ANGOLA

A WORRYING SITUATION

With the country in recession for the fifth consecutive year (latest estimates put the contraction in 2020 at 4%), the current crisis is acting as a catalyst for existing weaknesses and further damaging the country's economic prospects. The combined effect of lower oil prices and production and the depreciation of the currency has increased pressure on the capacity for external financing and the sustainability of Angola's debt. The country has seen a significant decline in its currency reserves, which could become insufficient as the financing deficit increases. Currently under negotiation, the expected support of bilateral creditors (most notably China) is becoming crucial.

THE ANGOLAN ECONOMY IN DEPRESSION

The consequences of the current crisis are substantial and come at a time when Angola has suffered negative growth since the oil shock of 2014-16: on average the economy contracted by 1.4% each year from 2016 to 2019. Despite President Lourenço's programme of reforms, the current shock will accentuate the structural vulnerabilities of the economy, namely the lack of diversification and its financial dependence on China. The weight of the fossil fuel sector makes Angola particularly vulnerable to falls in oil prices and to a shortfall in investment in the sector, which has resulted in a steady decline in production since 2016 (from 1.72 million b/d to an estimated 1.38 million b/d in 2019, a fall of 20%).

Although the slowdown in Q1 2020 was limited, the impact of the crisis can be seen much more clearly in Q2 2020. Overall, economic activity shrank by 6.1% year-on-year (compared to a 1.8% contraction in Q1 2020). Although production levels have picked up slightly since the beginning of the year[1], the oil sector made a negative contribution to GDP growth. In value terms, the decline has been even greater, due to falling oil prices. This contraction of oil revenue has knock-on effects throughout the rest of the economy. In addition, the trade sector has been particularly hard hit by the state of emergency and global restrictions.

Advance indicators suggest that the economic contraction will continue. The business confidence index continues to fall (a moving average in Q2 2020 of -21 points, compared to -15 points in Q1 2020) reflecting both the operational constraints on the resumption of business (disruption to both domestic and international production chains) and concerns about demand suffering a lasting hit. The sharp falls in confidence in the manufacturing sector (-36 points) and the trade sector (-43 points) reflect these twin issues. Despite the easing of preventative health measures, the weakness of private sector consumption has combined with a hesitant recovery in external demand.

Meanwhile, the IMF has revised its forecasts, ruling out any hope of an economic recovery in 2020 and predicting an unprecedented 4% contraction for 2020 as a whole (from 1.3% previously projected). The IMF then expects a modest rebound in 2021 (3.2% on the same set of estimates, from 2.6% previously), although this will be partly explained by a base effect.

Domestic demand (nearly 50% of added-value) is also constrained by high levels of inflation. The economic contraction and collapse in the oil price have weakened the local currency, the kwanza (AOA), which has lost 20% against the USD since the end of 2019, thus increasing inflationary pressures. Inflation, which had already been pushed upwards by the unpegging of the currency[2] and the introduction of VAT in October 2019, hit 13.1% y/y in Q2 2020 and is likely to move some way out of the BNA's target range of 7% to 9% over the year as a whole

FORECASTS

	2018	2019	2020e	2021e
Real GDP growth (%)	-1.2	0.9	-4.0	3.2
Inflation (CPI, year average, %)	19.6	17.1	21.0	20.6
Gen. Gov. balance / GDP (%)	2.2	0.8	-2.8	-0.1
Gen. Gov. debt / GDP (%)	89.0	109.2	120.3	107.5
Current account balance / GDP (%)	6.9	5.7	-1.3	0.1
External debt / GDP (%)	56.8	76.2	94.0	89.1
Forex reserves (USD bn)	15.4	17.3	15.5	16.9
Forex reserves, in months of imports	7.4	12.4	9.9	10.2
Exchange rate USDAOA (year end)	252.9	343.9	407.3	437.4

TABLE 1
e: ESTIMATES AND FORECAST
SOURCE: BNP PARIBAS GROUP ECONOMIC RESEARCH

ANGOLAN GROWTH AT HALF MAST

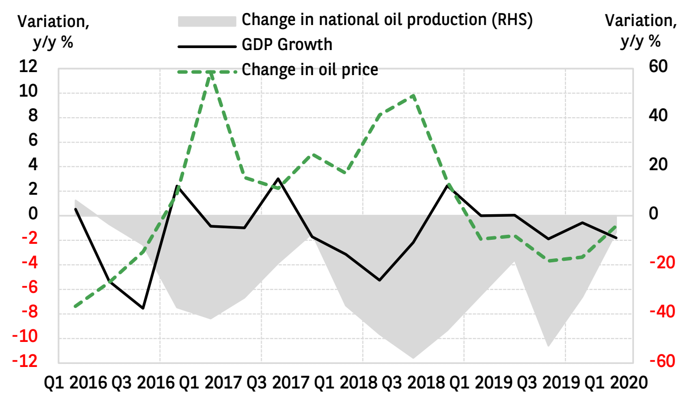

CHART 1
SOURCE: IMF, JODI, ANGOLAN NATIONAL AUTORITHIES

1 Angola having failed to respect OPEC's production quotas.
2 In October 2019, the National Bank of Angola (Banco Nacional de Angola or BNA) removed the +/-2% corridor on movements in the kwanza in order to deregulate the exchange rate and reduce the gap between official and parallel rates

– reaching 21% y/y on average over 2020 and then 20.6% in 2021[3] as a result of adjustments in regulated prices and the kwanza's rapid slide.

Quite apart from the increase in non-performing loans, the combined impact of inflation and the depreciation of the kwanza creates risks for the banking sector. The number of defaults is likely to surge, as 28% of lending is denominated in dollars. Moreover, the depreciation of the currency increases debt service costs and the country's external debt position and heightens the financing risk if this leads to growing pressure on currency reserves.

INCREASED PRESSURE ON FINANCING CAPACITY

The current crisis has significantly weakened the country's financial prospects, which had already been damaged by the 2014-2016 shock. The IMF has revised its forecast of the public debt to GDP ratio for 2020 to 120.3% to take account of current conditions. This change is due largely to the kwanza's depreciation, as 70% of outstanding debt is denominated in foreign currency.

The country's ability to meet its external financing needs has been significantly reduced as a result. Following the 2014-2016 shock, Angola was only able to finance its current account deficit by drawing heavily against its foreign currency reserves, which fell from USD 32.2 billion in 2013 to USD 17.3 billion by the end of 2019. In addition, the country's external debt has more than doubled as a percentage of GDP, rising from 20.6% in 2013 to 76.2% at the end of 2019, notably as a result of increased non-concessional borrowing made possible by the low interest rate environment.

In the current climate, the deterioration of both liquidity and external solvency has resulted in an increase in the cost of external financing that will be hard to sustain. This is most notably visible in an increase in the sovereign yield spread on sovereign debt of more than 500 basis points (bp) since the beginning of 2020, taking it from 557 bp at end-December 2019 to 1,063 bp in August. This is primarily because reserve levels are historically low, and the external financing requirement depends heavily on oil exports, which account for 95% of the country's foreign currency income. The fall in such income as a result of lower oil prices is exacerbated by a structural decline in production. The estimated external financing needs for 2020 is USD 5 billion (more than 8% of GDP) and the country's ability to cover this is limited. As the government's fiscal receipts from oil revenue do not account for the totality of fiscal receipts, the kwanza's depreciation makes repayments increasingly costly. Angola's financing capacity depends in particular on bilateral loan agreements denominated in foreign currencies, particularly with China (which accounted for more than half of total debt in 2019).

In the very short term, the country should be able to avoid a default on its foreign debt, with debt servicing costs estimated at around 36% of 2020 revenues (including USD 3.3 billion in debt repayment and USD 1.2 billion in interest).

For the time being, the country has received temporary relief from the financial support of the IMF, which has recently disbursed the 4th tranche of its loan facility (USD 1 billion) and a payment under the Extended Fund Facility established in 2018 (USD 767 million). Angola has also agreed a moratorium on debt service payments with bilateral and official creditors under the DSSI (Debt Service Suspension Initiative) introduced by the G20 nations and the Paris Club. This will produce savings of around USD 30 million by the end of 2020. However, this does not cover borrowings from China, meaning that negotiations with Beijing will be decisive (currently thought to get to positive outcomes). Nor do these measures cover debt to the private sector.

In the absence of an agreement, or if the sums involved remain insufficient, a rescheduling of the debt could be necessary to make it sustainable. Further ahead, the rebuilding of external financial buffers, which will depend on a significant increase in oil prices, and a genuine diversification of the economy will both be vital.

DETARIORATION OF THE EXTERNAL POSITION

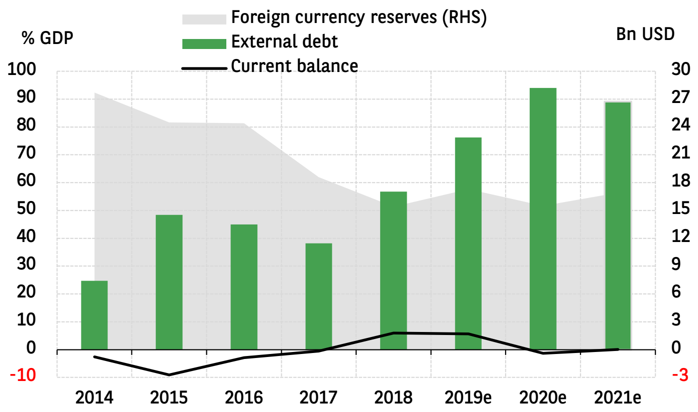

CHART 2 SOURCE: IMF, BNP PARIBAS

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3 According to the IMF, which has revised its pre-Covid estimates (October 2019). Its initial inflation forecast for 2020 was 15% (from more than 17% in 2019).