INTERNATIONAL MONETARY FUND

Staff Country Reports

December 2010
IMF Country Report No. 10/375

Mozambique: First Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria—Staff Report; and Press Release

In the context of the Mozambique - First Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria, the following documents have been released and are included in this package:

- The staff report for the Mozambique - First Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria, prepared by a staff team of the IMF, following discussions that ended on October 29, 2010, 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 November 16, 2010. 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.

- A Press Release issued on December 13, 2010.

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

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INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

First Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria

Prepared by the African Department
(In consultation with other departments)

Approved by Roger Nord and Dominique Desruelle

November 16, 2010

- **Discussions**: Discussions were held in Maputo, October 19–29. The mission team included Messrs. Mueller (head), Jacoby, Rosa, Staines (all AFR), Ms. Garcia (SPR), Mr. Lledo (resident representative), and Ms. Bosten and Mr. Wane (resident representative office). Mr. Gazel (World Bank) also participated in the discussions.

- **Counterparts.** The mission met with Prime Minister Aly, Minister of Finance Chang, Minister of Planning and Development Cuereneia, other line ministers, Bank of Mozambique (BM) Governor Gove, other senior government officials, and representatives of the private sector, civil society, and the donor community.

- **Fund relations**: The Executive Board approved Mozambique's second three-year PSI on June 14, 2010.

- **Article VIII status**: The authorities intend to accept Article VIII status by year-end. LEG/MCM are expected to complete an assessment of the foreign exchange system and the new draft foreign exchange regulations in November 2010. A separate Board paper will be prepared upon notification by the authorities.

- **Review**: Staff recommends completion of the first review under the PSI. In the attached Letter of Intent and Memorandum of Economic and Financial Policies (MEFP), the authorities request completion of the first PSI review, a waiver for the assessment criterion (AC) on reserve money for end-June 2010, and modification of several ACs for end-December 2010.

Contents

EXECUTIVE SUMMARY

Mozambique continues to show a generally strong economic performance. Largely unaffected by the global crisis, real GDP growth remains buoyant, with strong activity across all sectors. However, the external environment has been less supportive than expected, as the balance of payments has come under pressure from rising fuel and food import prices and lower private capital inflows. Rising food and fuel prices also triggered a surge in headline inflation, which has begun to cause second-round effects on core inflation.

The rising costs of living led to violent street riots by the urban poor in early September. This prompted the authorities to adopt emergency relief measures (e.g., a bread subsidy) to restore social peace. In light of the events and the results of the recent household survey that indicated lack of progress in reducing poverty, they also decided to use the drafting of the new poverty reduction strategy to assess options to make economic growth more inclusive and strengthen social safety nets.

The program is on track. All quantitative targets for end-June were met, except for reserve money which was missed by a small margin. The authorities also met the structural benchmarks on the new PPP law and the preparation of their first DSA.

The emerging inflation expectations require a tightening of the macroeconomic policy mix. The BM already raised its key policy rate and reserve requirements and stepped up sales of foreign exchange to mop up liquidity. Fiscal policy has been marked by a remarkably strong revenue performance and prudent execution of the budget, which should offset additional outlays on the emergency measures to restore social peace and on the costly fuel subsidy. The authorities committed to a further tightening of the monetary and fiscal policy stance for the remainder of 2010 and for 2011.

For the medium term, the program's focus on sustaining economic growth remains valid. This includes an acceleration of the public investment program, with full access to the program's overall limit on nonconcessional external borrowing from 2011 onwards, which will be embedded in a prudent policy mix to maintain macroeconomic stability and debt sustainability. The program's objectives will be shored up by key structural reforms in the areas of debt management, tax policy, wage policy, and financial sector supervision.

Staff supports completion of the review, the authorities' request for waiver for the nonobservance of the end-June AC on reserve money, and the modification of the end-December ACs in light of the changed economic environment and the authorities' policy response to it.

I. INTRODUCTION

1. **The program is off to a good start overall.** The authorities have shown the same strong ownership of, and commitment to, the program that have marked their past implementation of Fund-supported programs. They stayed a prudent policy course in responding to recent adverse developments triggered by street riots by the urban poor over the rising costs of living and have begun addressing a surge in inflation. Although the program's medium-term objectives and overall strategy remain valid, some adjustments are required in the short run to reflect the authorities' response to these adversities.

II. RECENT ECONOMIC DEVELOPMENTS

2. **Mozambique's growth performance remains robust** (Figures 1 and 2). Easing macroeconomic policies in response to the global crisis helped sustain economic growth, allowing Mozambique to fare better during the global downturn than its peers in sub-Saharan Africa (SSA) (Figure 3). Real GDP growth is projected to accelerate to 7¼ percent in 2010, well above growth rates in peer countries, driven by a recovery in external demand. Economic activity was broad based and particularly strong in the primary and tertiary sectors.

Mozambique: Comparison with Sub-Saharan Africa, Selected Indicators, 2004-10 [1]

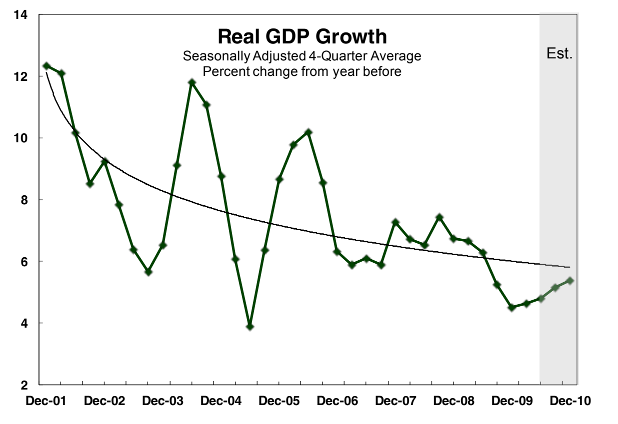
	Mozambique				SSA				SSA--Coastal non-resource intensive countries			
	2004-08	2008	2009	2010	2004-08	2008	2009	2010	2004-08	2008	2009	2010
Real GDP, % change	7.8	6.8	6.4	7.2	6.5	5.6	2.5	4.9	5.2	4.1	0.0	3.5
CPI period average, % change	10.2	10.3	3.3	12.7	8.3	11.7	10.4	7.5	6.5	11.6	7.6	5.7
REER, index	84.0	91.0	85.0	…	106.0	108.0	113.0	…	99.0	93.0	98.0	…
Current account balance after grants, % of GDP	-10.9	-11.9	-10.5	-13.4	0.8	-0.1	-1.6	-1.0	-5.9	-8.7	-5.5	-5.7
Gross international reserves, months of imports	4.8	4.3	5.4	4.6	4.6	6.1	5.5	5.1	3.2	4.1	4.4	4.3
Overal fiscal balance, inc grants, % of GDP	-2.6	-2.2	-5.4	-4.9	1.8	0.8	-5.7	-4.4	-0.9	-1.8	-5.5	-5.9
Broad money, % of GDP	30.8	33.6	39.8	40.6	42.5	48.4	49.2	51.1	62.9	69.2	67.0	71.5
Credit to the private sector, % of broad money	48.6	55.8	66.7	73.6	74.4	77.5	74.5	…	46.3	52.9	50.0	…

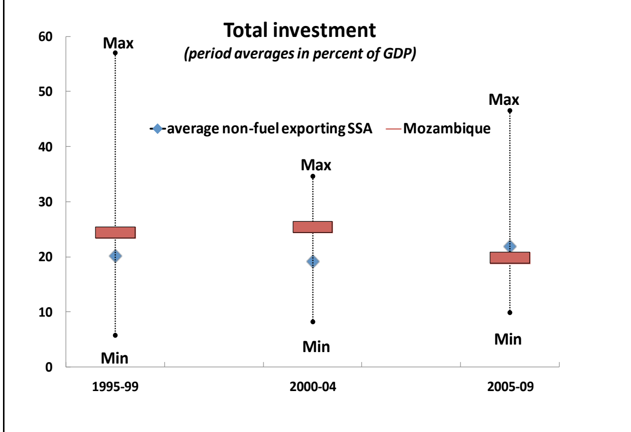
[1] Source: REO database, latest available data. Data for 2010 are preliminary projections.

3. **Nonetheless, the external environment has been less supportive than expected.** While the recovery in commodity prices has boosted megaproject exports, the balance of payments has come under pressure from rising fuel and food import prices and lower-than-expected private capital inflows, which continues to force large corporations to tap domestic bank financing. The accommodating monetary policy stance, accentuated by balance-of-payments pressures and thin market trading, has triggered a depreciation of the exchange rate; the meticais has lost about one-third against the US dollar and two-fifths against the South African rand since end-2009. The real effective exchange rate has nevertheless remained broadly stable since mid-2009.

Figure 1. Mozambique: Macroeconomic Developments

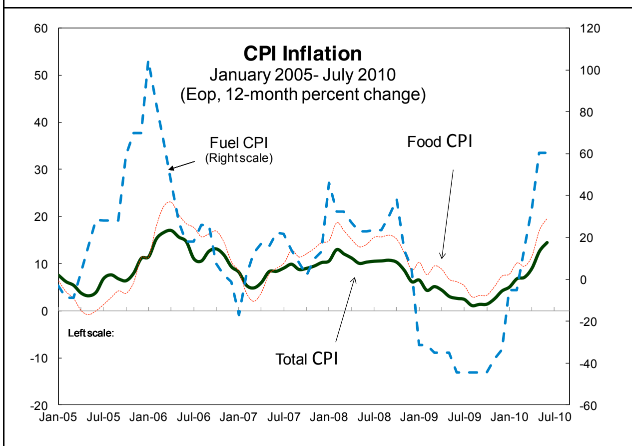
Notwithstanding some resilience during the global crisis, real GDP growth has recently fallen below trend…	*…as overall investment is declining.*

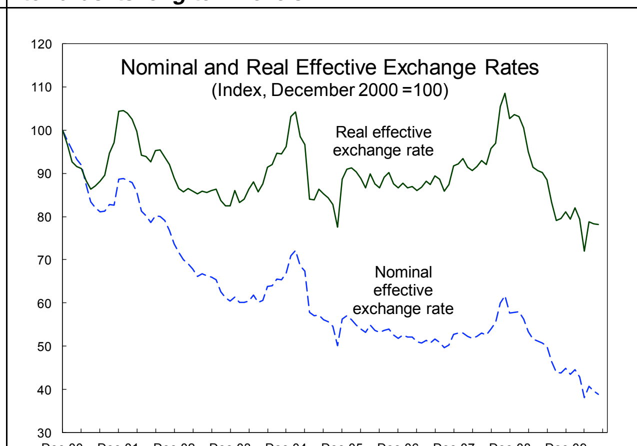




After falling markedly throughout 2009, food and fuel prices are on the rise again…

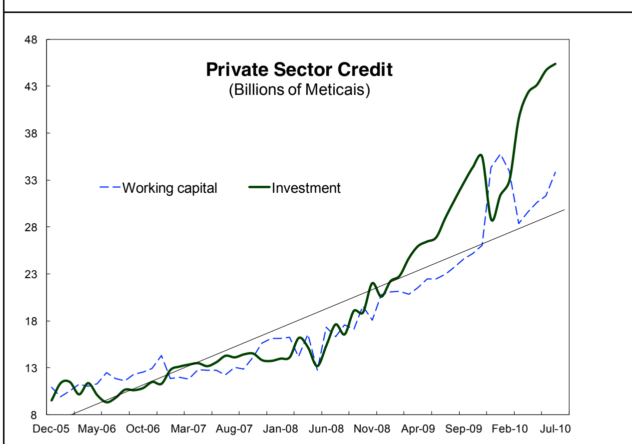
…partly reflecting the pass-through from the depreciating exchange rate. The real exchange rate has begun reverting towards its long-term levels.

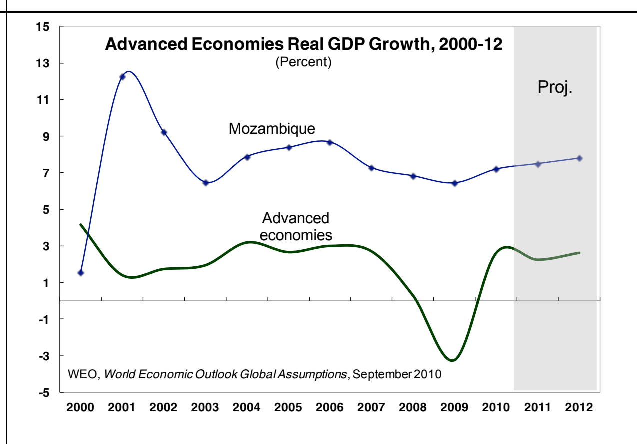




Private credit has surged, notably for investment purposes, as a result of a looser monetary policy stance.

Overall, Mozambique has weathered the global crisis well, and although the outlook is favorable, uncertainties remain.

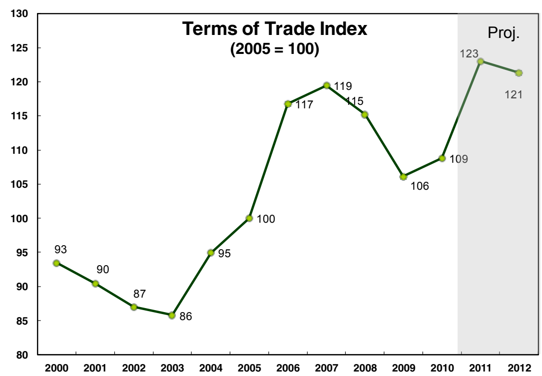




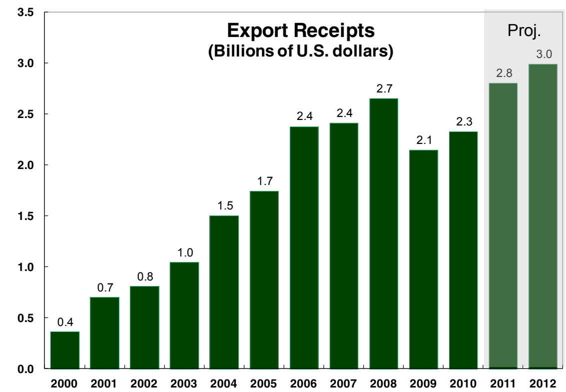
Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 2. Mozambique: Recovery from the Global Crisis

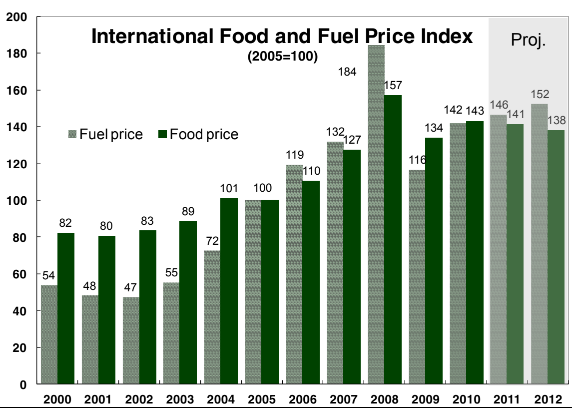
After the slump in global demand over the last two years, an uptick in commodity prices, including aluminum,…



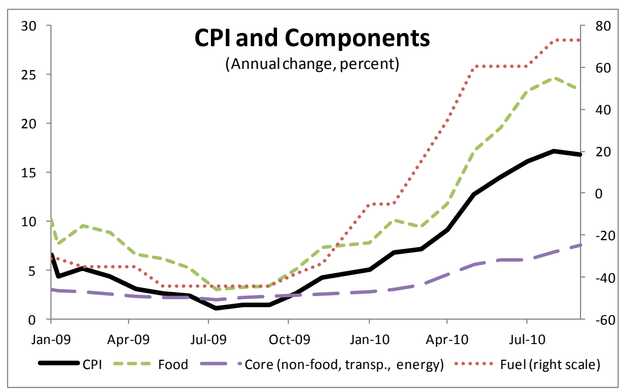
…as well as the coming online of new megaprojects, are expected to result in a recovery of export receipts to the pre-crisis level by 2011.



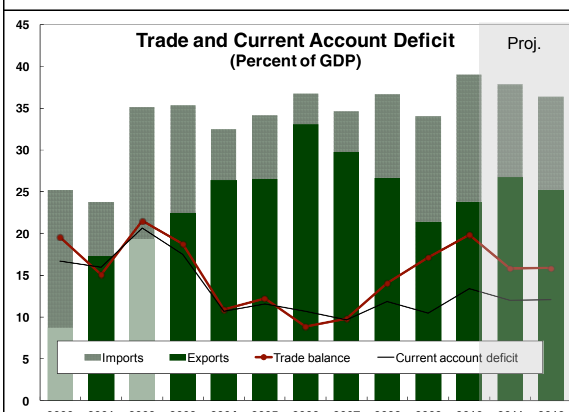
Resurgent global food and fuel prices in 2010 and beyond are burdening Mozambique's import bill…



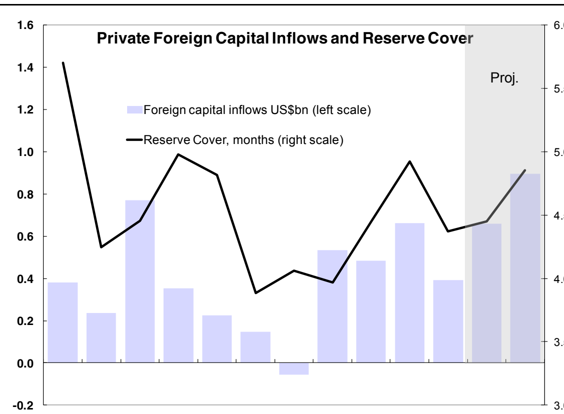
…and contributed to a marked increase in domestic prices, especially for food.



The trade and current account deficits are projected to peak in 2010,…



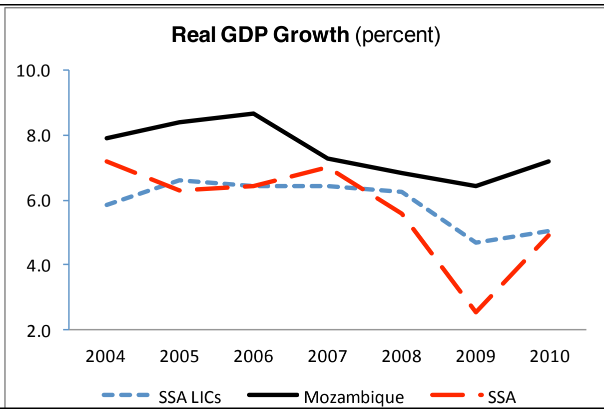
…while the recovery in private capital inflows is lagging.



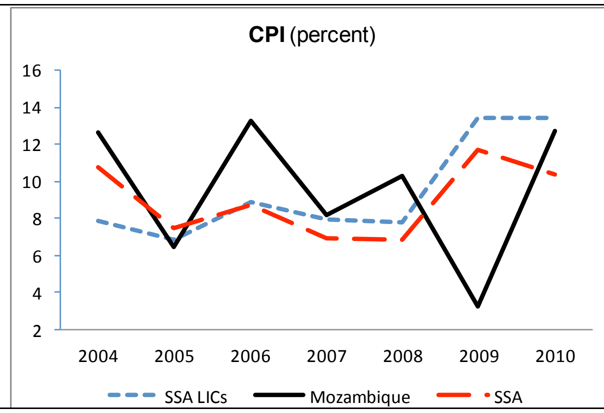
Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 3. Mozambique: Regional Comparison

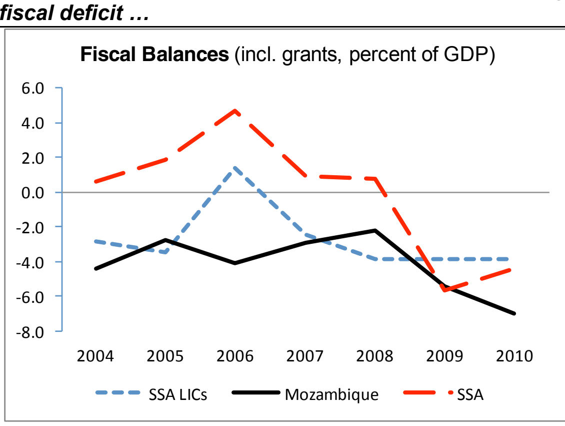
Real growth held up well, even in comparison to peers in SSA that were generally quite resilient to the global crisis.



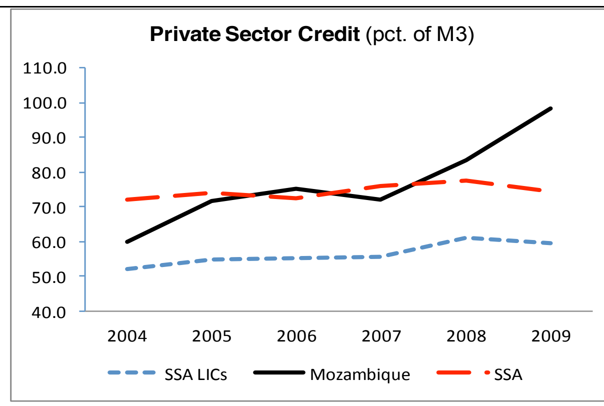
However, inflation recently surged back to regional levels.



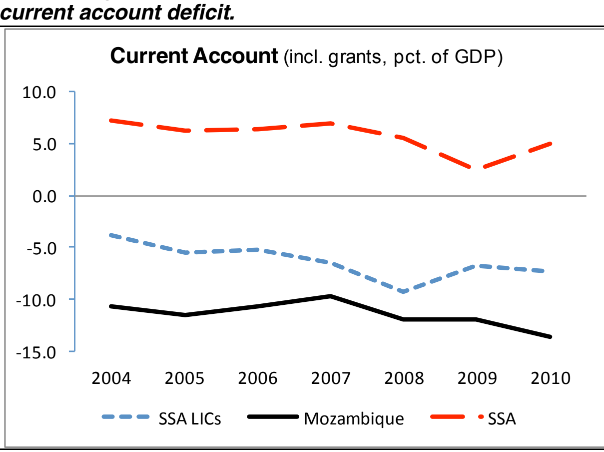
The economic stimulus was stronger and more sustained in Mozambique relative to other SSA LICs, with a widening fiscal deficit …



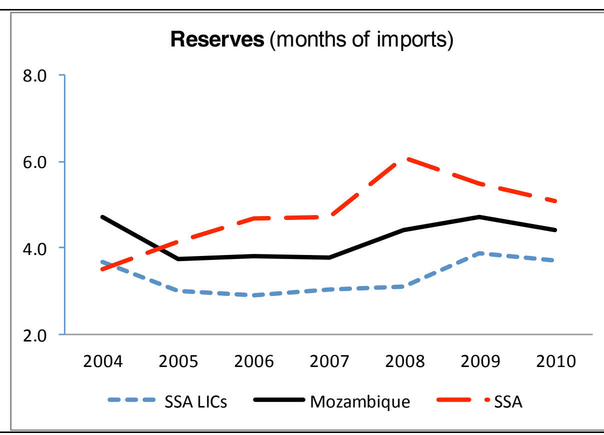
… and expanding credit to the private sector.



A drop in prices for Mozambique's main exports and a recent surge in food and fuel imports have increased the current account deficit.

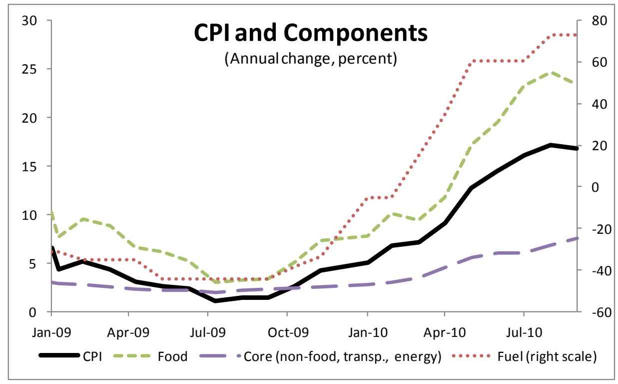


Nonetheless, reserves remained at a comfortable level



Sources: Mozambican authorities and IMF staff estimates and projections.

4. **Rising food and fuel prices triggered a surge in inflation, exacerbated by the depreciating exchange rate and the adjustment of administered prices.** Headline inflation reached 17 percent in the twelve months to September. Food prices, accounting for half of the CPI basket, surged by one-fourth during the period, while domestic fuel prices rose by more than half—which was aggravated by the gradual removal of the fuel subsidy, in line with program commitments (Box 1). Although global food and fuel price increases are projected to taper off, second-round effects on inflation are likely. Indeed, core inflation, while remaining subdued, has edged up from its trough earlier in the year.

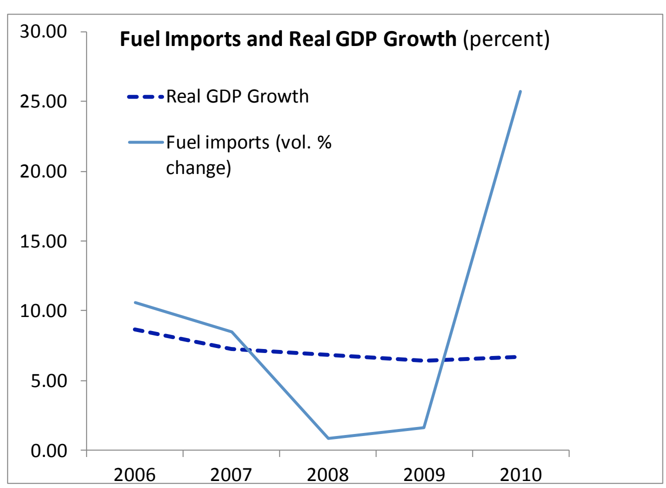


Box 1. The Removal of the Fuel Subsidy

Mozambique has traditionally adjusted fuel prices once per month based on a market-based formula. At the peak of the food and fuel price shock in February 2008, the government introduced an adjustment factor that kept fuel prices below market prices for social reasons. In April 2009, it locked pump prices and asked fuel importers to continue to provide fuel below market prices.

In March 2010, the government began gradually raising fuel prices to market levels, which was completed for petroleum products other than diesel in August 2010, with a cumulative price increase of 73 percent. Diesel prices were raised by 38 percent until May 2010 but remain below equilibrium levels, entailing continued losses to the industry.

An agreement between the government and fuel importers to settle outstanding claims for 2008-09 became effective in February 2010. The government also paid compensation for below-market fuel prices in 2010 until end-May. In November 2010, it clarified that it intends to compensate importers under the market-based formula through a cross-subsidization of diesel from other petroleum products that are less socially sensitive, but agreement with importers on this mechanism and run-up losses is still outstanding. It also plans to put in place a different price structure for wholesale customers which to date also benefited from the below-market price levels.



The fuel subsidy has resulted in higher budgetary costs in 2010 than budgeted (1.3 vs. 0.6 percent of GDP). It also burdened the balance of payments through a sharp rise in fuel imports, as consumers from neighboring countries sought to benefit from lower fuel prices in Mozambique. The planned measures should help reverse the surge in the import bill going forward.

5. **Once the rise in core inflation became evident, monetary policy responded to the emerging risks to macroeconomic stability.** The BM tightened monetary policy in June and again in September by cumulatively raising its key policy rate and reserve requirements by 4 and ¾ percentage points, respectively. It also stepped up sales of foreign exchange to mop up liquidity and help stabilize the exchange rate, given its direct pass-through to inflation. In light of the strong expansion in private sector credit, the BM has closely supervised the banking sector, although so far there have been no signs of deterioration in banks' credit portfolio quality or profitability.

6. **The conduct of fiscal policy until mid-year was broadly as programmed, with two exceptions.** First, the fuel subsidy proved more expensive than programmed, as outlined above. And second, capital expenditures fell substantially short, as the formation of the new government delayed the execution of new projects well into the second quarter. This, along with an overperformance of tax collections and cuts in non-priority spending, kept net credit to the government (NCG) within the program limit.

7. **The increase in the administered prices on bread, water, and electricity on September 1 led to two days of violent street riots in major cities, with 13 casualties.** Mozambique saw similar unrest some two years ago at the peak of the food and fuel price shock. This resurgence prompted the authorities to adopt a series of measures that are slated to be phased out by year-end, conditions permitting, and estimated to cost ¼ percent of GDP in 2010. Among other things, they introduced a bread subsidy, rescinded the tariff increases for electricity and water for low-usage households, and maintained subsidies for urban transportation. The measures are better targeted than the blanket fuel subsidy and believed to benefit the most vulnerable segments of the population.

III. Program Performance

8. **All the quantitative program targets for end-June 2010 were met, except the one for reserve money which was exceeded by a small margin.** Preliminary data for end-September suggest that the foreign exchange interventions have resulted in the BM missing the indicative NIR target, while reserve money was pushed well above the programmed path as a result of the higher nominal GDP growth, the increase in reserve requirements, and the sharp depreciation of the local currency which boosted the meticais counterpart of deposits in foreign currency.

9. **Compliance with structural conditionality was strong.** The authorities met the end-September structural benchmarks on the adoption of the PPP law and the drafting of their first debt sustainability analysis (DSA), which produced results broadly similar to those under the DSA prepared by Bank and Fund staff (EBS/10/98, Supp. 1). They also made good progress in implementing their other structural reforms, particularly in the areas of PFM and tax administration.

A. Overview

10. **The program is off to a good start, but needs to be adjusted in the short run because of two main developments.** First, concerns about rising inflation expectations signal a need for a stepped-up concerted policy response. And second, the authorities are eager to intensify their efforts to reduce poverty in light of the discontent among the more vulnerable segments of the population that came to the fore during the September street riots.

11. **The program's medium-term focus on sustaining economic growth remains valid.** The authorities aim to promote economic development embedded in an environment of macroeconomic stability. A key pillar of the strategy is to increase public investment in growth-enhancing sectors (transportation and energy), in part financed by nonconcessional external borrowing (NCB). This is expected to trigger a crowding in of private investment, create employment opportunities, and thereby help make a more meaningful dent in poverty.

MEFP ¶ 1

12. **The medium-term outlook remains favorable.** Megaprojects activity is projected to expand at a rapid pace, with the start of operations of several projects over the next few years. As a result, economic activity should accelerate to 7½ percent in 2011 and 8 percent over time. The strong expansion of megaproject exports should offset the still meager growth of traditional exports and the strong import demand related to public and private investment, thereby stabilizing the external current account (after grants) at around 12 percent of GDP and keeping the import cover of reserves at about 5 months over the medium term. Mirroring the concerted policy tightening, inflation is projected to return to single digits in 2011 and approximate the authorities' objective of 6 percent over the medium-term.

MEFP ¶ 11

Selected Indicators, 2008-15

	2008	2009	2010	2011	2012	2013	2014	2015
	Actual		Projections					
Real GDP, percent change	6.8	6.4	7.2	7.5	7.8	7.9	7.8	7.8
Inflation, eop, percent change	6.2	4.2	15.5	6.9	5.6	5.6	5.6	5.6
Inflation, average, percent change	10.3	3.3	12.7	8.0	5.6	5.6	5.6	5.6
Current account deficit (after grants), percent of GDP	-11.9	-10.5	-13.4	-12.0	-12.0	-12.2	-12.4	-13.1
Gross external reserves, months of projected imports	4.4	4.9	4.4	4.5	4.9	5.3	5.4	5.3
Primary domestic fiscal deficit, percent of GDP	-3.0	-4.3	-4.1	-3.3	-4.2	-3.9	-3.7	-3.7
Overall fiscal deficit (after grants), percent of GDP	-2.2	-5.4	-4.9	-7.0	-6.9	-6.1	-5.1	-5.1
Fiscal external financing, percent of GDP	4.0	5.0	4.5	6.8	6.2	5.4	4.4	4.3
Net credit to government, percent of GDP	-1.9	0.2	0.3	0.2	0.7	0.7	0.8	0.8
Private sector credit, percent change	45.9	58.6	36.0	22.6	16.6	15.3	15.2	15.1
Private sector credit, percent of GDP	18.7	26.5	29.8	31.5	32.3	32.7	33.1	33.4
Reserve money, percent change	7.8	27.3	25.0	13.0	15.5	15.3	15.1	15.0

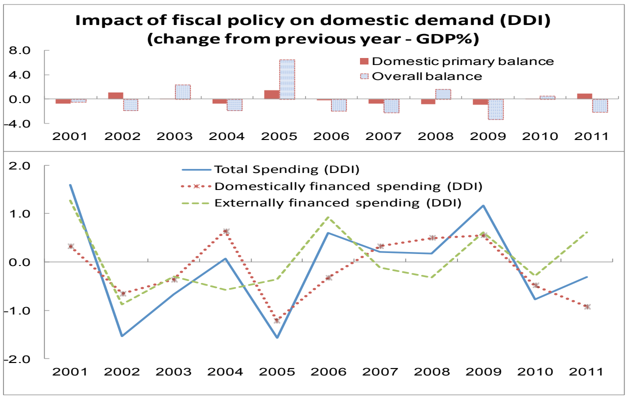
B. Exiting the Policy Stimulus and Curbing Inflation

13. **The authorities have started tightening macroeconomic policies, reverting from the expansionary stance adopted during the global economic crisis** (Figure 4). With economic growth on a sound footing, they recognized the need to accelerate their tightening of monetary and fiscal policies in 2011 to fight emerging inflation expectations.

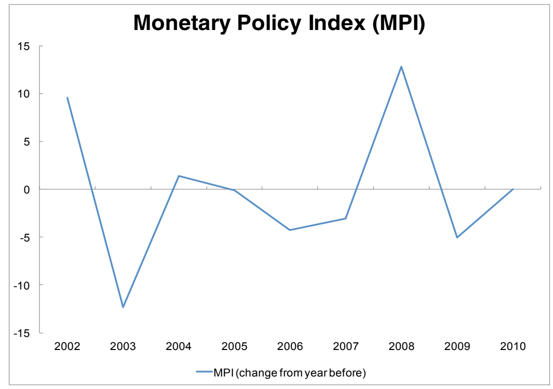
MEFP ¶ 13-19

Figure 4. Mozambique: Macroeconomic Policy Stance

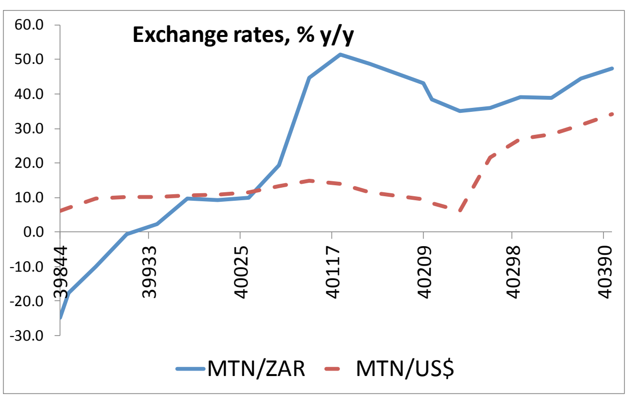
After an expansionary stance over the last two years, fiscal policy will be tightened in 2010-11 to help curb inflation



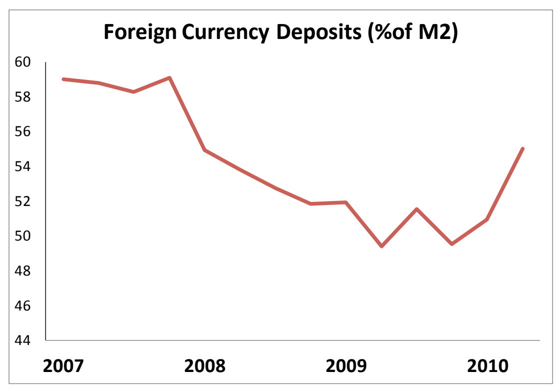
The Bank of Mozambique has started tightening monetary conditions in 2010



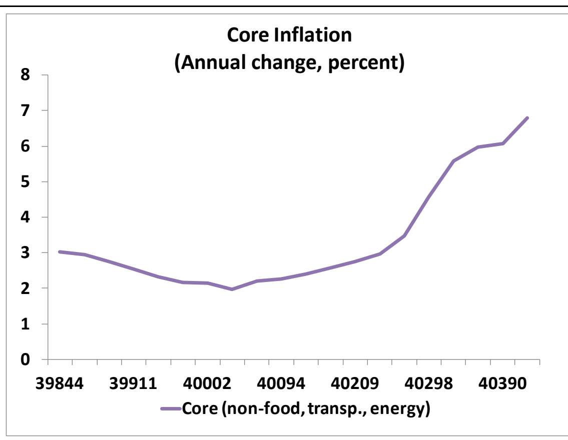
Partly as a consequence of the looser 2009/10 policy mix, the nominal exchange rate has depreciated markedly, …



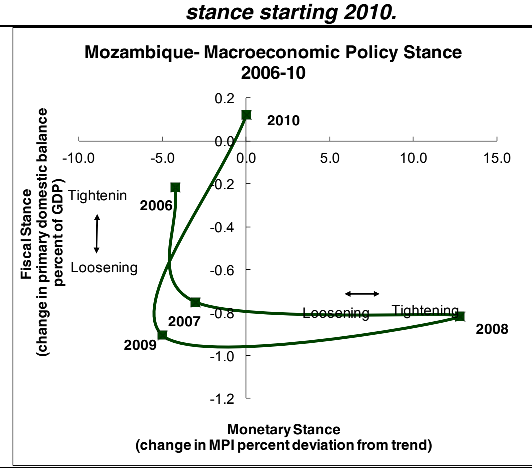
… which has resulted in increased appetite for foreign currency holdings to hedge inflation expectations, largely reversing a longer de-dollarization trend.



The depreciation has put upward pressure on core inflation, after a long period of a benign price environment, …



…which warrants the authorities' intention to curb inflationary expectations through a tighter policy stance starting 2010.



Sources: Mozambican authorities and IMF staff estimates and projections.

14. **The BM will use its full set of monetary policy instruments to withdraw the monetary stimulus and stabilize the exchange rate** (Figure 5). In doing so, it will aim to strike the proper balance between speed and the need to safeguard the soundness of the banking system, as banks need to orderly unwind the large rise in private sector credit made possible by the previous stimulus.

MEFP ¶ 16-17

15. **The envisaged mopping up of liquidity should lead to a slowdown in monetary expansion relative to GDP during the remainder of 2010 and, in particular, in 2011.** Quarterly reserve money growth will decelerate to 5 percent in the fourth quarter of 2010, after 12½ percent in the previous quarter, while annual growth will drop from 25 percent this year to 13 percent next year. This is expected to lead to a concomitant slowdown in private sector credit. The BM will also continue signaling its policy intentions by raising its key policy rates, as needed. The envisaged policy stance, together with the temporary impact of the global crisis and the surge in fuel imports on the balance of payments this year, necessitates a lower target on net international reserves (NIR) for 2010, resulting in a small dent in the import coverage of reserves, although it will quickly revert to about 5 months over the medium term.

16. **Fiscal policy is set to contribute its share to the tightening, but with limited scope in 2010** (Figure 5). The primary domestic fiscal deficit is projected to narrow to 4.1 percent of GDP, marginally lower than under the program. Notwithstanding buoyant revenues and a careful budget execution during the first half of 2010, room for a more decisive fiscal tightening during the remainder of this year has been reduced by emerging additional expenditure needs, such as the measures to restore social peace and the larger-than-expected costs for the fuel subsidy. In addition, the wage bill will reach the budgeted amount, as the revenue contingency under the organic budget law was removed in light of buoyant tax collections. The authorities' cuts in nonpriority domestic spending should nonetheless contain NCG such that it supports the BM's monetary tightening and avoids a crowding out of the private sector.

MEFP ¶ 19

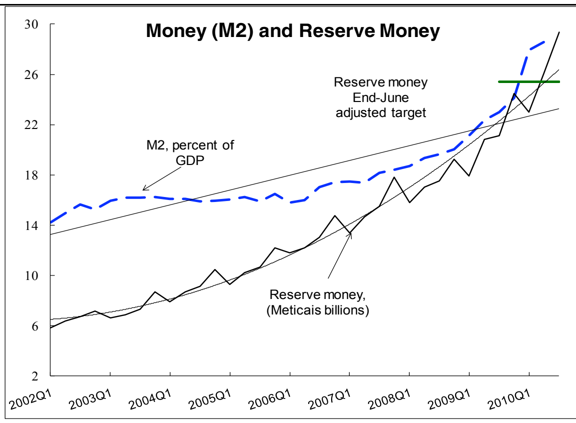
17. **In 2011, while the overall fiscal deficit will rise, reflecting the planned boost in infrastructure investment, domestic spending will be curtailed.** This, together with the strong revenue performance, will result in a decline of the domestic primary fiscal deficit by 0.8 percentage points, to 3⅓ percent of GDP.[1] This will sharply reduce the government's recourse to domestic financing to virtually nil, supporting the monetary tightening while preserving room for credit to the private sector.

MEFP ¶ 19

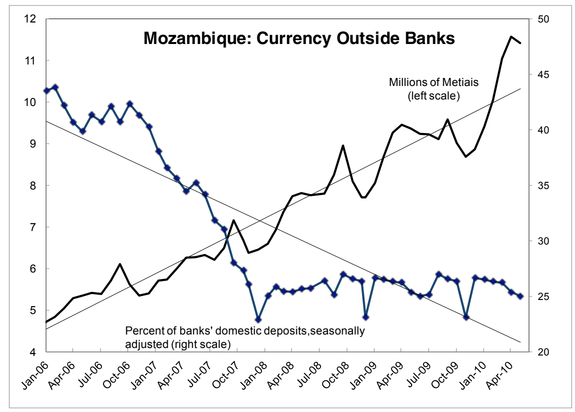
[1] The overall fiscal deficit is projected to widen in 2011 largely because of NCB-financed project spending. However, the domestic primary deficit is considered a better measure for the fiscal policy stance in Mozambique because of the high import content of investment projects that are generally directly or indirectly tied to external financing. The program's ringfencing of the NCB to infrastructure investment projects makes the approach comparable to donor-financed projects. The domestic demand impact of domestic primary spending is estimated to be contractionary for 2011 as a whole (-1.0 percent of GDP), offsetting the impact of the expansion in externally-financed spending on domestic demand (0.9 percent of GDP). As NCB-financed projects are estimated to be executed largely in the second half of 2011, the fiscal policy stance early in the year will be highly contractionary.

Figure 5. Mozambique: Monetary and Financial Sector Developments

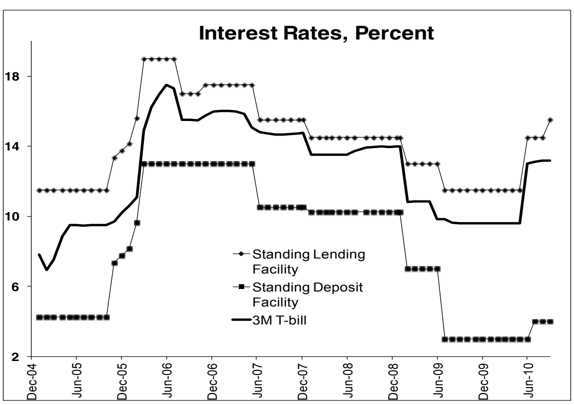
Money aggregates rose faster than expected, and reserve money exceeded its end-June target by a small margin...



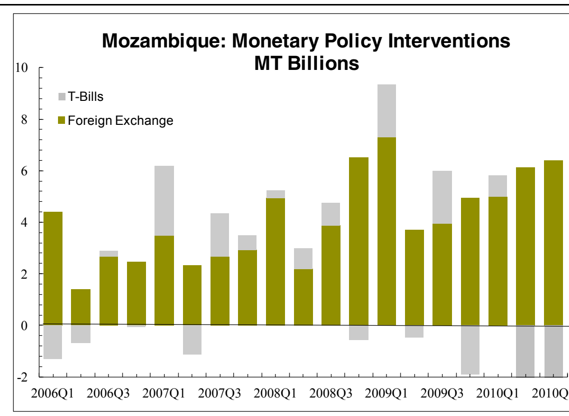
... in part due to an unusually strong seasonal surge in currency demand.



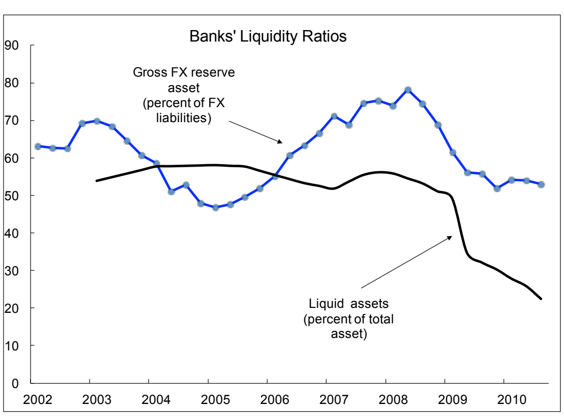
The BM has begun reversing its previous easing of monetary conditions, by decisively raising its policy rates…



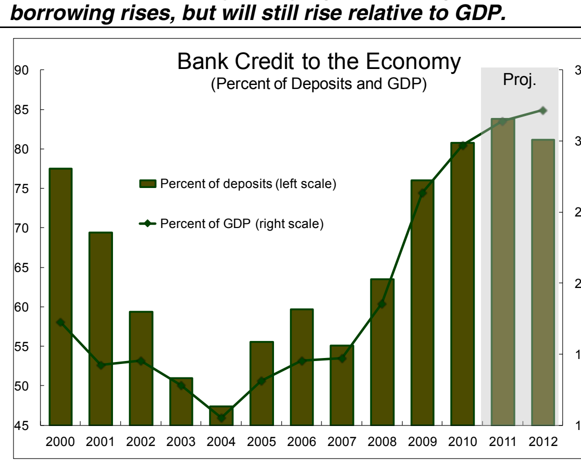
...and stepping up its open market operations to mop up liquidity.



Even so, the large expansion in private sector credit has tightened liquidity conditions, and banks' overall and FX liquidity ratios have declined sharply.



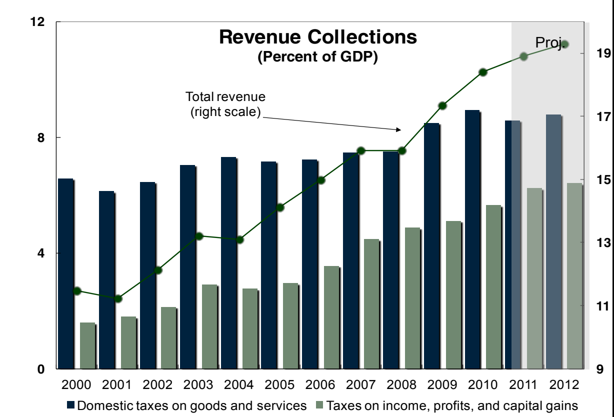
Private sector credit is expected to ease as a share of deposits, as monetary policy tightens and government borrowing rises, but will still rise relative to GDP.



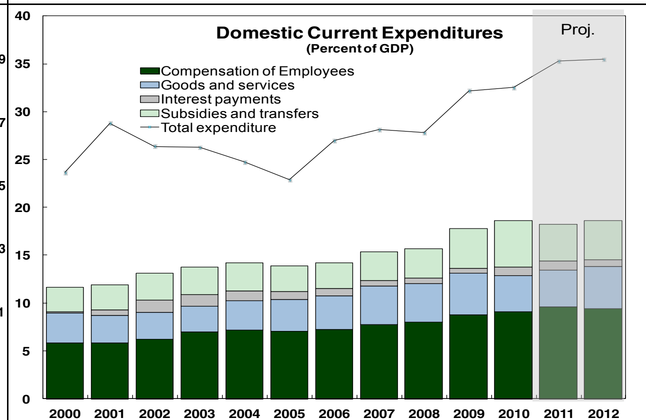
Sources: Mozambican authorities and IMF staff estimates and projections.

Figure 6: Mozambique: Fiscal Developments

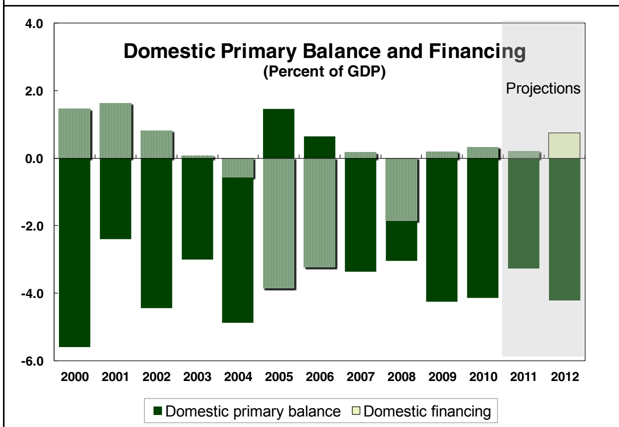
Revenue collections in 2009/10 have been buoyant despite the crisis, reflecting tax administration efforts and resilient growth. This is expected to continue in 2011/12.



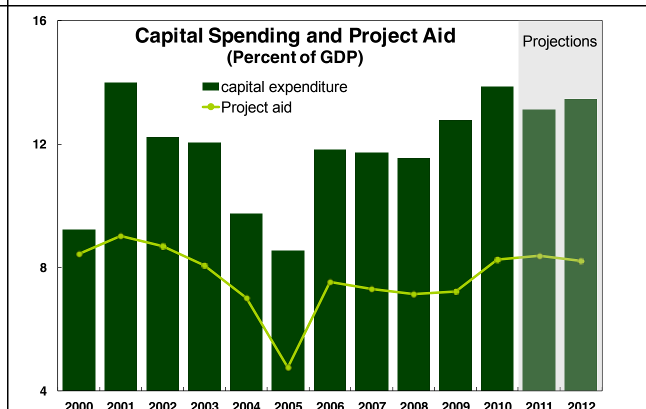
The wage bill continues to put pressure on domestic spending.



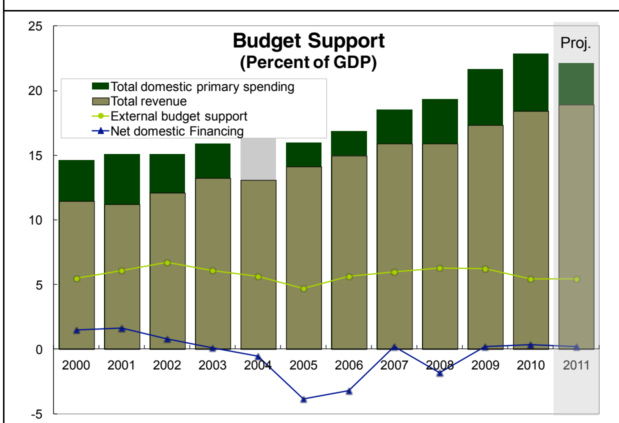
The domestic primary deficit in 2010 was higher than anticipated, partially reflecting the impact of the fuel subsidy, but will be reduced in 2011 to help reduce inflation.



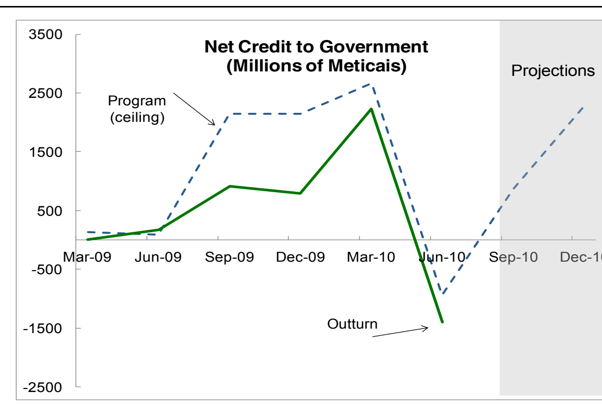
Capital spending relies heavily on external project support, and…



…external budget support reduces the need for domestic financing.



Net credit to government until end-June 2010 met the program target comfortably.



Sources: Mozambican authorities and IMF staff estimates and projections.

18. **Like in 2010, consistent with the organic budget law, the authorities agreed to put budget execution under a revenue contingency.** It would slow budget execution until evidence of an increase in revenue collections beyond ½ percent of GDP materializes; the draft 2011 budget assumes a rise in revenue of about 1 percent of GDP, similar to the projected revenue effort in 2010. While important reforms in tax policy and administration, closely accompanied by Fund technical assistance, have helped raise revenue collections by 5 percent of GDP since 2004, staff and the authorities agreed to initially base their economic program on the revenue contingency and revisit the pace of budget execution at the time of the next review.

MEFP ¶ 20

19. **In light of the projected sharp rise in the wage bill for 2011, the government committed to revisit the implementation strategy of its wage policy.** To date, it has pursued a rapid implementation pace of this multi-year plan in order to, among other things, simplify and decompress the salary scales and reform allowances. The government plans to adjust the implementation pace in line with macroeconomic constraints. In addition, under a structural benchmark for end-July 2011, it will take decisive steps to create an automated real-time civil service database on the number of civil servants and wage payments.

MEFP ¶ 22

C. Responding to the Riots and Supporting the Most Vulnerable

20. **The September riots illustrated the need to accelerate efforts to fight poverty.** As highlighted in EBS/10/98, Mozambique's strong growth performance has been skewed in the capital-intensive natural resource sector, which has had limited spillovers to the domestic economy and created few jobs. While the authorities' growth strategy underlying their PSI aims at crowding in private sector activity through stepped-up well-targeted public investment in the transportation and energy sectors, this will take time, and there is a need to adopt timely measures to more decisively fight poverty and help preserve social peace. The authorities plan to complete their new Poverty Reduction Strategy (PARP) next spring, in consultation with civil society, the private sector, and development partners (Box 2).

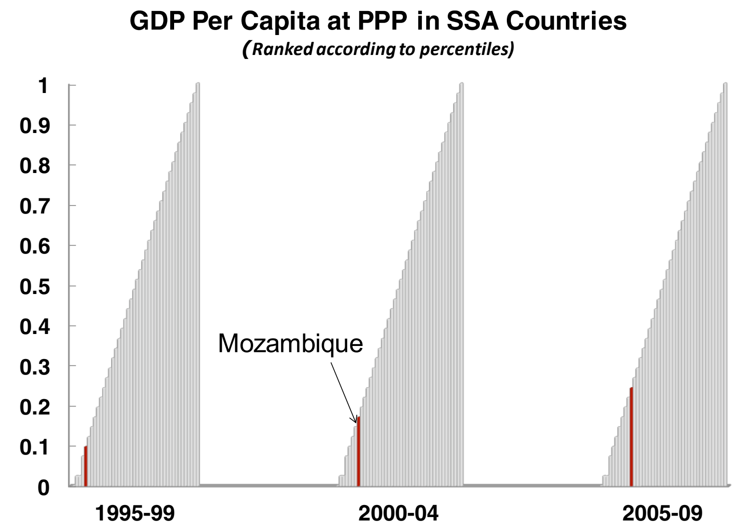
MEFP ¶ 8-10

21. **The authorities emphasized the transitional nature of the emergency measures adopted in the wake of the September riots.** While they created budgetary room for the various subsidies and tax suspensions in 2010 and 2011, they plan to review their effectiveness and possibly replace them with alternative measures in due course.

22. **They also expressed interest in studying, jointly with their partners, better targeted social safety nets that could more permanently support those truly in need.** This could be achieved within existing programs—current social transfer programs benefit only about one-twentieth of the population—or through the introduction of new initiatives, which, however, are likely to require extensive technical and financial assistance. The authorities indicated they would strive to reserve fiscal space for such measures in their medium-term fiscal program.

Box 2. Addressing Poverty

Mozambique's impressive growth performance has helped reduce poverty, but challenges remain. After a sizable 15 percentage point drop between 1997 and 2003, the just released 2008/09 household survey data indicate a broadly stable poverty headcount, at around 54 percent. The data point to a slight rise in urban, and drop in rural, poverty, and substantial regional changes. One-fifth of all households consume less than 800 calories per day. Overall, notwithstanding strong per-capita growth, Mozambique remains below the 25th percentile of the distribution for SSA countries.



The current PARPA will expire this year, and the authorities have launched the drafting of their successor strategy for 2011-14. Following the September riots, they opted to lengthen the drafting process to allow for a more thorough analysis and discussion with stakeholders.

The new PARP offers an **opportunity to make Mozambique's growth strategy more inclusive and provide better protection to the poor.** The authorities have reached out to development partners to discuss possible avenues to generate employment, increase household incomes, and improve food security. This could also include developing sectoral strategies, such as for agriculture and tourism. In addition, the mission urged the authorities to step up efforts to improve the business environment where Mozambique lags many of its African peers. A follow-up event to the March 2010 Namaacha conference on Mozambique's economic challenges, organized jointly by the authorities, the Bank, and the Fund (see Box 3 in EBS/10/98), is slated to take place in December.

23. **There are several possible pro-poor policy options advocated by various development partners.** Those include labor-intensive public works programs, a conditional cash transfer system, an agricultural sector reform strategy, school feeding programs, abolition of the remaining health care fees, and targeted urban transport subsidies. Work by Bank and Fund staff in the wake of the 2008 food and fuel price crisis had advocated several of these options.

D. Sustaining Economic Growth

24. **The planned acceleration of public investment will be embedded in a prudent policy mix to maintain macroeconomic stability and debt sustainability.** The authorities intend to limit the domestic primary fiscal deficit at the previously envisaged level of about 4 percent of GDP from 2012 onwards, coupled with a tight monetary policy stance to achieve their inflation objective, ward off demand pressures, and support financial deepening. They also reiterated their intention to boost the business environment, which will be supported under the Bank's PRSC.

MEFP ¶ 24-28

25. **Updated projections for the pipeline of public investment projects and their financing indicate little change relative to prior staff analysis.** Implementation of projects financed by NCB and the partially nonconcessional Portuguese credit line should peak over the next three years. This seems compatible with the capacity of the economy, given the high import component and external financing of the planned investment and underutilized labor markets. The current account impact will be more than offset by the expected recovery in external demand and the coming online of new megaprojects with a substantial export potential (e.g., the Rio Doce coal mine). The authorities reaffirmed their commitment to remain vigilant as to any signs of overextending the economy's capacity that would indicate a need to adjust policies.

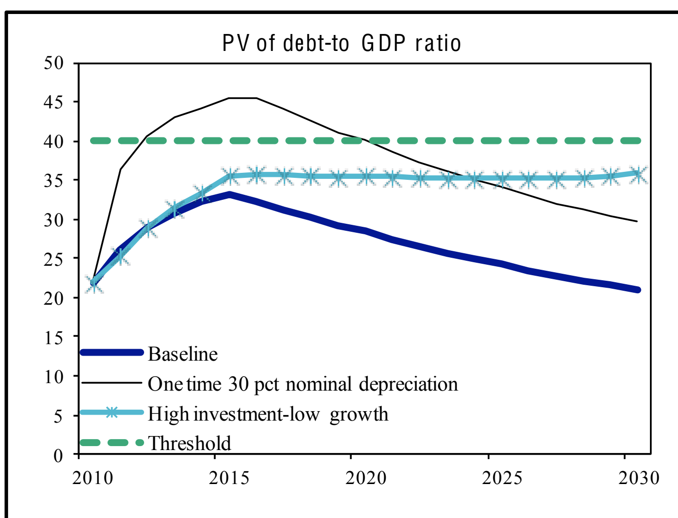
Mozambique: Total Public Investment Program, 2009-15

	2009	2010	2011	2012	2013	2014	2015
				(Percent of GDP)			
Total	12.8	14.3	17.8	17.6	16.8	15.8	15.4
On budget	12.8	13.9	16.0	16.0	15.4	14.6	14.4
Domestically financed	4.4	5.1	4.9	5.5	5.7	5.8	6.0
Donor financed, concessional	8.4	8.8	8.2	8.0	7.6	7.2	6.9
Non-concessional	0.0	0.0	2.9	2.5	2.2	1.6	1.5
Credit line from Portugal 1/	0.0	0.4	1.8	1.6	1.4	1.2	1.0
Concessional	0.0	0.2	1.0	0.9	0.8	0.7	0.6
Nonconcessional	0.0	0.2	0.8	0.7	0.6	0.5	0.4
Memorandum items:							
Total concessional and domestic	12.8	14.1	14.2	14.4	14.0	13.7	13.5
Total nonconcessional	0.0	0.2	3.6	3.2	2.8	2.1	1.9
GDP	269,346	325,547	377,880	430,072	489,825	557,776	635,069

Source: IMF staff calculations.

1/ Portuguese credit line that will be implemented by the Road Fund. 2010 data are preliminary projections.

26. **The authorities' envisaged investment and borrowing plans remain consistent with debt sustainability.** A DSA update prepared by staff suggests that Mozambique continues to face a low risk of external debt distress. External debt levels should remain below their indicative thresholds under the baseline scenario. The PV of external PPG debt peaks at about 33 percent of GDP in 2015, gradually falling to 23 percent of GDP over time. However, the government's plans would noticeably increase debt vulnerabilities. The PV of debt-to-GDP ratio under stress tests would temporarily and marginally exceed the relevant threshold. In addition, a high-investment/low-growth scenario indicates the potential risks to debt sustainability of scaling up public investment, if expected growth dividends do not materialize.



27. **The authorities reiterated their determination to pursue a cautious approach to NCB.** They saw NCB as complementary to their primary reliance on concessional donor funds. They clarified that any NCB would be considered case-by-case, based on economic return and impact on debt sustainability, which should be conducive to containing debt vulnerabilities.

28. **The authorities requested greater flexibility under the program to benefit from the program's overall NCB ceiling of US$900 million.** At the inception of the program, this ceiling was determined to be compatible with macroeconomic stability and debt sustainability. In light of the progress made in negotiating two Brazilian loans for Nacala airport (US$80 million) and the port of Beira (US$220 million), the start-up limit of US$200 million set for 2010 is proposed to be raised to US$300 million.[2] Considering the authorities' progress in implementing reforms in debt management and investment planning, further commitments in the current MEFP in this area, and the maintenance of program safeguards—the continuous structural benchmark on channeling NCB to transportation and energy infrastructure and the sharing of feasibility studies—granting the authorities full access to the remaining US$600 million out of the overall NCB program ceiling of US$900 million from 2011 onwards can be justified. This is also warranted in light of Mozambique's recent progress in public financial management (PFM),[3] and the new program commitments that would allow the authorities to slow implementation of NCB-financed projects should this be warranted by macroeconomic circumstances.

MEFP ¶ 25-27

E. Building Capacity

29. **The program's emphasis on building institutional capacity to shore up the authorities' policy objectives and improve economic decision-making will continue.** In addition to the afore-mentioned structural benchmark on enhancing real-time wage bill monitoring, conditionality was set in the areas of debt management and investment planning, tax policy, and financial sector supervision. As such, they would underpin achievement of the program's objectives of safeguarding macroeconomic stability and supporting economic development.

30. **Beyond structural conditionality, the authorities committed to important other reforms.** Among other things, they agreed to additional reforms in PFM, debt management (including to make the new PPP unit in the Ministry of Finance operational), tax administration, pension reform, and financial sector development and supervision. With respect to natural resources management, the authorities are well on track to become a full EITI member within the envisaged two-year candidacy period.

MEFP ¶ 28-33

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[2] Both infrastructure projects were identified as priorities in the MEFP accompanying the PSI request. The grant element of the Brazilian loans is estimated at 18 percent.

[3] The recent improvement in Mozambique's sub-CPIA rating would place the country in the higher capacity/lower vulnerability category. However, in this year's capacity assessment exercise Mozambique was kept in the lower capacity category until further improvements in the area of debt management have taken place.

Structural Conditionality, 2011

MEFP Paragraph	Measure	Target Date	Macroeconomic Importance
	Tax Policy		
31	Adopt an action plan to simplify the tax system, expand the tax base, and assess the merits and feasibility of possibly reducing the corporate tax rate and of rationalizing incentives under the tax benefits code.	End-March 2011	Support envisaged further rise in revenue-to-GDP ratio and help contain the fiscal deficit.
	Debt Management and Investment Planning		
30	Issue a ministerial decree to introduce a project selection protocol and standard project evaluation template to be used by all Government entities.	End-March 2011	Improve the analysis and selection of public investment projects, thereby supporting economic growth.
30	Create a Debt Management Committee (DMC) and Project Selection Committee (PCC) as advisory bodies.	End-March 2011	Enhance debt management and project selection, which will reduce fiscal risks and support economic growth.
	Financial Sector		
35	Begin putting in place the financial sector contingency plan, by implementing the plan modules on prompt corrective action procedures and coordination with foreign supervisors.	End-April 2011	Safeguard macroeconomic stability and the soundness of the banking system.
	Wage Policy		
22	Issue a first quarterly report in the civil service population and wage data, building on enhancements to the e-FOLHA and e-CAF real-time monitoring systems.	End-July 2011	Enhance the government's control and monitoring of the wage bill, thereby supporting planning and implementation of fiscal policy.

IV. Risks to the Program

31. **Although Mozambique's track record in implementing Fund-supported programs is strong, some risks remain.** First, the macroeconomic outlook could worsen, should the recovery of the global economy take longer than expected. This could adversely affect the projected strengthening in export prices for Mozambique's key commodities, especially aluminum, and burden the current account. It could also delay the anticipated recovery of private capital inflows. Second, disappointments related to the authorities' plans to make economic growth more inclusive and expand social safety nets could lead to the reemergence of social tensions. Third, the tightening of the macroeconomic policy mix to curb inflation expectations hinges on sustained efforts to raise government revenues and reign in non-priority spending, as well as the BM's determination to decisively remove the excess liquidity in the economy. Shortfalls in any of these areas, but also sustained international price increases for food and fuel products, could lengthen the period to bring headline inflation back into single digits. And fourth, with a more medium-term perspective, the authorities may encounter difficulties in preserving the focus of

government spending on priority infrastructure investment and social sectors, if efforts to contain the wage bill and address the fiscal risks emanating from the continued subsidization of diesel fuel are unsuccessful.

V. Program Monitoring

32. **Modifications are proposed for several ACs and indicative targets for end-December 2010.** This affects the ACs on NCG, reserve money, and NIR, and the indicative floor on government revenues; these changes largely reflect the changed economic environment and the authorities' policy response to it. In addition, with respect to the AC on NCB, it is proposed that the ceiling be raised from US$200 million to US$300 million to allow the authorities to contract two loans related to the construction of Nacala airport and the rehabilitation of the port of Beira.

33. **From 2011 onwards, it is proposed that the remainder of the full NCB amount of US$900 million that was envisaged for the entire three-year program period be made available.** Should the Brazilian loans of US$300 million be signed as expected by year-end, the available NCB amount in 2011 would thus be US$600 million. This should facilitate the authorities' contracting of NCB loans. The ringfencing of such borrowing should ensure the compatibility of the NCB with macroeconomic stability and debt sustainability.

VI. Staff Appraisal

34. **Mozambique has weathered the global crisis well.** While the country's external accounts have shown some strains in 2010, its growth performance has remained impressive, partially helped by the authorities' appropriate adoption of accommodating macroeconomic policies. Although this has partially contributed to the emergence of inflationary pressures, the authorities' swift response bodes well for preventing inflation expectations from taking a foothold in the economy. Nonetheless, the rising costs of living have taken a toll on the poor, and the recent unrest highlighted that economic growth over the last two decades has not generated a sufficient number of jobs and raised people's livelihoods.

35. **The authorities are appropriately rethinking their growth strategy in the context of the forthcoming drafting of the new four-year PARP.** Their eagerness to engage development partners and civil society on making their growth strategy more inclusive and allowing more Mozambicans to participate in the country's economic growth is welcome. In this context, the authorities are urged to also consider expanding the existing social safety nets in a well-targeted way, which may be beneficial in enhancing the country's long-term growth factors; development partners indicated their readiness to assist them in this undertaking. If well done, the new PARP could represent a milestone in building a basis for durable and sustainable growth shared by many. The next PSI review will provide an opportunity to embed any such efforts in the program design, complementing the program's current focus on macroeconomic stability and economic development through infrastructure investment.

36. **The authorities' determination in fighting inflation is welcome.** When core inflation was ratcheting up in mid-2010, the BM quickly signaled its policy intentions through increases in its key policy rate and reserve requirements. It also appropriately chose to focus on foreign exchange sales in its efforts to mop up excess liquidity, which, while helping smooth the exchange rate with its direct pass-through to inflation, necessitated tapping into the country's international reserves. For 2011, the BM needs to adhere to a strict course of monetary tightening to achieve its declared objective to return inflation to single digits. Over the medium term, achieving the authorities' inflation objective of 6 percent appears feasible, while continuing to provide the necessary space for financial deepening.

37. The government has shown strong resolve to support the monetary tightening. It was able to reallocate spending within an envelope that was strained by higher-than-expected outlays for the fuel subsidy and the emergency measures to restore social calm. Mozambique's revenue performance is remarkable, both over time and compared to other SSA countries; the strong gains reaped from the reforms in tax policy and administration in recent years are helping the authorities at a crucial time keep their fiscal program on course. Similarly, following two years of strong expansion of the wage bill, the planned review of the government wage policy, together with improvements to the civil service data base and the wage payment system, should allow the government to make prudent decisions on the way forward, consistent with macroeconomic circumstances. Finally, given the authorities' strong implementation track record, the PSI's continued emphasis on fiscal structural reforms will provide a strong footing for the envisaged medium-term fiscal framework.

38. **The authorities' fuel price policy has contributed to substantial costs to Mozambique's fiscal and external accounts and poses future risks.** Although the motivation is understandable, keeping retail prices below market prices over an extended period of time is unsustainable. The recent policy declaration to charge market prices to wholesale customers was overdue, and while the planned cross-subsidization between the various fuel categories could help contain fiscal risks, the authorities are encouraged to swiftly reach an agreement with fuel importers on settling accumulated losses. They also need to assess how the impact of the necessary price adjustments can be cushioned for the poor.

39. **Based on program performance to date and the authorities' traditionally strong** ownership of their Fund-supported programs, staff recommends: (i) completion of the first review under the PSI; (ii) the waiver for the nonobservance of the end-June AC on reserve money, as corrective action is being taken; and (iii) modification of ACs.

Table 1. Mozambique: Selected Economic and Financial Indicators, 2008-15

	2008	2009	2010		2011		2012	2013	2014	2015
	Act.	Act.	EBS/10/98	Proj.	EBS/10/98	Proj.				
			(Annual percentage change, unless otherwise indicated)							
National income and prices										
Nominal GDP (MT billion)	240	269	306	326	348	378	430	490	558	635
Nominal GDP growth	15.8	12.1	16.3	20.9	13.6	16.1	13.8	13.9	13.9	13.9
Real GDP growth	6.8	6.4	6.5	7.2	7.5	7.5	7.8	7.9	7.8	7.8
Consumer price index (annual average)	10.3	3.3	9.3	12.7	5.6	8.0	5.6	5.6	5.6	5.6
Consumer price index (end of period)	6.2	4.2	8.0	15.5	5.6	6.9	5.6	5.6	5.6	5.6
Exchange rate, MT per US dollar, eop	25.5	27.8	32.0	36.0	32.8	36.8	36.9	37.0	38.7	40.6
Exchange rate, MT per US dollar, per.avg.	24.2	26.8	30.0	33.3	32.4	36.0	36.2	36.3	37.2	38.9
External sector										
Merchandise exports	10.0	-19.1	12.7	8.4	27.2	20.5	6.6	7.1	7.4	7.7
Merchandise exports, excluding megaprojects	41.1	10.0	4.5	-23.0	2.7	2.7	1.4	3.9	6.9	11.4
Merchandise imports	29.6	-6.1	10.7	11.7	13.1	4.1	8.7	9.4	9.1	10.0
Merchandise imports, excluding megaprojects	34.7	-10.6	14.5	11.7	16.1	1.5	9.1	9.9	10.0	11.8
Terms of trade	-3.5	-7.9	1.5	2.5	12.0	13.1	-1.4	0.9	-4.0	-3.0
Nominal effective exchange rate (end of period)	11.1	-4.0	…	…	…	…	…	…	…	…
Real effective exchange rate (end of period)	11.8	-3.2	…	…	…	…	…	…	…	…
			(Annual percentage change, unless otherwise indicated)							
Money and credit										
Reserve money	7.8	27.3	19.5	25.0	14.7	13.0	15.5	15.3	15.1	15.0
M2	26.0	34.6	22.6	25.4	21.6	24.2	19.9	19.6	18.2	15.4
M3 (Broad Money)	20.3	32.6	21.1	27.0	23.1	18.3	19.4	18.2	16.8	14.0
Credit to the economy	45.9	58.6	19.1	36.0	14.0	22.6	16.6	15.3	15.2	15.1
					(Percent of GDP)					
Investment and saving										
Gross domestic investment	16.5	16.3	25.2	21.8	26.0	23.0	23.6	23.7	23.8	24.0
Government	11.5	12.8	13.9	13.9	14.3	13.1	13.4	13.2	13.0	12.9
Other sectors	4.9	3.5	11.3	8.0	11.8	9.9	10.2	10.4	10.8	11.1
Gross domestic savings (excluding grants)	-3.2	-1.0	4.6	1.2	5.5	3.2	4.0	4.1	4.3	4.3
Government	0.3	-0.4	1.2	-0.2	1.2	0.7	0.7	1.0	1.2	1.5
Other sectors	-3.5	-0.6	3.4	1.4	4.4	2.5	3.3	3.1	3.1	2.9
External current account, before grants	-19.7	-17.3	-20.6	-20.7	-20.5	-19.8	-19.6	-19.6	-19.4	-19.6
External current account, after grants	-11.9	-10.5	-13.6	-13.4	-12.8	-12.0	-12.0	-12.2	-12.4	-13.1
Government budget										
Total revenue	15.9	17.4	18.4	18.4	18.7	18.9	19.3	19.8	20.1	20.5
Total expenditure and net lending	27.8	32.2	31.9	32.5	35.4	35.3	35.5	34.9	34.0	33.9
Overall balance, before grants	-11.6	-14.8	-13.5	-14.1	-16.7	-16.4	-16.2	-15.1	-13.9	-13.4
Total grants	9.4	9.4	8.8	9.2	9.4	9.4	9.3	9.0	8.8	8.3
Overall balance, after grants	-2.2	-5.4	-4.7	-4.9	-7.2	-7.0	-6.9	-6.1	-5.1	-5.1
Domestic primary balance, before grants	-3.0	-4.3	-4.2	-4.1	-4.6	-3.3	-4.2	-3.9	-3.7	-3.7
External financing (incl. debt relief)	4.0	5.0	4.3	4.5	6.3	6.8	6.2	5.4	4.4	4.3
Net domestic financing	-1.9	0.2	0.3	0.3	0.9	0.2	0.7	0.7	0.8	0.8
Privatization	0.0	0.2	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Total public debt	25.4	28.6	…	…	…	…	…	…	…	…
Of which: external	21.2	25.5	…	…	…	…	…	…	…	…
Of which: domestic	4.2	3.2	…	…	…	…	…	…	…	…
				(US$ millions, unless otherwise indicated)						
External current account, before grants	-1,958	-1,741	-2,104	-2,024	-2,204	-2,082	-2,334	-2,644	-2,919	-3,204
External current account, after grants	-1,179	-1,054	-1,391	-1,308	-1,380	-1,258	-1,432	-1,654	-1,857	-2,130
Overall balance of payments	120	191	100	-157	405	220	427	495	367	282
Net international reserves (end of period) [1]	1,644	1,840	1,930	1,675	2,334	1,895	2,322	2,817	3,185	3,467
Gross international reserves (end of period) [1]	1,660	2,012	2,128	1,868	2,530	2,086	2,510	3,002	3,337	3,559
Months of projected imports of goods and nonfactor services	4.4	4.9	4.9	4.4	5.3	4.5	4.9	5.3	5.4	5.3

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

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

Table 2. Mozambique: Government Finances, 2009–11

(MT Billions)

	2009	2010				2011	
	Outturn	H1 - Prog.	H1 - Prel.	Prog.	Proj.	Prog.	Proj. /1
Total revenue	46.73	27.05	27.94	56.47	59.94	65.09	71.45
Tax revenue	41.47	23.94	24.93	49.91	53.31	57.64	63.22
Income and profits	13.72	8.85	9.14	17.50	18.40	18.56	23.58
Goods and services	22.89	12.49	13.10	27.00	29.06	32.83	32.44
International trade	4.08	2.11	2.21	4.36	4.59	5.04	5.85
Other	0.78	0.49	0.48	1.05	1.26	1.20	1.35
Nontax revenue	5.26	3.11	3.01	6.56	6.63	7.45	8.23
Total expenditure and net lending	86.70	43.81	44.72	97.87	105.87	123.07	133.39
Current expenditure	47.87	25.34	31.09	52.85	60.56	61.05	68.78
Compensation to employees	23.62	13.67	13.96	27.60	29.56	31.16	36.25
Goods and services	11.72	5.58	6.45	11.99	12.40	14.45	14.47
Interest on public debt	1.36	0.88	1.34	1.73	2.76	2.06	3.59
Domestic	0.82	0.55	0.97	1.05	1.92	1.19	2.66
External	0.54	0.33	0.37	0.68	0.84	0.87	0.93
Transfer payments	11.17	5.22	9.34	11.50	15.83	13.38	14.47
Of which: fuel subsidy	2.80	1.13	4.10	1.69	4.13	…	…
Domestic current primary balance	0.22	2.58	-1.81	5.35	2.15	6.10	6.26
Capital expenditure	34.41	17.48	14.35	42.64	45.14	49.63	49.59
Domestically financed	11.72	7.94	5.81	18.71	16.62	22.66	18.42
Externally financed	22.69	9.54	8.52	23.93	28.52	26.97	31.17
Net lending	4.42	0.98	0.86	2.38	0.17	12.39	15.01
Domestically financed	-0.02	-0.20	-0.16	-0.36	-1.01	-0.42	0.19
Externally financed loans to public enterprises	4.44	1.18	1.02	2.74	1.18	12.80	14.82
of which: nonconcessional net lending	0.00	0.00	0.00	0.00	0.00	9.71	10.79
Domestic primary balance, before grants, above the line /2	-11.47	-5.16	-7.45	-13.00	-13.46	-16.14	-12.35
Unallocated revenue (+)/expenditure (-) 3/	0.00	0.00	-1.58	0.00	0.00	0.00	0.00
Overall balance, before grants	-39.97	-16.76	-18.36	-41.40	-45.93	-57.98	-61.94
Grants received	25.30	13.59	14.05	26.85	29.94	32.79	35.53
Project support	16.18	5.96	7.31	16.20	17.22	21.42	23.40
Budget support	9.12	7.64	6.74	10.65	12.72	11.37	12.13
Overall balance, after grants	-14.67	-3.17	-4.31	-14.55	-15.99	-25.19	-26.40
Net external financing	13.50	4.83	4.04	13.28	14.62	21.95	25.59
Disbursements	14.20	5.56	5.13	14.74	16.21	23.01	26.77
Project	6.51	3.59	3.11	7.74	11.31	5.55	7.77
Nonproject support	7.69	1.97	2.03	7.00	4.91	17.46	19.00
Loans to public enterprises	3.89	1.18	1.01	2.74	1.18	12.80	14.82
of which: nonconcessional	0.00	0.00	0.00	0.00	0.00	9.71	10.79
Budget support	3.80	0.79	1.01	4.27	3.73	4.66	4.18
Cash amortization	-0.70	-0.73	-1.09	-1.46	-1.60	-1.06	-1.18
Net domestic financing 4/	0.52	-1.74	-1.29	0.93	1.04	3.23	0.81
Net privatization	0.41	0.08	-0.02	0.33	0.33	0.00	0.00
Memorandum items:							
Net aid flows	38.26	18.09	17.72	39.45	43.72	44.17	49.40
Gross aid flows	39.50	19.15	19.18	41.59	46.15	46.09	51.51
Budget support	12.92	8.43	7.75	14.92	16.45	16.02	16.31
Nonbudget support	26.58	10.72	11.43	26.67	29.70	30.07	35.20
Project support	22.69	9.54	10.42	23.93	28.52	26.97	31.17
Loans to public enterprises	3.89	1.18	1.01	2.74	1.18	3.10	4.03
External debt service	1.24	1.06	1.46	2.14	2.44	1.93	2.11

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

1/ In line w ith the organic budget law (SISTAFE 2002) budget execution w ill be limited to cautionary ceilings untill evidence of stronger revenue performance materializes.

2/ Revenue minus noninterest current expenditure minus locally financed capital expenditure and locally financed net lending.

3/ Residual discrepancy betw een identified sources and uses of funds.

4/ Excludes recapitilization bonds issued to the Bank of Mozambique.

Table 3. Mozambique: Government Finances, 2009–15
(Percent of GDP)

	2009	2010		2011		2012	2013	2014	2015
	Act.	Prog.	Proj.	Prog.	Proj. 1/	Proj.			
Total revenue	17.4	18.4	18.4	18.7	18.9	19.3	19.8	20.1	20.5
Tax revenue	15.4	16.3	16.4	16.6	16.7	17.1	17.6	17.9	18.3
Nontax revenue	2.0	2.1	2.0	2.1	2.2	2.2	2.2	2.2	2.2
Total expenditure and net lending	32.2	32.0	32.5	35.4	35.3	35.5	34.9	34.0	33.9
Current expenditure	17.8	17.3	18.6	17.5	18.2	18.6	18.8	18.9	19.0
Compensation to employees	8.8	9.0	9.1	9.0	9.6	9.4	9.3	9.1	8.9
Goods and services	4.3	3.9	3.8	4.2	3.8	4.4	4.4	4.5	4.4
Interest on public debt	0.5	0.6	0.8	0.6	1.0	0.7	0.8	0.9	1.0
Transfer payments	4.1	3.8	4.9	3.8	3.8	4.1	4.3	4.4	4.7
Of which: fuel subsidy	1.0	0.6	1.3	…	…	…	…	…	…
Domestic current primary balance	0.1	1.7	0.7	1.8	1.7	1.3	1.8	2.2	2.4
Capital expenditure	12.8	13.9	13.9	14.3	13.1	13.4	13.2	13.0	12.9
Domestically financed	4.4	6.1	5.1	6.5	4.9	5.5	5.7	5.8	6.0
Externally financed	8.4	7.8	8.8	7.8	8.2	8.0	7.6	7.2	6.9
Grants									
Loans	2.4	2.5	3.5	1.6	2.1	1.9	1.7	1.5	1.6
Net lending	1.6	0.8	0.1	3.6	4.0	3.4	2.9	2.2	2.0
Domestically financed	0.0	-0.1	-0.3	-0.1	0.1	0.1	0.0	0.1	0.1
Externally financed loans to public enterprises	1.7	0.9	0.4	3.7	3.9	3.4	2.9	2.1	1.9
of which: concessional	1.7	0.9	0.4	0.9	1.1	1.1	1.1	1.1	1.1
of which: nonconcessional net lending	0.0	0.0	0.0	2.8	2.9	2.3	1.8	1.0	0.8
Domestic primary balance, before grants 2/	-4.3	-4.2	-4.1	-4.6	-3.3	-4.2	-3.9	-3.7	-3.7
Overall balance, before grants	-14.8	-13.5	-14.1	-16.7	-16.4	-16.2	-15.1	-13.9	-13.4
Grants received	9.4	8.8	9.2	9.4	9.4	9.3	9.0	8.8	8.3
Project	6.0	5.3	5.3	6.2	6.2	6.1	5.9	5.7	5.2
Nonproject	3.4	3.5	3.9	3.3	3.2	3.2	3.1	3.1	3.1
Overall balance, after grants	-5.4	-4.7	-4.9	-7.2	-7.0	-6.9	-6.1	-5.1	-5.1
Net external financing	5.0	4.3	4.5	6.3	6.8	6.2	5.4	4.4	4.3
Disbursements	5.3	4.8	5.0	6.6	7.1	6.6	6.1	5.3	5.3
Project	2.4	2.5	3.5	1.6	2.1	1.9	1.7	1.5	1.6
Nonproject support	2.9	2.3	1.5	5.0	5.0	4.7	4.4	3.8	3.6
Loans to public enterprises	1.4	0.9	0.4	3.7	3.9	3.6	3.3	2.7	2.5
of which: nonconcessional	0.0	0.0	0.0	2.8	2.9	2.5	2.2	1.6	1.5
Budget support	1.4	1.4	1.1	1.3	1.1	1.1	1.1	1.1	1.1
Cash amortization	-0.3	-0.5	-0.5	-0.3	-0.3	-0.4	-0.6	-0.9	-1.0
Net domestic financing 3/	0.2	0.3	0.3	0.9	0.2	0.7	0.7	0.8	0.8
Net privatization	0.2	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:									
Net aid flows	14.5	12.9	13.4	12.7	13.1	12.5	11.8	11.0	10.5
Gross aid flows	15.0	13.6	14.2	13.2	13.6	13.3	12.9	12.5	12.1
Budget support	4.9	4.9	5.1	4.6	4.3	4.3	4.3	4.2	4.2
Nonbudget support	10.1	8.7	9.1	8.6	9.3	9.0	8.6	8.3	7.9
Project support	8.6	7.8	8.8	7.8	8.2	8.0	7.6	7.2	6.9
Loans to public enterprises	1.5	0.9	0.4	0.9	1.1	1.1	1.1	1.1	1.1
External debt service	0.5	0.7	0.7	0.6	0.6	0.8	1.1	1.4	1.6

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

1/ In line with the organic budget law (SISTAFE 2002) budget execution will be limited to cautionary ceilings untill evidence of stronger performance materializes.

2/ Revenue minus noninterest current expenditure minus locally financed capital expenditure and locally financed net lending.

3/ Excludes recapitilization bonds issued to the Bank of Mozambique.

Table 4. Mozambique: Monetary Survey, Quarterly, 2009-10[1]

	2009	2010								2011			
	Q4	Q1		Q2		Q3		Q4		Q1	Q2	Q3	Q4
	Act.	Prog.	Act.	Prog.	Act.	Prog.	Proj.	Prog.	Proj.	Projection			
	(Mt Billions, unless otherwise stated)												
Bank of Mozambique													
Net foreign assets	49.6	45.2	47.6	49.8	56.3	54.5	58.0	57.7	55.5	57.7	58.4	59.8	64.8
(US$ billions)	1.7	1.6	1.5	1.6	1.6	1.8	1.6	1.8	1.5	1.6	1.6	1.7	1.8
Net international reserves	53.7	48.8	52.4	53.5	61.0	58.3	62.8	61.7	60.4	62.6	63.3	64.6	69.7
(US$ billions)	1.8	1.7	1.7	1.8	1.7	1.9	1.7	1.9	1.7	1.7	1.8	1.8	1.9
Net domestic assets	-25.2	-22.7	-24.7	-24.0	-30.2	-28.7	-28.7	-28.5	-25.0	-30.2	-28.5	-28.3	-30.2
Credit to government (net)	-25.3	-18.7	-23.3	-18.1	-24.9	-22.4	-18.7	-20.9	-14.8	-19.3	-18.7	-19.4	-16.7
Credit to banks (net)	2.3	-0.5	1.7	-0.5	1.8	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Credit to the economy	0.4	0.4	0.4	0.4	0.5	0.4	0.5	0.4	0.5	0.5	0.5	0.5	0.5
Other items (net; assets +)	-2.6	-3.9	-3.5	-5.9	-7.6	-6.2	-9.9	-7.6	-10.1	-10.8	-9.8	-8.8	-13.5
Reserve money	24.5	22.5	23.0	25.7	26.1	25.8	29.3	29.2	30.6	27.5	29.9	31.6	34.6
Currency in circulation	16.1	14.1	14.5	16.4	16.7	16.4	18.4	19.2	19.1	16.1	17.6	18.6	21.1
Bank deposits in BM	8.3	8.5	8.5	9.3	9.3	9.3	11.0	10.0	11.5	11.4	12.4	12.9	13.4
Commercial Banks													
Net foreign assets	14.1	14.0	13.4	17.5	17.2	17.4	21.2	20.6	18.6	9.0	11.8	4.3	9.4
(in millions of U.S. dollars)	0.5	0.5	0.4	0.6	0.5	0.6	0.6	0.6	0.5	0.2	0.3	0.1	0.3
Net domestic assets	79.3	80.4	82.4	87.4	86.5	87.8	98.1	93.0	101.0	110.4	117.5	130.6	132.1
Banks' reserves	11.7	10.1	11.0	11.5	11.8	11.3	13.8	13.2	14.2	13.1	13.5	13.9	15.2
Credit to BM (net)	-2.5	0.5	-1.6	0.5	-1.8	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Credit to government (net)	13.8	12.6	14.9	7.3	12.4	14.2	6.7	11.0	4.3	10.2	6.5	8.5	7.1
Credit to the economy	71.0	72.8	74.1	84.3	82.4	77.8	93.9	84.7	96.7	99.2	107.0	115.5	118.6
Other items (net; assets +)	-14.8	-15.6	-15.9	-16.1	-18.3	-16.1	-16.8	-16.3	-14.6	-12.6	-10.1	-7.7	-9.3
Deposits	93.4	94.4	95.8	104.9	103.7	105.3	119.3	113.7	119.6	119.4	129.3	135.0	141.5
Demand and savings deposits	60.2	59.2	60.3	65.6	63.9	66.6	74.3	71.4	73.4	72.2	77.9	82.2	85.2
Time deposits	33.2	35.2	35.4	39.4	39.8	38.6	45.0	42.3	46.2	47.2	51.4	52.7	56.4
Monetary Survey													
Net foreign assets	63.7	59.2	61.0	67.3	73.5	71.9	79.2	78.4	74.1	66.7	70.2	64.2	74.2
(US$ billions)	2.2	2.0	2.0	2.2	2.1	2.3	2.2	2.5	2.1	1.8	2.0	1.8	2.0
Net domestic assets	43.3	47.6	47.3	51.9	45.0	47.7	55.7	51.3	61.9	67.2	75.4	88.4	86.6
Domestic credit	60.0	67.2	66.1	73.9	70.4	70.0	82.4	75.2	86.7	90.6	95.3	105.0	109.4
Credit to government (net)	-11.5	-6.1	-8.5	-10.8	-12.5	-8.2	-12.0	-9.9	-10.5	-9.1	-12.2	-11.0	-9.7
Credit to the economy	71.4	73.2	74.5	84.7	82.8	78.2	94.4	85.1	97.1	99.7	107.5	116.0	119.1
Cred. economy in foreign currency	22.8	25.5	25.3	28.6	29.5	25.8	33.5	27.4	34.0	35.9	37.0	38.9	38.2
Other items (net; assets +)	-16.6	-19.6	-18.8	-22.0	-25.3	-22.3	-26.8	-23.9	-24.8	-23.4	-19.9	-16.6	-22.8
Money and quasi money (M3)	107.1	106.8	108.3	119.2	118.5	119.7	134.8	129.6	136.0	133.9	145.7	152.6	160.9
Foreign currency deposits	34.5	35.5	37.2	39.6	42.2	38.4	47.5	40.7	45.0	43.1	48.9	47.9	47.9
(US$ billions)	1.2	1.2	1.2	1.3	1.2	1.2	1.3	1.3	1.2	1.2	1.4	1.4	1.3
M2	72.5	71.3	71.1	79.6	76.3	81.3	87.3	89.0	91.0	90.8	96.8	104.7	113.0
Memorandum Items													
Avg daily reserve money in 3rd month of quarter	23.6	22.0	22.8	24.6	25.4	25.8	28.9	28.2	29.5	27.4	29.2	31.1	33.3
12-month percent change	28.5	25.8	30.4	23.7	27.9	22.1	37.1	19.5	25.0	19.9	14.8	7.5	13.0
Avg daily currency in 3rd month of quarter	15.7	13.8	14.3	15.3	16.1	16.1	17.9	18.7	18.6	15.9	16.9	18.1	20.6
12-month percent change		32.8	38.2	25.7	31.9	17.4	30.7	19.3	18.7	10.9	5.0	1.3	10.5
NCG stock (prog def.) [2]	-14.6	-11.3	-12.1	-15.7	-15.9	-13.1	-15.1	-13.0	-13.6	-12.5	-15.6	-14.1	-12.8
NCG flow (prog def.) cum from end-year [2]	0.5	2.6	2.5	-1.7	-1.3	0.9	-0.5	0.9	1.0	1.1	-2.0	-0.5	0.8
12-month percent change													
Reserve money	27.3	25.8	28.4	23.7	25.2	22.1	39.1	19.5	25.0	19.9	14.8	7.5	13.0
M2	34.6	32.9	32.6	33.7	28.1	27.3	37.0	22.6	25.4	27.7	26.9	20.0	24.2
M3	32.6	29.8	31.6	33.7	32.9	23.9	39.8	21.1	27.0	23.6	22.9	13.2	18.3
Credit to the economy	58.6	47.9	50.5	60.0	56.5	27.5	53.8	19.1	36.0	33.7	29.7	22.8	22.6
Money multiplier (M2/reserve money)	2.97	3.17	3.10	3.09	2.93	3.16	2.97	3.04	2.97	3.30	3.24	3.32	3.27
Velocity (GDP/M2)	3.71	4.30	4.58	3.85	4.27	3.77	3.73	3.44	3.58	4.16	3.90	3.61	3.34
Nominal GDP	269	306	326	306	326	306	326	306	326	378	378	378	378
Nominal GDP growth	12.1	16.3	20.9	16.3	20.9	16.3	20.9	16.3	20.9	16.1	16.1	16.1	16.1
Currency outside banks, percent of reserve money	53.4	55.1	51.9	55.5	53.6	56.0	52.9	54.7	53.6	52.5	54.8	55.9	55.9
Currency in banks, percent of reserve money	12.5	7.4	11.3	8.4	10.6	7.8	9.7	11.1	8.9	5.9	3.9	3.1	5.3
Bank reserves, percent of reserve money	34.1	37.6	36.8	36.1	35.8	36.2	37.4	34.2	37.5	41.6	41.3	41.0	38.8

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

[1] Includes disbursements of Fund resources under the ESF and the August 2009 SDR allocation.

[2] As defined in the TMU, this equals the NCG in the monetary survey excluding Moatize deposits, earmarked donor funds, and bonds issued to capitalize the BM.

Table 5. Mozambique: Balance of Payments, 2009−15

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

	2009	2010		2011		2012	2013	2014	2015
	Act.	Prog.	Proj.	EBS/10/98	Projections				
Current account balance	-1,054	-1,391	-1,308	-1,380	-1,258	-1,432	-1,654	-1,857	-2,130
Trade balance for goods	-1,273	-1,500	-1,492	-1,403	-1,170	-1,328	-1,522	-1,715	-1,964
Of which: Megaprojects	474	693	765	1,226	1,113	1,215	1,315	1,429	1,554
Exports, f.o.b.	2,147	2,089	2,328	2,656	2,804	2,991	3,203	3,440	3,706
Of which: Megaproject exports	1,265	1,474	1,648	2,026	2,107	2,283	2,468	2,655	2,831
Imports, f.o.b.	-3,420	-3,589	-3,819	-4,059	-3,974	-4,319	-4,725	-5,156	-5,670
Of which: Megaproject imports	-791	-782	-883	-800	-993	-1,068	-1,153	-1,226	-1,276
Trade balance for services	-450	-451	-452	-495	-493	-558	-664	-738	-802
Income balance	-95	-233	-169	-390	-514	-556	-581	-603	-587
Of which: Dividend payments by megaprojects	-17	-220	-222	-369	-461	-477	-475	-473	-439
Current transfers balance	764	793	805	908	920	1,011	1,112	1,198	1,222
Of which: External grants	687	713	716	824	824	903	990	1,062	1,073
Capital and financial account balance	1,439	1,491	1,151	1,785	1,477	1,859	2,149	2,225	2,412
Capital account balance	422	371	349	391	375	424	482	535	581
Financial account balance	1,016	1,119	802	1,394	1,103	1,435	1,667	1,690	1,831
Net foreign direct investment	878	917	808	732	923	1,016	1,088	1,171	1,252
Net foreign borrowing by the general government	434	583	567	836	861	869	862	773	750
Net foreign borrowing by the nonfinancial private sector	-456	-203	-305	-37	-191	-39	-16	-64	-24
Other [1]	160	-177	-268	-137	-490	-410	-266	-191	-148
Of which: Special drawing rights	170	0	0	0	0	0	0	0	0
Net errors and omissions	-193	0	0	0	0	0	0	0	0
Overall balance	191	100	-157	405	220	427	495	367	282
External financing	-197	-100	157	-405	-220	-427	-495	-367	-282
Reserve assets [1, 2]	-352	-120	136	-403	-218	-424	-492	-334	-222
Net use of Fund credit [2]	152	20	21	-2	-2	-3	-3	-33	-60
Exceptional financing	2	0	0	0	0	0	0	0	0
Memorandum items:									
Effective exchange rate indexes (percent change)									
Nominal effective exchange rate	-4.0	…	…	…					
Real effective exchange rate	-3.2	…	…	…	…	…	…	…	…
Terms of trade index (percent change)	-7.9	1.5	2.5	12.0	13.1	-1.4	0.9	-4.0	-3.0
International aluminum price	-35.3	14.8	24.2	10.5	1.6	6.9	4.4	4.3	0.0
International food price index	-14.7	2.7	6.8	-0.4	-1.3	-2.2	-0.7	-0.8	-0.4
International fuel price index	-36.9	19.9	21.9	7.5	3.1	4.0	2.5	1.3	1.3
Current account balance (percent of GDP)	-10.5	-13.6	-13.4	-12.8	-12.0	-12.0	-12.2	-12.4	-13.1
Excluding external grants	-17.3	-20.6	-20.7	-20.5	-19.8	-19.6	-19.6	-19.4	-19.6
Gross aid inflows (percent of GDP)	15.6	14.8	15.2	14.5	15.0	14.4	13.9	13.4	12.9
Of which: To central government	15.0	13.5	14.2	13.2	13.6	13.3	12.9	12.5	12.1
Budget support	4.9	4.9	5.1	4.6	4.3	4.3	4.3	4.2	4.2
Nonbudge support	10.1	8.6	9.1	8.6	9.3	9.0	8.6	8.3	7.9
Project support	8.6	7.8	8.8	7.8	8.2	8.0	7.6	7.2	6.9
Onlending	1.5	0.9	0.4	0.9	1.1	1.1	1.1	1.1	1.1
Net foreign assets	1,701	1,800	1,544	2,205	1,763	2,190	2,685	3,052	3,335
Net international reserves [1, 2]	1,840	1,930	1,675	2,334	1,895	2,322	2,817	3,185	3,467
Gross international reserves [1, 2]	2,012	2,128	1,868	2,530	2,086	2,510	3,002	3,337	3,559
Months of projected imports of goods and nonfactor services	4.9	4.9	4.4	5.3	4.5	4.9	5.3	5.4	5.3
Months of current imports of goods and nonfactor services	5.4	5.4	4.6	5.8	4.9	5.4	5.8	5.9	5.7

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

[1] Accounts for disbursement of an SDR allocation of SDR 108.8 million in 2009Q3 above the line under other investment liabilities of the monetary authorities, and below the line as an increase in reserve assets.

Table 6. Mozambique: Financial Soundness Indicators for Banking Sector, 2001–10

(Percent unless otherwise indicated)

	2001	2002	2003	2004	2005	2006	2007	2008	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10
Capital adequacy													
Regulatory capital to risk-weighted assets	5.5	14.0	16.5	18.0	13.4	12.5	14.2	13.9	16.6	15.1	14.8	15.2	15.3
Regulatory Tier I capital to risk-weighted assets	6.0	12.0	14.7	16.0	13.6	10.7	12.1	12.4	14.3	13.0	12.2	13.3	13.7
Capital (net worth) to assets	8.2	9.4	7.4	7.4	6.6	6.3	7.2	7.5	8.4	7.7	7.6	8.0	8.0
Asset composition and quality													
Sectoral distribution of loans to total loans (through August 2010)													
Agriculture	18.0	15.0	12.7	9.5	8.5	6.4	9.4	8.1	6.9	7.0	4.1	4.6	4.3
Industry	25.0	22.0	16.9	11.9	16.8	22.2	19.5	16.7	17.7	15.4	23.2	21.0	21.4
Construction	4.0	4.0	5.2	3.4	4.1	5.6	5.7	4.2	4.9	6.4	7.1	7.5	7.5
Commerce	20.0	17.0	18.1	21.3	27.4	27.4	24.4	25.6	19.6	23.4	20.9	21.2	21.4
Transportation and communication	7.0	5.0	7.1	7.2	5.8	6.2	12.2	11.2	13.8	12.2	12.7	12.6	13.1
Other	27.0	36.0	37.1	36.2	35.1	32.3	28.7	34.2	37.1	35.7	37.5	37.7	37.0
of which: Private 1/	…	…	7.6	12.1	13.0	13.5	14.4	19.9	12.5	16.7	17.6	17.7	16.3
Housing	…	…	7.1	8.2	4.2	4.1	3.7	3.7	2.8	2.9	3.0	2.5	8.4
Diverse 2/	…	…	22.4	15.9	17.8	14.7	10.6	10.0	14.8	15.9	16.9	17.5	12.3
Foreign exchange loans to total loans	64.7	69.9	60.8	62.0	51.4	33.2	28.5	32.8	36.2	32.4	33.2	34.4	32.7
Nonperforming loans to gross loans 3/	23.4	22.0	13.8	5.9	3.5	3.1	2.6	1.9	2.0	1.8	2.1	2.1	2.0
Nonperforming loans net of provisions to capital 3/	11.0	9.4	8.8	3.8	1.9	3.6	0.5	2.5	5.8	5.9	5.9	7.9	7.0
Earnings and profitability													
Return on assets	0.1	1.6	1.4	1.5	1.9	4.0	3.8	3.5	3.1	3.0	4.3	3.4	3.0
Return on equity	3.5	22.1	18.6	20.6	26.9	60.8	50.7	44.7	37.0	36.6	53.1	42.7	37.8
Interest margin to gross income	10.2	61.4	62.1	65.8	63.6	67.4	70.2	58.8	57.4	55.7	47.9	53.7	56.7
Noninterest expenses to gross income	16.9	67.0	81.9	81.6	75.2	60.2	60.8	58.7	59.0	58.4	51.1	56.5	57.7
Personnel expenses to noninterest expenses	51.7	44.7	42.4	43.1	43.5	42.6	46.3	45.1	46.4	45.9	45.9	45.8	45.2
Trading and fee income to gross income	33.1	39.7	37.9	34.2	36.4	32.6	29.5	40.5	41.5	44.3	52.1	43.2	39.0
Spread between reference loan and deposit rates (90 days, local curren	14.0	19.0	17.4	14.9	13.8	14.6	11.1	10.7	11.0	11.1	11.7	12.5	…
Funding and liquidity													
Liquid assets to total assets 4/	34.6	53.9	45.2	38.3	31.1	33.9	36.0	36.2	30.3	27.9	25.9	22.5	21.5
Customer deposits to total (non-interbank) loans	217.0	240.0	193.6	205.0	177.6	169.5	184.9	165.7	147.9	138.2	131.5	126.6	127.5
Foreign exchange liabilities to total liabilities	63.3	61.3	30.0	32.3	36.6	32.7	35.6	33.8	35.1	32.4	33.2	34.4	32.7

Source: Bank of Mozambique (BM).

1/ Includes credit cards and consumer credit lines for vehicle and durable goods.
2/ Includes credit to all other sectors not discriminated above or yet to be identified.
3/ Nonperforming loans are defined according to Mozambican accounting standards (they include only part of the past-due loans).
4/ Includes deposits at parent banks.

Table 7. Mozambique: Quantitative Assessment Criteria and Indicative Targets [1]
(Millions of meticais, unless otherwise specified)

	2010									2011	
	End-March Indicative Target			End-June Assessment Criteria			End-Sept Indicative Target	End-Dec Assessment Criteria		End-March Indicative Target	End-June Assessment Criteria
	Prog.	Adj. Prog.	Act.	Prog.	Adj. Prog.	Act.	Prog.	Prog.	Proposed	Proposed	Proposed
Assessment/Performance Criteria for end-June/December											
Net credit to the government (cumulative ceiling)	-124	2,669	2,472	-1,743	-660	-1,287	868	933	1,039	1,097	-2,012
Stock of reserve money (ceiling)	21,031	21,531	22,970	24,567	25,067	25,402	25,753	28,173	29,493	27,368	29,156
Stock of net international reserves of the BM (floor, US$ millions)	1,711	1,611	1,685	1,759	1,714	1,742	1,885	1,930	1,675	1,715	1,765
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 (ceiling, US$ millions) [2]	5	5	0	200	200	0	200	200	300	600	600
Stock of short-term external public debt outstanding (ceiling)	0	0	0	0	0	0	0	0	0	0	0
External payments arrears (ceiling)	0	0	0	0	0	0	0	0	0	0	0
Indicative targets:											
Government revenue (cumulative floor)	10,810	10,810	12,156	27,049	27,049	27,943	41,732	56,474	59,940	14,929	34,311
Priority spending (cumulative floor)	...	...	...	...		...	43,562	58,424	58,424	15,899	34,547

Sources: Mozambican authorities and IMF staff estimates
1 For definition and adjustors see the attached Program Monitoring Section of the Memorandum of Economic and Financial Polices and the Technical Memorandum of Understanding.
2 Should the signature of the Brazilian loans for the Nacala and Beira projects be delayed from 2010 to 2011, the relevant AC ceiling for 2011 will be increased by US$300 million.

Table 8. Mozambique: Structural Benchmarks

Structural Benchmarks	Expected Date of Implementation	Status
Any new contracting of nonconcessional external borrowing or guarantees by the Central Government and selected state-owned entities (SOEs) subject to the related continuous quantitative AC will be for transportation and electricity infrastructure investment, as described in paragraph 14 of the MEFP dated May 24, 2010.	Continuous	Ongoing
Adoption by Council of Ministers of PPP, Concessions and Megaprojects Law, as described in paragraph 22 of the MEFP dated May 24, 2010.	End-September 2010	Met
Finalization of a comprehensive debt strategy that will assess the risk profile and the fiscal and macroeconomic implications of new borrowing, as described in paragraph 16 of the MEFP dated May 24, 2010.	End-November 2010	...
Completion of first Government Debt Sustainability Analysis, as described in paragraph 17 of the MEFP dated May 24, 2010.	End-September 2010	Met
The Minister of Planning and Development will issue a ministerial decree requiring that a project selection protocol and a standard project evaluation template be used by all Government entities in the analysis and selection of public investment projects, as described in paragraph 30 of the MEFP dated November 8, 2010.	End-March 2011	...
An action plan of priority measures will be adopted to simplify the tax system, expand the tax base, and assess the merits and feasibility of possibly reducing the corporate tax rates and of rationalizing incentives under the tax benefits code, as described in paragraph 31 of the MEFP dated November 8, 2010.	End-March 2011	...
The Government will issue two ministerial decrees to create a Debt Management Committee (DMC) and a Project Coordination Committee (PCC), as described in paragraph 30 of the MEFP dated November 8, 2010.	End-March 2011	...
The BM will begin putting in place the recently-completed financial sector contingency plan, by implementing the plan modules on prompt corrective action procedures and coordination with foreign supervisors, as described in paragraph 35 of the MEFP dated November 8, 2010.	End-April 2011	...
Building on the enhancements to e-FOLHA and e-CAF, a first quarterly report will be issued on the civil servant population, wage payments by sector, and the impact of promotion and recruitment decision at all levels, as described in paragraph 22 of the MEFP dated November 8, 2010.	End-July 2011	...

APPENDIX 1—REPUBLIC OF MOZAMBIQUE: LETTER OF INTENT

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

November 8, 2010

Dear Mr. Strauss-Kahn:

The Government of Mozambique requests the completion of first review under the Policy Support Instrument (PSI). In support of this request, we are transmitting the attached Memorandum of Economic and Financial Policies (MEFP), which reviews implementation of our economic program under the PSI and sets out the Government's objectives and policies over the short and medium term.

The Government's economic program aims to maintain macroeconomic stability, promote diversified and strong economic growth, and reduce poverty. The Government intends to finalize its next Poverty Reduction Strategy Paper (PARP) for 2011-14 in early 2011, before the second review of the PSI-supported program.

The Government met all quantitative assessment criteria (AC) through end-June 2010, except for the one on reserve money, which was exceeded by a small margin and for which we request a waiver. We also made strong progress in implementing our structural reform program.

The Government believes 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—at its own initiative or whenever the Managing Director requests such a consultation—should revisions be contemplated regarding the policies contained in the attached MEFP. 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.

Sincerely yours,

/s/	/s/
Manuel Chang	Ernesto Gouveia Gove
Minister of Finance	Governor, Bank of Mozambique

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

ATTACHMENT 1

REPUBLIC OF MOZAMBIQUE: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

I. INTRODUCTION

1. **We firmly reiterate our commitment to the medium-term objectives of our economic program supported under the PSI.** The program aims to preserve macroeconomic stability while supporting the Government's economic development objectives, with a view to creating an environment conducive to private sector activity. To this end, as laid out in the MEFP dated May 24, 2010, we aim to (i) encourage additional national and foreign direct investment in the natural resources sector; (ii) significantly step up our public investment in transport and electricity infrastructure, to be partly financed by nonconcessional external resources; (iii) improve the business climate; and (iv) reap the benefits from regional integration.

2. **The forthcoming drafting of the new five-year PARP will offer an opportunity to step up our pro-poor development agenda.** Conjointly with the private sector, civil society, and development partners, we will assess the scope to redouble our efforts to strengthen inclusive economic growth and improve the plight of the poor.

II. RECENT ECONOMIC DEVELOPMENTS AND PERFORMANCE UNDER THE PROGRAM

3. **Mozambique has been faced with a difficult external environment.** Although the global crisis has not slowed down economic growth, it has impacted Mozambique's balance of payments and required accommodating monetary and fiscal policies. Taken together, these developments have contributed to a depreciating exchange rate and a rise in inflation, which have caused a considerable burden for the most vulnerable segments of the population.

4. **Nonetheless, Mozambique's macroeconomic performance remains strong overall.** Real GDP growth could reach 7¼ percent in 2010, benefiting from strong activity across all sectors. The external current account deficit (after grants) is projected to widen to 13½ percent of GDP in 2010, as the rise in megaprojects exports largely offsets the drop in nontraditional exports, and surge in fuel imports, and rise in global food prices. Private capital inflows have begun to recover, but Mozambican companies continue to offset their traditional reliance on international credit markets with domestic bank financing. Inflation is expected to average close to 13 percent in 2010.

5. **Faced with the rise in inflation, the Bank of Mozambique (BM) has tightened monetary policy since mid-year.** In June and September, it cumulatively raised the key policy rate and reserve requirements by 4 and ¾ percentage points, respectively. It has also stepped up sales of foreign exchange in particular to mop up liquidity and help stabilize the exchange rate.

6. **Fiscal policy implementation has been prudent to date.** Tax collections have been buoyant, as economic activity has remained strong and the Government reaps the gains from our ongoing tax administration reforms. The Government has proceeded very carefully in executing

the 2010 budget. This provided welcome room, since we needed to adjust spending composition during the course of the year. First, in early September, we adopted emergency measures to help shield the poor from rising prices, which is expected to cost MT 0.5 billion (¼ percent of GDP) in 2010. Second, the costs of the fuel subsidy exceeded the budgeted amount by MT 2.9 billion (0.9 percent of GDP), as global fuel prices and fuel demand rose stronger than projected.

7. **The Authorities have persevered in meeting their commitments under the program.** All the quantitative targets for end-June 2010 were met, except the AC for reserve money which was exceeded by a small margin and for which we request a waiver. The new methodology of averaging reserve money helped the BM improve its monitoring of the program target, although the spike in currency toward the end of the month continues to be difficult to predict. With respect to the structural benchmarks, (i) the new PPP, Concessions and Megaprojects Law was adopted by the ministerial Economic and Social Council on September 30, 2010 and the Council of Ministers on October 5, 2010; and (ii) the first Government debt sustainability analysis was completed on September 30, 2010 and, following discussion with Fund staff, will be published on the Government's website by November 15, 2010.

III. Poverty Reduction and Growth Strategy

8. **The Government remains concerned about the extent of poverty.** The recently released *Third National Poverty Assessment*, based on 2008/09 household survey data, indicates that the poverty incidence has remained broadly constant over the last six years, despite Mozambique's impressive growth over the last decade. On the other hand, it also highlights that progress has been good with respect to access to education, health, and other basic social services, thanks to the Government's policies and donor support.

9. **Against this background, the Government has initiated the process of drafting its new Poverty Reduction Strategy (PARP).** As in the past, we intend to pursue a consultative process with the private sector, civil society, and development partners in drafting the document, which is expected to be adopted by the Council of Ministers by end-March 2011. The Government's focus is on making economic growth more inclusive, by broadening economic activity outside the megaprojects sector, thereby generating employment opportunities, raising household livelihoods, and improving food security. This could include the development of sectoral strategies, such as for agriculture and tourism, as well as a redoubling of efforts to improve the business environment. The Government expects that such efforts would complement their current emphasis on rapidly expanding the country's infrastructure in the transportation and energy sectors, which has been a key pillar of its economic program supported under the PSI.

10. **The Government aims at building sustainable social safety nets to help reduce poverty while stimulating the local economy.** We will assess the emergency measures adopted in early September by year-end in order to determine the scope to replace them with more permanent and possibly better targeted measures over time. Through the implementation of our multi-sectoral *National Basic Social Security Strategy* (ENSSB), approved by the Council of Ministers in April 2010, and the *Strategic Program for the Reduction of Urban Poverty* (PERPU), the Government will gradually expand support to the most vulnerable. Drawing on the

experience of other countries, we place emphasis on creating productive safety nets that aim at providing cash and other support in the short run while strengthening Mozambique's long-term growth potential. We have begun discussing possible options with the World Bank, UNICEF, and other development partners to secure their technical and financial support. The Government intends to create adequate fiscal space in the medium-term fiscal framework (CFMP) to support the implementation of such safety nets.

IV. Macroeconomic Policies

A. Economic Objectives

11. **The Government sees a favorable economic outlook for Mozambique.** Economic growth could reach 7½ percent in 2011 and accelerate to 8 percent over the medium term. Following a concerted effort by the Authorities, average inflation is expected to decelerate to 8 percent in 2011 and approximate our medium-term objective of 6 percent from 2012 onward. The external current account deficit (after grants) should hover at around 12½ percent of GDP over time, reflecting a continued recovery in export receipts that more than compensates the large import demand related to the country's strong public and private investment needs. Strengthening private capital inflows, continued donor support, and Government external borrowing for infrastructure investment should keep Mozambique's international reserves at a comfortable level, at about 5 months of imports over the medium term.

B. Macroeconomic Policy Mix

12. **We reiterate our commitment to preserving macroeconomic stability.** The Government and BM recognize that macroeconomic stability is one of Mozambique's strongest assets and instrumental in creating a predictable framework for private sector activity.

13. **In the short run, the Government and BM will give priority to reigning in inflation.** To this end, in 2011, we will unwind the monetary and fiscal stimulus adopted in the wake of the global crisis. The BM will rebalance the extent of liquidity in the economy, as the impact of the global crisis on Mozambique tapers off. In order to contribute to a lowering of demand pressures, the Government will temporarily pursue a tighter fiscal policy stance, thus limiting its recourse to domestic financing and helping avoid a crowding out of the private sector. We expect that the macroeconomic policy mix will return to normalcy during the course of 2011.

14. **Over the medium term, we will follow a policy stance that preserves macroeconomic stability and debt sustainability while supporting economic development.** Our objective is to keep the domestic primary fiscal deficit at around 4 percent of GDP over the medium term and limit the Government's domestic financing requirement through a determined revenue effort and the prioritization of domestic spending. This, coupled with a prudent monetary policy stance, should ward off demand pressures and support achievement of our inflation objective. At the same time, we intend to step up our capital spending to boost infrastructure investment, to be partially financed by nonconcessional external borrowing (NCB). The Government will pace the

implementation of public investment in a way that is consistent with macroeconomic and capacity constraints so as to avoid the emergence of domestic demand pressures.

C. Monetary and Exchange Rate Policies

15. **The BM is determined to bring inflation back to single digits in 2011 and reiterates its medium-term objective of 6 percent.** In light of the current surge in headline inflation, it will use its full set of monetary policy instruments to decelerate money growth. This will result in a significant slowdown in reserve money growth relative to nominal GDP growth during the remainder of 2010 and in 2011. The BM will use open market operations to swiftly mop up liquidity, mainly through foreign exchange interventions and t-bill sales. It will continue to signal its determination to markets through adjustments in its key policy rates and reserve requirements, if needed.

16. **In its monetary policy implementation, the BM will continue to pay close attention to the real effective exchange rate vis-à-vis a broad basket of currencies.** The BM reiterates its adherence to the general principle that the exchange rate should adjust freely to evolving patterns of trade and financial flows while safeguarding Mozambique's international reserves.

17. **The BM intends to strengthen its monetary policy operations framework, in line with Fund technical assistance recommendations.** All those enhancements are part of the BM's efforts to move to an inflation targeting framework in the long run, as specified in the relevant action plan. Specifically, the BM will take the following steps in this direction:

- With a view to strengthening repo operations, eliminating distortions in the pricing of Government securities, and facilitating the build-up of a yield curve, the BM will issue, by end-January 2012, regulations and institute procedural changes that would (i) make t-bills fungible in the MMI (*Meticalnet Interbank Money Market*); and (ii) allow all Government securities to be used as collateral for monetary policy operations.

- In order to improve liquidity forecasting and the predictability of budget execution through the treasury single account (CUT), by end-March 2011 the Ministry of Finance and the BM will sign a Memorandum of Understanding stipulating (i) the phased–in provision to the BM of timely information on all Government actual and projected expenditures and receipts; (ii) the regular exchange of information on the government's cash flow forecast, liquidity projections, and foreign exchange flows; and (iii) the timely provision of reliable data by the BM on government financial transaction through the CUT.

18. **We intend to notify the Fund of our acceptance of the obligations under Article VIII sections 2, 3, and 4 of the Fund's Articles of Agreement by end-December 2010.** In our view, the new foreign exchange regulations, which we expect to be adopted during December 2010, will remove all existing and potential exchange restrictions, consistent with the recommendations of the recent Fund technical assistance mission. Apart from the regulatory aspects, the BM is committed to continue monitoring the functioning of the foreign exchange market, with a view to avoiding practices that could turn out to be inconsistent with Article VIII principles.

D. Fiscal Policy

Fiscal policy stance

19. **The Government will follow a fiscal policy stance consistent with the monetary tightening to avoid a crowding out of the private sector:**

- For 2010, it will limit the domestic primary fiscal deficit to 4.1 percent of GDP, which should contain the banking system's net credit to the Government (NCG) at 0.3 percent of GDP. Achieving these targets requires a substantial dedication to enhance tax collections and reduce non-priority spending. This is in light of the larger-than-expected outlays for the fuel subsidy and the emergency measures to restore social peace. Consequently, while the wage bill will be at budgeted levels, the Government is prepared to forego executing domestically-financed capital spending and current spending during the remainder of 2010 should this become necessary to achieve the NCG target.

- Fiscal policy will step up its contribution to containing inflation in 2011. We will reduce the domestic primary fiscal deficit by 0.9 percentage points, to 3.3 percent of GDP, resulting in a virtually zero recourse to domestic financing. The program's indicative revenue floor is prudently set ½ percent of GDP below the ambitious objectives of the 2011 budget law, but the Revenue Authority will be instructed to collect the full revenue target under the budget law (19½ percent of GDP).

20. **The implementation of the 2011 budget law will be subject to the revenue contingency under the organic budget law (SISTAFE 2002).** This legal framework limits budget execution to cautionary ceilings as long as revenue collections remain uncertain. To this end, and in accordance with the legal provisions of the 2011 budget law, the Government will take the following steps by end-January 2011: (i) the Council of Ministers will approve the decree on the provisions regarding budget execution (*Delegacao de Competencia sobre a Excecucao do Orcamento*); and (ii) the Minister of Finance will issue an interministerial regulation (*Circular Ministerial*) providing guidance for line ministries for budget execution and contingencies. Accordingly, the following contingency ceilings will apply: (i) 90 percent for goods and services and other current expenditures; (ii) 85 percent for civil service wages and transfers; and (iii) 90 percent for domestically-financed capital spending.

Priority spending

21. **The tight fiscal policy stance will not affect allocations for priority sectors.** The Government will protect priority spending, as defined by PARP, and meet the program's indicative floor on such spending for 2010 (MT 58.4 billion). The relevant target for 2011 is MT 63.0 billion; however, the Government expects that priority spending will be redefined under the new PARP, in consultation with development partners and civil society, requiring a likely revisiting of the 2011 spending floor at the time of the second PSI review.

Wage policy

22. **The Government aims to strike the proper balance between modernizing the civil service and keeping the wage bill in line with macroeconomic needs.** While furthering ongoing reforms, we will aim to stabilize the wage bill, after two years of rapid increases.

- The new salary policy, adopted in 2008, aims to (i) simplify and rationalize the salary scales across ministries, (ii) decompress the scales consistent with qualifications and responsibility, (iii) reform the system of housing and other allowances, and (iv) harmonize the salary policy with the pension system. By end-March 2011, the Government will review the implementation strategy of the new salary policy, with a particular focus on its budgetary implications. The future implementation of the new salary policy will be gradual, consistent with macroeconomic circumstances.

- To enhance the real-time control over the wage bill, we will expand the electronic payroll reporting system (e-FOLHA) and have all salaries paid at the level of central Government institutions reported through e-FOLHA by end-June 2011. We will also roll out e-FOLHA to at least three Directorates in each province by end-December 2011. In parallel, we will strengthen the mechanism for updating the civil servant master database record (e-CAF) at the central, provincial, and district level. The enhancements to e-FOLHA and e-CAF will allow the generation of quarterly reports on the civil servant population, wage payments by sector, and the impact of promotion and recruitment decision at all levels. After a testing phase, the first such report will be issued by end-July 2011 (**structural benchmark**).

- Given the current inflationary pressures, the Government issued circular 05/2010 dated September 9, that, inter-alia, restricts promotions for this year in order to stay within the ceiling on the wage bill in the annual budget law.

- These efforts notwithstanding, we will continue our recruitment program for priority sectors, hiring 13,000 staff in 2011, of which 73 percent are for health and education.

Fuel subsidy

23. **The Government is committed to a full pass-through of fuel prices.** To limit fiscal risks, lessen the country's import bill, and safeguard international reserves, the Government will regularly review the price structure of fuel products. It will consider various options to limit the costs coming from the remaining discrepancies between import and retail prices for diesel. This could include a cross-subsidization between various fuel categories, but also limiting the current adjustment factor in the monthly fuel price formula to retail prices at the pump, thus charging market prices to wholesale customers. The Government will consider the implications of its fuel price policy on the most vulnerable segments of the population and introduce other support measures, as deemed appropriate. To ensure transparency, the Government will explicitly show the full costs of any Government outlays for fuel products in budget documents.

Public investment in infrastructure

24. **The Government attaches great importance to expanding Mozambique's infrastructure in the energy and transportation sectors.** This is motivated by our desire to strengthen the country's productive base and provide a catalytic effect for private sector activity. In this undertaking, the Government will give priority to safeguarding the significant support from development partners whose concessional resources have helped Mozambique preserve very comfortable debt indicators. Nonetheless, the extent of the infrastructure gap requires the Government to also consider NCB for selected projects that promise a high economic return.

25. **The Government's economic program supported under the PSI envisages an overall NCB envelope of US$900 million for the period 2010-13.** This amount has been deemed compatible with the Government's efforts to preserve macroeconomic stability and debt sustainability.

- The continuous AC on NCB for 2010 will be raised to US$300 million at the time of the first PSI review to allow the Government to contract two loans from Brazil for the construction of Nacala airport (US$80 million) and rehabilitation of the port of Beira (US$220 million).

- The AC on NCB for 2011 will be set at the full remaining amount of US$ 600 million under the program envelope in order to facilitate the government's negotiations with potential creditors. Should the signature of the Brazilian loans for the Nacala and Beira projects be delayed from 2010 to 2011, the relevant AC for 2011 will be increased by the 2010 shortfall.

26. **The NCB subject to the related AC will be channeled to growth-enhancing sectors.** It will only be applied to infrastructure investment in energy and transportation (**continuous structural benchmark**). For any NCB-financed projects, the Government will share project feasibility studies—including those from co-financing donors—with Bank and Fund staff.

27. **Among the projects under evaluation by the Government, the following specific projects enjoy the highest priority at present:**

- An expansion of electricity production at the Cahora-Bassa dam in central Mozambique, which should enhance the reliability of the supply of electricity;

- The construction of a power line between the Cahora-Bassa dam and Maputo, which would reduce the dependency on electricity re-imports;

- An expansion of the road network, as currently only about one-third of Mozambique's road infrastructure is asphalted. Possible priority projects could include transit corridors from key economic centers to the borders with neighboring countries, such as the 287 km road connecting the port city of Beira to Machipanda at the border with Zimbabwe or the 131 km road between the capital city Maputo and the Ponta d'Ouro border post with South Africa.

28. **The Government recognizes that the acceleration of the public investment program would need to be consistent with Mozambique's macroeconomic circumstances.** Therefore, the Government commits to carefully monitoring the execution of the public investment program of the central Government, SOEs, agencies, and funds, by making full use of the institutional and budgetary safeguards existing in the current legal framework, and to promptly adapting budget implementation in case of emerging demand pressures. The following safeguards will be applied:

- For entities receiving NCB from the budget, the Minister of Finance will issue a ministerial decree (*Diploma Ministerial*) directing that they submit timely reports of all their financial transactions to the Treasury, via e-SISTAFE or through an agreed data reporting template, as precondition for disbursements. Project execution will be based on the provisions of Decree 23/2004 approved by the Council of Ministers. It requires the Treasury to elaborate a rolling quarterly cash plan to control and eventually slow down spending consistent with available resources. It also provides the legal basis to phase spending in response to macroeconomic conditions.

- For those SOEs, agencies, and funds receiving nonconcessional resources directly from the lender, the relevant contract will be negotiated such that project implementation will be in several phases, providing the Minister of Finance with the authority to slow down initiation of the next project phase should this be warranted by macroeconomic circumstances. Those entities will submit timely quarterly reports on project execution to the Treasury through an agreed data template.

- The annual and quarterly budget execution reports will provide a full account of the state of implementation of those projects.

V. Fiscal Structural Reforms

Public financial management

29. **The Government's focus will be on continuing the rollout of automated systems to facilitate budget execution, and on monitoring and strengthening control of spending execution outside the central Government perimeter:**

- We will further extend the e-SISTAFE budget execution system to cover 45 percent of total spending by end-December 2011, following a projected 37.5 percent for 2010. In the same vein, we will strengthen the direct reporting from e-SISTAFE into the annual budget report (Conta Geral do Estado), which should improve timeliness and reliability of data and accelerate the budget drafting process.

- We will improve the integration of the audit functions into e-SISTAFE. The Court of Auditors (*Tribunal Administrativo*) will issue, by end-December 2010, a decree that external audits can henceforth be based on paper documentation and electronic e-SISTAFE reports, wherever the system is used.

- Finally, by end-April 2011, the *Inspectorate General of Finance* will define specific audit targets for the operations of SOEs, agencies, and funds, and issue an internal regulation guiding the work of the auditors in this area.

Debt management and investment planning

30. Debt management and investment planning will be strengthened to ensure that our borrowing and investment decisions provide us with the highest value for money:

- The PPP unit in the Ministry of Finance, intended to serve as a gateway for the PPP pipeline approval process, will be created by end-January 2011 and made fully operational by end-April 2011, with sufficient staffing and resources to implement its work program.

- Following the expected completion of our medium-term borrowing strategy at end-November 2010, we will begin to operationalize the strategy through detailed annual borrowing plans. Such plans will cover domestic and external financing, take into account the likely timing of Government cash flow during the year, and reflect our efforts to develop domestic financial markets and establish a yield curve. Considering the near-zero NCG for 2011 and the need for domestic market development, a first annual borrowing plan will be developed by end-October 2011 for 2012, consistent with the draft 2012 budget law.

- To enhance debt management and project selection, the Government will, by end-March 2011 (i) issue a ministerial decree (*Diploma Ministerial*) to create a *Debt Management Committee (DMC*) as an advisory body to facilitate a systematic and regular coordination of debt management activities and related policies; and (ii) issue a ministerial decree (*Diploma Ministerial*) to create a *Project Coordination Committee* (PCC) to advise the Government on the prioritization and selection of projects. Both committees will comprise representatives of the Ministries of Finance and of Planning and Development, the National Statistical Institute (INE), and the BM. The decrees will specify that the opinions of the DMC and PCC will be an integral part of the Government's process of making investment and financing decisions (structural benchmark).

- With the same objective, the Minister of Planning and Development will issue, by end-March 2011, a ministerial decree (*Diploma Ministerial*) requiring that a project selection protocol and a standard project evaluation template be used by all Government entities in the analysis and selection of public investment projects. Among other things, the decree will establish the roles and responsibilities of individual ministries in project planning and implementation, and set minimum standards for feasibility studies, cost-and-benefit analyses, and financing options. It will also clarify that adherence to the protocol requirements will be a prerequisite for the consideration of an investment project by the Government (structural benchmark).

Tax policy and administration

31. **We will underpin our revenue efforts with continued reforms in tax policy and administration:**

- With a view to expanding the tax base and improving the business climate, we will adopt by end-March 2011, an action plan of priority measures to continue to simplify the tax system, expand the tax base, and assess the merits and feasibility of possibly reducing corporate tax rates and of rationalizing incentives under the tax benefits code (**structural benchmark**).

- With a view to offsetting the revenue losses from the elimination of SADC customs duties, the Government will strengthen the efficiency of the customs administration. To this end, it will (i) launch the single-window customs management system by March 2011 to streamline customs procedures; (ii) complete the rollout of the single-window system in all main ports and airports by end-2011; (iii) make fully operational, by end-June 2011, a mandatory seals system for alcoholic beverages to ensure that excise duties are duly paid.

- The Revenue Authority will, by end-January 2011, adopt an action plan to expand coverage of the large taxpayers unit. The plan will aim to raise the share of collections from the current 50 percent to 70 percent of revenues in the long run.

EITI Membership

32. **We are committed to become a compliant member of the EITI by end-May 2011.** The EITI Coordination Committee, consisting of representatives from the private sector, civil society, and the Government, has adopted a work program to achieve full EITI membership by that date. With the support of development partners, an EITI secretariat was created to implement the planned activities, such as public awareness campaigns, as well as the selection of an independent auditor and an EITI validator. It is expected that the audit report will be finalized by end-December 2010, reconciling Government tax receipts with tax payments from selected extractive companies. A validator, accredited by the international EITI secretariat in Oslo, is expected to complete the review of the audit report and of the EITI adherence process and submit its report for acceptance by the international EITI secretariat by end-April 2011.

Reform of the National Social Security Institute (INSS)

33. **The Government is committed to strengthening INSS to ensure its financial viability.** The INSS investment strategy will be completed by end-March 2011, stipulating that investment decisions will solely aim at protecting the interests of INSS beneficiaries. The audited and validated 2008 accounts will be approved by the INSS Board and published by end-December 2010, and those for 2009 by end-June 2011. With ILO assistance, we will complete an actuarial study, based on the audited accounts of 2004-08, by end-March 2011; the study will suggest specific measures needed to ensure the financial sustainability of the INSS. Finally, we plan to complete the reform of the INSS organizational structure and IT system in 2011.

VI. Financial Sector Policies

34. **The financial sector has played a key role in Mozambique's economic development, which is likely to continue.** It has also been able to provide additional financing when global credit markets became less accessible for local companies in the wake of the global crisis. Despite the progress made, there is a significant need to further promote financial intermediation and access to finance and credit while safeguarding the soundness of the banking system. To this end, we are in the process of finalizing a financial sector development strategy that will be validated in a workshop in early December 2010 and based on the findings and recommendations of the 2009 FSAP update, as well as the results of implementation of the Financial Sector Technical Assistance Project (FSTAP) program and other donor programs. In light of the rapid rise in private sector credit and the envisaged tightening of liquidity, the BM will closely supervise the banking system and monitor overall credit risk.

35. **The Government and BM will pursue the following key financial sector reforms:**

- We intend to open a dialogue with the financial sector, the private sector, and civil society on developing a financial services charter aimed at improving access to finance and credit. This will include discussion of measures to broaden financial sector products, enhance their marketing and distribution channels, strengthen competition, establish a consumer protection program, and improve financial literacy.

- We will speedily embark on putting in place the recently-completed financial sector contingency plan, which was developed with FSTAP support. To this end, by end-April 2011, we will implement the plan modules on prompt corrective action procedures and coordination with foreign supervisors (**structural benchmark**). All other plan modules will be implemented by end-December 2011. A Financial Stability Committee, comprising the Minister of Finance and BM Governor, will meet as needed to assess financial sector stability issues.

- The BM recently adopted a roadmap for implementing Basel II in its banking supervision and regulation framework, aiming to conclude the migration by early 2014. The emphasis in 2011 will be on providing training to BM staff, for which we will seek technical assistance.

- We have submitted to parliament the draft amendment to the 2002 AML law that will make it compliant with the recommendations of the Financial Action Task Force (FATF) and remove incompatibilities between the law establishing the financial intelligence unit (GIFIM) and the AML law. GIFIM has started recruitment and capacity building, supported by development partners, and should be fully operational by end-June 2011.

VII. Program Monitoring

36. The modified quantitative AC and indicative targets for end-December 2010, the indicative targets for end-March 2011, and the AC and indicative targets for end-June 2011 are shown in Table 1. Table 2 lists the structural benchmarks for the first half of 2011. The second PSI review is expected to be completed by end-June 2011 and the third PSI review by end- 2011.

MEFP Table 1. Mozambique: Quantitative Assessment Criteria and Indicative Targets [1]
(Millions of meticais, unless otherwise specified)

	2010									2011	
	End-March Indicative Target			End-June Assessment Criteria			End-Sept Indicative Target	End-Dec Assessment Criteria		End-March Indicative Target	End-June Assessment Criteria
	Prog.	Adj. Prog.	Act.	Prog.	Adj. Prog.	Act.	Prog.	Prog.	Proposed	Proposed	Proposed
Assessment/Performance Criteria for end-June/December											
Net credit to the government (cumulative ceiling)	-124	2,669	2,472	-1,743	-660	-1,287	868	933	1,039	1,097	-2,012
Stock of reserve money (ceiling)	21,031	21,531	22,970	24,567	25,067	25,402	25,753	28,173	29,493	27,368	29,156
Stock of net international reserves of the BM (floor, US$ millions)	1,711	1,611	1,685	1,759	1,714	1,742	1,885	1,930	1,675	1,715	1,765
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 (ceiling, US$ millions) [2]	5	5	0	200	200	0	200	200	300	600	600
Stock of short-term external public debt outstanding (ceiling)	0	0	0	0	0	0	0	0	0	0	0
External payments arrears (ceiling)	0	0	0	0	0	0	0	0	0	0	0
Indicative targets:											
Government revenue (cumulative floor)	10,810	10,810	12,156	27,049	27,049	27,943	41,732	56,474	59,940	14,929	34,311
Priority spending (cumulative floor)	…	…	…	…		…	43,562	58,424	58,424	15,899	34,547

Sources: Mozambican authorities and IMF staff estimates
1 For definition and adjustors see the attached Program Monitoring Section of the Memorandum of Economic and Financial Polices and the Technical Memorandum of Understanding.
2 Should the signature of the Brazilian loans for the Nacala and Beira projects be delayed from 2010 to 2011, the relevant AC ceiling for 2011 will be increased by US$300 million.

Table 2. Mozambique: Structural Benchmarks Under the PSI

Any new contracting of nonconcessional external borrowing or guarantees by the Central Government and selected state-owned entities (SOEs) subject to the related continuous quantitative AC (see Table 1) will be for transportation and infrastructure investment, as described in paragraphs 25 and 26.	Continuous
Building on the enhancements to e-FOLHA and e-CAF, a first quarterly report will be issued on the civil servant population, wage payments by sector, and the impact of promotion and recruitment decision at all levels, as described in paragraph 22.	End-July 2011
The Minister of Planning and Development will issue a ministerial decree requiring that a project selection protocol and a standard project evaluation template be used by all Government entities in the analysis and selection of public investment projects, as described in paragraph 30.	End-March 2011
An action plan of priority measures will be adopted to simplify the tax system, expand the tax base, and assess the merits and feasibility of possibly reducing the corporate tax rates and of rationalizing incentives under the tax benefits code, as described in paragraph 31.	End-March 2011
The Government will issue two ministerial decrees to create a Debt Management Committee (DMC) and a Project Coordination Committee (PCC), as described in paragraph 30.	End-March 2011
The BM will begin putting in place the recently-completed financial sector contingency plan, by implementing the plan modules on prompt corrective action procedures and coordination with foreign supervisors, as described in paragraph 35.	End-April 2011

ATTACHMENT 2

REPUBLIC OF MOZAMBIQUE: TECHNICAL MEMORANDUM OF UNDERSTANDING

November 8, 2010

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.

I. DEFINITIONS

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 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, and the administration of 11 provinces. Although local governments (43 municipalities or *autarquias*) are not included in the definition because they are independent, the bulk of their revenue is registered in the state budget as transfers to local governments.

Government revenue and financing

4. 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. 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).

5. 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.

Priority social spending

6. Priority social spending is based on the PARPA program categories. 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; and (vii) governance and judicial system.

Reserve money

7. 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.

Net international reserves

8. 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.

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

9. 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), and the electricity company (EDM). It also applies to debt contracted by these three state-owned enterprises from domestic banks or from other state-owned enterprises that is contractually inter-related to external nonconcessional loans.

10. 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. 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. The ceiling also applies to commitments contracted or guaranteed for which value has not been received. This assessment criterion will be assessed on a continuous basis.

Stock of short-term external public debt outstanding

11. The central government will not contract or guarantee external debt with original maturity of less than one year. This assessment criterion applies not only 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, but also to commitments contracted or guaranteed for which value has not been received. Excluded from this assessment criterion are short-term, import-related trade credits. This assessment criterion will be assessed on a continuous basis.

External payments arrears

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

Foreign program assistance

13. 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).

Actual external debt service payments

14. Actual external debt service payments are defined as cash payments on external debt service obligations of the 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).

II. Adjusters

Net international reserves

15. 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.

Net credit to central government

16. 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.

Reserve money

17. The quantitative target (ceiling) for reserve money will be adjusted upward by the excess of the stock of currency in circulation above the level envisaged in the program. For programming purposes, both the stocks of reserve money and currency in circulation are defined in terms of the average of the daily end-of-day stocks in the month of the test date. The target will be adjusted up to MT 500 million for end-March, end-June, and end-September and up to MT 750 million for end-December (Table 1).

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

18. Should the signature of the Brazilian loans for the Nacala and Beira projects (US$80 and 220 million, respectively) be delayed from 2010 to 2011, the relevant AC ceiling for 2011 will be increased by the relevant shortfall.

III. Data and Other Reporting

19. 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 information on the balance of government savings accounts abroad;
- monthly data on domestic arrears;
- monthly budget execution reports (that will also be published) with a time lag not exceeding 45 days;
- monthly monetary survey data with a time lag not exceeding 30 days; and
- monthly data on gross international reserves, with the composition by original currencies and converted to US dollars at the actual exchange rates.

19. 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.

20. 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, 2010-11

	2010										2011	
	Q1		Q2		Q3		Q4		Year		Q1	Q2
	Prog.	Act.	Prog.	Act.	Prog.	Proj.	Prog.	Proj.	Prog.	Proj.	Proj.	Proj.
Net foreign program assistance (US$ mn)	163	57	181	151	27	74	145	115	424	396	129	106
Gross foreign program assistance	182	74	203	168	42	92	165	132	496	467	144	121
Program grants	151	74	176	139	42	92	55	50	359	355	144	89
Program loans	30	0	27	30	0	0	110	82	137	112	0	32
External debt service	18	18	22	18	15	18	20	18	71	71	15	15
Net foreign program assistance (MT mn)	4,843	1,706	5,378	4,581	829	2,673	4,582	3,975	12,781	12,935	4,732	3,838
Gross foreign program assistance	5,220	2,076	6,021	5,673	1,278	3,287	5,218	4,738	14,923	15,775	5,253	4,375
Program grants	4,344	2,076	5,229	4,659	1,278	3,287	1,741	1,798	10,655	11,821	5,253	3,229
Program loans	876	0	792	1,014	0	0	3,476	2,940	4,268	3,954	0	1,147
External debt service	376	370	643	1,092	449	614	636	763	2,142	2,840	521	537
Stock of outstanding currency (MTm)	13,278	14,515	16,445	16,721	16,436	18,372	19,222	19,134	19,222	19,134	16,098	17,556
Stock of outstanding currency (MTm), Prog. D	13,278	14,317	15,324	16,080	16,052	17,874	18,702	18,616	18,702	18,616	15,878	16,883

Source: Mozambican authorities and IMF staff estimates

INTERNATIONAL MONETARY FUND

REPUBLIC OF MOZAMBIQUE

First Review Under the Policy Support Instrument and Request for Modification of Assessment Criteria—Informational Annex

Prepared by the African Department
(In consultation with other departments)

November 16, 2010

- Relations with the Fund
- World Bank-IMF Joint Management Action Plan
- Statistical Issues

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APPENDIX I. MOZAMBIQUE: RELATIONS WITH THE FUND

(as of September 30, 2010)

I. Membership Status: Joined: September 24, 1984; Article XIV

II. General Resources Account:	SDR Million	% Quota
Quota	113.60	100.00
Fund holdings of currency	113.60	100.00
Reserve Position	0.01	0.01

III. SDR Department:	SDR Million	% Allocation
Net cumulative allocation	108.84	100.00
Holdings	108.48	99.67

IV. Outstanding Purchases and Loans:	SDR Million	% Quota
ESF Arrangements	113.60	100.00
ECF Arrangements	9.58	8.43

V. 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 [1]	Jun 28, 1999	Jun 28, 2003	87.20	78.80

[1] Formerly PRGF.

VI. Projected Payments to Fund[2]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2010	2011	2012	2013	2014
Principal		0.97	1.46	1.95	1.95
Charges/Interest	0.01	0.00	0.31	0.30	0.30
Total	0.00	0.97	1.76	2.25	2.24

[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.

VII. Implementation of HIPC Initiative:

I. Commitment of HIPC assistance	Original Framework	Enhanced Framework	Total
Decision point date	Apr 1998	Apr 2000	
Assistance committed			
by all creditors (US$ Million) [1]	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 [2]	--	1.10	1.10
Total disbursements	93.17	14.83	108.00

[1] 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 can not be added.

[2] 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.

VIII. Implementation of Multilateral Debt Relief Initiative (MDRI):

I. MDRI-eligible debt (SDR Million)[1]	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

[1] 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.

Safeguards assessment

An update safeguards assessment of the Bank of Mozambique's (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 BM legal structure. It recommended that the BM commission an external quality assurance review of the internal audit function. Staff will follow-up on progress in implementing the assessment's recommendations.

Exchange arrangements

Mozambique has a floating exchange system. Commercial banks may buy and sell foreign exchange to individual customers on a fully negotiable basis. The Bank of Mozambique introduced a foreign exchange auction system in January 2005. Foreign exchange transactions are conducted mainly bilaterally and there is no pre-established frequency for auctions.

Mozambique still avails itself of the transitional arrangements under Article XIV of the Fund Articles of Agreement, but has eliminated all Article XIV restrictions. It maintains, however, restrictions on the making of payments and transfers for current international transactions subject to Fund approval under Article VIII, as evidenced by: (i) the discretionary prior approval for remittances of family living expenses; (ii) the authorization for the purchase of foreign exchange in excess of US$5,000 for certain transactions; (iii) the prohibition for the conversion of balances of nonresidents' domestic currency accounts into foreign currency or transfer abroad; (iv) the prohibition on advance payments for a service; and (v) the prohibition on advance payments for the import of goods. At the authorities' request, an Article VIII mission was conducted by LEG and PDR in March 2004. A new foreign exchange law was submitted to the Assembly in May 2007 and came into effect on March 11, 2009. The jurisdictional review of the foreign exchange system, including the draft implementation regulations, by Fund staff is ongoing, which will provide clarity on whether all restrictions have been eliminated. The authorities intend to accept their obligations under Article VIII sections 2, 3, and 4 of the Fund's Articles of Agreement by end-2010.

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 a PSI in June 2007. The 2009 Article IV consultation was completed by the Executive Board on June 30, 2009 (Country Report No. 09/227).

In concluding the 2009 Article IV consultation, Executive Directors welcomed Mozambique's continued strong macroeconomic performance in 2008 despite a challenging external environment. They commended the authorities' flexible policy response to higher

fuel and food import prices, which helped to mitigate the impact of these shocks. Directors noted that Mozambique remains vulnerable to the global economic slowdown and agreed that the country's strong track record of prudent macroeconomic policy implementation has provided room to ease fiscal and monetary policy in the near term. In the medium term, Directors underscored the importance of preserving macroeconomic stability and supported efforts to enhance domestic revenue mobilization and to improve public financial management. They welcomed the authorities' intention to limit recourse to domestic financing of the budget so as to preserve sufficient room for private sector credit growth. With respect to the overvaluation of the exchange rate in real effective terms, Directors suggested paying closer attention to a basket of currencies, which could help support Mozambique's competitiveness and economic diversification. Further progress in structural reforms and in developing and safeguarding the soundness of the banking system were seen as instrumental in supporting the business environment.

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. The Managing Director visited Mozambique on August 2007 for a meeting with the African Consultative Group on Quotas, Voice, and Representation.

Resident representative

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

IMF Technical Assistance Provided to Mozambique (2006–10)				
Departments	Timing	Form	Purpose	Counterparts
Finance	February 2008	Mission	Update of Safeguard Assessment	Bank of Mozambique
Fiscal Affairs	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
	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
Monetary and Capital Markets	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	Mission	Strengthening Monetary Policy Formulation and Implementation	Bank of Mozambique
	November 2009	Mission	Strengthening Monetary Policy Formulation and Implementation	Bank of Mozambique
	May 2009	Mission	2009 FSAP Follow up	Bank of Mozambique

IMF Technical Assistance Provided to Mozambique (2006–10)				
Departments	Timing	Form	Purpose	Counterparts
	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
	Jan–Feb 2006	Short-term consultant	Monetary Operations	Bank of Mozambique
	January 2006	Short-term consultant	Exchange Rate Management	Bank of Mozambique
Statistics	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

APPENDIX II. WORLD BANK-IMF JOINT MANAGEMENT ACTION PLAN

Title	Products	Timing of Missions	Expected delivery date
1. Bank Work program	Updated poverty analysis using the 2008/09 household survey (in collaboration with DNEAP).	Work carried out through 2008-10	October 2010
	PRSC-7 Board presentation	November 2010	December 2010
	FSTAP project support to financial sector reforms	Ongoing	Ongoing
	Updates on advancing structural reforms: procurement, decentralization, business environment, financial sector	Ongoing	June 2010 to June 2011
	Establishing a collection of relevant papers in the field of "Growth and Fiscal Space" in light of the Namaacha 2 Workshop (see below)	December 2010	February 2011
	Recommendations on targeted, sustainable safety net measures (including conditional cash transfer system)	Ongoing	December 2012
2. Fund Work program	First PSI Review	October 2010	December 2010
	Second PSI Review and 2011 Article IV	March 2011	June 2011
	Updated macro framework data and PSI review staff report	PSI reviews	June 2010 - June 2011
	TA mission on debt management and debt strategy	June 2010	Jul-10
	TA mission on PFM and government accounting systems	November 2010	December 2010
	Assessment Letter for the WB on Mozambique's Economic and Financial Policies	End of October 2010	End of October 2010
	Short-term TA mission on revenue administration (Seminar on Planning and Management Indicators)	November 2010	December 2010
	TA follow-up mission on building capacity to define and implement a debt strategy	November 2010	January 2011
	TA mission on PFM and government accounting systems	February 2011	March 2011
	TA follow-up mission on revenue administration	April 2011	June 2011
	TA follow-up mission on PFM	April 2011	June 2011
	TA on banking supervision and regulation	May 2011	June 2011
	TA on monetary policy formulation within an inflation targetting framework (tentative)	June 2011	July 2011
3. Joint Work	Conference on Mozambique's growth challenges (Namaacha 2)	December 2010	December 2010
	Medium Term Debt Strategy	June 2010	November 2010
	PFM: update of work plan for 2009-11 in light of findings from PEFA and ROSC	March 2011	March 2011
	PFM: continue to monitor consolidation and expansion of e-SISTAFE.	Ongoing	Ongoing
	Policy advice on public sector aalary reforms (incl. pensions)	Ongoing	Ongoing
	Review of tax policy	TBD	TBD
	JSAN on the authorities' new Poverty Reductionfor 2011-14	March 2011	June 2011

APPENDIX III. MOZAMBIQUE: 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 2002–03 household survey was released in February 2006. A national index obtained by integrating the indices for Maputo, Beira, and Nampula was released in April 2006. Several issues remain outstanding, however, to correct probable downward bias caused by carry forward techniques for discontinued products, improve the housing market rent sample, and expand coverage to include 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.
Government finance statistics: Government finance statistics (GFS) are not compiled using an internationally accepted statistical methodology and no staff has been identified to do so. A complete list of public sector entities is lacking. Work on a correspondence table between budgetary information and GFS needs to be completed. In addition, work on an integrated information system to capture completely stocks and flow information needs further development.

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 October 31, 2010)

	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	Oct. 2010	Oct. 2010	D	W	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	August 2010	Oct. 2010	D	W	D		
Reserve/Base Money	August 2010	Oct. 2010	M	M	M	LO, O, LO, O	LO, LO, O, O, LO
Broad Money	August 2010	Oct. 2010	M	M	M		
Central Bank Balance Sheet	August 2010	Oct. 2010	M	M	M		
Consolidated Balance Sheet of the Banking System	August 2010	Oct. 2010					
Interest Rates[2]	August 2010	Oct. 2010	M	M	M		
Consumer Price Index	Sept. 2010	Oct. 2010	M	M	M	O, LO, LNO, O	LNO, LO, LO, O, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	August 2010	Oct. 2010	M,Q	Q	Q	LO, LNO, LO, O	LO, O, LO, O, LNO
Stocks of Central Government and Central Government-Guaranteed Debt[5]	June 2010	Sept. 2010	Q	Q	Q		
External Current Account Balance	June 2010	Oct. 2010	Q	I	I	LO, LNO, LO, O	LO, LNO, LO, LO, LNO
Exports and Imports of Goods and Services	June 2010	Oct. 2010					
GDP/GNP	2010 Q2	Oct. 2010	Q	Q	I	O, LO, O, LO	LNO, LO, LO, O, LO
Gross External Debt	Dec. 2009	March 2010	A	I	I		
International Investment Position[6]	2007	May 2009	A	A	A		

1 Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
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, extrabudgetary 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 Includes external gross financial asset and liability positions vis-à-vis nonresidents.
8 Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), and Not Available (NA).
9 Reflects the assessment provided in the data ROSC or the Substantive Update for the dataset corresponding to the variable 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); not observed (NO); and not available (NA).

INTERNATIONAL MONETARY FUND

EXTERNAL RELATIONS DEPARTMENT

Press Release No. 10/488
FOR IMMEDIATE RELEASE
December 13, 2010

International Monetary Fund
Washington, D.C. 20431 USA

IMF Completes First Review Under the Policy Support Instrument for Mozambique

The Executive Board of the International Monetary Fund (IMF) has completed the first review under the three-year Policy Support Instrument (PSI) for the Republic of Mozambique.[4] The Board's decision was taken on a lapse of time basis.[5]

Mozambique´s macroeconomic performance has been strong overall, and its economic program supported under the PSI remains on track. Real GDP growth is projected to accelerate to 7.2 percent in 2010, driven by a recovery in external demand. However, the external environment has been less supportive than expected, as the balance of payments has been burdened by rising fuel and food import prices and lower private capital inflows. Rising food and fuel prices also triggered a surge in headline inflation. In response, the central bank has initiated a tightening of monetary policy. Fiscal policy has been marked by a remarkably strong revenue performance and an overall prudent execution of the budget, which helped offset unexpected outlays, such as for the fuel subsidy. Most of the program's quantitative targets for end-June 2010 were met —though reserve money growth was higher than envisaged—and there has been good progress in implementing structural reforms.

The authorities' economic program under the PSI will continue to emphasize preserving macroeconomic stability and debt sustainability while promoting economic development. This includes an acceleration of public investment in infrastructure, partially financed by nonconcessional external borrowing. In the short run, the authorities will pursue a tightening of

[4] The IMF's framework for PSIs is designed for low-income countries that may not need IMF financial assistance, but still seek close cooperation with the IMF in preparation and endorsement of their policy frameworks. PSI-supported programs are based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners. A country's performance under a PSI is reviewed bi-annually.

[5] The Executive Board takes decisions under its lapse of time procedure when it is agreed by the Board that a proposal can be considered without convening formal discussions.

fiscal and monetary policies to curb inflation expectations. They will also draft, in consultation with civil society and development partners, a new four-year poverty reduction strategy, with a particular focus on making economic growth more inclusive and protecting the population's more vulnerable segments. The program's structural reforms will focus on improving public financial management, debt management, tax policy, and financial sector supervision.

The Executive Board approved Mozambique's second three-year PSI on June 14, 2010 (see Press Release No. 10/242), upon expiration of the previous PSI and completion of the final review under a 12-month high-access arrangement (SDR 113.6 million) under the Exogenous Shocks Facility, aimed at providing temporary balance of payments support in dealing with the global crisis (see Press Release No. 09/247).