Angola

Under the IMF supervision

The country has renewed relationship with the IMF and obtained its financial support in late 2018. Under the Fund supervision, a mild recovery is expected in the near term but outlook remains weak due to a still tight foreign currency liquidity, a troubled banking system and a poor external environment. Amid higher oil price volatility, Angola continues to rely on the oil sector as a source of economic growth, fiscal income and foreign exchange earnings. Despite supportive measures to attract international investors, important deficiencies keep FDI weak. Some fiscal reforms are also ongoing, but governement room for maneuver remains slim.

Angola is successfully undergoing business-friendly reforms aiming to improve governance and transparency, diversify the economy and reduce its reliance on bilateral loans. Beyond political transition, hydrocarbon sector reshaping and new fx exchange policy, the government has restored relations with the IMF resulting in a three-year extended agreement for about USD 3.7 billion in December 2018, with disbursements until 2021. Nevertheless, the promising IMF's program starts in the context of a weakened near-term outlook due to higher oil price volatility, more restrictive external financial conditions and trade tensions between the US and China, which is Angola's major trading partner.

A mild growth recovery is possible

After recession for the third consecutive year in 2018, Angola GDP seems to struggle to recover and remained in negative territory in the first quarter of 2019. According to the National Statistical Institute (INE) data, the economy contracted by 0.4% on an annual basis in Q1, contrasting with the previous quarter's expansion of 2.6%. Q1 2019 contraction mainly comes from oil sector (-6.9%) which continues to play a very dominant role in Angola's economy[1], alongside with a contraction in the telecommunications (-6.8%) and financial services (-4.8%). The negative oil growth is largely the result of a falling oil production[2] along withan uptick in crude prices, due to a combination of maturing fields that are producing less oil, maintenance stoppages and a lack of new exploration opportunities into Angola's deepwaters' explorations.

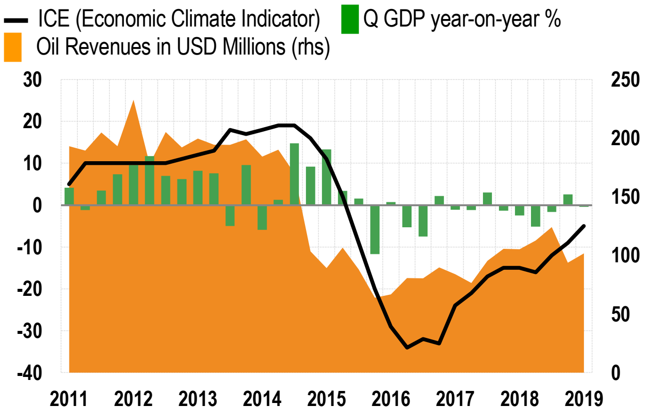
Overall economic sentiment improved in Q1 despite remaining firmly entrenched in negative territory. Indeed, the economic climate indicator (ICE: Indicador de Clima Económico) published by the Statistical Institute, that increased from -12 points in Q4 2018 to -9 points in Q1 2019. In 2019, GDP growth is likely to post a mere 0.3% with still contracting oil growth (despite the ramping up of Total South Kaombo field). The tepid recovery should also be driven by modest non-oil growth benefiting from the implementation of the IMF programme. In June 2019, the government has successfully completed the first review of the Extended Fund Facility with the release of the second tranche of financing (USD 248 mn), thus bringing to around USD 1.24 billion the total disbursement obtained so far. The government continues its efforts to improve the business environment and sustain the private-sector-led growth[3], but the still-ailing banking system and constraints on FX access for banking activity keep on straining the overall economic dynamics.

1- Forecasts

	2017	2018	2019e	2020e
Real GDP growth (%)	-0.2	-1.7	0.3	2.8
Inflation (CPI, year average, %)	29.8	19.6	17.4	11.1
Gen. Gov. balance / GDP (%)	-6.3	2.1	-0.1	0.3
Gen. Gov. debt / GDP (%)	69.3	87.8	90.6	83.6
Current account balance / GDP (%)	-0.5	6.6	-2.0	0.4
External debt / GDP (%)	38.2	56.0	58.5	54.9
Forex reserves (USD bn)	18.6	16.1	15.2	16.5
Forex reserves, in months of imports	8.7	7.3	6.6	7.2
Exchange rate USDAOA (year end)	166	310	368	380

e: BNP Paribas Group Economic Research estimates and forecasts

2- A difficult start to the year



Source: INE, Reuters, EIA, BNP Paribas

[1] It contributes to about 30% of GDP, 95% of exports, and over 60% of fiscal revenues at end 2018.

[2] According to the OPEC data, Angola's crude oil production was reported at 1,394.000 Barrel/Day in August 2019, which represents a record low over the last decade.

[3] Such as, for example, raw diamonds commerce liberalization, or establish a Regulatory Authority for Competition and privatization resolution, with a list of 32 state-owned enterprises earmarked to be sold on the country's stock exchange, the Bolsa de Dívida e Valores de Angola (BODIVA) by 2022.

Still hard access to foreign currencies

Despite the abandon of currency peg in January 2018, access to foreign currency remains difficult. The Central Bank continues to keep a local currency trading band and prioritise currency access for specifically selected activities (food, health, and petroleum), which have triggered a restriction on 54 imported-substitution goods. Most of dollar denominated contracts are paid in euros because of the loss in the US dollar correspondent banking[4]. Authorities are trying to resume sales of dollars within local commercial banks but the correspondent banking in dollars would be restored once efficient reforms to combat money laundering and reduce the institutional corruption will be implemented.

Meanwhile, the country continues to rely on the oil sector as a source of fx earnings. But a persistent declining oil production, albeit oil prices partial revival, affects export growth while maintaining an acute shortage of fx reserves. Indeed, the country does not have oil refineries and must use hard currency to import refined oil[5]; moreover, fx earnings from energy are used to service debt payments (both external and domestic), which accounted for more than 16% of GDP at end 2018.

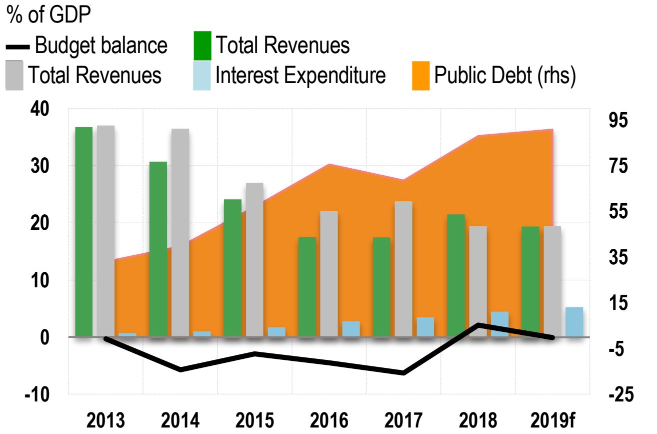
Exports have declined by 10% yoy in Q1 2019 while imports have risen by more than 40% in the same framework. Fx reserves erosion continues further (they have declined by 5% since January 2019). The current account balance is expected to swing back to a 2% deficit in 2019, after the strong surplus in 2018. Therefore, although FDI inflow has resumed in the first quarter of the year, external financing requirements are expected to increase further this year. The IMF support (USD 0.5 bn in 2019 and USD 1.1 bn per year in 2020-2021) would allow official fx reserves to recover in 2020 only.

At the same time, after having lost more than 40% in 2018, the kwanza registered a further 15% fall since the beginning of the year and it is now traded at AOA 365 per USD at the official rate. If the partial fx regime liberalisation has helped to reduce the kwanza overvaluation, the local currency continues to trade considerably higher in the parallel market (at above AOA 500 per USD in September). Even if the likelihood of a large exchange rate shock has been lessened by the transition to a more flexible exchange rate regime, further devaluations remain very likely in the medium term.

Fiscal reforms but worsening debt metrics

Ongoing fiscal reforms are mainly related to the ending of fuel subsidies, improving SOEs accountability and arrears clearance. Last year, budget execution was beyond expectations, with a fiscal balance moving back into a strong surplus thanks to contained government spending (below 20% of GDP), oil prices rebound and the kwanza depreciation. Fiscal consolidation is expected to continue in 2019, as evidenced by the supplementary budget presented end of May 2019, which recalibrates expenditure envelope to lower oil prices and identifies new non-oil revenue measures[6] to offset the expected revenue loss (around 3.8% of GDP according to the IMF). Nevertheless, revenues projections would suffer from postponed value added tax (VAT) introduction, with expected fiscal balance likely to go back to deficit this year.

3- Fiscal adjustements but increasing interest costs



Source: IMF, BNPParibas

But the room for maneuver is very slim. Indeed, the debt-to-GDP ratio has more than doubled in the last four years to reach 88% in 2018 and the debt burden (interest-to-revenue ratio) has soared up to 21% in 2018. The Government is committed to pursuing a prudent debt management strategy by decreasing public debt issuing and by developing the primary domestic debt market in local currency with increasingly longer maturities (instead of fx currency which increases its exposure to exchange risk). It will also enforce prudent SOE borrowing by moderating issuance of sovereign guarantees. A large privatization program[7] has also been considered. Albeit public debt-to-GDP ratio may be able to be reduced, it remains highly vulnerable to further local currency depreciation and further declining oil price.

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[4] The USD Correspondent Baking was closed in 2016 by the FED owing to concerns about weak anti-money laundering/combating the financing of terrorism.
[5] A severe fuel shortage occurred in March 2019 due to difficulties in accessing USD.
[6] Such as adjusting excise rates on energy, soda drinks and real estate, removing some personal income tax exemptions, widening the stamp tax base to include self-employed professionals and transactions that are not subject to VAT.
[7] Amongst the 190 major privatizations there are Sonangol, Endiama, TAAG, Bancos de Comércio e Indústria (BCI), Banco Angolano de Investimentos (BAI), Bolsa da Dívida e Valores de Angola (Bodiva), and some major telecom companies.