

Recent macroeconomic and financial developments

The onset of the COVID-19 pandemic caused a sudden stop to Mozambique's good economic performance. Real GDP contracted by an estimated 0.5% in 2020, the first decline in 28 years, after growing 2.2% in 2019. A slowdown in construction, tourism, and transport, and a decrease in demand for commodities exports were the main drivers of the deceleration. Economic activity was also hurt by the escalating conflict in the northern province of Cabo Delgado, which has displaced more than 250,000 people and resulted in more than a thousand deaths. The economic contraction was expected to drag 850,000 people below the international poverty line in 2020, an increase of 1.2 percentage points to 63.7% of the population, according to the World Bank, while GDP per capita was expected to contract by -3.4% in 2020.

Despite negative growth, a slight increase in inflation was expected for 2020, from 2.8% in 2019 to 3.1%, pushed by a 21.7% depreciation of the metical against the US dollar. The Monetary Policy Committee reduced the policy interest rate by 250 basis points from March through August, to 10.25%, to ensure liquidity and minimize potential credit crunches in the private sector. Nevertheless, non-performing loans, which were already high at 10.2% in 2019, increased to 12.6% in June 2020 as businesses struggled to meet their obligations. Both the fiscal and external balance deteriorated. The fiscal deficit was estimated to reach 7.0% of GDP in 2020, larger than the 2.7% deficit in 2019, pushed by lower revenues from tax relief and the economic slowdown and increasing public debt, which already was high at 108.4% of GDP in 2019. The current account deficit was estimated to widen to 30.8% of GDP in 2020 from 19.9% in 2019, mainly because of lower export earnings. International reserves remained at 7 months coverage of imports until November 2020, excluding megaprojects, the same as in December 2019.

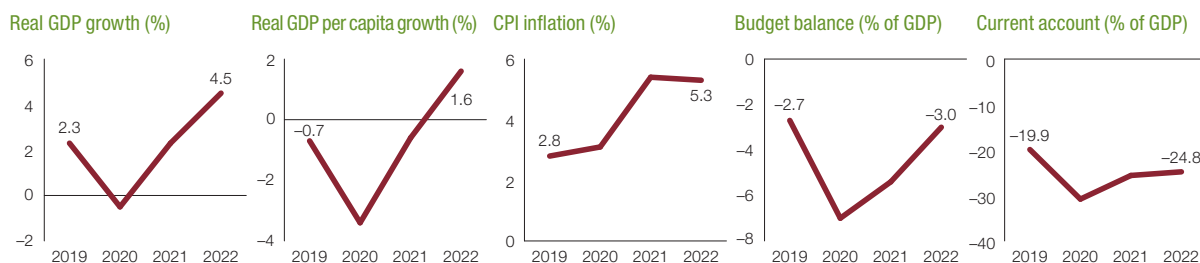
Outlook and risks

Growth prospects are more positive for the medium-term, with GDP expected to grow by 2.3% in 2021 and 4.5% in 2022, when it will surpass the prepandemic level on the back of gas investments. Inflation is expected to average 5.3% during 2021-22, pushed mostly by domestic demand during an economic recovery. Higher domestic growth and international demand for commodities are expected to generate more tax revenues and support resumption of the fiscal consolidation process. The budget deficit will narrow to 5.4% in 2021 and to 3.0% in 2022. The current account deficit will fall to 25.6% in 2021 but will remain elevated at 24.8% in 2022, above the prepandemic level of about 20%. Poverty would fall to 63.1%.

The main risks to such a recovery are climate shocks, low commodity prices, and increasing military disturbances in the center and north of the country—which could increase military expenditures, disrupt regional commerce, and limit creating local content and jobs associated with the megaprojects value chain.

Financing issues and options

The already constrained national budget and the high levels of public debt offer limited fiscal space to stimulate private sector-led growth and leverage social programs to increase the coverage of vulnerable groups to minimize the short and medium term impacts of the pandemic. To open room for such policies, the country should pursue financing options backed by donors' grants or highly concessional loans to reduce the impact on the budget during the crisis, while allowing for the resumption of fiscal consolidation in the medium term. Debt service reductions from the G20 debt moratorium should be used to offset the loss in tax revenues. In the medium-term, the country should explore fiscal and tax policies to stimulate the domestic nonextractive sector to foster job creation and reduce the economy's vulnerability to commodity shocks.



Source: Data are as of December 2020 and are from domestic authorities; figures for 2020 are estimates and figures for 2021 and 2022 are projections by the African Economic Outlook team.