

FLASH NOTE

Nº 08.2024 | April 02, 2024

BNA tightens monetary policy again

Inflation accelerates and leads CPM to raise reference interest rates

A. DESCRIPTION

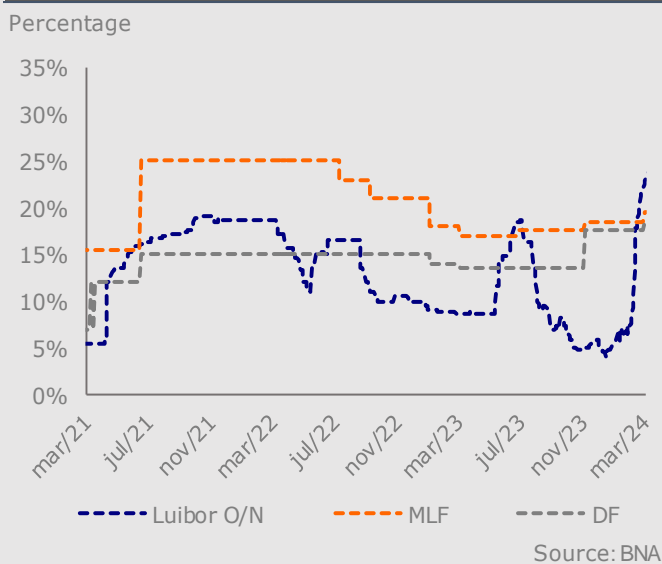
1| At the Monetary Policy Committee (MPC) meeting held on March 14th and 15th, the Angolan central bank (BNA) decided to change the main instruments for conducting monetary policy. The Basic Interest Rate rose 100 basis points (bps) to 19%, the Marginal Lending Facility (MLF) rose to 19.5% (+100 bps) and the Deposit Facility (DF) rose to 18,5% (+100 bps), while the coefficient of mandatory reserves in local currency remained at 20%.

2| Year-on-year inflation stood at 24.1% in February, registering the tenth consecutive month of increases. According to INE data, monthly inflation stood at 2.58% (+0.05pp), close to the highs of September 2018. Among the classes that recorded significant variations, the most notable are "Food and Non-Alcoholic Beverages", with 3.1%, "Health" with 3.1% and "Miscellaneous Goods and Services", with 2.9%. On the other hand, the classes "Education", "Transport" and "Communications" had the smallest variations with 0.0%, 0.4% and 0.8%, respectively.

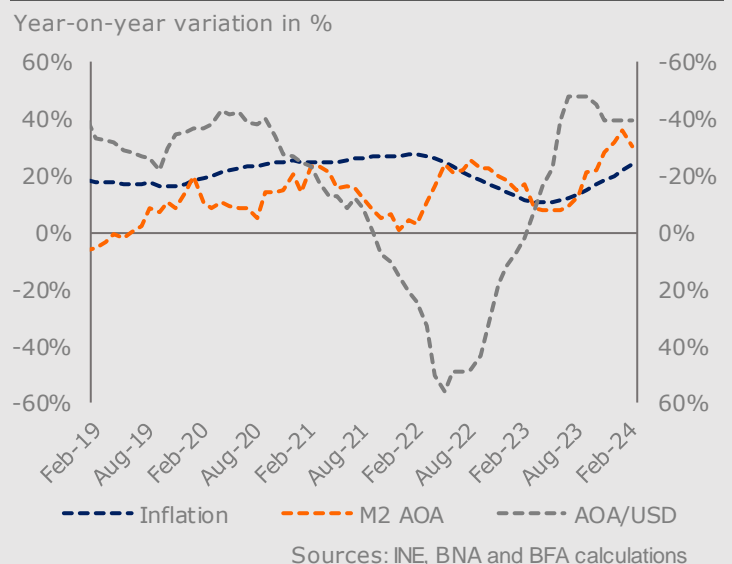
B. ANALYSIS

1| At the previous meeting, held in January, the MPC had once again tightened monetary policy, raising the mandatory reserves coefficient in local currency to 20%, with the aim of restricting market liquidity levels. In fact, this is a very effective measure in terms of reducing

Overnight Luibor rises despite evidence of liquidity in the market



M2 grows consistent with the increase in liquidity in the market



liquidity, since the +2pp increase was able to remove from the market via private deposits AOA 1.68 trillions. However, despite the contraction of the monetary base in monthly terms, in year-on-year terms it continues to grow, signaling that the market remains liquid and forcing the BNA to reinforce its restriction policy, raising the main interest rates.

Luibor Overnight appears to be reacting to the occasional availability of foreign exchange resources in the Fx market, although there is still evidence of Kwanzas liquidity in the market. The Treasury carried out currency sales operations that had an impact in the short term. This impact occurred mainly in banks that, in need of foreign exchange, had low availability in local currency, relying on the market for the missing liquidity. Combining this factor with a lack of access to liquidity support through the BNA, an imbalance was generated with a series of institutions looking for liquidity, leading to pressure for higher rates in the interbank market.

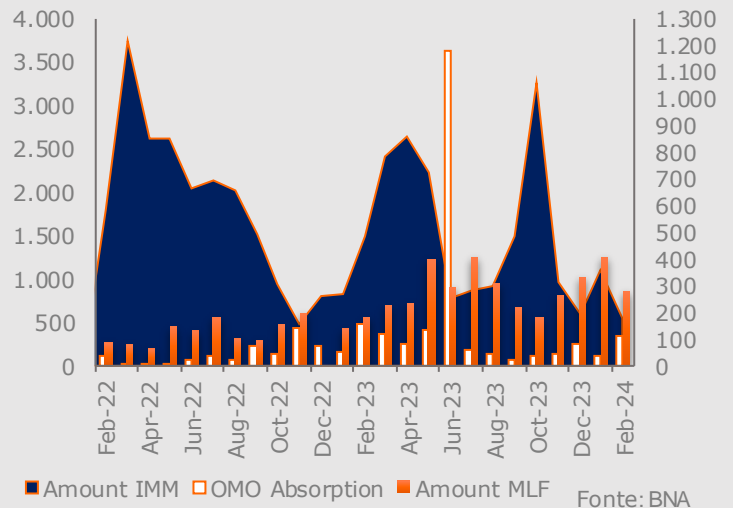
Interest rates on the interbank money market (IMM) and on treasury bills and bonds have been rising, in line with the reduction in liquidity in the market in the short term: Overnight (O/N), which signals the level of liquidity of the economy, is now at 24.37%, the maximum in 2019. The evolution of the O/N does not visibly impact credit, considering that the remaining IMM rates, which are indexes for credit, have not followed the evolution of the O/N because strictly speaking there are no transactions in the money market for these periods. Even so, the LUIBOR calculation mechanism in the remaining terms leads us to believe that it is possible for rates to rise, thus dragging down credit rates through these indexes used by the various banks.

Our expectation is that the market will correct in the coming weeks as this effect of Treasury auctions on bank liquidity fades.

Giving some context to the functioning of the money market: the increase in the overnight rate not only affects the IMM itself, but also the entire money market. The adjustment of the MLF and DF is a clear sign that the BNA intends to tighten monetary policy a little more, after having started this restriction path in previous meetings and still checking the liquid market. Changes in liquidity supply and absorption rates lead to increases or decreases in liquidity and economic activity: the supply rate defined by the Central Bank influences overnight rates and treasury bond rates. On the other hand, the rates at which the BNA remunerates extra liquidity depend on the BNA, but also on the banks' appetite for this liquidity,

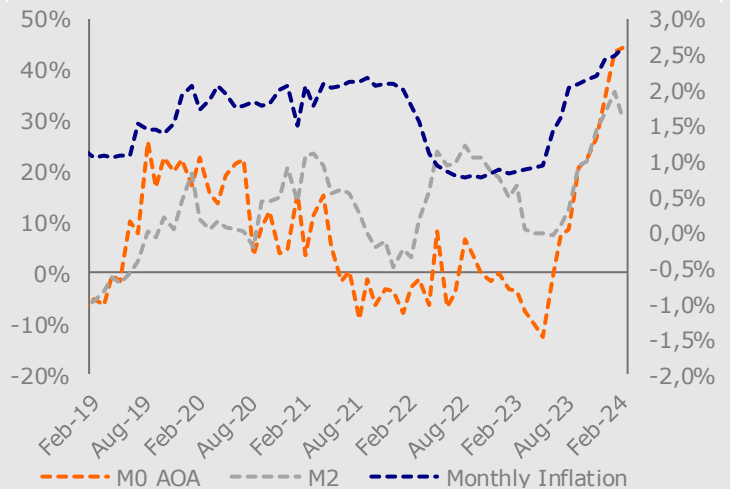
FPCL records the highest monthly increase after the sharp drop in July/2023

Volume in AOA Billions



M0 grows year-on-year, influenced by the rise in excess reserves

Percentage



this same appetite also influenced by other rates in force in the market, which contribute to making bank resources profitable.

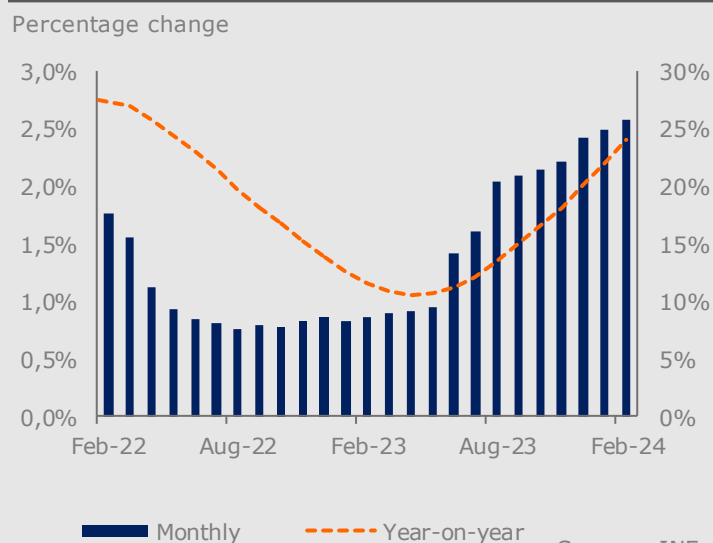
The Monetary Base (M0) in local currency has been accelerating, strongly influenced by the excess reserves of the banking system, which registered a yoy growth of 176.4% in February. The money supply measured in M2 marked a monthly contraction of around 2.4% (AOA -221 Million compared to AOA 9.22T in January). In relation to the same period last year, there was an expansion of M2 of around 30.4%: this movement was influenced by the growth of the indicators that make up this aggregate, with emphasis on quasi-money, notes and coins held by the public and deposits transferable assets that grew 20.5%, 39.7% and 38.0%, respectively.

2| According to recent statements by the Minister of State for Economic Coordination, José de Lima Massano, Angola managed to negotiate new conditions for debt payments with the China Development Bank (CDB), reducing the amounts set in the guarantee account: it is important to remember that the tension registered in the foreign exchange market in 2023, as a result of the depreciation of the local currency, was also influenced by the end of the debt moratorium period with China that began in the pandemic era, 2020. In 2015, the China Development Bank (CDB), granted a loan of USD 15B to the Angolan Government and required the borrower to maintain a minimum balance of no less than USD 1.5B in an escrow account. Due to this period of debt moratorium, the Escrow Account balance was reduced to almost zero in mid-2022, motivating the CDB to demand that the borrower replenish the account by 2023. This "effort" by the Angolan State in the context of reestablishing the guarantee account, together with the disbursements defined for that period, limited the National Treasury's ability to intervene in the foreign exchange market. Currently, the Minister of State's statements highlight that there will be a reduction in the amounts set in the Escrow Account, which will free up liquidity of around USD 150 – 200 million per month, which can be used in the Fx market; This could be another factor of pressure on liquidity in local currency from the 2nd quarter onwards.

3| Monthly inflation has been accelerating, in line with the reduction in imports of goods and services recorded during 2023. We have been monitoring the trajectory of monthly inflation, which in February registered its twelfth consecutive month of increases and is being dragged by the classes "Food and Non-Alcoholic Beverages", "Miscellaneous Goods and Services" and "Health" with a contribution to the CPI that is currently around 71.7pp, 7.9pp and 4.7pp, respectively. The classes "Health" and "Food and Non-Alcoholic Beverages" are those that have registered the greatest variations in prices: they have demonstrated behavior in line with the reduction in imports of goods, mainly due to insufficient domestic production.

Despite the persistent growth of the CPI, the BNA showed no evidence of possible changes to its short-term inflation target, 19%. This decision was taken based on the premise that from the second half of the year onwards, monthly inflation could grow at a slower pace, also combined with the fact that the USD/AOA pair has been stable.

Year-on-year inflation in February accelerates to 2018 highs



Sources: INE

In our view, we believe that annual inflation could accelerate again in March and grow less and less from the third quarter onwards. Still, we do not discard our forecast for the end of the year, around 24%. As for the next meeting, scheduled for May 16th and 17th, the MPC decisions, which extend to defining the instruments for conducting monetary policy, will depend substantially on the trajectory of inflation.

C. CONCLUSION

1| The BNA's monetary policy options will always depend on the performance of inflation, and this should begin to slow down from the second half of the year, as a result of the stability of the local currency against the main foreign currencies, as well as an increasingly reduced impact of inflation imported, as global inflation levels are reducing. In our opinion, with the continued management of monetary policy by the BNA, and the strengthening of the Treasury's presence in the Fx market, it cannot be ruled out that the central bank will be able to counteract the inflation trend. However, the 19% target seems difficult to achieve by the end of 2024. Therefore, from our perspective it will make sense to pay extra attention to the maturity dates of securities during this year, and their effect on liquidity. These amounts have significantly impacted liquidity and, therefore, the interest rates in force in the money market. More vigorous coordination and communication will therefore be necessary between the BNA's management of monetary policy and treasury and debt management.

This publication is exclusively for private use. The information contained in this publication was obtained from sources considered reliable, but its accuracy cannot be fully guaranteed. Any recommendations given herein are intended exclusively for internal use and may be changed without prior notice. The opinions expressed herein are entirely the responsibility of its authors; they reflect only the authors' points of view and may not follow the position of BFA in the markets in question. BFA or any of its affiliates, through its employees, cannot be held responsible for any direct or potential loss resulting from the use of this publication or its contents. BFA and its employees may hold positions in any assets referred to in this publication. Reproduction of part or all of this publication is permitted, subject to the indication of the source. Figures are expressed using the comma as thousands separator and the point as decimal separator and using the term "billion" to signify 10^9 .