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Following a sharp 4 percentage point decline in real GDP growth in 2015, in the wake of the 2014 oil price shock, the Angolan economy went into recession in 2016 and remained there for five years. The authorities launched a wide-ranging reform program to stabilize and diversify the economy, and requested a Fund EFF arrangement in 2018 to support the reform effort. While a slow recovery seemed imminent at the end of 2019, this was interrupted by COVID-19 and a deep recession in 2020. The non-oil economy is however recovering, having assumed a sustained upward trajectory in real GDP growth through 2019, that was interrupted with a 5.2 percent contraction in 2020, before resuming again in 2021.

INTRODUCTION

1. On behalf of the Angolan authorities, we thank Mr. Mills and his team for their constructive discussions during the fifth review under the Extended Fund Facility (EFF) program as well as the detailed report. The authorities broadly share staff's views on the economic outlook and risks and appreciate the advice on policy priorities.

2. The COVID-19 pandemic and the collapse of oil demand and prices had a large impact on the Angolan economy. Following a rebound in oil prices, the economy is beginning to emerge from the crisis, as what has been a very difficult adjustment process, continues. The authorities are determined to push forward with their reform agenda, however, despite the challenging economic environment. They intend to entrench macroeconomic and financial stability, build resilience against external shocks, and pursue supply-side policies needed to accelerate economic diversification and spur broad-based growth. In their view, the guideposts of the EFF arrangement provide a robust anchor that helps to sustain the reform agenda.

3. The immediate policy agenda is to protect fiscal and debt sustainability through a conservative budget for 2021; to safeguard monetary and price stability by tightening monetary policy, including by adhering to quantitative targets for reserve money and supporting exchange rate flexibility; to improve efficiency and growth prospects by advancing the structural reform agenda; and to safeguard financial stability including by monitoring relevant indicators, promulgation of the revised Financial Institutions Law and restructuring a large troubled state owned bank.

RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

4. Notwithstanding the nascent recovery and higher international oil prices, the COVID-19 pandemic's impact on the economy of Angola remains substantial. Growth contracted by 5.2 percent in 2020, the most severe out of five successive years of recession. A marginal contraction in GDP is projected for 2021, while non-oil GDP is expected to increase by 2.3 percent.

5. Inflation rose from 20.81 percent in 2020 to 24.8 percent in April 2021 reflecting rising food prices. Higher food inflation comes in the wake of shocks, including drought and the recent locust invasion which hampered crop production and food supplies. A tighter monetary policy is expected to reduce inflation to around 19.5 percent by end 2021.

6. Notwithstanding the adverse impact of containment measures, the external position in 2020 was stronger than anticipated, reflecting some recovery in oil prices and the Kwanza depreciation, resulting in lower imports of goods and services. Overall, gross international reserves declined relative to 2019, but they remain at a comfortable level, representing around 10.6 months of imports cover at end-May 2021.

7. The outlook for the near-term remains subject to significant downside risks. The ongoing effect of the pandemic on oil exploration and operations is expected to reduce oil production in 2021, with additional spillover effects for non-oil GDP growth.

RESPONSE TO THE PANDEMIC

8. Angola's economic outlook depends on the successful rollout of the vaccination program. Following the partial reopening of the economy during the second half of 2020, a new wave began to emerge including new variants. The authorities put in place new containment measures to mitigate the impact of the second wave, while also ramping up the vaccination process. As at June 4, 2021, well over 1 million people had received at least the first dose, while 390,000 were fully vaccinated. After receiving the first 624,000 doses of AstraZeneca (of the expected 12.8 million) from the COVAX initiative, and 100,120 of Pfizer, and 200,000 of Sinopharm, the authorities purchased 6 million doses of Sputnik V and intend to purchase an additional 4.19 million doses via African Union. They plan to inoculate 16.8 million people, representing about 52 percent of the total population (see National Vaccination Plan Against COVID-19). Cognizant of scarring effects from the pandemic, the authorities are sustaining essential social spending to protect the vulnerable.

PROGRAM PERFORMANCE

9. The program remains broadly on track. All end-December 2020 performance criteria (PCs) were met with exception of that on central bank advances to the central government as the authorities sought to contain the effects of the pandemic. However, this PC was met in March 2021 and the central bank is on track to meet the June 2021 PC. All December 2020 indicative targets (ITs) were met, except for the stock of central government and Sonangol debt. This IT was met in March 2021. The authorities continue to retire foreign currency debt and have stated their commitment to the program's debt targets with a prudent approach to borrowing focused on carefully prioritized public investment. All PCs and ITs by end-March 2021 were met, except for net accumulation of the stock of payments arrears (domestic arrears) by the central government, as COVID-19 related payments were prioritized. There was strong performance on some targets. The non-oil primary fiscal deficit (NOPFD) at end-December 2020 outperformed the target, while the end-March 2021 IT on reserve money was met with a large margin. Preliminary indications are that all end-June 2021 PCs and ITs will be met.

10. Progress has also been made in the implementation of structural benchmarks (SBs). Of the nine structural SBs up to end-March 2021, five were completed, albeit with a delay for three of these, and progress is continuing toward the remaining four. The authorities remain committed to meeting all SBs and have made considerable progress despite delays caused by the impact of the COVID-19 pandemic. Some SBs were reset for end-July and end-September 2021 due to human and institutional constraints caused by the pandemic. This includes the enactment of the Financial Institutions Law (FIL) in May 19, 2021 and the submission to the National Assembly of the BNA Law in December 2020.

11. A new securities and collateral law was enacted in April 2021, supporting development of infrastructure to promote sound credit-risk management standards, with the objective of adopting an international valuation standard for securities and collateral held by banks. This should also enhance the insolvency and enforcement frameworks.

12. Notable progress has also been made with PFM reforms. After the approval of the Fiscal Responsibility Law (FRL) by the National Assembly in August 2020, the authorities are now in the process of improving the efficiency and transparency of public procurement. They are also committed to strengthening accountability by publishing the initial project appraisal report for all new public investment projects above Kz 10 billion.

MACROECONOMIC POLICIES

13. The authorities remain committed to the steadfast implementation of the reform agenda and the goals of macroeconomic stability, economic diversification, and private sector-led growth.

Fiscal policy and debt management

14. Fiscal priorities remain focused on attaining a primary fiscal balance consistent with fiscal and debt sustainability. Building on tight budget execution in 2020, the authorities approved a prudent 2021 budget, supported by tax reforms implemented during the first half of 2020. The authorities anticipate an overall fiscal surplus of 2.2 percent for 2021, reflecting expenditure retrenchment alongside improved revenue performance. The authorities plan to implement additional measures to strengthen tax capacity, including inspections to improve tax compliance.

15. The authorities will continue to restrain non-priority spending and work to enhance the quality of spending. In 2020 they introduced a medium-term fiscal framework (MTFF) and its related fiscal strategy per the new requirements under the Fiscal Responsibility Law (FRL). The pilot MTFF anchored the 2021 budget and will guide the 2022 budget preparation. Alongside medium-term fiscal targets, it internalizes the implications of public investment decisions for the medium-term. The authorities will develop a comprehensive domestic arrears management plan that will rely on a real-time arrears surveillance system, to mitigate against domestic arrears accumulation.

16. As part of proactive debt management policies, the fiscal authorities recently reprofiled debt service with three large creditors, resulting in significant cash-flow savings in the medium term. They have also requested the extension of debt relief under the DSSI and are in the process of requesting a further extension through end-2021. They will continue to impose ceilings on issuance of debt guarantees by the State, and aim to better align interest rates on domestic

debt obligations with market rates, to better support domestic debt rollover rates and maturity extension, and contribute to the development of the domestic debt market. They also intend to save most of the windfall oil revenue in 2021 stemming from higher-than-expected oil prices - and accelerate debt reduction.

17. The authorities remain committed to reducing the poverty and inequality exacerbated by the pandemic, and are fast-tracking the registration of beneficiaries of the cash transfer program, Kwenda, with the objective of reaching 1.6 million households by end 2022. In addition, they are discussing a possible extension of the program timeframe and augmenting the cash transfer amounts per family, with the World Bank. They will continue to increase spending on education and health over time.

Monetary, exchange rate and financial sector policies

18. While the central bank tightened monetary policy in 2019 to reduce inflation, the adverse effects of the pandemic in 2020 resulted in the BNA temporarily loosening its monetary policy stance to ensure adequate liquidity in the system. Nevertheless, in response to recent inflationary pressure caused by weather-related shocks, the central bank initiated a gradually tightening of the monetary stance using open-market operations in 2021Q1 and increased reserve requirement ratios, to contain excess liquidity. Given ongoing inflationary pressures, the BNA will continue to monitor price developments closely. It is also committed to bringing the real interest rate into positive territory.

19. The BNA continues to reduce its role in the domestic FX market. The recent adoption of the Bloomberg FX trading platform and measures to enhance full price discovery in the FX market also support this goal. Progress in developing the market is expected to help limit the spread between the official and parallel exchange rates. Further, progress has also been made in eliminating exchange rate restrictions.

20. To safeguard financial stability, the authorities are promoting the prudent recognition of banks' loan loss provisions in line with expected credit losses, as well as the early recognition and active management of non-performing loans (NPLs) by commercial banks. With the measures taken, the banking system's NPL ratio has continued to fall, but remains high, hence the authorities' continued attention to protecting the sector's stability. Despite a slight decrease in capital buffers, they remain above the regulatory threshold. Moreover, after the completion of the recapitalization and restructuring process of the Banco de Poupança e Crédito (BPC), the authorities initiated the privatization process for the Banco de Comércio e Indústria (BCI). The authorities are also finalizing the restructuring of Banco Económico (BE) following the promulgation and publication of the new Financial Institutions Law in May 19, 2021. The authorities also remain committed to addressing the remaining governance and operational challenges at Recredit in line with recommendations of the Fund's TA, to help advance the implementation of macroprudential and resolution frameworks.

21. The new BNA Law submitted to the National Assembly in December-2020, is expected to be approved as soon as amendments are introduced to the Constitution to accommodate the autonomy and reinforce the mandate, of the central bank. Meanwhile, the BNA is putting in place complementary guidelines on effective bank boards and effective credit-risk-management practices and updating asset-classification and provisioning rules.

Structural reforms and governance

22. As the immediate pressures of the pandemic abate, advancement of structural reforms has become more of an imperative for the authorities. They have made progress in improving public financial management following the enactment of the Fiscal Responsibility Law and the ongoing work on the medium-term fiscal framework. Efforts to increase the share of investment projects that go through public tenders and the number of budget units, whose annual purchase plans are published on the Public Purchases Portal, are continuing. Furthermore, to improve transparency and accountability of extractive industries, the authorities are concluding requirements to join the Extractive Industries Transparency Initiative (EITI).

23. The Government Privatization Program (PROPRIV 2019-2022) aimed at privatizing 172 SOEs, including Sonangol's non-core assets, remains on course albeit with some delays due to the COVID-19 interruption in 2020. A total of 39 SOEs were privatized by end-2020 through public tenders. The authorities intend to accelerate PROPRIV as the situation improves. They are developing a roadmap on the overall SOE reform with staff's support. Privatization receipts will be used primarily for infrastructure financing, strengthening viable SOEs to be privatized, and repayments of central government debt.

24. The authorities continue to make significant progress in fighting corruption and improving the rule of law. A strategy is being framed with the support of the United Nations (UN), which will include the establishment of a UN agency in the country to fight drugs, crime, corruption, and terrorism. The National Asset Recovery Service, a special agency created by the Attorney General's Office continues to recover assets financed illegally through public funds, including by freezing bank accounts linked to the related individuals.

CONCLUSION

25. The authorities reiterate their commitment to the reform agenda and restoring macroeconomic stability, recouping sustainable growth and securing inclusive outcomes. To this end, they will continue implementing appropriate fiscal, monetary, and structural policies. They appreciate ongoing Fund engagement and policy advice and look forward to Executive Directors' support towards completion of this fifth review under the EFF arrangement.