-2015	6	7	8	9	9	10	10	9	8	8	9
B2. Primary balance is at historical average minus one standard deviations in 2014-2015	6	7	8	8	9	9	9	8	8	7	7
B3. Combination of B1-B2 using one half standard deviation shocks	6	7	8	8	9	9	10	8	8	7	8
B4. One-time 30 percent real depreciation in 2014	6	8	10	11	12	13	13	11	11	10	12
B5. 10 percent of GDP increase in other debt-creating flows in 2014	6	7	9	9	10	10	10	8	8	8	8

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

June 10, 2013

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION, SIXTH REVIEW UNDER THE POLICY SUPPORT INSTRUMENT, REQUEST FOR A THREE-YEAR POLICY SUPPORT INSTRUMENT AND CANCELLATION OF CURRENT POLICY SUPPORT INSTRUMENT—INFORMATIONAL ANNEX

Prepared By | African Department

CONTENTS

RELATIONS WITH THE FUND

(As of March 31, 2013)

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

General Resources Account:	**SDR Million**	**%Quota**
Quota	113.60	100.00
Fund holdings of currency (Exchange Rate)	113.60	100.00
Reserve Tranche Position	0.0.1	0.0.1

SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	108.84	100.00
Holdings	105.23	96.69

Outstanding Purchases and Loans:	**SDR Million**	**%Allocation**
ESF Arrangements	113.60	100.00
ECF Arrangements	6.34	5.58

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ESF	Jun 30, 2009	Jun 28, 2010	113.60	113.60
ECF[1]	Jul 06, 2004	Jul 05, 2007	11.36	11.36
ECF	Jun 28, 1999	Jun 28, 2003	87.20	78.80

[1]Former PRGF.

Projected Payments to Fund[2]

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2013	2014	2015	2016	2017
Principal	1.95	1.95	23.09	23.70	23.21
Charges/ Interest	0.29	0.30	0.26	0.20	0.14
Total	2.24	2.25	23.35	23.90	23.35

Implementation of HIPC Initiative:

	Original Framework	Enhanced Framework	Total
I. Commitment of HIPC assistance			
Decision point date	Apr 1998	Apr 2000	
Assistance committed by all creditors (US$ Million)[3]	1,716.00	306.00	
Of which: IMF assistance (US$ million)	124.60	18.46	
(SDR equivalent in millions)	93.17	13.73	
Completion point date	Jun. 1999	Sep. 2001	
II. Disbursement of IMF assistance (SDR Million)			
Assistance disbursed to the member	93.17	13.73	106.90
Interim assistance	--	2.31	2.31
Completion point balance	93.17	11.42	104.58
Additional disbursement of interest income[4]	--	1.10	1.10
Total disbursements	93.17	14.83	108.00

Implementation of Multilateral Debt Relief Initiative (MDRI):

[2]When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

[3]Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts cannot be added.

[4]Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

I.	MDRI-eligible debt (SDR Million)[5]	106.56
	Financed by: MDRI Trust	83.05
	Remaining HIPC resources	23.51

II. Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	**GRA**	**PRGF**	**Total**
January 2006	N/A	106.56	106.56

Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable

Safeguards assessment

An update safeguards assessment of the Bank of Mozambique (BM) was completed on January 11, 2010 for the ESF. The assessment found improvements in financial reporting practices following the implementation of IFRS. It noted vulnerabilities in the oversight mechanism for external and internal auditing, controls, financial reporting, and in the BM's legal structure. It recommended that the BM commission an external quality assurance review of the internal audit function.

Exchange Rate Arrangement

Mozambique has a de jure and de facto floating exchange rate arrangement. The exchange rate is largely determined in the interbank foreign exchange market (MCI). The BM regularly intervenes in the market to smooth seasonal fluctuations, provide foreign exchange liquidity received by the government in the form of aid, and sterilize domestic liquidity as part of its monetary policy operations.

On May 20, 2011, Mozambique accepted its obligations under Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement (www.imf.org). A new foreign exchange law—"Foreign Exchange Law" Law No. 11/2009—came into effect on March 11, 2009. A new foreign exchange regulation to implement the foreign exchange law—the "Regulation for the Foreign Exchange Law" (the "Regulation") (Decreto No. 83/2010)—was issued on December 31, 2010. The Regulation, in conjunction with the implementing norms subsequently issued by the BM, fully removed the existing exchange restrictions subject to Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement as of July 11, 2011. The two existing multiple currency practices (MCP) were also removed. The MCP arising from the foreign exchange auction system was removed on April 27, 2011 through the adoption of a new regulation on the interbank exchange market and that discontinued the previous multiple price foreign exchange auction system, which in any case had not been used since 2009. The

[5] The MDRI provides 100 percent debt relief to eligible member countries qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 outstanding at the time the member qualifies for debt relief.

MCP arising from the absence of a mechanism to prevent potential deviations between the rate used by the BM in its foreign exchange transactions in the interbank foreign exchange market and in its transactions with the government, public entities and the World Bank was removed on July 1, 2011 through the adoption of a new mechanism for the determination of the exchange rate for such transactions of which the relevant parties have been notified on August 11, 2011.

AML/CFT framework

Mozambique's first AML/CFT Mutual Evaluation Report by the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) has been formally adopted by ESAAMLG and published on its website. Based on the deficiencies identified in the report, the Financial Action Task Force's (FATF) International Co-operation Review Group (ICRG) maintains Mozambique in a pool of jurisdictions which may be taken up for review. This process is designed to publicly identify high-risk jurisdictions, and could ultimately result in a public statement by the FATF to apply counter-measures. In order to improve compliance with the FATF Recommendations, the Financial Intelligence Unit (GIFIM) has begun its operations and is working towards membership of the Egmont Group of Financial Intelligence Units. However, the number of suspicious transaction reports (STRs) still appears to be low. Once the AML/CFT law is approved by Parliament, the BM intends to issue implementing guidelines. In order to ensure a consistent application of the AML/CFT framework across various regulators, the Government has established and appointed the members of the National AML/CFT Task Force in December 2011. The AML/CFT strategic plan has been approved by the Council of Ministers and will be submitted to ESAAMLG.

Article IV Consultation

In accordance with Decision No 12794–(02/76), as amended by Decision No 12854–(02/96), Mozambique is on a 24-month Article IV cycle due to the approval of the successor PSI in June 2010. The 2011 Article IV consultation was completed by the Executive Board on June 17, 2011 (Country Report No. 11/149).

In concluding the 2011 Article IV consultation, Executive Directors commended the authorities for their prudent policies that have resulted in a strong economic performance. They noted that, although Mozambique's medium-term prospects continue to be favorable, significant challenges remain in managing macroeconomic risks and ensuring that the benefits from growth are shared fairly across the population. In this regard, Directors underscored that safeguarding price stability and containing inflation expectations remain key policy priorities for the period ahead. They welcomed the authorities' new Poverty Reduction Strategy (PARP), including its focus on continued structural reforms to improve productivity and production in labor-intensive sectors such as agriculture, create jobs through improvements in the business environment, and pursue social and human development. These focus areas will be important to achieve sustained growth and poverty reduction. Directors supported the authorities' prudent fiscal stance aimed at preserving macroeconomic stability and debt sustainability, and encouraged the authorities to adopt a prudent approach to generating additional budgetary revenue from the natural resource sector while protecting Mozambique as a destination for foreign investment. Directors emphasized the importance of adhering to a prudent borrowing strategy, further strengthening debt management, and improving investment planning. They noted the resilience of the banking system during the global crisis, and recommended continued vigilance in light of remaining vulnerabilities.

Ex post assessment of performance under Fund-supported programs

An ex post assessment (EPA) of Mozambique's performance under Fund-Supported Programs since 1987 was undertaken in December 2003 under the guidelines on assessments of countries with a longer-term program engagement. The EPA was circulated to the Executive Board on November 21, 2003 (Country Report No. 04/53).
Directors commended the authorities for their pursuit of sound macroeconomic policies and wide ranging structural reforms over the past fifteen years which contributed to strong growth of the economy, and a steady decline in poverty rates. Noting that despite considerable progress Mozambique remains a very poor and vulnerable country, Directors urged the authorities to persevere in their efforts to consolidate macroeconomic stability and accelerate and deepen structural reforms with a view to sustaining economic growth, encouraging employment creation, and further reducing poverty.

FSAP participation and ROSCs

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

Management's visit

At the invitation of the authorities, Mr. Kato, Deputy Managing Director, visited Maputo, Mozambique in July 2005. Mr. de Rato, Managing Director, visited Mozambique on August 2007 for a meeting with the African Consultative Group on Quotas, Voice, and Representation. Mr. Lipton, Deputy Managing Director, visited Maputo, in May 2013.

Resident representative

Mr. Victor Lledo has been the IMF's resident representative to Mozambique since June 21, 2010.

Technical Assistance (2005–2013)

IMF Technical Assistance Provided to Mozambique (2005–13)
(As of May 8, 2013)

Departments	Timing	Form	Purpose	Counterparts
Finance	February 2008	Mission	Update of Safeguard Assessment	Bank of Mozambique
Fiscal Affairs	May 2013	Mission	MNRW-TTF - Public Consultation of the revised Fiscal Regime for Mining and Petroleum	Ministry of Finance, Ministry of Mineral Resources
	April 2013	Mission	Annual follow-up on PFM reforms	Ministry of Finance
	April 2013	Peripatetic expert	Public Accounting	Ministry of Finance
	March-April 2013	Mission	Follow-Up on Revenue Administration (including an expert specialized in HR)	Ministry of Finance
	March-April 2013	Peripatetic expert	Taxpayer Service	Ministry of Finance
	March-April 2013	Mission	MNRW-TTF – Tax administration action plan for effectively managing increased natural resources collections (jointly with FAD annual Follow-Up on Revenue Administration)	Ministry of Finance, Ministry of Mineral Resources
	March 2013	Peripatetic expert	Transfer Pricing	Ministry of Finance
	November 2012	Peripatetic expert	Large Taxpayers	Ministry of Finance
	November 2012	Mission	MNRW-TTF - Macro-fiscal framework	Ministry of Finance, Ministry of Mineral Resources
	July 2012	Mission	MNRW-TTF - Revised fiscal regimes of the Extractive Sector	Ministry of Finance, Ministry of Mineral Resources
	April-May 2012	Mission	Follow-Up on Revenue Administration	Ministry of Finance
	April 2012	Mission	Follow-Up on Tax Policy	Ministry of Finance
	April 2012	Mission	Fiscal Regime of the	Ministry of Finance

IMF Technical Assistance Provided to Mozambique (2005–13) (As of May 8, 2013)				
Departments	**Timing**	**Form**	**Purpose**	**Counterparts**
			Extractive Sector	Ministry of Mineral Resources
	March-April 2102	Peripatetic expert	Public Accounting	Ministry of Finance
	March-April 2102	Mission	Public Financial Management Reforms	Ministry of Finance
	March 2012	Peripatetic expert	Tax Administration	Ministry of Finance
	November 2011	Mission	Tax Administration	Ministry of Finance
	September 2011	Peripatetic expert	Public Accounting	Ministry of Finance
	September 2011	Peripatetic expert	Tax Administration	Ministry of Finance
	April 2011	Peripatetic expert	Tax Administration	Ministry of Finance
	April 2011	Mission	Follow-Up on Revenue Administration	Ministry of Finance
	March 2011	Mission	Public Financial Management Reforms	Ministry of Finance
	March 2011	Peripatetic expert	Public Accounting	Ministry of Finance
	November 2010	Peripatetic expert	Public Financial Management Reforms	Ministry of Finance
	April–May 2010	Mission	Revenue Administration Reform	Ministry of Finance
	April 2010	Mission	Public Financial Management Reforms	Ministry of Finance
	Feb.-Mar. 2010	Mission	Tax Policy Review	Ministry of Finance
	May 2009	Mission	Tax Administration Reform	Ministry of Finance
	April 2008	Mission	Public Financial Management Reforms	Ministry of Finance
	April–May 2008	Mission	Revenue Administration Reform	Ministry of Finance
	Oct.–Nov. 2007	Mission	Tax Administration Inspection	Ministry of Finance
	September 2007	Mission	Public Private Partnerships and Fiscal Risks	Ministry of Finance
	August 2007	Peripatetic expert	Tax Policy and Administration	Ministry of Finance

IMF Technical Assistance Provided to Mozambique (2005–13) (As of May 8, 2013)				
Departments	**Timing**	**Form**	**Purpose**	**Counterparts**
	August 2007	Mission	Fiscal ROSC Update and Public Financial Management inspection	Ministry of Finance
	April–May 2007	Mission	Tax Administration Inspection	Ministry of Finance
	April–May 2007	Mission	Petroleum Fiscal Regime	Ministry of Finance Ministry of Mineral Resources
	December 2006	Mission	Tax Administration	Ministry of Finance
	March 2006	Mission	Tax Policy Review	Ministry of Finance
Legal	April 2013	Mission	AML/CFT Diagnostic Project (Part Two)	Bank of Mozambique/GIFI M
	June 2012	Mission	AML/CFT Diagnostic Project (Part One)	Bank of Mozambique/GIFI M
Monetary and Financial Sectors	December 2012	Mission	Payment Systems Oversight and Stress Testing (Follow up)	Bank of Mozambique
	December 2012	Short-term Expert	Medium-Term Debt Management reforms (Follow-up)	Ministry of Finance
	October 2012	Mission	Developing a Payment System Oversight Function (Follow up)	Bank of Mozambique
	April-May 2012	Mission	Developing a Payment System Oversight Function (Follow up)	Bank of Mozambique
	May 2012	Short-term Expert	Monetary Policy Framework	Bank of Mozambique
	April 2012	Short-term Expert	Stress testing	Bank of Mozambique
	February 2012	Short-term Expert	Developing a payment system oversight function	Bank of Mozambique
	December 2011	Short-term Expert	Developing a payment system oversight function	Bank of Mozambique
	September 2011	Mission	Follow-up on Medium-Term Debt Strategy and Capacity to Conduct Debt and Project Analysis	Minister of Finance Bank of Mozambique

IMF Technical Assistance Provided to Mozambique (2005–13) (As of May 8, 2013)				
Departments	**Timing**	**Form**	**Purpose**	**Counterparts**
	August 2011	Short-term Expert	Monetary Policy Framework	Bank of Mozambique
	September 2010	Mission	Follow-up on Medium-Term Debt Strategy, Debt Markets, and Capacity to Conduct Debt and Project Analysis	Minister of Finance Bank of Mozambique
	June 2010	Mission	Medium-Term Debt Strategy Debt Markets, and Capacity to Conduct Debt and Project Analysis	Minister of Finance Bank of Mozambique
	April 2010	Short-term Expert	Strengthening Monetary Policy Formulation and Implementation	Bank of Mozambique
	November 2009	Short-term Expert	Strengthening Monetary Policy Formulation and Implementation	Bank of Mozambique
	May 2009	Mission	2009 FSAP Follow up	Bank of Mozambique
	February 2009	Mission	TA on Central Banking and Monetary Policy Formulation	Bank of Mozambique
	May 2008	Mission	Strengthening Monetary Policy Formulation and Implementation	Bank of Mozambique
	December 2007	Mission	Implementation of IFRS for Central Bank Accounts.	Bank of Mozambique
	August 2007	Mission	Post-FSAP TA Assessment: Banking supervision, Monetary Policy and Operations	Bank of Mozambique
	April 2007	Short-term consultant	Banking Supervision	Bank of Mozambique
	October 2006	Mission	Post-FSAP TA Assessment: Banking supervision, Monetary Policy and Operations	Bank of Mozambique
	Feb-March 2006	Mission	AML/CFT legislation	Bank of Mozambique
	Jan–Feb 2006	Short-term consultant	Monetary Policy Framework	Bank of Mozambique

IMF Technical Assistance Provided to Mozambique (2005–13) (As of May 8, 2013)				
Departments	**Timing**	**Form**	**Purpose**	**Counterparts**
	Jan–Feb 2006	Short-term consultant	Monetary Operations	Bank of Mozambique
	January 2006	Short-term consultant	Exchange Rate Management	Bank of Mozambique
Statistics	February 2013	Mission	Balance of Payments Statistics and International Investment Position Statistics (Follow-up)	Bank of Mozambique
	April 2012	Mission	Government Finance Statistics	National Institute of Statistics
	March-April 2012	Mission	Consumer Price Statistics	National Institute of Statistics
	November-December 2011	Mission	Balance of Payments	Bank of Mozambique
	February 2010	Mission	Multitopic GDDS	National Institute of Statistics
	March–April 2008	Mission	National Accounts Statistics	National Institute of Statistics
	February 2008	Mission	Balance of Payments Statistics	Bank of Mozambique
	December 2007	Mission	Balance of Payments Statistics	Bank of Mozambique
	November 2007	Mission	Monetary and Financial Statistics	Bank of Mozambique
	June–July 2006	Mission	Consumer Price Statistics	National Institute of Statistics (INE)
	August 2005–July 2006	Long-term consultant	National Accounts Statistics	National Institute of Statistics
	July 2005	Mission	Government Finance Statistics	National Institute of Statistics
AFRITAC South	April-May 2013	Peripatetic expert	Post Control Audit (mainly focused on customs but also on joint auditing with taxes)	Ministry of Finance
	April-May 2013	Peripatetic expert	Audit Training in specialized sectors of activity (taxes)	Ministry of Finance
	March-April 2013	Peripatetic expert	VAT refunds system	Ministry of Finance
	February–March 2013	Peripatetic expert	Public Investment Management	Ministry of Finance, Ministry of Planning and Development

IMF Technical Assistance Provided to Mozambique (2005–13) (As of May 8, 2013)				
Departments	**Timing**	**Form**	**Purpose**	**Counterparts**
	December 2012	Peripatetic expert	PFM Careers Restructuration	Ministry of Finance
	August 2012	Peripatetic expert	Cash Management	Ministry of Finance
	April 2012	Mission	PFM reforms / Planning mission	Ministry of Finance
	April 2012	Mission	Revenue Administration / Planning mission (AFS)	Ministry of Finance

WORLD BANK-IMF COLLABORATION

(As of May 8, 2013)

59. The Fund Mozambique team met with the World Bank Mozambique team in Maputo during the sixth PSI review mission in April 2013. The objective was to identify macro-critical structural reforms and to coordinate the two teams' work for the period May 2013 to April 2014.

2. **The teams agreed that Mozambique's main macroeconomic challenge is to sustain higher and more inclusive economic growth going forward**. To meet this challenge, Mozambique needs to enable broader-based economic activity led by the private sector, in particular in areas where it has competitive advantages, such as agriculture, trade-related services in support of booming commodity export sectors, labor-intensive manufacturing, and tourism. Given the low level of infrastructure, this will entail policies and reforms to boost public investment, coupled with enhancements in the business environment. As traditional aid is on a gradual declining trend, increasing public investment may require resorting to nonconcessional financing and stepping up capacity in the investment selection and debt management areas.

3. **Based on this shared assessment, the teams identified seven structural reform areas as macro-critical, in view of their central role in achieving higher and more inclusive growth:**

Debt management and investment planning. The authorities' ambitious investment program will need to be backed by a strong reform agenda to enhance capacity to manage fiscal risks and ensure value for money. In the field of investment selection, several measures are being implemented to establish an investment pipeline and define project selection standards and protocols. A new legal framework supporting private-public partnership and concessions is being implemented. Debt management will be strengthened to ensure that borrowing and investment decisions entail value for money. This is underpinned by a new medium-term debt strategy.

Public financial management. The focus will be on enhancing the capacity to manage risks outside the central government, including in the area of state-owned enterprises (SOEs) and decentralized administrative units. To achieve this objective, the authorities will step up risk-based controls and audits, continue rolling out their new PFM system, and enhance budget execution and monitoring reports. Other critical measures aim at enhancing control of the wage bill, both in budget preparation and execution. These reforms are macro-critical since they will create fiscal space needed to reduce poverty and increase priority spending, while managing risks related to SOE's large-scale investment plans and enhancing the government's oversight.

Tax administration. Despite the strong increase in revenue collections, the tax system is still complex to administer and comply with. It is marked by numerous tax benefits and an overall low contribution from the mega-project sectors. Going forward, the government plans to facilitate tax compliance through electronic tax payment and continue to expand the tax base to cover the large informal sector. The revenue management system will be enhanced, in line with a set of agreed performance indicators. The large tax-payers unit will be made fully operational.

Social safety nets. Two decades of high GDP growth have not yet resulted in significant poverty reduction. This, in turn, undermines the country's long-term growth potential. To address this, the authorities have started to strengthen their safety nets. Measures include: (i) rationalizing and expanding health insurance coverage; (ii) strengthening higher education and vocational training; (iii) strengthening the financial sustainability and administration of the National Social Security Fund, and creating a new pension system for private sector workers; and (iv) improving the targeting of social protection systems to the most needy. These measures are macro-critical, as better health and education services, stronger pensions systems, and a more effective social safety net can enhance the productivity of the workforce and support social cohesion.

Natural resource wealth. Mozambique is endowed with rich natural resource reserves which are largely not exploited so far. With the recently started coal projects in Tete and a series of other projects in the coming years, the extractive sector is slated for a boom which could make significant contributions to the country's economic growth and government revenues. This poses challenges for economic management, the sector's legal and regulatory frameworks and the government's capacity in managing contracts and revenues. In addition, Mozambique has attained full membership of the Extractive Industries Transparency Initiative (EITI).

Investment climate. Mozambique's private sector is held back by the high costs of doing business. These arise mainly from weaknesses in governance, access to finance, power supply, tax and regulatory systems, and contract enforcement. Wide-ranging reforms are needed to address these issues. They are macro-critical because a better investment climate is conducive to supporting private sector activities, thereby broadening the country's productive and export base, creating jobs, and thus helping reduce poverty.

Financial sector stability and development. Strong past growth of credit to the private sector, the expansion of the banking system and its potential exposure to cross-border risks call for strengthening the continuous supervision of the financial sector, as well as the capacity to identity and address potential sources of vulnerabilities. Meanwhile, improving financial intermediation and access to credit remains a top priority. To this end, the authorities have prepared the 2013-22 Financial Sector Development Strategy which includes a wide-ranging and clearly sequenced action plan, covering ways to, among other things, enhance financial inclusion, competition, consumer protection, and financial literacy.

4. **The teams agreed on the following division of labor:**

Debt management and investment planning reforms. The Fund will continue to play a key role in building government capacity to assess debt sustainability and define a coherent debt strategy through TA and continued support from HQ. Both institutions will assist the authorities in strengthening their debt management capacity, with TA support from the Fund and on-site assistance from the Bank. The Fund will continue to play a key role in helping the authorities plan investments, in line with recent TA and program commitments. The Bank will continue providing technical assistance for enhancing project investment management. The Fund review missions will provide further opportunities to assess progress in this field and discuss possible actions with the Bank.

Public financial management reform. The Bank and the Fund will cooperate in the field of rolling out the new PFM system to cover local administrations and SOEs engaging in large-scale infrastructure investments. The Fund will secure its support through regular TA missions from its AFRITAC South office. The Bank will provide ongoing consultation from its local office and supervision missions of projects under implementation in this area. The Fund program review missions will provide further opportunities to assess progress in this field.

Tax administration reforms. The Fund will provide support through ongoing advice based on regular TA. The Bank will advance reforms in this area in the context of its business environment policies and portfolio.

Social safety net reform. The Bank will take the lead in this field through continued TA in the design of more comprehensive and performing safety nets, in cooperation with other development partners and international organizations (including UNICEF and ILO). The Fund will play its role in identifying the fiscal space for the safety nets. The results will be discussed among the collaborators on a regular basis, so as to inform policy discussions with the authorities. The Bank is also taking the lead in public pension reforms.

Natural resource wealth. The Fund will provide TA under the newly established Topical Trust Fund for Managing Natural Resource Wealth (TTF-MNRW), relating to the fiscal regime of the extractive sector, revenue forecasting, and natural resource statistics, all being crucial to increase the sector's contribution to the budget and support the country's development agenda. The Bank is supporting Mozambique's implementation of EITI through its Multi-donor Trust Fund (MDTF). The Bank also funds the update of the mining law and regulations and the model mining contract, and the development of a concessions database for gas and mining projects to support the government's forecasting and contract monitoring functions. The Bank is also implementing a program of analytical support for enhanced fiscal policy in a resource rich setting, including a public expenditure review.

Investment climate reform. The Bank will take the lead in working with government to enhance the investment climate, by deepening its agenda to help the authorities cut red tape and simplify the legal and regulatory framework. The results will be shared on an ongoing basis and discussed during the Fund program review missions.

Financial sector stability and development. The Fund will continue to help the Bank of Mozambique to build its capacity to assess risks to financial stability of the banking sector, while the Bank will take the lead in supporting financial sector development and reforms, including through enhanced financial inclusion, competition, consumer protection, and financial literacy. The results of their respective work will be shared and discussed regularly.

5. **The teams have the following requests for information from their counterparts:**

- The Fund team requests to be kept informed of progress in the above macro-critical structural reform areas. Timing: when milestones are reached; and at least semiannually during Fund program review missions.

- The Bank team requests to be kept informed of the Fund's assessments of macroeconomic policies and prospects, and analytical work on areas under the Fund’s lead, as well as on recommendations of Fund TA missions. Timing: in the context of Fund program review and other missions, and at least semi-annually.

6. **The table below lists the teams' separate and joint work programs during May 2013-April 2014.**

Mozambique: Bank and Fund planned activities in macro-critical structural reform areas, May 2013-April 2014			
Title	**Products**	**Timing of Missions**	**Expected delivery date**
1. Bank Work Program	FSTAP project support to financial sector reforms	Ongoing	Ongoing
	Structural reforms: procurement, decentralization, business environment, financial sector	Ongoing	Ongoing
	Support on targeted, sustainable safety net measures (including public works system)	Ongoing	Ongoing
	TA on public investment management	Ongoing	Ongoing
2. Fund Work Program	First Review under the 2013-16 PSI	October 2013	December 2013
	Second Review under the 2013-16 PSI	March 2014	June 2014
	Annual TA follow-up mission on PFM	Mar-Apr. 2014	June 2014
	Annual TA follow-up on tax administration	Mar-Apr. 2014	June 2014
	MNRW-TTF: FARI, macro fiscal issues	2013	2013
	TA on Natural Resources Statistics	2013	2013
	TA on price statistics	2013	2013
	TA on GDP by production and by expenditure	2013	2013
	TA on risk Based supervision framework	2013	2013
3. Joint Work Program	PFM: continue to monitor consolidation and expansion of e-SISTAFE	Ongoing	Ongoing
	Policy advice on public sector salary reforms (incl. pensions)	Ongoing	Ongoing
	Review of tax policy	TBD	TBD
	Policy advice on natural resource wealth management	Ongoing	Ongoing
	Social Protection: Design of programs and assessment of fiscal space	Ongoing	Ongoing

STATISTICAL ISSUES

I. Assessment of Data Adequacy for Surveillance
General: Data provision has some shortcomings, but is broadly adequate for surveillance. Despite the increase in budget resources allocated to the compilation of official statistics, continued high reliance on external funding raises concerns about the sustainability of the programs of the National Institute of Statistics (INE). The authorities are making efforts to improve the quality and timeliness of economic and financial data through participation in the Fund's General Data Dissemination System (GDDS) and in the external sector module of the GDDS Project for Anglophone African Countries (funded by the U.K. Department for International Development (DFID)). Weaknesses exist, particularly in the areas of national accounts, prices, and government finance statistics.
Real sector statistics: The national accounts are prepared by the INE in accordance with the *1993 System of National Accounts* (*1993 SNA*). In August 2007, the INE released quarterly GDP estimates at constant prices covering 2000–07 for the first time, along with a revised annual GDP series for the period 1991–2006, with 2003 as the new base year. The authorities are working to strengthen quarterly national accounts compilation at current prices. The INE's new household income and expenditure survey and economic censuses leading to a new business registry still need to be incorporated to strengthen the national accounts. A revamped consumer price index for Maputo based on weights derived from the 2008–09 household survey was released in February 2011. A national index obtained by integrating the indices for Maputo, Beira, and Nampula was released in April 2006. INE has adopted a new software from INE Portugal which helps to correct a probable downward bias caused by carry-forward techniques for discontinued products. Several issues remain outstanding, however, including how to improve the housing market rent sample and expand coverage to include the Quelimane and Greater Maputo areas. There are insufficient sectoral labor market and employment data, and where available, they have limited coverage. A one-year labor market survey of the entire country, undertaken by INE in collaboration with the Labor Ministry, was launched in October 2004.
Monetary and financial statistics: A 2004 work plan was developed to implement the *Monetary and Financial Statistics Manual (MFSM*) and develop an integrated monetary database (IMD) to meet the needs of the Bank of Mozambique (BM), AFR, and STA. In November 2007 the IMD was completed and allows the derivation of accurate and timely monthly monetary statistics, while reducing BM's reporting burden.
Balance of payments: With assistance from STA, provided in the context of the GDDS regional project, the BM has made significant progress toward compiling and disseminating balance of payments (BOP) and international investment position (IIP) statistics that are fully aligned with the *Balance of Payments Manual, fifth edition* (*BPM5*). The BM has an adequate institutional framework for the compilation of BOP and IIP statistics. However, further strengthening of

external sector statistics needs to focus on: strengthening information technology (especially to apply data warehouse and on-line analytical processing tools); excluding the effects of price and exchange rate fluctuations from reserve asset flows; applying a methodology (provided through STA technical assistance) to estimate reinvested profits and stocks of financial assets and liabilities held abroad by the nonfinancial public sector; improving business surveys; publishing methodological notes, in general, and more data covering the Reserves Template, foreign direct investment, goods trade and current transfers; and beginning the gradual process to implement the new Balance of Payments and International Investment Position Manual, sixth edition. Joint work with other institutions to improve the quality of external trade data, especially with regard to price and volume indices, also merits attention.	
II. Data Standards and Quality	
Mozambique commenced its participation in the General Data Dissemination System (GDDS) in November 2003; but has since then not updated much of its metadata.	In May 2005, an update of the June 2002 data module of the Report on the Observance of Standards and Codes (Data ROSC) was prepared. Improvements in the institutional environment and increased allocation of resources for the compilation of national accounts and balance of payments statistics aimed to address weaknesses in the prerequisites for the quality of the statistics. Methodological soundness, accuracy, and reliability of macroeconomic statistics began to show improvements as a result of these efforts.
III. Reporting to STA	
Mozambique does not report fiscal data for publication in the *IFS* or the *Government Finance Statistic Yearbook (GFSY)*. Mozambique now reports monthly monetary data to STA using the standardized reporting forms (SRFs). As a result, these enhanced data are being published in the *International Financial Statistics (IFS) Supplement*. In 2007, the BM started to compile and report comprehensive IIP data in the *Balance of Payments Statistics Yearbook*.	

Mozambique: Table of Common Indicators Required for Surveillance

(As of May 8, 2013)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of publication[7]	Memo Items: Data Quality – Methodological soundness[8]	Memo Items: Data Quality Accuracy and reliability[9]
Exchange Rates	May 2013	May 2013	D	W	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	May 2013	May 2013	D	W	D		
Reserve/Base Money	May 2013	May 2013	M	M	M	LO, O, LO, O	LO, LO, O, O, LO
Broad Money	March 2013	April 2013	M	M	M		
Central Bank Balance Sheet	March 2013	April 2013	M	M	M		
Consolidated Balance Sheet of the Banking System	March 2013	April 2013	M	M	M		
Interest Rates[2]	March 2013	April 2013	M	M	M		
Consumer Price Index	April 2013	May 2013	M	M	M	O, LO, LNO, O	LNO, LO, LO, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	March 2013	April 2013	M,Q	Q	Q	LO, LNO, LO, O	LO, O, LO, O, LNO
Stocks of Central Government and Central Government-Guaranteed Debt[5]	March 2013	April 2013	Q	Q	Q		
External Current Account Balance	2012 Q4	Feb. 2013	Q	I	I	LO, LNO, LO, O	LO, LNO, LO, LO, LNO
Exports and Imports of Goods and Services	2012 Q4	Feb. 2013	Q	I	I		
GDP/GNP	2012 Q4	March 2013	Q	Q	I	O, LO, O, LO	LNO, LO, LO, O, LO
Gross External Debt	Dec. 2012	March 2013	A	I	I		
International Investment Position [6]	2007	May 2009	A	A	A		

[1]Any reserve assets that are pledged of otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2]Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.
[3]Foreign, domestic bank, and domestic nonbank financing.
[4]The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5]Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7]Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).
[8]Reflects the assessment provided in the data ROSC published in August, 2008, and based on the findings of the mission that took place during November 29–December 7, 2007 for the dataset corresponding to the variables in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).
[9]Same as footnote 8, except referring to international standards concerning source data, assessment and validation of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 13/75
FOR IMMEDIATE RELEASE
July 3, 2013

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2013 Article IV Consultation with Mozambique

On June 24, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Mozambique.[1]

Background

Mozambique has sustained strong economic growth over nearly two decades, helped by foreign investment, mainly in mega-projects in the natural resource sector, and generous support by development partners. However, while poverty has been reduced, more than half of the population still lives below the national poverty line. Improvements have been most pronounced in the more affluent Southern regions and in urban centers, especially the Maputo area. This underlines the need for building a more inclusive growth through economic diversification, employment creation, and the expansion of social protection.

Mozambique's economy remains robust, despite a still-fragile world economic environment resulting from the financial crisis. Reflecting the rapid expansion in coal production as well as in financial services, transport and communications, and agriculture, Mozambique's real gross domestic product (GDP) growth is estimated to have reached 7½ percent in 2012. Severe floods in early 2013 have had a significant impact, destroying crops in the South and severely damaging infrastructure. But real GDP is still projected to grow by around 7 percent this year as mining expands further and overall agricultural production is set to recover speedily. Consumer price inflation slowed sharply to 2.2 percent in December 2012, one of the lowest in the region. In early 2013, floods pushed up food prices, though inflation is projected to remain low at

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

around 5-6 percent over the medium term. External transactions are increasingly dominated by large private investments in the mining and hydrocarbon sectors, financed mostly by foreign direct investment and some private borrowing abroad. Fiscal performance has been largely in line with the program. External borrowing has risen in 2012 as the authorities have stepped up borrowing on commercial terms to fund investments; overall debt levels remain low.

Executive Board Assessment

Directors commended the authorities for their policies, which have translated into a strong macroeconomic performance in recent years. While the medium-term growth outlook is favorable, it will be important to manage risks stemming from the external and internal environments. Directors called for continued commitment to sound policies and structural reforms to preserve macroeconomic stability, foster inclusive growth, and reduce poverty.

Recognizing the need to support public investment and social development, Directors emphasized the importance of fiscal prudence as revenues from extractive industries will remain modest in the near term. To limit fiscal risks, they advised prioritization of current spending, in particular containing the wage bill. They also called for steps to modernize revenue administration, strengthen public financial management, and ensure timely settlement of VAT refunds. Directors also saw merit in developing a fiscal policy framework that incorporates the anticipated natural resource receipts over the medium term.

Directors acknowledged that the current high level of public investment can make an important contribution to improving infrastructure and enabling Mozambique to access its natural resource wealth. However, they recommended careful monitoring of the pace and effectiveness of these investments in order to maximize returns, avoid hitting absorptive capacity constraints, and preserve debt sustainability. In this context, Directors encouraged the authorities to continue to strengthen their medium-term debt strategy as well as project selection and monitoring.

Directors endorsed the authorities’ monetary policy stance but underscored the need to remain vigilant and tighten policy if inflationary pressures emerge. They welcomed steps underway to improve monetary operations and strengthen the transmission mechanisms.

Directors agreed that the banking system has shown resilience during the global financial crisis. In light of the ongoing expansion of the financial sector, they endorsed the authorities’ efforts to develop stress-testing capacity and strengthen prudential regulations. Directors welcomed progress in establishing a banking crisis resolution framework and adopting risk-based surveillance. Implementation of the new Anti-Money Laundering/Combating the Financing of Terrorism (AM/CFT) law should support further anti-corruption efforts. They looked forward to the vigorous implementation of the new Financial Sector Development Strategy.

Directors encouraged the authorities to continue to implement their Poverty Reduction Strategy. A renewed focus on job creation, improvements in agricultural productivity, and economic diversification hold the key to more inclusive growth in the period ahead.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Mozambique: Selected Economic and Financial Indicators, 2011-14

	2011	2012	2013	2014
	Act.	Est.	Proj.	Proj.
	(Annual percentage change, unless otherwise indicated)			
National income and prices				
Nominal GDP (MT billion)	365	404	454	520
Nominal GDP growth	16.0	10.6	12.3	14.6
Real GDP growth	7.3	7.4	7.0	8.5
GDP per capita (US$)	571	634	640	684
Consumer price index (annual average)	10.4	2.1	5.5	5.6
Consumer price index (end of period)	5.5	2.2	6.1	5.4
Exchange rate, MT per US dollar, eop	27.1	29.7	...	...
Exchange rate, MT per US dollar, per.avg.	29.1	28.4	...	...
External sector				
Merchandise exports	33.6	11.3	13.8	20.9
Merchandise exports, excluding megaprojects	65.8	15.6	4.0	26.2
Merchandise imports	52.8	14.9	15.3	11.3
Merchandise imports, excluding megaprojects	46.2	4.9	15.2	8.4
Terms of trade	2.5	-10.0	-1.9	-0.1
Nominal effective exchange rate (annual average)	12.4	7.4	...	...
Real effective exchange rate (annual average)	19.7	5.4	...	...
Money and credit				
Reserve money	8.5	19.7	17.9	15.0
M3 (Broad money)	9.4	29.4	19.0	15.5
Credit to the economy	6.4	18.3	21.5	19.1
(Percent of GDP)	26.9	28.8	31.1	32.3
	(Percent of GDP)			
Investment and saving				
Gross domestic investment	36.7	48.3	49.4	51.8
Government	14.9	13.6	16.2	17.2
Other sectors	21.9	34.7	33.2	34.6
Gross domestic savings (excluding grants)	5.5	8.0	6.0	7.0
Government	2.0	4.1	3.8	3.6
Other sectors	3.6	3.9	2.2	3.4
External current account, before grants	-31.2	-40.3	-43.4	-44.8
External current account, after grants	-24.3	-36.5	-39.9	-41.3
Government budget				
Total revenue [1]	20.7	23.5	24.5	23.5
Total expenditure and net lending	33.6	32.9	36.3	35.5
Overall balance, before grants	-13.1	-9.6	-11.8	-12.0
Total grants	7.8	5.4	5.1	4.8
Overall balance, after grants	-5.3	-4.2	-6.7	-7.2
Domestic primary balance, before grants	-2.9	-1.0	-2.7	-1.7
External financing (incl. debt relief)	3.7	4.2	5.7	6.4
Net domestic financing	1.6	0.7	1.0	0.8
Privatization	0.0	0.0	0.0	0.0
Total public debt [2]	39.3	42.2	47.8	50.9
Of which: external	32.6	36.3	41.6	44.7
Of which: domestic	6.7	5.9	6.2	6.2
	(Millions of U.S. dollars, unless otherwise indicated)			
External current account, before grants	-3,922	-5,737	-6,373	-7,158
External current account, after grants	-3,059	-5,198	-5,854	-6608
Overall balance of payments	323	373	100	320
Net international reserves (end of period) [3]	2,239	2,605	2,704	3,023
Gross international reserves (end of period) [3]	2,428	2,799	2,894	3,211
Months of projected imports of goods and nonfactor services	2.9	3.0	2.8	2.6
Months of imports of goods and nonfactor services, excl. megaprojects	5.2	6.2	4.2	4.2

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

[1] Net of verified VAT refund requests.

[2] Consistent with DSA definition, the nonconcessional Portuguese credit line is included under the external debt.

[3] Includes disbursements of IMF resources under the ESF and August 2009 SDR allocation.

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FOR IMMEDIATE RELEASE
June 24, 2013

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes Sixth Review Under Policy Support Instrument for Mozambique and Approves a New Three-Year PSI

The Executive Board of the International Monetary Fund (IMF) today completed the sixth and final review under Mozambique's Policy Support Instrument (PSI) and approved a new three-year PSI. To this end, the Executive Board took note of the member's cancellation of the current PSI, which was scheduled to expire on July 31, 2013 (see Press Release No. 10/242). In completing the review, the Board also approved waivers for the non-observance of the end-December 2012 assessment criteria on the stock of reserve money and the net credit to the central government of Mozambique by the banking system.

The IMF's framework for PSIs is designed for low-income countries that may not need, or want, IMF financial assistance, but still seek IMF advice, monitoring, and endorsement of their policies (see Public Information Notice No. 05/145).

The PSI for Mozambique aims to maintain macroeconomic stability and target poverty reduction through capacity building in economic management; more focused priority spending; enhanced debt management; financial sector efficiency; and improvements in the business climate and competitiveness.

Following the Executive Board's discussion of Mozambique, Min Zhu, Deputy Managing Director and Acting Chair, stated:

"Mozambique's economic performance and outlook remain strong. Helped by appropriate macroeconomic policies, the economy proved resilient to the global financial crisis. The country is poised for continued strong economic growth over the medium term, reflecting expanded production in the natural resource sector.

"While inflation remains moderate, inflationary pressures should be closely monitored. The authorities should stand ready to tighten policies should inflation exceed projections. "The Poverty Reduction Strategy outlines a challenging development agenda aimed at fostering inclusiveness and improve social development indicators. Its emphasis on economic diversification and job creation is appropriate.

"The authorities' development strategy needs to adapt to an increasing contribution of the extractive industry to the economy. It will thus be important to continue to modernize revenue administration and public financial management. Tapping Mozambique's natural resource wealth will require an elevated level of infrastructure spending. It is critical, however, that the pace of public investment be commensurate with absorptive capacity and debt sustainability. Accordingly, the authorities are well advised to strengthen medium-term debt management as well as project selection and implementation.

"The banking system has proven resilient during the global financial crisis. Recent improvements in the crisis resolution framework, banking supervision, and AMF/CTL legislation are welcome. Vigorous implementation of the new Financial Sector Development Strategy will be important going forward."

Statement by Mr. Momodou Bamba Saho, Executive Director for Mozambique
June 24, 2013

My authorities greatly appreciate the Fund's constructive engagement and support that is helping Mozambique lay a strong foundation for sustainable economic growth. They share the broad thrust of the staff report which provides a comprehensive assessment of recent economic developments and program performance. My authorities welcome the staff's understanding of the difficult challenges facing Mozambique now and in the near future.

Recent economic developments

Mozambique's strong economic growth is a reflection of the authorities' commitment to prudent fiscal and monetary policies in line with their Poverty Reduction Strategy (PARP) set for 2011 – 2014 supported by the Policy Support Instrument (PSI). Real economic growth has been sustained above 7 percent over the past twenty years, and remained high in 2012 at 7.4 percent, bolstered by the substantial contribution from the mineral sector, agriculture and financial services. In spite of recent estimates that indicate that growth could contract slightly as a result of the flood that damaged infrastructures during the first quarter of 2013, GDP growth is expected to remain above 7 percent by year end.

Nevertheless, my authorities are aware that economic growth itself does not provide appropriate responses to the adverse socio- economic environment and despite perseverance in undertaking prudent macroeconomic policies and embarking on structural reforms, achieving poverty reduction and inclusive growth remain serious policy challenges. **My authorities' fiscal policy shall continue to focus on prudent use of non-concessional external borrowing to help bridge the gap between the country's vast infrastructure financing needs and a trend decline in donor support, while ensuring macroeconomic stability.**

Monetary policy remains geared towards domestic credit expansion in support of private sector investment while remaining committed to the maintenance of price stability. My authorities have successfully kept inflation in the lower single digits. At 2.2 percent, Mozambique achieved the lowest inflation rate in the sub region. However, a slight increase in the inflation rate in 2013 is expected due to the rise in food prices as a result of lower performance in agriculture following heavy floods.

The authorities remain committed to strengthening banking supervision to enhance monetary policy transmission mechanism. *Bank of Mozambique (BM) has taken actions aimed at creating adequate capital buffers in the banking system through better diversified banking instruments.*

The Mozambican authorities are also strengthening financial inclusion as part of Mozambique's Financial Sector Development Strategy (FSDS) for 2013-2022. The aim is to deepen the government debt market. My authorities envisage enhancing financial sector surveillance mechanisms through improved banking supervision. In this respect, they have recently concluded the financial sector contingency plan and are making the Deposit Insurance Fund operational. Furthermore, my authorities have reviewed the legal framework with the aim of implementing AML/CFT. In its determination to sustain a strong banking system the BM launched its own stress-test exercise and in March 2013 established a risk management guideline and a legal and analytical framework for risk-based surveillance, preparing the way for the adoption in 2014 of the Basel II Capital Accord.

***Mozambique's external sector remains viable despite the high current account to GDP deficit ratio. Driven by the real exchange rate, the export sector has witnessed steady growth while FDI flows* have also remained buoyant resulting in a declining external current account deficit in percentage of GDP.** However, delays in financial disbursement by some donors and significant increases in imports of goods, in response to domestic shortages caused by floods, reduced international reserves more than expected. Overall, available reserves can finance three months of goods and services.

Program performance under the PSI program

Performance under the program has been good with all but two quantitative assessment criteria (AC) set for end-December 2012 being met. Reserve money (RM) surpassed the end-December target due to temporary high seasonal demand for money at end-year. Net credit to the government (NCG) surpassed the programmed amount on account of a shortfall in revenue and higher than anticipated investment spending. However, NCG was within projections at end-March 2013. The authorities also took important steps to achieve the end-December 2012 program's structural benchmarks for the Annual Domestic Borrowing Plan for 2013 that was approved as scheduled in January 2013. The Financial Sector Contingency Plan and the Financial Sector Development Strategy- two structural benchmarks set for end-2012 were also approved in April 2013. **In view of the strong program performance, my authorities request waivers for the nonobservance of the two missed end-December assessment criteria and request the Executive Board's support for the completion of the sixth review under the PSI**. **My authorities also request the Executive Board's approval of a new three-year PSI and cancelation of the current PSI.**

Fiscal Policy

While being supportive of the disinflation effort, the fiscal policy stance would accommodate a revival in public investment over the next years to rebuild infrastructure damaged by floods and address the social and human development objectives, including expansion in social protection, enhancing productivity in agriculture and fisheries and strengthening job opportunities and job creation. The authorities have increased social spending to more than U$57 million in 2013 from around U$11 million in 2007, and are committed to further improvements in social safety nets in the medium term. The National Strategy for Basic Social Security approved in 2010 was expanded through new social protection programs with the aim of targeting the more vulnerable.

On account of the tax reforms undertaken through the introduction of the *Janela-Unica* (single trade window for taxpayers), tax revenues were higher than programmed in March 2013. Ongoing reforms in taxation of the mining and hydrocarbon sectors are enabling increased coverage and broadening of the tax base. My authorities have agreed to change the VAT law that will allow the application of VAT on a net basis starting from the 2015 budget and the implementation of tax payments through banks in order to simplify the tax collection.

While Mozambique's transition from *agricultural to mineral resource economy represents a strong evidence of a structural change, nevertheless* ***the structural reform agenda of my authorities remains focused on improving public finance management and enhancing its human and institutional capacity in anticipation of the role the extractive sector shall play in the long-term. Against this backdrop, my authorities are determined in ensuring high fiscal transparency in the execution of its megaprojects. They remain committed to strengthening proficiency in regulatory and fiscal framework, and will remain compliant with the Extractive Industry and Transparency Initiative (EITI) requirements.***

Revised Budget for 2013

My authorities are determined to foster investment and ensure social and political stability. This is necessary to sustain robust growth**.** In this regard**, a revised budget was presented to the Parliament aimed at rebuilding economic infrastructure in the six provinces badly affected by floods.** They intend to finance most of the reconstruction with the revenue accumulated from capital gains tax in extractive activities in 2012. The authorities agreed with staff to draw on the envisaged windfall revenues to reduce government debt and to refund the VAT backlog starting from 2015. They also agreed that the current fiscal surplus should be used, in part, to ramp-up capital investment and socio-economic development which would in turn improve their ability to reduce the pending refunds going forward.

In 2013, they are allocating 72.3 percent of total capital expenditure to prioritized sectors such as agriculture and fisheries, energy, health and education, with the aim of reducing poverty and strengthening productivity and competitiveness, while protecting the most vulnerable. Furthermore, to compensate fuel importers for losses incurred in 2012 the authorities allocated Mt1.3 billion in the 2013 budget. This allows the overall fiscal deficit after grants to fall in the range of 5-8 percent of GDP between 2013 and 2015.

Managing the public wage bill

My authorities have implemented a decompressed salary structure aimed at reducing gross wage inequality in the public sector, as well as boosting domestic consumption. In this regard, the wage bill increased particularly for civil servants in the education and health sectors. Consequently, the public wage bill absorbs 10.8 percent of GDP and my authorities intend to freeze new recruitments in the non-priority sectors. Going forward, they are determined to keep the wage bill at around 8.5 percent of GDP in the medium term.

Non-concessional borrowing and debt sustainability

As envisaged in their *Visao das Financas Publicas* 2011 – 2025 (*Long-term Public Financial Strategy 2011 – 2025*) my authorities remain committed to prudent public debt management that enhances Mozambique's credibility. In this regard, they have established a Public Debt Management Unit and Project Selection and Coordination Committee in 2011, aimed at achieving a more comprehensive investment program.

In 2012, Mozambique contracted non-concessional loans of about U$ 1.2 billion, reaching a cumulative amount of U$1.387 billion; which, as at end-June 2013 remains

below the threshold agreed under the PSI program of U$ 1.6 billion. My authorities are of the view that new loans would only accommodate infrastructure projects, particularly in energy and transport. These projects are expected to generate positive spillovers in the economy. They agreed with staff to increase the non-concessional borrowing threshold from U$1.6 to U$2.0 billion over the next three years providing more space for additional capital spending until 2016. My authorities provided the staff with the list of the proposed integrated projects all of which are based on supportive feasibility studies, cost-benefits analysis and full evaluation of the opportunity costs.

With the benefit of Fund TA, my authorities completed a DSA in 2010, 2011 and 2012. They have also concluded the Medium-Term Public Debt Management Strategy for 2012 – 2015 that was approved by Parliament in September 2012. Anxious to promote domestic savings and stimulate capital market development, my authorities also completed the first Borrowing Plan for 2013 based on 2013 budget projections, which enhances sovereign bond issuance, revamps the stock market and strengthens investor confidence. Overall, debt sustainability remains moderate in the medium term and my authorities will continue to prioritize grants over concessional loans going forward.

Managing natural resources

My authorities intend to strengthen their ability to manage the country's natural resource endowment through the improvement of the mining and hydrocarbon fiscal regime and full implementation of the EITI membership requirements. In that respect, they will persevere with reforms in debt management and investment planning as well as in tax administration in order to continue with sustained strong revenue mobilization. The implementation of a single taxpayer database and registration that allows steady improvements in tax collection, are steps in the right direction. My authorities are in the early stages of TA that will reorient their fiscal framework to that of a resource based economy. Constructive discussions were initiated during the last staff visit and sixth review under the PSI and my authorities are willing to continue with these analyses going forward.

Relationship with the Fund

My Mozambican authorities truly appreciated the recent visit of the First Deputy Managing Director. They interpreted as additional evidence of good cooperation with the Fund. Mozambique has agreed to host the Africa-IMF Conference in 2014 that would bring together African Finance Ministers and Central Bank Governors as well as IMF management, business leaders and civil society, to discuss ways of building a stronger partnership between the Continent and the Fund. My authorities are of the view that it will be a good opportunity for Mozambique to showcase its achievements while playing an important role in bringing to the fore issues that are important for Africa in its engagement with the IMF. My authorities remain engaged with the Fund and will focus the new PSI framework in the areas of poverty reduction, achieving inclusive growth and consolidating macroeconomic stability.