Economic Research Office
Contact: +244 222 638 957
E-mail: bfa@bfa.ao

FLASH NOTE
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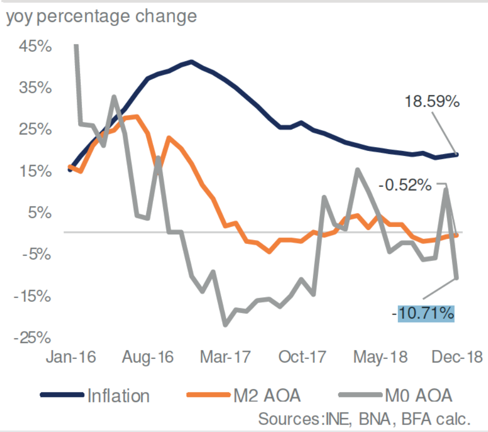
Reference rate lowered again, as inflation decreases

Mandatory reserve ratios kept unchanged in latest decision

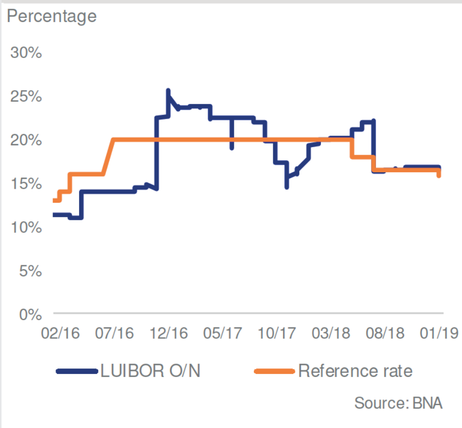
A. DESCRIPTION

1- The Monetary Policy Committee (MPC) of the Angolan central bank (BNA) decided to reduce the BNA Rate from 16.50% to 15.75% last Friday, following two policy easing moves in May and July of 2018. The reference rate is now at its lowest since March 2016, when it stood at 14%. The mandatory reserve ratios, in local and foreign currency, remained at 17% and 15%, respectively.

Monetary base and M2 decreased during 2018, as inflation receded



New drop give signals of intentions to relax the monetary policy when possible



B. ANALYSIS

1-This decline was not expected by most market viewers (including ourselves), as it looked like the BNA would not change the monetary policy at this first meeting of the year before having data on inflation for January, a time when price and wage updates can put some upward pressure on prices. However, the Monetary Policy Committee justifies this reduction with the decline of inflation in 2018 (which ended the year significantly below the expectation of both Government and international institutions, such as the IMF), as well as the sharp fall in M0, the BNA's monetary policy tool variable. **As the Angolan central bank puts it, monetary policy in Angola is essentially transmitted through the reduction/increase of the monetary base, and the seen tumble of 10.71% yoy in December translates into a more restrictive policy than desired by the apex bank.** By reducing the BNA rate, the central bank expects it to lead to lower interest rates in the banking sector, thereby increasing the money creation by retail banks.

2- The decision signals the market that there is an intention to lower interest rates, and a willingness to ease the monetary policy in the near future. Why do we think so? On one side, this is a slight rate drop; moreover, in the current environment, where some banks have known vulnerabilities and there are still significantly negative economic expectations (at least in the short-run), interest rates are not the only constraints to credit concession. **In fact, a shift in the mandatory reserves ratios would go a longer way towards the goal of effectively easing monetary policy.**

1 This means that the various components of GDP cannot be added in the expectation of reaching the total GDP.
2 The sum of sectoral GDPs would even lead to a downward revision, since the upward correction is justified by changes in the calculation of taxes and subsidies, and by a residual component that is not clear in the INE data.
3 Financial Intermediation Services Indirectly Measured.

3- Taking this decision into account, further easing moves are likely to happen during the year, including possibly both rate cuts and drops in reserve ratios. There will be two more MPC meetings in the first half of the year, respectively March and May: we expect a further reduction at one of those meetings if inflation continues to decline. A change in reserve ratios, however, is only likely to occur after an assessment of the inflationary impact of VAT implementation in July, meaning that it could occur in the September or November meeting. **However, it is worth to highlight that the BNA seems to be very data-dependent, on both inflation and MO. And this means that we will have to wait and see in which manner this monetary policy easing cycle will be conducted.**

C. CONCLUSION

1- I The deal between the authorities and the IMF stresses the need to maintain a tight monetary policy, although it also mentions a balance with supporting the economic recovery. It seems to us that, taking into account the negative effect of MO on the Angolan non-oil economy, the BNA intended to signal that its strategy is, whenever possible, to use available slack in order to relax monetary policy, just as long as inflation keeps receding. **As previously said, this decrease will have a modest impact.** Yet, it signals that similar moves are possible, and that some form of easing is coming, possibly in the second half of the year, given a benign effect on prices of VAT (and reduction of price subsidies) - perhaps with further changes in mandatory reserves.