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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 18/44-2

11:55 a.m., May 18, 2018

2. Angola—2018 Article IV Consultation

Documents: SM/18/90 and Supplement 1, and Supplement 2, SM/18/98

Staff: Velloso, AFR; Goodman, SPR

Length: 30 minutes

Executive Board Attendance

T. Zhang, Acting Chair

Executive Directors	**Alternate Executive Directors**
M. Mkwezalamba (AE)	
D. Sembene (AF)	
	J. Corvalan (AG), Temporary
	C. Barron (AP)
	P. Fachada (BR)
	X. Cai (CC), Temporary
	J. Rojas (CE)
	C. Williams (CO), Temporary
	C. Just (EC)
	F. Bellocq (FF), Temporary
	K. Merk (GR)
	M. Roy (IN), Temporary
	F. Spadafora (IT), Temporary
	Y. Saito (JA)
	C. Sassanpour (MD), Temporary
	M. Choueiri (MI), Temporary
	C. Botel (NE), Temporary
T. Ostros (NO)	
	L. Palei (RU)
	R. Alkhareif (SA)
	E. Villa (ST)
	P. Trabinski (SZ), Temporary
	J. Stockill (UK), Temporary
	M. Svenstrup (US), Temporary

T. Rumbaugh, Acting Secretary
K. Hviding, Summing Up Officer
J. Acheson / R. Smith Yee, Board Operations Officers
L. Nagy-Baker, Verbatim Reporting Officer

Also Present
World Bank Group: N. Fiess. African Department: R. Chawani, N. Ferreira Souza Sobrinho, A. Gulde, T. McGregor, A. Mengistu, P. Munguambe, A. Selassie, R. Velloso. European Central Bank: T. Persico. Information Technology Department: F. Gheriss. Legal Department: W. Bergthaler, F. Fernando. Monetary and Capital Markets Department: C. Ribas Visconti. Strategy, Policy, and Review Department: F. Liu, M. Goodman.

Alternate Executive Director: D. Mahlinza (AE), H. Razafindramanana (AF). Senior Advisors to Executive Directors: W. Abdelati (MI), M. Alle (AF), S. Rouai (SA), E. Sishi (AE), T. Sitima-wina (AE), A. Tivane (AE), B. Varga (EC). Advisors to Executive Directors: P. Abradu-Otoo (MD), H. Alias (ST), J. Essuvi (AE), J. Garang (AE), G. Gunnarsdottir (NO), M. Ismail (AE), N. Komura (JA), W. Kuhles (GR), A. Nainda (AE), W. Nakunyada (AE), L. Nankunda (AF).

2. ANGOLA—2018 ARTICLE IV CONSULTATION

Mr. Mkwezalamba, Mr. Tivane and Mr. Essuvi submitted the following statement:

Introduction

Angola has made great strides in tackling its post-conflict development challenges over the past decade. Sustained economic reform efforts propelled socio-economic development, improved macroeconomic conditions, and strengthened institutional capacity. Nevertheless, the economy continues to face risks due to uncertainty in oil prices, gaps in basic infrastructure, and limited human capital development. In this context, reaping the benefits from the oil sector to support priority public investments required to accelerate economic diversification, while promoting a private sector-led growth model, remains the most pressing challenge facing the country going forward.

To address the challenge, the authorities recently launched the Macroeconomic Stabilization Plan (MSP) and the second National Development Plan (NDP 2018-2022) in January and April 2018, respectively. The MSP envisages addressing macroeconomic imbalances, insulating the fiscal position from volatile oil revenues, and accelerating external adjustment through greater exchange rate flexibility. On the other hand, the NDP seeks to restore macroeconomic stability, foster sustainable inclusive growth, boost competitiveness in the non-oil sector, stabilize public debt, and improve governance and institutions. In this respect, the authorities broadly concur with the staff appraisal and policy recommendations, and appreciate the Fund's candid engagement during the 2018 Article IV consultation.

Recent Economic Developments and Outlook

The Angolan economy continues to gradually adjust since the onset of the oil price shock in mid-2014. The pace of adjustment has, however, recently slowed down due to limited fiscal space that has constrained implementation of priority infrastructure investments required to boost non-oil GDP growth.

Real GDP growth recovered moderately to 1.0 percent in 2017 from 0.1 percent in 2016, owing to a rebound in the non-oil sector, increased public spending, renewed business confidence, and improved foreign exchange market conditions. Looking ahead, growth is projected to edge up to 2.2 percent in 2018, driven by a faster recovery of the oil and non-oil sectors, and a general improvement in macroeconomic fundamentals.

Inflation declined sharply from an average of 41.2 percent in 2016 (y-o-y) to 26.3 percent in 2017, owing to a moderation in food prices, greater availability of foreign exchange, and a tighter monetary policy stance. Average inflation is forecast to further decline to 23 percent in 2018. To further dampen inflationary pressures, the Banco Nacional de Angola (BNA) raised its policy rate by 200 basis points, to 18 percent, at the end of November 2017, the first increase since mid-2016. Similarly, in early 2018, the BNA abandoned the exchange rate peg to the U.S. dollar, and introduced a more flexible exchange rate regime.

The current account deficit narrowed from 10.0 percent of GDP in 2015 to 4.5 percent of GDP in 2017, following a rebound of oil exports, supported by improved terms of trade. Owing to the need to clear the longstanding backlog of foreign exchange purchase orders in the market, presently estimated at US$2.5 billion, gross international reserves are projected to decline from 6 months to 5.2 months of import cover at the end of 2017.

The medium-term growth outlook for Angola remains positive owing to firming oil prices, improved global financial conditions, and renewed business confidence. Nonetheless, uncertainty in oil price developments remain the main source of risks to the country’s prospects of a faster recovery.

Fiscal Policy and Debt Management

Following considerable fiscal adjustment efforts made in 2016, the fiscal stance was loosened in 2017, mostly reflecting expenditure pressures in the run-up to the August 2017 elections. Consequently, the non-oil primary fiscal deficit edged up from 10.2 percent of GDP in 2016 to 10.8 percent in 2017. Similarly, public and publicly guaranteed debt reached 64 percent of GDP in 2017, partly reflecting a buildup of payments arrears, currently estimated at 4 percent of GDP.

The authorities’ medium term fiscal strategy seeks to foster fiscal consolidation while preserving fiscal space for development needs and social outlays. To this end, the 2018 budget approved by the National Assembly in February 2018 contemplates a set of measures aimed at scaling back public spending, intensifying non-oil revenue mobilization efforts, and boosting public expenditure efficiency. The implementation of these measures is expected to yield a targeted reduction of the non-oil primary deficit, equivalent to 2 percentage points of GDP in 2018, broadly in line with the MSP objective of lowering the public debt-to-GDP ratio to nearly 60 percent over the medium term. Furthermore, the authorities are committed to use windfall oil revenues to clear domestic arrears and reduce public debt.

To create additional fiscal space and insulate the fiscal position from oil price volatility, the authorities intend to intensify reforms aimed at diversifying the sources of non-oil revenues. This will be achieved through implementation of measures to widen the tax base and enhance tax compliance, mostly through introducing a VAT on January 1, 2019; improving tax inspections; enforcing real estate taxation; and creating incentives to unlock tax potential from the informal sector. Regarding VAT, a set of preparatory actions are being implemented, including drafting legislation, defining tax parameters, and putting in place appropriate systems and IT infrastructure with the support of Fund Technical Assistance (TA).

On the expenditure side, policy priorities remain focused on rebalancing expenditures towards productivity-lifting sectors and streamlining recurrent expenditures, notably the wage bill as well as goods and services. In addition, the 2018 budget provides for the elimination of subsidies in the energy and water sectors. Other reform priorities include strengthening the capacity for improved public investment efficiency and enhanced oversight of fiscal risks emanating from state-owned enterprises (SOEs), coupled with efforts to fully implement a medium-term fiscal framework (MTFF) by 2019 to reduce pro-cyclicality of spending.

Monetary, Exchange Rate, and Financial Sector Policies

The BNA is firmly committed to sustaining efforts to maintain price stability, rebalance the foreign exchange market, enhance the monetary policy framework, and preserve financial sector stability. In November 2017, the BNA adopted base money as the new monetary policy anchor to better stem inflationary pressures. This was complemented by adoption of a flexible exchange rate regime in January 2018, which resulted in depreciations of 30 and 42 percent of the kwanza against the U.S. dollar and the euro, respectively. Consequently, the spread between the parallel and the official exchange rates narrowed from 150 percent in 2017 to nearly 85 percent in April 2018.

Going forward, policy priorities will focus on upgrading the monetary policy framework and strengthening oversight of the banking system. More specifically, these include fully rebalancing the foreign exchange market and increasing reliance on the exchange rate flexibility as a shock absorber; strengthening capacity for liquidity forecasting and management, as well as inflation modeling and forecasting; and developing strategies to eliminate exchange restrictions and multiple currency practices. Other priority actions comprise upgrading macro-prudential regulations; strengthening the AML/CFT framework and financial sector resilience to mitigate the loss of correspondent banking relationships (CBRs); and shifting to risk-based supervision. Further, the authorities submitted to the National Assembly a billon repatriation of illegal capital, and redoubled efforts aimed at addressing the high NPLs and rebuilding balance sheets of state-owned banks.

The authorities will continue to improve financial sector resilience, including through accelerating the process of recapitalization of the Banco de Poupança e Crédito (BPC). In this regard, the 2018 budget envisages injecting a third tranche of the recapitalization funds, while Recredit will continue to acquire the NPLs of BPC and other banks. Further, they will continue to step up efforts to mitigate the loss of CBRs. In this connection, BNA has actively participated in international fora and continued to engage authorities from international jurisdictions to better understand the expectations and required improvements in the supervisory framework to lessen the impact of the loss of CBRs. Similarly, the authorities intend to maintain an open dialogue with local private institutions on measures underway to strengthening macro-prudential regulations and enhancing the country's AML/CFT framework.

Structural Reforms

Addressing the longstanding competitiveness challenges remains paramount to achieving better economic outcomes, curbing the incidence of poverty and inequality, and incentivizing private sector development. Against this background, the authorities are prioritizing the mobilization of the non-oil revenues for infrastructure investments needed to accelerate economic diversification, while creating an adequate set of incentives and institutions to promote a friendly business environment, improve governance and fight corruption. In this connection, the National Assembly approved a Competition Law and anew Private Investment Law in April and May 2018, respectively. These legislative steps are expected to greatly improve the country's investment appeal. Similarly, the authorities have launched a program for export diversification and import substitution (PRODESI). The program is intended to bring about improvements in the business environment by simplifying procedures for business licensing, property registration, and enforcement of contracts. In addition, procedures for facilitating export processing and the capacity of investment-promotion agencies will be enhanced.

Additional steps to improve the business climate include expediting visa procedures for citizens of 61 countries and providing visa exemptions for 5 others. These measures will also boost tourism and facilitate foreign direct investment.

Furthermore, the new administration is firmly committed to strengthening governance and fighting corruption. In this regard, a series of investigations into possible mismanagement of public affairs have been launched in several public entities, accompanied by several dismissals of high level officials. In addition, a specialized anti-corruption unit with the overall mandate to fight corruption was established in March 2018.

The authorities attach great importance to strengthening institutional capacity for policy design, monitoring, and implementation. In this regard, they are making efforts to improve the timeliness and quality of data, including through enhanced recording of debt statistics and coverage of non-financial corporations in monetary statistics.

Concluding Remarks

The Angolan authorities remain committed to advancing far-reaching structural reforms to achieve durable macroeconomic stability, tackle longstanding structural challenges to broad-based growth, and improve institutions. The new administration is determined to achieve these goals through sustained implementation of reform measures articulated in the MSP and the NDP (2018-2022). The Fund's continued engagement and policy advice remains essential to support the authorities' reform agenda going forward.

Mr. Doornbosch and Mr. Botel submitted the following statement:

We thank staff for the comprehensive report and insightful SIP and Messrs. Mkwezalamba, Tivane, and Essuvi for their informative buff statement. The highly oil-dependent economy of Angola has been significantly affected by the sharp drop in oil prices that started in 2014. The initially adequate policy responses were reversed in the run-up to the 2017 elections, resulting in the erosion of fiscal and external buffers despite the recent partial recovery of oil prices. We welcome the new government's macroeconomic stabilization program. The broad consensus between the authorities and staff on policy recommendations is encouraging and we wish to stress the importance of a resolute and time-consistent implementation of these policies to achieve a sustainable recovery. Since we agree with staff's assessment and recommendations the next remarks are for emphasis.

Reducing the economy's dependence on oil by diversifying and improving the allocation of resources towards most efficient activities are vital to reduce vulnerabilities, boost competitiveness, and foster sustainable and inclusive growth. This requires comprehensive reforms in both the real and financial sectors, for which policy complementarity is critical to be successful. Improving governance, fighting corruption, and streamlining the business environment are needed to support the evolution of the private sector as the main driver of growth. Downsizing the public sector would allow transfer of employment towards private production while reducing the fiscal burden, including the risks associated with contingent liabilities, consistently with the projected medium-term fiscal consolidation. Moreover, reducing the public wage bill would help create the necessary fiscal space for well-targeted social programs aimed at reducing the costs of reforms for the most vulnerable. Allowing greater exchange rate flexibility and eliminating exchange rate restrictions and multiple currency practices would remove distortions in resource allocation. This would allow the market discovery of the most efficient activities to guide the diversification necessary to increase the economy's resilience and competitiveness. Addressing the vulnerabilities of the financial sector by strengthening banks' monitoring, by developing the frameworks for crisis management and resolution and for AML/CFT, as well as by recapitalizing, restructuring, and improving the governance of state-owned banks (which account for four-fifth of NPLs), is necessary to increase the role of credit in financing the development of the private sector.

We welcome the strong political ownership manifested at the authorities' highest levels for the reform agenda, which led to promising decisions taken towards its implementation, such as the favorable first-round vote on the Law of Competition in the National assembly; the launching, with World Bank support, of a program for diversifying exports and substituting imports seeking greater private sector participation; the creation of a high-level inter-ministerial commission for preparing a privatization program. However, we agree with staff that building and steadily improving the institutional capacity for actual and consistent implementation of these decisions is crucial and we wish the authorities all the success in this endeavor.

Mr. Inderbinen and Mr. Trabinski submitted the following statement:

The Angolan economy continues to adjust to the oil price shock of 2014. Recent elections, and the first change in the head of government since 1979, provide the opportunity to focus on much needed reforms. We welcome the recently launched Macroeconomic Stabilization Program (MSP). For the more favorable medium-term outlook to materialize, sustained efforts will be needed to curb the fiscal deficit and the growing public debt, to progress further toward a flexible exchange rate regime, and to address the weaknesses in the banking sector. We thank staff for the good documentation, as well as Mr. Mkwezalamba, Mr. Tivane and Mr. Essuvi for their helpful buff statement. We share the thrust of the staff appraisal and we would like to offer some comments for emphasis.

Upgrading the monetary policy framework and moving toward greater exchange rate flexibility should remain a priority. We welcome the recent steps to introduce a flexible exchange rate regime. Considering the high liquidity fluctuations experienced at the end of 2017, and the substantial interventions by the BNA, we strongly encourage the authorities to further strengthen the monetary and exchange rate policy framework, as outlined in paragraph 20 of the staff report. We note from the buff that the authorities intend to develop a strategy to abolish the existing exchange restrictions, as well as the multiple currency practices. This is welcome, and we encourage the authorities to follow-through with timely and concrete measures. We agree that the tight monetary stance remains appropriate in facilitating the shift in regimes, and we also see improved communication of monetary policy objectives and actions to the market to be critical.

The authorities are encouraged to undertake sustained fiscal consolidation and rebuild buffers. We commend the Angolan authorities for the prudent 2018 budget. As envisaged by the MSP, fiscal consolidation is necessary to put debt-to-GDP ratio on a firm downward path. We welcome the plans to diversify the tax base and increase the very low levels of non-oil revenue, including through the introduction of a VAT, strengthening tax compliance, and formalizing businesses. At the same time, we encourage the authorities not to withdraw from social programs targeting poverty and facilitating inclusive growth.

Measures are needed to address the vulnerabilities in the Angolan banking system. Priorities should include the reinforcement of capital and liquidity buffers, the strengthening of governance and, where necessary, the timely restructuring of state-owned banks. We take good note of the authorities' efforts aimed at completion of the asset quality reviews, and encourage them to progress with the further strengthening of the AML/CFT framework. Considering the importance of Recredit and the still high level of NPLs, could staff provide more information about the restructuring process, and the timeline for clearing distressed assets?

We welcome the efforts to improve non-oil competitiveness, diversify the economy, and improve governance. To facilitate private-sector led growth and a more inclusive economy, it will be critical to address corruption, the weak business environment, and the significant regional disparities. We encourage the authorities to strengthen property rights and anti-corruption institutions, and note the recent steps taken to this end, including the establishment of a specialized unit to fight corruption. Finally, we support staff's call for improvement in data compilation and dissemination, specifically in regard to the national accounts, finance statistics and balance of payments statistics.

Mr. Rojas Ramirez submitted the following statement:

The Angolan economy is resilient after a period of low oil prices. The new authorities have undertaken appropriate policy adjustments oriented toward fiscal consolidation and exchange rate flexibility, lowering inflation and controlling oil volatility impact. In the medium term, authorities are working on restoring economic stability, promoting sustained inclusive growth and economic diversification. We welcome and thank staff for the report and Messrs. Mkwezalamba Tivane and Essuvi for their candid statement on the 2018 Article IV consultation.

The Angolan economy has been facing low oil prices, compromising its main source of fiscal revenues and consequently experiencing high deficits. In this context, fiscal policy has been appropriate, the authorities have aimed to achieve non-oil primary fiscal consolidation in the 2018 budget and are using additional oil revenues to clear domestic arrears and reduce public debt. We encourage authorities on the implementation of a fiscal stabilization fund to tame oil price volatility and reduce pro-cyclicality in expenditures, improve tax collection by the TVA adoption, and creating space for public investment and social protection

On the monetary stance, the central bank (BNA) has implemented appropriate measures. Monetary policy has been tight adopting a base money anchor. This policy has been appropriate in supporting exchange rate flexibility and addressing imbalances in the forex market. We encourage authorities to continue working toward implementation of market-clearing exchange rate in a framework of inflation targeting and prudent fiscal policy while strengthening the external balance according to fundamentals.

The banking system business model is highly dependent on the oil sector and needs to be diversified. The banking system remains capitalized, nevertheless, this makes the system vulnerable to oil rent volatility, liquidity situations, and high NPL, as well as dependent on fiscal expenditures. We note that BNA has introduced liquidity requirements for commercial banks and increased the minimum regulatory capital requirements. Authorities are committed to improving and fully enforcing AML/CFT regulations and supervision, and addressing corruption-related risks. We encourage the BNA to continue efforts to reinforce capital and liquidity controls, as well as strengthening the prudential and crisis management framework.

Economic diversification in the oil and non-oil economy sectors is crucial for Angola. We commend authorities for their efforts on improving the business environment and transparency to build the appropriate economic framework for economic diversification and inclusive sustainable growth, as with the Law on Competition establishing the anti-trust authority to enforce the application of the law. Nevertheless, we agree with staff's recommendation that authorities face the challenge of adopting structural reforms on governance, an appropriate legal framework and transparency and the transformation toward a more market-oriented economy.

Mr. Sembene, Mr. Alle and Ms. Nankunda submitted the following statement:

We thank staff for the comprehensive set of reports, and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for their informative buff statement.

In recent years, Angola's economy has been adversely affected by unfavorable oil price developments and capacity weaknesses. In addition, policy implementation in the run-up to the 2017 election contributed to further deterioration in the fiscal and external positions. In this context, the authorities' macroeconomic stabilization plan (MSP) launched earlier this year appropriately aimed at addressing these imbalances and turning the economy around, including by promoting fiscal consolidation, greater exchange rate flexibility, public debt reduction, and domestic payments arrear clearance. Going forward, we concur that structural reforms also need to be stepped up with a view to fostering economic diversification away from oil.

We welcome the authorities' commitment to fiscal consolidation to curb down public debt. The 2018 budget appropriately targets a significant reduction in both the overall fiscal deficit and the non-oil primary fiscal deficit. In this endeavor, we welcome the planned introduction of VAT in early 2019 as well as efforts to contain public expenditure, including by streamlining the wage bill and spending on goods and services. At the same time, we take good note of the authorities' intention to create additional space for public investment and social programs. Furthermore, the steps being taken by the authorities to improve the debt profile are welcome. They are encouraged to give due consideration to staff recommendations in this regard.

We are encouraged by the BNA's strong commitment to sustain efforts to maintain price stability and strengthen its monetary policy framework, while preserving financial sector stability, as reported in Mr. Mkwezalamba's buff statement. In this endeavor, we take note of the introduction by the BNA of a more flexible exchange rate regime in early 2018 which helped reduce the spread between the parallel and the official exchange rate. Going forward, the authorities are well-advised to maintain a tight monetary policy to reduce inflation while increasing further exchange rate flexibility.

In parallel, building a sound financial system and bolstering financial deepening and inclusion will be of critical importance. To this end, key sources of vulnerabilities in the banking system need to be addressed, including high NPLs and the significant exposure of banks to the state. In view of banks' appetite for government T-bills, we wonder to what extent the private sector is being crowded out? Going forward, the BNA will find it useful to enhance its regulatory and supervisory frameworks to address systemic risks, including those that could be triggered by the deterioration in asset quality and weak regulatory compliance by systemically important banks. The authorities may need to explore avenues for strengthening further the banking sector's soundness and resilience, including by better enforcing new capital requirements and restructuring inefficient state-owned banks. We also encourage the BNA to continue strengthening its crisis management tools and resolution framework.

Strengthening structural reforms for advancing economic diversification is critical to expand the non-oil sector and reduce dependency on oil. We welcome steps being taken to improve governance, fight corruption and improve the overall business environment. We particularly see merit in implementing the recently approved Law on Competition aimed at supporting competition in domestic markets; and the draft Private Investment Law which should help boost FDI by removing barriers. We take good note of the authorities' readiness to contemplate additional measures to further improve governance and business environment.

Mr. Fachada and Mr. Pinheiro de Melo submitted the following statement:

We thank staff for the reports and Messrs. Mkwezalamba, Tivane, and Essuvi for their statement. We commend the Angolan authorities for the smooth political transition that took place last year. The current rebound in oil prices offers the new authorities an opportunity to rebuild external buffers and advance fiscal consolidation, thereby enhancing the country's resilience against external shocks.

If fully implemented, the authorities' Macroeconomic Stabilization Program will help put Angola in a stronger fiscal position. The staff estimates that an annual average reduction of ¾ percent of GDP in the non-oil primary balance would lower the public debt-to-GDP ratio to under 60 percent over the medium-term. Introducing a value added tax (VAT) will help achieve that target, but the authorities will also need to better control public sector wages and other current spending. At the same time, improving the overall quality of public spending is fundamental to create space for public investment and social spending. Further, we agree with staff that the authorities should use any oil revenue windfall to clear domestic arrears and/or retire public debt.

We welcome the January decision to abandon the peg and move towards greater exchange rate flexibility. According to staff, Angola's external position in 2017 was weaker than implied by medium-term fundamentals, with a relatively large—albeit declining—current account deficit. The defense of the peg last year led to substantial losses of international reserves. Against this background, we welcome the move to greater exchange rate flexibility earlier this year. However, imbalances in the foreign exchange market remain significant, attested by a still large parallel-official exchange rate spread and multiple exchange restrictions. We take note that, despite the decline in net international reserves, staff assesses that "buffers remain substantial given the sovereign wealth fund (FSDEA) assets of about US$5 billion." Could staff clarify if these assets are liquid and marked to market? What volume of resources from the FSDEA would be readily available in case of need?

Recent economic developments have adversely impacted the soundness of the banking sector. Although overall capital levels remain above minimum requirements, non-performing loans represent more than ¼ of total loans, with one state-owned institution (BPC) particularly affected.

Reinforcing capital and liquidity buffers of underperforming banks while accelerating the restructuring of BPC should be priorities. In parallel, we agree that strengthening the AML/CFT framework remains crucial and could help recover correspondent banking relationships (CBR). Although the current use of nested U.S. dollar CBRs may reduce short-term pressures, this solution is costly and unreliable over the medium-term.

We welcome the new government's focus on improving the business environment and governance, including fighting corruption. Compared to other middle-income Sub Saharan African countries, Angola performs relatively weak in doing business indicators. A fragile institutional environment and strong participation of the public sector in the economy have limited private investment. We encourage the National Assembly to swiftly enact the new laws on competition and private investment.

Mr. Merk and Ms. Kuhles submitted the following statement:

We thank staff for its informative report and Mr. Mkwezalamba, Mr. Tivane and Mr. Essuvi for their insightful buff statement. We concur with the thrust of the staff appraisal. Lower oil prices and an unsustainable policy mix in the run-up to the 2017 elections have led to an erosion of fiscal and external buffers and placed the Angolan economy under increasing stress. While growth slowly recovers, significant imbalances remain, such as a high inflation rate, a high fiscal deficit, ongoing decline in reserve buffers, eroding banking sector soundness and imbalances in the forex market. We thus strongly encourage the authorities to continue their reform implementation and maintain the ownership of the macroeconomic stabilization program over the longer term. It will be crucial to decisively implement a comprehensive structural reform package in order to achieve sustainable and inclusive growth going forward.

We take positive note of the envisaged upfront fiscal consolidation to be followed by further gradual adjustment to bring back debt to a sustainable level. The tight fiscal stance appears appropriate given the high gross financing needs in 2018 and elevated public debt levels. In this context, staff's analysis of the debt situation strikes us as rather optimistic. Potential additional fiscal risks include a decrease in oil production as projected by the International Energy Agency and contingent liabilities stemming from state-owned enterprises (SOEs) and the sovereign wealth fund. Against this background, we encourage the authorities to strengthen tax revenue generation and create a broad tax base and not to rely solely on increased oil revenues. Moreover, we encourage the authorities to increase efficiency on the spending side and streamline the wage bill and government consumption. We agree that potential fiscal revenue windfalls should be used to clear domestic arrears and retire public debt. In this context, we welcome the authorities' conservative oil price assumptions in the 2018 budget, limiting room for downside surprises. We agree that a continued gradual fiscal consolidation over a longer time horizon is needed to put public debt firmly on a downward path. This will create much needed fiscal space that could be used for efficient investment in infrastructure and well-targeted spending on social programs.

Regarding monetary policy, we take positive note that the authorities remain committed to maintain their prudent policy stance. The adoption of base money as the new anchor for monetary policy was welcome but we agree that, given still high inflation rates, enhancing the credibility of the new nominal target would help stabilize market expectations. We strongly encourage the authorities to strengthen their efforts to achieve greater exchange rate flexibility and restore the equilibrium in the forex market. This seems particularly warranted in light of the drawdown of reserves due to the previous exchange rate peg to the USD. Moreover, we strongly encourage the authorities to take appropriate actions to eliminate the existing foreign exchange restrictions and multiple currency practices.

While we take positive note that the banking system is generally assessed as being stable, vulnerabilities remain. Subdued lending activity, very high levels of NPLs in state-owned banks and the sector's strong links to the oil production companies present significant challenges to the soundness of the banking sector. We strongly encourage the authorities to remain vigilant, improve the monitoring of the financial sector to avoid a further build-up of vulnerabilities and decisively tackle the identified weaknesses. We agree with staff's recommendations to strengthen the banking system and would particularly highlight the need to fully implement and enforce the AML/CFT regulation.

We strongly encourage the authorities to implement a comprehensive structural reform agenda to diversify the economy, foster productivity growth and improve the business environment. Weak governance, prevailing corruption and inefficient SOEs are important factors which considerably hamper investment and constrain human capital formation. The authorities should thus strive to strengthen their efforts to improve governance, fight corruption, increase transparency and accountability, ensure judicial independence and enforcement of the rule of law, and strengthen institutions and capacities to remove structural impediments to private sector development.

Lastly, we encourage the authorities to improve the quality and timeliness of data provision.

Mr. Leipold and Mr. Spadafora submitted the following statement:

We thank staff for an informative set of reports and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for their candid buff statement. We broadly share the staff's analyses and policy recommendations and offer some additional comments for emphasis.

Angola's economy is recovering from a severe oil price shock in mid-2014, helped by higher oil prices and an ambitious macroeconomic stabilization plan that is being undertaken by the new government to address still significant imbalances.

The new government is commendably focused on restoring macroeconomic stability, primarily through upfront fiscal consolidation and greater exchange rate flexibility; at the same time, to pave the way for stronger and sustained growth in the medium term the government is committed to advancing structural reforms, reforming governance and fighting corruption.

Given the recent large increase in the public debt-to-GDP ratio – which doubled between 2014 and 2016 – we support the gradual improvement in the large non-oil primary fiscal deficit targeted by the 2018 budget and the pace of consolidation suggested by staff through 2023. Adoption of the VAT is clearly instrumental to this end and would help make stable room for additional social programs and public investment. We also agree that the plausible fiscal revenue windfall should be used to clear domestic payment arrears in 2018 and reduce public debt. We would like to know if the authorities have devised a clearer strategy on how to allocate any revenue windfall between these two priorities, given the declared goal of clearing the arrears by 2019 at the latest.

Looking ahead, diversifying the sources of non-oil revenue is key to help insulate the fiscal position from volatile oil prices. To this end, the authorities should seize on the rebound in oil prices and consider establishing a stabilization fund, drawing on the staff's analysis in the SIP.

Gross financing needs for 2018 are planned to be met by a combination of external borrowing (including a new Eurobond issue) and placements of government bonds in domestic banks. We see merit in the staff's advice on better diversifying the financing mix by expanding the use of Eurobonds and we appreciate the reference to paying attention the "right conditions." At the same time, we caution that reliance on external financing should be well-timed at a time of rising interest rates.

The new monetary policy framework, anchored on base money as an operational target, is a major step towards reducing inflation and the current tight stance is appropriate to counter pass-through on prices from the needed depreciation of the kwanza. We also welcome the move to a more flexible exchange rate and support the staff's call to aim at a market clearing exchange rate and a forex market that, rather than acting as a drag on the real economy, can properly support it.

We agree on the need to preserve the stability of the banking system along the lines proposed by staff. Serious problems at the state-owned BPC should be addressed decisively. While the establishment of a state-funded asset management company to tackle very high NPLs is welcome, we share the staff's concerns on Recredit's design features, as well illustrated in Appendix I. On the staff's recommendation to establish a sunset clause to Recredit's operations, while recognizing the risk of an "NPL warehouse" we wonder if this clause could unintendedly lead to disposals of NPLs at fire-sale prices. The staff's comments are welcome.

We welcome the insightful SIP on governance, which adequately reflects the recent approved IMF framework to tackle these issues. The staff's analysis makes clear how weak governance and corruption have major macro-critical implications for Angola, while recognizing the bold measures that the new government has already taken as well as the major challenges ahead. In this regard, enhanced fiscal transparency is instrumental in effectively implementing fiscal policy.

Mr. Alogeel and Mr. Rouai submitted the following statement:

We thank staff for a well-written set of reports and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for their informative buff statement. While economic developments in Angola were mixed since the 2014 oil price shock, it is encouraging that the new Administration is strongly committed to put the economy on the right track and address the significant imbalances and fragilities. In this regard, we welcome the authorities' Macroeconomic Stabilization Program (MSP) centered on fiscal, together with efforts to reduce public debt, eliminate domestic arrears, and improve governance. As the outlook is more favorable, Angola has a unique window of opportunity to strengthen reforms and would benefit, in our view, from a deeper engagement with the Fund, perhaps through a signaling arrangement, that could help the country anchor macroeconomic stabilization, send positive signals to investors, and initiate the needed reforms to improve the allocation of resources and diversify the economy away from the oil sector. Could staff indicate if the authorities have expressed any interest in closer engagement with the Fund?

We are encouraged by the policy adjustment initiated in recent months, including the upfront fiscal consolidation. We appreciate the indication that the 2018 budget is built on the conservative oil price assumption of US$50/barrel, with excess revenues to be used to clear domestic payments arrears and/or retire public debt. In view of recent firming up of oil prices, could staff indicate if the authorities are still considering issuing US$2 billion Eurobond, particularly in an environment of increasing yields? In the same vein, could staff elaborate on the actual implementation of the authorities' strategy of clearance of domestic arrears? Still on fiscal policy, we encourage the authorities to make good use of the joint Bank-Fund TA recommendations to further develop the domestic debt market and to ensure a smooth introduction of the VAT on January 2019.

We welcome staff work on Governance and Economic Performance in Angola in the selected issues paper. This work is relevant and timely as Angola is still perceived as a high-risk jurisdiction with the loss of direct U.S. dollar correspondent banking relationships (CBRs) in October 2016. We appreciate the authorities' commitment at the highest level to address governance vulnerabilities. We encourage the authorities to pay due consideration to staff recommendations detailed in ¶60 to improve governance.

Finally, Angola is among the few member countries that still avail themselves of the transitional arrangements under Article XIV. While we can support the proposed decision, we encourage the authorities to work with staff toward moving gradually to Article VIII status.

With these remarks, we wish the authorities all the success.

Ms. Barron and Mr. Kikiolo submitted the following statement:

The Angolan economy has rebounded from the sharp fall in oil prices in recent years. While activities in the oil sector remain subdued, the non-oil sector is projected to be the lead driver behind medium term growth.

Removing business impediments through structural and legislative reforms is crucial for the development of the non-oil sector to support and achieve sustained and inclusive growth. We look forward to the implementation of the Macroeconomic Stabilization Plan and National Development Plan (2018-2022). We thank the staff for the report and Mr. Mkwezalamba, Mr. Tivane and Mr. Essuvi for their insightful buff statement. We agree with the thrust of staff's recommendations and make the following comments.

The staff and the authorities agree on the need to embark on fiscal consolidation measures over the medium term to put public debt on a downward path. The efforts by the government to harness revenue, particularly from non-oil as well as containing expenditure including on operational costs, is therefore welcome. Noting Angola's low performance on the socio-economic scorecard, we are pleased to note from the buff that the authorities will preserve fiscal space for capital projects and social programs.

We welcome the changes to the monetary and exchange rate policies considering the need to stabilize inflation and correct external imbalances. While we acknowledge that the depreciation helps correct existing misalignments in the real effective exchange rate, could staff shed more light on the inflation dynamics in Angola in terms of the passthrough effects of exchange rate, oil price and other major determinants? We also noted there was limited discussion of inflation in the paper. While inflation showed a downward trend, it remained high at 26.25 percent in 2017. Does staff have any concerns over the level of inflation?

We agree with staff for the authorities to address the banking vulnerabilities discussed in the "Macro-Financial Linkages in Angola" chapter in the selected issues papers. We commend staff for providing the selected Issues paper which gave valuable insights into critical issues that affect Angola. We note in particular the need to strengthen banking supervisory frameworks and associated regulations to achieve financial sector stability. Authorities active participation in international fora and with the private financial institutions to mitigate the loss of Correspondent Banking Relationship is commendable.

We agree with staff recommendations for Angola to implement structural and legislative reforms that promote private sector activities to support sustainable and inclusive growth. We welcome the new administration's commitment to fight corruption which led to the establishment of the specialized anti-corruption unit in March this year. This commitment should be backed up by adequate resourcing in terms of financing and personnel.

We encourage the authorities to address gaps in key macroeconomic statistics and ensure these are provided to the Fund on timely basis.

Finally, we note the extensive list of recommendations that are contained in the report for the authorities to implement. While we broadly agree with the recommendations, could staff set out what they see as the priorities and the appropriate sequencing? And do these align with the priorities in the National Development Plan?

Mr. Sun and Ms. Cai submitted the following statement:

We thank staff for the informative reports and Messrs. Mkwezalamba, Tivane, and Essuvi for the helpful buff statement. We welcome the authorities' efforts in restoring macroeconomic stability, improving governance and the business environment. We broadly agree with the thrust of staff's appraisal and limit our comments to the following for emphasis.

We commend the authorities' efforts in improving their fiscal position through adopting a VAT, as well as streamlining the wage bill and spending on goods and services. More needs to be done to improve the quality of public spending to avoid recurrence of domestic arrears. We share staff's proposal to continue broadening the non-oil tax base and strengthen tax compliance, and adjust domestic fuel prices to reflect changes of international fuel prices. While gross financing needs appear manageable, given the benign external environment, there are still possibilities that the authorities' financing mix could not be achieved. That said, we share staff's view that Eurobond placement could be considered. Could staff elaborate more on the debt burden impact if the authorities rely more on the Eurobond instead of domestic debt issuance?

The Banco Nacional de Angola (BNA)'s tight monetary policy remains warranted considering inflationary pressures. We welcome the BNA's efforts to move to base money targeting and increase the exchange rate flexibility. We encourage the authorities to continue enhancing the central bank's liquidity forecasting and management capacity, with the help from the Fund's technical assistance to strengthen credibility and efficiency of the monetary policy framework. Maintaining financial sector stability should be a priority considering forex liquidity mismatches and high NPLs. We encourage the authorities to closely monitor banks' liquidity position in both foreign and local currencies, and conduct system-wide liquidity stress tests, when appropriate.

In view of the economy's high dependency on oil revenue, the authorities need to continue their efforts to diversify the economy and expand export base. We welcome the authorities' efforts to strengthen governance, fight corruption, and improve the business environment, including by introducing a framework to support competition in domestic markets, addressing monopolistic practices in key sectors, establishing an anti-trust authority, as well as removing FDI entry barriers. We encourage the authorities to continue building institutions with technical assistance, where necessary, and steadily implement the reform measures.

With these remarks, we wish the authorities every success in their policy endeavors.

Mr. Gokarn and Mrs. Roy submitted the following statement:

We thank staff for the documents on Angola and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for the informative buff statement. Given the country's dependence on oil, economic performance has suffered since the oil price crash in 2014, accompanied by a fall in foreign exchange reserves, weakening private sector activity, scaling back of public infrastructure investment, and high inflation. Authorities need to make vigorous efforts towards improving economic conditions, reducing fiscal deficit, improving the health of the banking sector, reducing inflation, and maintaining adequacy of reserves.

The staff report states that the economy's heavy dependence on oil is a challenge for banks. Weak performance of real and financial variables tends to be associated with oil price downturns. Such a situation in a resource-rich nation like Angola calls for accelerating the pace of economic diversification which had been discussed in the earlier Article IV report as well. It is encouraging that with support of the Bank, the authorities have launched a program for diversifying exports and substituting imports that focuses on six priority areas (including easing constraints to doing business) and seeks greater private sector participation. Have any initiatives/projects been undertaken so far to materially quicken the pace of diversification?

After a loss of 40 percent of its forex reserves reflecting largely prioritization of strategic imports ahead of the elections, Angola exited the peg to the U.S. dollar in early 2018 and adopted a more flexible exchange rate regime. The kwanza depreciated by 30 percent to the U.S. dollar. Foreign exchange reserve levels are expected to more than halve from 10.7 months of imports in 2015 to 5.2 months of import cover in 2018. What would the staff propose as a strategy to build up reserves in Angola, especially in view of the recent recovery in oil prices?

The staff report mentions that recent actions have been taken to ease constraints on private investment, including improving legislation to support competition in domestic markets and attract FDI. One such law passed to attract foreign investment relates to scrapping rules that previously forced foreign investors to partner with local firms. As a large share of the FDI flows to (from) Angola reflect liquidity management by oil companies in the context of lack of local capital markets, in the absence of a sustained increase in oil prices, would this relaxation be able to increase FDI flows into Angola? The staff may comment on how this relaxation would affect the transfer of technology into the domestic sector.

The staff report states that the BNA tightened domestic monetary conditions by about 1 percent of GDP by reducing kwanza reserve requirements from 30 percent to 21 percent while eliminating the option for banks to meet this obligation by resorting to T-bills and/or loans to priority sectors. What was the extent of liquidity immobilized by this measure?

The credit market needs to function more efficiently. To contain inflation pressures and gradually address imbalances in the foreign exchange market, the Central Bank of Angola (BNA) has tightened its policy rate to 18 percent, reducing excess liquidity and preserving reserve buffers. However, this has also led to reduced private sector credit off-take. Due to weak economic activity in the last three years, banking sector soundness has been eroded with NPLs reaching 28.8 percent of total credit at end-2017 growth. The staff report expects credit growth to increase significantly to 27.2 percent in 2018 from 1.3 percent in 2017, shored up by resumption of economic activity, clearance of domestic payments arrears, and NPL resolution at state-owned banks. For NPL resolution, the primary reliance is on the state-funded asset management company, Recredit, which has agreed to acquire a large portion of the distressed assets. BNA has noted that resolving NPLs would be contingent on Recredit, which did not fall under its supervisory purview. The resolution of NPLs seems to be entirely predicated on the performance of Recredit. If Recredit is not able to speedily clean up the NPLs, how would this affect the expected pace of credit recovery in 2018? Are there any other modalities of cleaning up the NPLs?

Ms. Pollard and Ms. Svenstrup submitted the following statement:

We welcome the Angolan authorities' ambitious macroeconomic program, which has already helped stabilize inflation and, combined with higher oil prices, contributed to more favorable fiscal and growth outlooks for 2018. Angola still faces considerable risks, and more work is needed to fully entrench stability and rebuild external and fiscal buffers. Structural reform—particularly addressing endemic corruption and governance deficiencies—will also be critical for Angola to reap the full benefits of the current stabilization process. Continued high-level ownership will be needed to sustain reform momentum amidst these challenges and tackle long-standing vested interests.

Governance and corruption: We commend the authorities' recent efforts to root out high-level corruption, including the dismissal of top officials at Sonangol and the sovereign wealth fund. The Angolan economy has for too long been synonymous with weak governance and endemic corruption, including at the highest levels of government—a problem that has underpinned Angola's myriad complex structural challenges. Decades of non-transparent allocation of oil resources has discouraged investment and diverted resources from the country's vast development needs. Strong and unwavering credibility on tackling corruption and governance issues is critical to incentivize private investment and lay a foundation for more inclusive and diversified growth. To this end, we appreciate the new administration's firm commitment to continue strengthening governance and fighting corruption, as outlined in Messrs. Mkwezalamba, Tivane, and Essuvi's helpful buff statement.

Given the clear macro-critical significance of this issue in Angola, we welcome staff's in-depth coverage in the staff report and especially in the selected issues paper. We found the analysis to be appropriately consistent with the Board-approved Framework for Enhanced Engagement on Governance, which this Chair strongly supports. We particularly appreciated the SIP's analysis of the potential gain in GDP per capita from addressing weak governance and corruption. Given high inequality in Angola, could staff also discuss the impact of tackling these issues on inclusive growth? However, we would have liked to see more direct language on the nature and macro-critical effects of corruption, including high-level corruption, in the staff report. Moreover, staff should have integrated the SIP's key messages on corruption more forcefully into the main report—for instance in the Key Policy Recommendations—which would have more clearly illustrated the urgency of addressing this issue.

We also appreciated staff's comprehensive discussion of the various reforms underway across areas such as establishing a clear legal framework, strengthening fiscal transparency and governance, and improving the business climate. The list is indeed broad and ambitious, and we wonder if staff and the authorities have discussed prioritization and sequencing. The staff's comments are welcome. Additionally, while some of the measures are technical in nature, others will require tackling vested interests and reconciling competing mandates between government agencies. For example, there appears to be overlap between the newly created anti-corruption agency within the Ministry of Interior and the existing DNPCC. Could staff discuss any updates on how these two units will operate in practice? Have staff discussed any plans for asset recovery with the authorities?

We welcome the authorities' focus on strengthening the AML/CFT framework as part of its macroeconomic program. We urge the authorities to work to demonstrate effectiveness of its AML/CFL framework, which is the focus of the FATF mutual evaluations, and not just comply with the FATF 40 Recommendations as paragraph 53 of the SIP recommends. Further, to maintain and eventually regain correspondent banking relationships, we would emphasize the importance of improving and effectively implementing AML/CFT regulation. This is currently listed as one of many actions in paragraph 25 of the staff report, but we believe it should be highlighted more prominently as the top priority.

Exchange rate policies: We welcome the BNA's move to a more market-determined exchange rate regime, which will help rebuild external buffers and improve competitiveness. We strongly concur with staff's recommendation that the authorities design and implement a strategy to eliminate exchange restrictions and multiple currency practices, in line with their obligations under Article VIII. We found staff's analysis of these foreign exchange policy measures in Figure 9 to particularly helpful – certainly the clearest presentation of these issues we have seen in a country report to date. We recommend that Figure 9 be a template for surveillance work going forward.

PCI request: Finally, we understand that the authorities have requested a Fund-supported Policy Coordination Instrument. We welcome this discussion, given the window of opportunity for meaningful reform in Angola. It will be critical that any program be based on a robust range of policy actions to support the credibility of both the authorities' reform agenda and the new instrument itself. In particular, we would like to see clear benchmarks on economic governance—including increasing the transparency of fiscal accounts and concrete steps to combat corruption at all levels of government—as well as steps to remove exchange restrictions and multiple currency practices. Further, we expect that the ambitious fiscal adjustment plan will prioritize spending on areas that would boost inclusive growth and incorporate a minimum threshold for social spending. We would also welcome specific benchmarks to protect the poor and reduce income inequality.

Mr. Ostros and Ms. Gunnarsdottir submitted the following statement:

We thank staff for the set of reports and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for the informative buff statement. Angola continues the recovery from the oil price shock in 2014. Its outlook, however, rests on the authorities' decisiveness to follow through with their action plan of containing public debt and implementing structural reforms for higher and more inclusive growth. We share the thrust of the staff appraisals and make the following comments for emphasis.

Fiscal consolidation to contain the elevated public debt remains key for Angola, particularly as buffers were eroded during last year's election year. We welcome the new government's emphasis on restoring macroeconomic stability and tackling corruption. The medium term fiscal strategy is rightly focused on fiscal consolidation, with the aim of reducing the wage bill and enhancing revenue mobilization. Furthermore, expenditures shall be prioritized towards development needs and social outlays, which are currently insufficient. Measures to widen the tax base remain vital, including the introduction of a VAT and enhancing tax compliance. We agree with staff that any fiscal revenue windfalls shall be used to clear domestic arrears and/or to retire public debt. We take positive note of the authorities' intentions to fully implement a medium-term fiscal framework, with focus on spending rules and a fiscal stabilization fund to reduce the pro cyclicality in spending.

Given Angola's high gross financing needs, vulnerabilities to changes in the external environment, and the intention to issue a Eurobond, we wonder if the market conditions are still as favorable as at the submission of the staff report? What are the market interest rates compared to other available borrowing sources and how much of Angola's outstanding debt is in concessional terms?

Given the high dependence on oil, diversification of the economy should be the primary focus going forward. We welcome the authorities' National Development Plan in this regard. Quality public investment to close infrastructure gaps and effort towards human capital development, for example by enhancing the education system, are key to support this adjustment. Addressing the impediments of doing business to strengthen the role of the private sector in the economy is also crucial for further economic development. The continuation of fighting corruption also plays an important role in this context, as weak governance and challenging business climate create opportunities for corruption and entrench vested interests. We commend staff for good coverage of this issue in the selected issues

We welcome the move towards a more flexible exchange rate and that imbalances in the FX market are being addressed. Further efforts are still needed to strengthen monetary policy effectiveness and the credibility of the new nominal anchor needs to be enhanced to stabilize market expectations. We agree with staff that a strategy should be designed to eliminate the existing exchange restrictions and multiple currency practices.

The financial sector's resilience needs to be strengthened, with high level of NPLs and FX liquidity mismatches at some banks as sources of concern. Completing the second phase of banks' asset quality reviews will be welcome in this regard, to inform on banks capitalization needs. In addition, the authorities should continue strengthening the regulatory and supervisory frameworks, in line with relevant international standards, and further work on strengthening the AML/CFT framework to counteract the loss of correspondent banking relationships.

Lastly, we encourage the Angolan authorities to further work on enhancing the data supply, in particular the quality and timeliness of fiscal and balance of payments data, including the operational balance of SOEs, coverage of non-financial corporations for monetary statistics and strengthen the monitoring of domestic payments arrears, as noted in the staff report.

Mr. Beblawi and Mr. Mojarrad submitted the following joint statement:

We thank staff for the well-written papers, and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for their informative buff statement. Angola's oil-reliant economy is still adjusting to the oil price shock. The authorities' policy response made some initial inroads, but adjustment stalled in the run-up to the 2017 elections, as higher government spending combined with the currency peg further eroded the internal and external balances. We are encouraged that the authorities under the new administration have strengthened policies in early 2018 within the frameworks of the Macroeconomic Stabilization Plan (MSP) and the 2nd National Development

Plan (NDP). As recognized in these initiatives, and supported by firmer oil prices, a sustained program of fiscal adjustment to put public finances on a sound footing and rebuild buffers to guard against the vagaries of the oil market, and greater exchange rate flexibility to accelerate external adjustment, coupled with long-term structural reforms to improve the business climate and governance, would go a long way in restoring Angola's macroeconomic balances and laying the foundation for sustainable and inclusive growth. We agree with the thrust of the staff appraisal and support the proposed decision on exchange restrictions.

The 2018 budget is a good start: it envisages a 2 percentage points of GDP reduction in the non-oil primary fiscal deficit (to 8.8 percent of GDP), reflecting higher oil taxes, elimination of water and energy subsidies, and restrained spending on wages and goods and services. Oil prices in 2018 are likely to be higher than the budget assumption, and we are encouraged that the authorities intend to use the oil windfall to clear domestic arrears and retire public debt. Over the medium-term, fiscal policy should continue to focus on sustained consolidation of the non-oil primary deficit to firmly anchor public debt reduction within a medium-term fiscal framework, while creating fiscal space to accommodate infrastructure spending and social programs. The longer-term structural fiscal reforms and improvements in the quality of public spending—as set out by Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi—are well placed, especially: introducing a VAT in 2019; reforming and streamlining public administration and pay awards; reforming state-owned enterprises; and improving the quality of public investments.

We welcome the recent moves by the Banco National de Angola (BNA) towards greater exchange rate flexibility. The premium that the parallel rate holds on the official rate has narrowed but remains substantial. The inflation rate has declined significantly since 2016 through tighter monetary policy, but is still elevated, and further price pressures are expected from the pass-through of the recent sharp currency depreciation, underscoring the need for an even tighter monetary policy stance that is recognized by the authorities. We take note of the shift to base money growth as the new operational target that should be set in line with achieving lower inflation and maintaining positive real interest rates. We concur with staff on the need for continued improvement in the BNA's liquidity forecasting capabilities, including its analytical toolkit, and enhancing the effectiveness of monetary policy instruments.

In the financial sector, the introduction of a new liquidity requirement to curtail banks' net forex liquidity position and strengthening banks' capital positions are welcome. In paragraph 22, we note the recent BNA directive to increase commercial banks' minimum regulatory capital requirement threefold by the end of the year. How confident is staff of full compliance in such a short time frame, especially in case of heavily undercapitalized banks? We also note the projected growth in credit to the private sector by 27 percent in 2018 (figure 5), which could warrant strengthened supervisory oversight by the central bank. While this follows two years of no credit growth, could staff provide additional information on this increase and indicate how the central bank plans to mitigate potential risks in this area? We are encouraged that an asset management company—Recredit—has been set up to clean up banks' high NPLs that are mostly concentrated in state banks and related to politically exposed persons. However, according to staff, some critical features that are common in typical asset management companies are lacking in Recredit. Are the authorities planning to rectify these shortcomings? We also support the staff recommendation to set a sunset clause for Recredit operations given the concentration of NPLs in one state bank. We take positive note of the authorities' efforts to strengthen the AML/CFT framework in line with the 2010 assessment and to engage regulators in parent jurisdictions and maintain open channels between domestic and foreign banks to gradually restore corresponding banking relationships.

The government's structural reform agenda embodied in the 2nd NDP is rightly focused on encouraging private investment and facilitating economic diversification by improving the business climate, strengthening governance, and fighting corruption. The recent legislative initiatives in support of competition in domestic markets and FDI entry, and the presidential order to establish a specialized anti-corruption unit are welcome. The authorities should continue to build capacity and strengthen state institutions in support of the reforms, drawing on technical assistance from the Fund, the Bank and other partners.

We wish the authorities all the success with their economic policies going forward.

Mr. Just and Mr. Varga submitted the following statement:

We thank staff for the well-written set of reports, and Messrs. Mkwezalamba, Tivane, and Essuvi for their helpful buff statement. We commend the authorities' efforts to stabilize the economy after the unsustainable policy mix in the run-up to the elections. We echo staff's advice to restore fiscal sustainability, move to a fully flexible exchange rate regime over time, reduce corruption, and address the misallocation of resources and opacity to enable higher growth. We encourage the authorities to use the environment of higher-than-budgeted oil prices to clear arrears as well as reduce debt levels faster and with less burden on the population. While we can support the proposed decision, we call on the authorities to develop a medium-term plan to gradually eliminate their Multiple Currency Practices (MCPs).

To put fiscal accounts on a sustainable downward trend, the authorities should increase the share of non-oil revenues and adjust expenditures. We welcome the authorities’ commitment to a front-loaded fiscal adjustment, as well as the intention to use the higher-than-budgeted oil revenue to reduce debt and clear arrears. We support the planned introduction of VAT in the beginning of 2019 and, as 50 percent of non-oil revenue still comes from large enterprises, encourage the authorities to broaden the non-oil tax base and strengthen compliance. In order to stabilize expenditure but also to reorient it toward combatting rampant inequalities, the authorities should reduce fuel subsidies and streamline the wage bill. The recently announced plans for privatizing (large) state-owned entities as well as the ambition to continue with the restructuring efforts of the state oil company Sonangol are good steps to mitigate contingent liability risks and further reduce fiscal risks, which is all the more necessary in view of the significantly increased debt burden. We welcome staff’s views on the usefulness of more proactive debt operations, including issuing Eurobonds, to lengthen and smoothen the debt profile. This will require more transparency on quasi-fiscal debt levels, in addition to more prudent macroeconomic policies. The staff’s comments would be appreciated on the prospects of Angola tapping Eurobond markets in the foreseeable future, as well as an indication of the likely spread.

The current tight monetary stance is appropriate and the authorities should complete the transition to a fully flexible exchange rate regime. The enhanced exchange rate flexibility has helped ease pressures on international reserves, and reduced the significant imbalances in the nominal and real exchange rates. However, the remaining restrictions and preferential forex market auctions keep the exchange rate overvalued and perpetuate the existence of a parallel exchange rate market. This is ultimately dragging growth and is bolstering vested interests. Angola maintains several exchange restrictions and MCPs subject to Fund approval, as well documented in Figure 9. We are concerned about the absence of a monitorable strategy by the authorities to address these restrictions and ideally remove them. Can staff comment on their discussions with the authorities on the way forward to remove these exchange restrictions under Article VIII, as well as on the MCPs and whether the Fund has the necessary tools to help the authorities comply with the Articles of Agreement?

Strengthened governance and a more effective fight against corruption is critical to achieve private sector-led growth. We welcome staff's focus on governance in the selected issues papers, which strike the perfect balance between the use of economic governance factors based on the Fund's own information, and third-party indicators. Poor governance and corruption are persistent issues in Angola, with the country ranking lowest on governance and corruption indices. Therefore, we broadly welcome the President's announcements to improve governance and combat corruption, also reassured by Mr. Mkwezalamba in his buff statement. We encourage the authorities to implement the measures identified by staff, most notably the establishment of an anti-corruption agency; increase fiscal transparency; and ensure compliance with AML/CFT regulation.

These measures, together with staff's well-formulated capacity development strategy, will help Angola not only to become a more attractive destination for foreign investment, but could also restore its direct access to U.S. dollar correspondent banking relationships.

Mr. Palei and Mr. Snisorenko submitted the following statement:

We thank staff for their comprehensive report and insightful selected issues papers. We also thank Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for their informative buff statement. Angola is gradually recovering from the oil price shock. Growth rate is estimated at one percent in 2017 and is projected to increase to 2.2 percent in 2018. However, last year was marked by further erosion of fiscal and external buffers. Overall fiscal balance widened to six percent, while the NIR fell by 36 percent and are projected to decline further. Still high inflation and impaired foreign exchange allocation system delay the restoration of macroeconomic stability. Given the formidable policy challenges in Angola, we commend the authorities for their commitment to gradual fiscal consolidation and envisaged improvements of the monetary policy framework.

While fiscal deficit is likely to decline to two percent of GDP in 2018, debt-to-GDP ratio remains high and is likely to rise to 73 percent in 2018. High public debt points to the need for further efforts to put it on a downward path. We agree with staff that the objective of lowering the public debt-to-GDP ratio to the level below 60 percent over the medium term articulated in the authorities' Macroeconomic Stabilization Program provides a useful fiscal anchor. We note that the stress tests conducted in the DSA show that Angola's public debt remains highly vulnerable to growth, exchange rate, oil price, and contingent liability shocks. In this context, we find the analysis in one of the SIP chapters of possible creation of a well-designed fiscal stabilization fund to be timely and highly relevant. Such a fund could reduce the inherent pro-cyclicality of spending, insulate public investment from oil price volatility, and promote sustainable non-oil GDP growth. From the DSA we also noted that there is no information on private sector external debt. Do staff have estimates of its possible size?

Improvements in the monetary and exchange rate policies are likely to facilitate sustainable recovery. Inflation fell from 42 percent in 2016 to 26 percent in 2017, and staff expect it to remain at this high level in 2018. We note, however, that in the beginning of this year the pass-through effect surprised on the low side, and it led the authorities to be more optimistic in their projections of inflation. Can staff comment on the various estimates of the pass-through effect and its impact on inflation projections for 2018? Adoption of the base money targeting and greater flexibility of the exchange rates are welcome steps toward improving the monetary policy framework. We encourage the Angolan authorities to develop a robust strategy to eliminate existing exchange restrictions and multiple currency practices. This will require developing the liquidity management system, an open market operations framework, and a well-functioning foreign exchange market. Could staff elaborate on the main measures, which would help the authorities to avoid further NIR losses in 2018?

Banking system was affected by the weak performance of the economy and impaired access to foreign exchange liquidity. We note the subdued lending and high NPLs. As the analysis in the SIP on macro-financial linkages suggests, the health of the banking system in Angola is heavily dependent on oil price dynamics and is closely linked to the sovereign's performance. Against this background, we agree with the recommendation to carry out a comprehensive asset quality review with subsequent cleaning up and strengthening of banks' balance sheets. The authorities need to improve the AML/CFT framework and restore correspondent banking relationships.

Diversification of the economy and promotion of the private sector-led growth remain the top priorities for Angola. In this respect, we welcome the recent revision of the Private Investment Law and the approval of new Competition Law. Going forward, the authorities' structural reform agenda should aim at improving the business environment. Given that Angola ranks 175 in the Ease of Doing Business ranking, the authorities in cooperation with the World Bank could design a plan to simplify regulation and cut the excessive number of procedures required to conduct business. We also agree with staff that human capital bottlenecks are significant obstacles to economic development and should be an important part of the structural reform agenda. In this context, recalibration of the social spending strategy including the introduction of the efficient CCT program is warranted.

Further reforms are also needed to strengthen governance and fight corruption. We welcome the list of measures proposed in the SIP on Governance and Economic Performance in Angola. We also welcome staff's attention to the evidence-based indicators, such as the ones in the Doing Business database. More importantly, staff should rely even more on their own analysis of fiscal transparency, AML-CFT, and other relevant areas.

With these remarks, we wish the authorities further success.

Mr. Lopetegui and Mr. Corvalan Mendoza submitted the following statement:

We thank staff for the report and selected issues paper (SIP) and Mr. Mkwezalamba, Mr. Tivana and Mr. Essuvi for their informative buff statement.

The oil price shock in mid-2014 hit the economy of Angola hard and it is still slowly adjusting. Few buffers were built at the time of high oil prices and now in difficult times, limited space contraints the priority investments needed to support non-oil GDP growth. GDP growth is slowly recovering from 1 percent in 2017 and it is projected to be 2.2 percent in 2018, pushed by the recovery of the non-oil sector and oil prices and an expected improvement of macroeconomic fundamentals. Inflation declined to 26.3 percent in 2017 and is expected to decrease to 23 percent in 2018.

Angola's window of opportunity for the economy is twofold. On the one hand, the external sector might yield a positive shock driven by an increase in oil prices, while on the internal front, some positive signs to accelerate reforms and improve the governance coming from the new government might boost confidence for domestic and foreign investors. We concur with the new authorities' macroeconomic stabilization plan launched earlier this year to address macroeconomic imbalances, restore the equilibrium in the forex market, and apply an upfront fiscal consolidation while at the same time, safeguarding the fiscal position from volatile revenues from oil.

Taking into account the more favorable oil price outlook for the economy, it makes good sense to accelerate steps toward setting up a market-clearing exchange rate mechanism, while unwinding exchange rate restrictions and multiple currency practices. The experience of multiple exchange rates in global history has always ended badly. Given the spread and volatility between the parallel-official exchange rate, swift measures are needed to reduce the gap.

Important challenges lie ahead to further improve social indicators and attack poverty and inequality, as well as modernize and diversify the economy. As described in the staff report, the country underinvested for too long in human capital and public infrastructure. The strong reduction in these two spending components, during the hostilities that ended in 2002, increases the urgency to tackle the demand for public goods. We encourage the authorities to increase revenues and prioritize expenditures and to stick to the macroeconomic stabilization program launched earlier in 2018 to avoid potential slippages in its implementation.

The section of the SIP on "Governance and Economic Performance in Angola" caught our attention. We encourage the authorities to redouble their efforts to enhance the quality of governance and reduce corruption perceptions. As described in the SIP, improvements on this front could increase real GDP annual growth by up to 2 percentage points. We are aware of the process of State building continuity since the end of the long civil conflict in 2002, but, 16 years later, there is still ample room to catch up with its peers in sub-Saharan Africa on good governance and combating corruption.

We encourage the authorities to accelerate the processes to deal with the financial institutions that are dragging down the economy and to reinforce the supervision of these institutions to avoid any costly slippage. Could staff give more details on state-owned banks' high NPLs and the time frame envisaged to solve this situation?

With these comments, we wish the people of Angola every success in their future endeavors.

Ms. McKiernan and Mr. Williams submitted the following statement:

We thank staff for their comprehensive set of reports and Messrs. Mkwezalamba, Tivane and Essuvi for their informative buff statement. It was rather unfortunate that certain political decisions in the run-up to the 2017 elections derailed the nascent economic recovery following the 2014 oil price shock. Nevertheless, we take positive note of the authorities' meaningful steps to restore macroeconomic stability and promote inclusive growth through a number of initiatives outlined in their Macroeconomic Stabilization Program, and National Development Plan. We broadly concur with staff's assessments and recommendations and offer the following remarks for emphasis.

Looking ahead, an appropriate macroeconomic policy mix will be critical to delivering the authorities' economic development goals. We are encouraged by the recent pickup in economic activities, with expectations of a steady rebound over the medium term. This outlook however relies on continuing the path of fiscal consolidation, as well as maintaining the monetary policy stance aimed at further reducing inflation, and supporting greater exchange rate flexibility. In this regard, the authorities' 2018 budget that reduces the non-oil primary deficit by 2 percentage points of GDP is a step in the right direction and should be augmented by further actions to mobilize non-oil revenue over the medium term. Moreover, a strong fiscal stance will be critical to maintaining the debt at sustainable levels amid the risks posed by tighter global financial conditions. Given the expected impact of the fiscal adjustment on vulnerable groups, we support the authorities' initiatives to improve social protection, with the help of development partners. While we welcome the recent decision by the authorities to adopt a more flexible exchange rate regime, we also encourage them to eliminate foreign exchange restrictions and multiple currency practices as soon as possible.

Further structural reforms are needed to bolster the resilience of the economy and support inclusive growth. The risks posed by oil price volatility underscore the need for the authorities to complement sound macroeconomic policies with structural reforms that support private investment in the non-oil sector. In this regard, we welcome efforts aimed at reducing corruption and enhancing governance, alongside others to improve the regulatory and operational environment for businesses, including the authorities' draft Private Investment Law. These initiatives are integral to promote diversification, shield the economy from fluctuating oil prices, and invigorate growth. A sound financial sector will be critical to support these initiatives. In this context, we welcome actions to strengthen the AML/CFT framework and enhance the capital requirements, and we agree with staff that the authorities should move decisively to strengthen governance at state-owned banks. We invite staff to elaborate on the likely impact from the threefold increase in regulatory capital requirement.

Finally, we urge the authorities to quickly resolve internal data discrepancies. Based on staff's assessments, adopting the National Institute of Statistics' nominal GDP rather than that provided by the Ministry of Economy and Planning would lower the Debt/GDP below the authorities' medium-term target of 60 percent. Can staff comment on how this lower debt ratio would impact the DSA and their recommended fiscal adjustment?

Mr. Saito and Mr. Komura submitted the following statement:

We thank staff for the comprehensive reports and Messrs. Mkwezalamba, Tivane, and Essuvi for their informative statement. As Angola economy highly relies on the oil industry, lower oil prices since 2014 has dampened significantly its economic activities. Looking ahead, we welcome that its economic outlook is favorable in the medium-term, while it depends on the successful implementation of reforms as the staff report points out. In this regard, we support that the Government of President João Lourenço has focused on restoring macroeconomic stability, improving governance and business environment. We believe that those reforms would help Angola to fully demonstrate its high potential. As we broadly agree with a thrust of staff appraisals, we will make a few comments for emphasis:

Fiscal Policy

Fiscal consolidation is warranted to put public debt on a clear downward pass. It is disappointing that fiscal policy was loosened in the run-up to the election, with the underlining overall fiscal deficits worsened to 7 percent of GDP in 2017. Against this backdrop, the authorities should proceed with fiscal consolidation to entrench public debt sustainability. In this regard, we welcome the budget for 2018, which includes a set of measures aimed at scaling back public expenditures and intensifying non-oil revenue mobilization. Furthermore, we also welcome that the macroeconomic stabilization program (MSP) specifies concreate measures for fiscal consolidation, such as adopting a VAT and streamlining the wage bill. This would help to create space for much needed public investment and social program. Could staff comment on whether recent public infrastructure investments have been selective enough? Regarding gross financing needs (GFN), staff mentions that the substantial financing needs in 2018 are expected to be met by domestic and external sources, including bilateral creditors. Does staff expect any financing difficulties after 2018?

Monetary and Exchange Rate Policy

The authorities need to achieve rebalancing the FX market while containing inflationary pressures. We agree with staff that greater exchange rate flexibility would help to preserve external buffers and improve competitiveness. At the same time, inflation rates remain high although it declined recently. Against this backdrop, the authorities should carefully calibrate its monetary and exchange rate policy, taking into account the inflationary pressure stemming from depreciation of kwanza. In this context, the authorities' commitment to upgrade monetary policy framework, including strengthening capacity for liquidity and inflation forecasting is welcomed. As the BNA has moved to base money targeting, we would like to ask staff whether the relationship between base money and inflation has been stable in Angola. Related to this point, could staff comments on whether the recent pace of contraction of base money is sufficient to contain inflation pressures?

Structural Reform

The authorities' reform agenda appropriately includes improving governance, fighting corruption, and making business environment better. We highly welcome recent efforts on strengthening governance and combating corruption, including creating a specialized anti-corruption unit. Steady implementation of reforms in this area would help Angola to build a solid foundation for private sector led growth. In this regard, as the staff report indicates implementation risks due to weak institutional capacity, we encourage the authorities to closely communicate with the Fund to steadily implement vital reforms with clear prioritization and capacity development.

Ms. Villa and Mr. Alias submitted the following statement:

We thank staff for the insightful set of reports and Messrs. Mkwezalamba, Tivane and Essuvi for their useful buff statement.

The Angolan economy continues to face major challenges from the oil price shock in 2014. The lower oil price and unsustainable policy mix in the run-up to the August 2017 election led to further erosion of fiscal and external buffers, and placed the economy under stress. We welcome that, despite these challenges, the economy is experiencing a recovery, with a favorable outlook for 2018 and a higher annual growth outlook of 5 percent over the medium-term. The relatively positive outlook for oil prices provides the opportunity to further stabilize macroeconomic conditions, focusing on entrenching debt sustainability and strengthening the external position, as well as implementing structural reforms for higher and inclusive growth. We broadly concur with the staff appraisal and make the following remarks for emphasis.

Angola's public debt is high and debt dynamics are sensitive to macroeconomic shocks. We therefore encourage the authorities to stay the course to put the public debt-to-GDP ratio on a clear downward path. We welcome the front loaded non-oil primary fiscal balance consolidation based on conservative oil price assumption, and support staff's recommendation to use the fiscal revenue windfall to clear domestic payments arrears and/or retire public debt. Could staff share if there is already a firm plan to clear the domestic payment arrears should the oil price outturn be higher than the baseline? We agree that VAT would provide a broad-based and more stable fiscal revenue stream and strongly encourage the authorities to press ahead with its implementation. We are pleased to note that the authorities broadly agreed with proposed measures to improve medium-term fiscal sustainability and the quality of public spending, that are listed on pages 9 and 10 of the staff report. Given this long list of measures, it may be more beneficial to authorities if staff would recommend prioritization of a set/subset of these measures that they believe would significantly improve the fiscal position in the next 2 to 3 years, consistent with local institutional capacity. We are also interested to know how staff prioritize the works listed in the joint IMF-World Bank Management Action Plan (page 5 of Informational Annex report). The staff's comments are welcome.

We support an orderly transition to a more flexible exchange rate regime that is supported by a robust monetary policy framework. A flexible exchange rate regime should act as the first line of defense against external shocks and provide opportunities to accumulate adequate buffers. We thus encourage authorities to strengthen monetary policy effectiveness through, among others, the active use of open market operations, enhancing liquidity forecasting capabilities and instruments, and analytical toolkits. The removal of exchange rate restrictions and multiple currency practices would help restore confidence in the exchange rate market. We urge the authorities to prioritize setting a clear timeframe for the unification of the exchange rate system.

Preserving the health of the banking sector is crucial to support the economic recovery. The persistently high NPLs could significantly limit the banks' ability to extend credit to the private sector and hamper economic recovery. In this context, we support staff's recommendations to intensify efforts to complete the asset quality review and recapitalize banks. The limit on banks' daily net forex liquid position is a welcome measure to help reduce forex liquidity mismatches and promote risk diversification. We also encourage the authorities to strengthen the AML/CFT framework to be better positioned for the 2020 mutual evaluation assessment of the framework. We note the authorities have made significant progress to address concerns on loss of CBRs, although measures taken by the authorities appear inadequate according to the staff report. Could staff comment on further measures to be taken to mitigate the loss of CBRs.

The structural reform agenda should focus on fostering private sector-led growth and economic diversification, through strengthening public sector management and institutional capacity. In meeting these objectives, we view as crucial the measures to improve the country's appeal as an investment destination, including the passage of the Competition and Private Investment Laws that are meant to further strengthen the legal framework for public-sector efficiency. We therefore urge the authorities to ensure the effective implementation of these measures. Moreover, the authorities' determination to improve governance and address corruption in the public sector are commendable. It is our view that political ownership at the highest level must be sustained. This is necessary for the successful implementation of economic reforms and to allow the economy to reap higher growth dividends over the medium and long term.

With these remarks, we wish the authorities further success.

Mr. de Villeroché, Mr. Castets, Mr. Bellocq, Ms. White and Ms. Stockill submitted the following statement:

We thank staff for an insightful set of reports and Mr. Mkwezalamba, Mr. Tivane and Mr. Essuvi for a helpful buff statement.

Angola is experiencing a slow recovery with protracted financial and fiscal imbalances resulting from the decrease of oil prices and the unsustainable policy mix in the run up to the August 2017 elections. Against this challenging background, we welcome the adjustment strategy that the new government has implemented since early 2018, as well as the willingness of the new government to enhance governance and fight against corruption. On governance issues and their links with economic performance, we value the in-depth analysis provided in the selected issues and we agree with staff's recommendations: enhancing fiscal governance should remain a key objective and we consider that Angola currently has a window of opportunity to make significant progress in that field. Could the staff provide more details about the creation of the specialized corruption-unit which was recently announced by the Authorities of Angola?

On the fiscal side, we agree with staff that a gradual fiscal consolidation should be implemented over the medium-term. We note positively that under the Macroeconomic Stabilization Program (MSP), the authorities' objective is to bring back the public debt-to-GDP ratio to below 60 percent over the medium term. We fully support this objective, notably for bringing down the large Gross Financing Needs (22 percent of GDP this year) which is weighing on the financial and economic outlook of Angola. The medium term fiscal consolidation will be implemented through a mix of measures combining the introduction of a VAT and the streamlining of wage bills and other spending on goods and service. We note the risks associated with the authorities' domestic borrowing plans, and welcome steps towards diversifying the financing mix (for example through the recent Eurobond issuance). Additionally, we encourage the authorities to pay close attention to staff's recommendations in the SIP on oil revenues to reduce procyclicality and increase productive investment.

We would have appreciated further details regarding the authorities' Domestic Resource Mobilization strategy, notably the strategy for developing non-oil taxation. Indeed, we are concerned by the poor performances which have been observed with non-oil tax revenue since 2010 (non-oil tax revenue reached 7.8 percent of GDP in 2010; 8.1 percent of GDP in 2013; 5.8 percent of GDP in 2017). Moreover, under the baseline scenario, the non-oil tax revenue is only projected to reach 8.2 percent of GDP in 2023, a level similar to the one observed in 2013. As in the last Article IV review (presented to the board on January 18, 2017), the staff's report highlights that the authorities will introduce VAT in January 1st, 2019. Could the staff provide further details on concrete steps taken since the last Article IV review to implement this critical reform? According to staff's estimates, what are the additional revenues this reform could result in? Regarding real estate taxation (mentioned in paragraph 16), the staff considers that better enforcement is needed. Could the staff provide the level of public revenues coming from real estate taxation and further elaborate on the reason why better enforcement is needed? Additionally, we would have appreciated the inclusion of analysis on the distributional impact of the recommended tax measures.

With regard to the banking system, ongoing efforts are needed to strengthen asset quality and ease liquidity pressures. We encourage the authorities to remain committed to addressing balance-sheet vulnerabilities coming from currency mismatches and, in the case of public banks, poor asset quality. We also encourage the Central bank to keep on strengthening the AML-CFT framework.

Over the long run, diversification is key for fostering the economic growth of this highly oil-dependent economy. We agree with staff that improving the business environment is critical, in particular when it comes to the insolvency framework, contract enforcement and access to banking credit. The Law on Competition recently approved in a first-round vote by the National Assembly is also a step in the right direction in dealing with monopolistic behaviors. Regarding the program recently set up for promoting export diversification and import substitution (PRODESI) which targets six sectors, we would like staff to provide more details about the economic policy tools that will be engaged for implementing this program.

We encourage the Angolan authorities to maintain an open and frank dialogue with the IMF and to continue to seek Fund advice and support to help maintain reform momentum. Any update from staff on this would be appreciated.

Finally, we thank staff for presenting us with the Capacity Development strategy in annex to the report. Going forward, a clearer prioritization of the main areas of focus might be helpful.

Mr. Mkwezalamba made the following statement:

I would like to make two points. One relates to the illegal capital repatriation bill, which has been submitted to parliament, as we noted in our buff statement. I wanted to inform the Board that the bill was passed into law yesterday.

The second point relates to deepening engagement with the Fund. I know the questions that have been raised, but I have also been approached by some colleagues, particularly about the request by the authorities for a Policy Coordination Instrument (PCI), and I wanted to confirm that the authorities did submit an official request at the end of May to support the implementation of their reform agenda, and they did follow up with management and the staff during the Spring Meetings. But given that this is one of the questions that the staff will address in this meeting, I will leave it to staff to provide the details.

Mr. Tranbinski made the following statement:

> I thank the staff for a well-written report and selected issues paper, and Mr. Mkwezalamba, Mr. Tivane, and Mr. Essuvi for their buff statement. The recently launched macroeconomic stabilization program and second national development plan indicate the newly elected government's commitment to stabilizing the economy and facilitating more inclusive growth. Having said that, I would like to make one specific comment.
>
> Referring to the point made by Ms. Pollard and Mr. Alogeel in their gray statements, and considering the more favorable economic outlook in Angola, we would like to tackle the issue of the potential PCI request from the Angolan authorities. The country has an opportunity to strengthen its economy and implement needed reforms; and in that context, we would welcome a frank discussion on potential deeper engagement with the Fund. Such an engagement could help further stabilize the economy, provide additional incentive for the authorities to implement reforms, enhance further diversification away from the oil sector, and build up the credibility of the newly-appointed government. Nevertheless, we would stress that any program should be based on a credible reform agenda and also clear benchmarks, specifically regarding anti-corruption measures. We would appreciate more insight from the staff on that matter.

Mr. Ostros remarked that the chapter on governance in the selected issues paper was a good example of how the Fund could deepen its discussion of governance issues. He asked if the staff planned to incorporate governance issues into the discussion of the PCI program and what measures could be considered.

Ms. Svenstrup commended the staff for the detailed work on corruption and governance in the selected issues paper. He remarked that his chair had been a consistent and strong advocate for the Fund's efforts to strengthen governance and combat corruption, and that the staff's work was appropriately in line with the recently approved framework. Like Mr. Ostros, he expressed interested in further discussions of how such issues could be incorporated into the PCI request.

The staff representative from the African Department (Mr. Velloso), in response to questions and comments from Executive Directors, made the following statement:[1]

> I will start with the questions from the gray statements that the staff did not answer in writing, and then I will touch on the issues raised during the

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

Board meeting. The staff responded in writing to the technical questions posed by Directors, and I would be happy to clarify, including bilaterally, any of those answers as needed.

Turning to the questions that were not answered in writing—namely on future relations with Angola and whether staff is well equipped to advise the authorities on phasing out exchange restrictions and multiple currency practices. On the first question, I will start by saying that relations between the Fund and the Angolan authorities are probably the best that they have ever been. The staff engaged early on with the economic team of the new administration, and to a substantial extent the advice given during last November's staff visit was taken on board in the authorities' macroeconomic stabilization program, which was unveiled in early 2018.

Our close engagement then continued in the run-up to the Article IV mission in the first half of March, as well as during that mission and the 2018 Spring Meetings. In mid-April, the authorities wrote to the Managing Director and requested that the staff start discussions on a two-year program that could be supported by the PCI. As the Article IV cycle was well advanced, there was agreement that preparations for program discussions would start soon after the conclusion of the Article IV consultation discussions, as mentioned during Deputy Managing Director Zhang's press release of April 18. This would give the staff and the authorities the opportunity to hear Directors' views and recommendations on key economic policy issues.

We take this request to start program discussions as a clear sign that the new government wants to strengthen even further the already close and productive collaboration with the Fund. Angola is undergoing significant political and economic transformation, the type of transformation that happens perhaps once in a generation. The fact that the new government wants to work closely with the Fund to help shape the future of Angola is very positive and should be embraced by the institution.

On the second question, and the short answer is yes, the staff is well equipped to help the authorities phase out exchange restrictions and multiple currency practices. However, as shown in Figure 9 of the staff report, some actions are easier to take in the near-term than others. In the case of the foreign exchange Dutch auction system, there is a tension between what is more desirable from an economic point of view and what is needed to eliminate that multiple currency practice.

In terms of program discussions, we will start preparing internally in consultation with functional departments only after this Board meeting is concluded, so it would be a bit early to mention what would or what would not be in our policy note or what line we should take with the authorities.

Governance is a big issue in Angola. The new administration has clearly shown a strong commitment to start doing things differently to improve governance and fight corruption. They understand that there is a payoff for doing this; and the payoff is higher growth, as we show in our Selected Issues Paper on governance and growth. It is not an issue that only we want to push. It is an issue that the authorities themselves want to move forward and, in the areas of expertise of the Fund, we will be able to help them in this process.

Mr. Spadafora strongly supported the authorities’ efforts to transform Angola’s economy, and welcomed their interest in the PCI. He noted that the Selected Issues Paper had emphasized that Angola was facing a once-in-a-generation opportunity to transform its economy, and wondered if the same sentiment could be expressed in the main body of the staff report.

Mr. Palei made the following statement:

Since many Directors commented on the Selected Issues Chapter on governance and corruption, I will say a few words as well. In our gray statement, we emphasized only the positive side of this paper, but it is far from being perfect. In particular, we were concerned about the mix of various indicators. Some of them are purely perception based. We do not trust these indicators. We have had many discussions on this subject at the Board. The staff apparently used these indicators to run regressions with the Corruption Control Index (CCI) from World Governance Indicators and also the Corruption Perceptions Index, and then came up with these beautiful numbers of 1.5 percent and 2 percent of higher growth annually. Those are big numbers. We have heard them before. We do not believe in them at all. I think it is not speaking truth to the authorities. It is “truthiness”, if we use the term coined by one of the U.S. comedians. It is based on perceptions and belief but presented as scientifically researched and based on empirical evidence. We have serious concerns about mixing perception- and evidence-based indicators. The Doing Business indicators are evidence-based. That is what we like, and we emphasized that it was a good choice. But when they are mixed with perceptions, the picture becomes muddy, and it is difficult to separate what can realistically be done from an expectation that is not based on any facts or empirical evidence.

Another concern is that we agreed that there would be no ranking of countries in selected issues papers, but there are many charts with many countries labeled on them; and one can see if one country is supposedly higher in the ranking than another country—not supposedly, it is a fact because the staff used these perception-based indicators.

In terms of economic significance and how it is demonstrated in the staff papers, we have serious doubts. I would be happy to hear why the staff used 2 percent instead of 1.5 percent? The CCI results in 1.5 percent and the Corruption Perceptions Index results in 2 percent. Why did the staff not use the range of indicators? Both are unreliable numbers, but I am curious.

We do not believe these papers are an example for others to follow. They are far from perfect, and the staff needs to work more on how to find the balance between presenting the perceptions that dominate the media and the facts.

The staff representative from the African Department (Mr. Velloso), in response to further questions and comments from Executive Directors, made the following additional statement:

Governance is a big issue in Angola. The new administration has clearly shown a strong commitment to start doing things differently to improve governance and fight corruption. They understand that there is a payoff for doing this; and the payoff is higher growth, as we show in our Selected Issues Paper on governance and growth. It is not an issue that only we want to push. It is an issue that the authorities themselves want to move forward and, in the areas of expertise of the Fund, we will be able to help them in this process.

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Mr. Palei remarked that all changes to the text should be consistent with the Transparency Policy.

The staff representative from the Strategy, Policy, and Review Department (Ms. Goodman) noted that it was frequently the case that slightly different wording was used in different documents related to an Article IV consultation. It was not necessary to align the language, and that would not be standard practice under the Transparency Policy.

Mr. Mkwezalamba made the following concluding statement:

> On behalf of my authorities, I thank Directors for the completion of Angola's 2018 Article IV consultation. The policy advice and recommendations aimed at supporting the authorities' efforts to restore macroeconomic stability, diversify the economy, and foster sustainable and inclusive growth are appreciated and will be conveyed to the authorities in earnest.
>
> As noted by Directors, while the near-term growth outlook remains positive, the economy still faces risks, including those related to uncertainty in

oil price developments and gaps in socioeconomic infrastructure. The authorities are determined to tackle these challenges through sustained implementation of their reform agenda, as articulated in the macroeconomic stabilization plan, as well as the second national development plan. They also look forward to the PCI to support their efforts.

To improve fiscal sustainability and stabilize public debt, the authorities are committed to foster fiscal consolidation, steadfastly increase capacity for non-oil revenue generation, and enhance public financial management. Meanwhile, the fiscal policy stance will remain restrictive, including through a significant reduction in the size of the public sector wage bill and containment of expenditures on goods and services. Further reforms will be intensified to broaden the non-tax revenue base through introducing a VAT, as well as enforcing real estate taxation.

To contain inflationary pressures arising from pass-through effects due to depreciation of the kwanza, monetary policy will remain tight. This monetary policy stance will be complemented by sustained efforts aimed at upgrading the monetary policy framework and strengthening bank supervision.

The authorities are committed to pursuing structural reforms with a view to strengthening governance and fighting corruption and achieving broad-based growth. In this regard, they intend to step up efforts to implement reforms directed at supporting economic diversification through increased fiscal space for high-quality infrastructure investments, enhanced public administration efficiency, and an improved business climate.

Furthermore, they will strengthen the implementation of the Anti-Money Laundering and Combating the Financing of Terrorism framework and maintain open channels of dialogue and communication between domestic and foreign banks to help address the loss of correspondent banking relationships. In relation to this, the National Assembly approved the legal capital repatriation law, which is a legal instrument to fight illicit enrichment.

In conclusion, on behalf of my authorities, I thank management and the staff for their continued engagement with the authorities, and I also thank the mission chief, Mr. Velloso, and his team, for their constructive dialogue with the authorities.

The Acting Chair (Mr. Zhang) noted that Angola is an Article XIV member. Angola maintained three exchange restrictions and three multiple currency practices subject to Fund approval under Article VIII. Approval of those measures was not recommended.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They welcomed the government's reform program aimed at addressing its post-conflict development challenges, restoring macroeconomic stability, and improving the business environment. Directors welcomed the recent improvements in economic conditions and noted that more favorable oil prices present a unique opportunity to address macroeconomic imbalances, including the erosion of fiscal and external buffers, and reduce dependency on oil. In this context, Directors underscored the need for steadfast implementation of the government's macroeconomic stabilization program and for structural reforms to diversify the economy and support inclusive growth.

Directors supported the fiscal deficit reduction outlined in the 2018 budget and stressed that any revenue windfalls should be used to clear domestic arrears and reduce public debt. With oil prices predicted to decline over the medium term, Directors underscored the need for additional but gradual fiscal consolidation to put public debt on a clear downward path. Directors emphasized that the consolidation should be underpinned by mobilizing additional non-oil fiscal revenue, including by improving tax compliance and the planned introduction of a VAT, as well as further rationalizing public expenditure and improving the quality of public investment while expanding well-targeted social programs.

Directors agreed that monetary and exchange rate policies should play a vital role in rebalancing the foreign exchange market and containing inflation. They welcomed the transition to greater exchange rate flexibility and the new monetary policy framework anchored on base money targeting consistent with the inflation objective. Directors stressed the need to gradually phase out direct foreign exchange sales by the central bank, and to set a clear strategy and timetable for eliminating exchange restrictions and multiple currency practices.

Directors stressed the importance of preserving the health of the banking sector, including the need for concrete actions to complete asset quality reviews, and to strengthen crisis management, emergency liquidity assistance, and the AML/CFT frameworks. They supported ongoing efforts to reinforce capital and liquidity buffers while strengthening governance at the state-owned banks.

Directors noted that the new government’s structural reform agenda is appropriately focused on improving governance, fighting corruption, and improving the weak business environment. They urged concerted efforts to ensure that the reforms are implemented consistently for Angola to reap the expected gains. Directors stressed the need to continue building strong institutions to help ensure that the ongoing reforms have a lasting positive impact on the lives of the Angolan people.

It is expected that the next Article IV consultation with Angola will be held on the standard 12-month cycle.

The Executive Board took the following decision:

Angola—2018 Article IV Consultation

1. The Fund takes this decision in concluding the 2018 Article XIV consultation with Angola.

2. Angola continues to maintain restrictions on the making of payments and transfers for current international transactions under the transitional arrangements of Article XIV, Section 2. The measures maintained pursuant to Article XIV are: (i) limits on the availability of foreign exchange for certain invisible transactions, i.e. travel; and (ii) limits on unrequited transfers to foreign-based individuals and institutions. In addition, Angola maintains three exchange restrictions subject to Fund jurisdiction under Article VIII, Section 2(a) resulting from (i) the discriminatory application of the 0.1 percent stamp tax on foreign exchange operations by natural persons; (ii) the operation of the priority list for access to U.S. dollars at the official exchange rate; and (iii) a special tax of 10 percent on transfers to non-residents under contracts for foreign technical assistance or management services. Angola also maintains three multiple currency practices that are subject to approval under Article VIII, Section 3 arising from the lack of a mechanism to prevent potential spreads in excess of 2 percent emerging (i) between successful bids within the BNA’s foreign exchange auctions; and (ii) for transactions that take place at the reference rate in place and the rate at which transactions take place in the foreign exchange auctions on that day; and (iii) the discriminatory application of the 0.1 stamp tax on foreign exchange operations by natural persons. The Fund encourages Angola to eliminate the measures maintained under Article XIV as soon as the

circumstances permit, and urges Angola to eliminate the exchange restrictions and the multiple currency practices that are subject to approval under Article VIII as soon as possible. (SM/18/90, 4/27/18).

Decision No. 16374-(18/44), adopted
May 18, 2018

APPROVAL: April 20, 2020

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Fiscal Policy and Debt Sustainability

1. ***We would like to know if the authorities have devised a clearer strategy on how to allocate any revenue windfall between these two priorities, given the declared goal of clearing the arrears by 2019 at the latest.***

- The authorities have yet to disclose exactly how potential revenue windfalls in 2018 would be allocated between repaying public debt and clearing domestic payments arrears. But given that the process of certifying part of the domestic payments arrears is still ongoing and that debt rollover needs are expected to remain high this year, we can see a case for giving greater priority to repaying public debt maturing in 2018.

2. ***In view of recent firming up of oil prices, could staff indicate if the authorities are still considering issuing US$2 billion Eurobond, particularly in an environment of increasing yields? In the same vein, could staff elaborate on the actual implementation of the authorities' strategy of clearance of domestic arrears?***

- The authorities issued a US$3 billion Eurobond—US$1.75 billion with 10-year maturity and 8.25 percent coupon rate and US$1.25 billion with 30-year maturity and 9.375 percent coupon rate. The coupon rate on the 10-year Eurobond is lower than that paid on a US$2 billion Eurobond with similar maturity issued in November 2015.

- The authorities' strategy for clearing the arrears includes the following steps: with the help of external auditors, they are reviewing and certifying the claims; as the certification process is concluded and agreements are reached with suppliers, payments to these creditors would be made. As envisaged in the Macroeconomic Stabilization Program, the authorities aim at clearing all (recognized/certified) outstanding arrears by 2019 at the latest.

3. ***Could staff elaborate more on the debt burden impact if the authorities rely more on the Eurobond instead of domestic debt issuance?***

- Greater reliance on external financing has two countervailing effects on debt sustainability. On one hand, it helps mitigate near-term rollover pressures. On the other hand, it increases exposure to exchange rate shocks. On balance, staff sees room for greater reliance on external financing compared to the authorities' borrowing plan, including because domestic banks report being close to their internal exposure limits to sovereign risk. Also, the shift to a more flexible exchange rate regime in early 2018 and the large upfront adjustment of the exchange rate may lessen the likelihood of large exchange rate shocks in the future.

4. ***Given Angola's high gross financing needs, vulnerabilities to changes in the external environment, and the intention to issue a Eurobond, we wonder if the market conditions are still as favorable as at the submission of the staff report? What are the market interest rates compared to other available borrowing sources and how much of Angola's outstanding debt is in concessional terms?***

- On the Eurobond issuance, please see answer to question # 3 above.

- Almost two-thirds of Angola's outstanding external debt as of end-2017 was comprised by multilateral and bilateral loans whose terms are somewhat more favorable than the market's. In part reflecting these semi-concessional terms, staff estimated the NPV of Angola's public debt at 55¾ percent of GDP at end-2017, or almost 10 percentage points of GDP lower than the nominal debt-to-GDP ratio.

5. ***The staff's comments would be appreciated on the prospects of Angola tapping Eurobond markets in the foreseeable future, as well as an indication of the likely spread.***

- Please see answer to question # 3 above.

6. ***From the DSA we also noted that there is no information on private sector external debt. Do staff have estimates of its possible size?***

- There is currently no available information on private sector external debt for Angola.

- STA envisages technical assistance in FY2019 to help the BNA with the compilation of private external debt data.

7. ***Based on staff's assessments, adopting the National Institute of Statistics' nominal GDP rather than that provided by the Ministry of Economy and Planning would lower the Debt/GDP below the authorities' medium-term target of 60 percent. Can staff comment on how this lower debt ratio would impact the DSA and their recommended fiscal adjustment?***

- Last week, INE released new estimates for annual national accounts (revised for 2009-15 and preliminary for 2016). INE's nominal GDP for 2015 was 13½ percent higher than that from the Ministry of Economy and Planning, which most analysts currently use. This difference was virtually eliminated for 2016.

- Fund TA is expected to take place in the coming weeks to verify the robustness of INE's new estimates. Therefore, it is early to draw definitive conclusions on the potential implications for debt sustainability and the fiscal space.

8. ***Could staff share if there is already a firm plan to clear the domestic payment arrears should the oil price outturn be higher than the baseline*?**

- As noted in the answer to question # 2 above, the authorities intend to clear all (recognized/certified) outstanding domestic payments arrears by 2019 at the latest.

9. ***We are pleased to note that the authorities broadly agreed with proposed measures to improve medium-term fiscal sustainability and the quality of public spending, that are listed on pages 9 and 10 of the staff report. Given this long list of measures, it may be more beneficial to authorities if staff would recommend prioritization of a set/subset of these measures that they believe would significantly improve the fiscal position in the next 2 to 3 years, consistent with local institutional capacity. We are also interested to know how staff prioritize the works listed in the joint IMF-World Bank Management Action Plan (page 5 of Informational Annex report). The staff's comments are welcome.***

- Indeed, prioritization is critical. It should be highlighted that, as discussed with the authorities (and mentioned in paragraph 15 of the staff report), two policy recommendations are critical for achieving the needed medium-term fiscal consolidation: adopting a VAT on January 1, 2019, as planned, and reducing the wage bill as a share of GDP.

- The work by the World Bank envisaged in the Action Plan is critical for the success of the policies supported by the Fund, such as improving the business environment and strengthening social safety nets. It also complements the Fund TA program for Angola in areas such as AML/CFT.

Monetary and Exchange Rate Policies

10. ***While we acknowledge that the depreciation helps correct existing misalignments in the real effective exchange rate, could staff shed more light on the inflation dynamics in Angola in terms of the passthrough effects of exchange rate, oil price and other major determinants?***

- The passthrough of the exchange rate is still somewhat large but declining over time. The staff estimated the pass-through at one-third during 2011-15 (WP/16/191). More recently, after the adoption of greater exchange rate flexibility, the passthrough has been more limited because prices had already adjusted last year in anticipation of a devaluation this year, and/or because to a larger than expected extent prices reflected the (weaker) parallel market exchange rate which has recently appreciated

11. ***While inflation showed a downward trend, it remained high at 26.25 percent in 2017. Does staff have any concerns over the level of inflation?***

- Inflation in Angola is still too high and should be reduced. Given the limited passthrough of the exchange rate to inflation and tight macroeconomic policies, staff is confident that inflation will continue declining to acceptable levels.

12. ***We note, however, that in the beginning of this year the pass-through effect surprised on the low side, and it led the authorities to be more optimistic in their projections of inflation. Can staff comment on the various estimates of the pass-through effect and its impact on inflation projections for 2018?***

- Please see answer to question # 11 above.

13. ***As the BNA has moved to base money targeting, we would like to ask staff whether the relationship between base money and inflation has been stable in Angola. Related to this point, could staff comments on whether the recent pace of contraction of base money is sufficient to contain inflation pressures?***

- The move to base money targeting became effective in November 2017 and was activated following the exit of the exchange rate peg in early January 2018.

- The historical relationship between base money and inflation in Angola does not provide much guidance going forward given that one way or another the exchange rate was the nominal anchor over the past several years.

- The recent pace of contraction of base money contributed to slowing down inflation through a tightening of liquidity conditions. But the situation will need to be monitored carefully and flexibly going forward.

14. ***Foreign exchange reserve levels are expected to more than halve from 10.7 months of imports in 2015 to 5.2 months of import cover in 2018. What would the staff propose as a strategy to build up reserves in Angola, especially in view of the recent recovery in oil prices?***

- While the adoption of greater exchange rate flexibility alleviates the need to retain very large levels of international reserves, it would be important that, after equilibrium is fully restored in the foreign exchange market, the BNA start rebuilding international reserves to eventually cover 100 percent of the IMF's ARA metric.

15. ***Could staff elaborate on the main measures, which would help the authorities to avoid further NIR losses in 2018?***

- It will be difficult to completely avoid further NIR losses in 2018 because the use of international reserves is part of the authorities' strategy to restore equilibrium in the foreign exchange market, together with tight macroeconomic policies and greater exchange rate flexibility.

16. ***Angola maintains several exchange restrictions and MCPs subject to Fund approval, as well documented in Figure 9. We are concerned about the absence of a monitorable strategy by the authorities to address these restrictions and ideally remove them. Can staff comment on their discussions with the authorities on the way forward to remove these exchange restrictions under Article VIII, as well as on the MCPs and whether the Fund has the necessary tools to help the authorities comply with the Articles of Agreement?***

- The staff will respond to this question during the Board meeting.

17. ***We take note that, despite the decline in net international reserves, staff assesses that "buffers remain substantial given the sovereign wealth fund (FSDEA) assets of about US$5 billion." Could staff clarify if these assets are liquid and marked to market? What volume of resources from the FSDEA would be readily available in case of need?***

- FSDEA's assets are mostly liquid and the investments in securities are marked to market.

- We estimate that about ¾ of the sovereign wealth funds' assets could be available in case of need. However, accessing these funds could take some time given that FSDEA's Board appointed by President João Lourenço is in the process of switching the fund's managers and external auditors are reassessing FSDEA's past and prospective investment strategies.

18. ***The staff report states that the BNA tightened domestic monetary conditions by about 1 percent of GDP by reducing kwanza reserve requirements from 30 percent to 21 percent while eliminating the option for banks to meet this obligation by resorting to T-bills and/or loans to priority sectors. What was the extent of liquidity immobilized by this measure?***

- The elimination of the option for banks to meet reserve requirements obligations by resorting to T-bills and/or loans to priority sectors immobilized about 2.9 percent of GDP of liquidity while the reduction of the reserve requirement coefficient injected about 1.9 percent of GDP.

Financial Sector

19. ***Considering the importance of Recredit and the still high level of NPLs, could staff provide more information about the restructuring process, and the timeline for clearing distressed assets?***

- The recapitalization process of the state-owned banks, which hold most of the banking system's NPLs, started in 2016 and is ongoing, with another round of recapitalization envisaged for this year. In addition, Recredit agreed to purchase about ⅓ of the state-owned BPC bank's NPLs. This, together with the envisaged recapitalization and measures to improve the bank's cost efficiency, should bring the process closer to completion.

20. ***On the staff's recommendation to establish a sunset clause to Recredit's operations, while recognizing the risk of an "NPL warehouse" we wonder if this clause could unintendedly lead to disposals of NPLs at fire-sale prices. The staff's comments are welcome.***

- A sufficiently long lifespan, commensurate with the nature and maturity structure of the eligible assets, should provide a reasonable compromise between incentives for the effective resolution of those assets and preventing/minimizing losses due to premature sales.

21. ***The resolution of NPLs seems to be entirely predicated on the performance of Recredit. If Recredit is not able to speedily clean up the NPLs, how would this affect the expected pace of credit recovery in 2018? Are there any other modalities of cleaning up the NPLs?***

- The pace of credit recovery in 2018 would be slower if Recredit is not able to speedily clean up NPLs but this would be mitigated by other banks taking advantage of clearance of domestic payments arrears.

- An alternative would be simply to write-off NPLs through adequate recapitalization.

22. ***We are encouraged that an asset management company—Recredit—has been set up to clean up banks' high NPLs that are mostly concentrated in state banks and related to politically exposed persons. However, according to staff, some critical***

features that are common in typical asset management companies are lacking in Recredit. Are the authorities planning to rectify these shortcomings?

- The staff is not aware of any plans to adjust the operational features of Recredit but provided technical papers on the experiences of other countries in addressing the highlighted shortcomings.

23. ***Could staff give more details on state-owned banks' high NPLs and the time frame envisaged to solve this situation?***

- The bulk of the state-owned banks' NPLs are concentrated in private companies mainly involved in the construction and services sectors.

- The coming on-stream of Recredit is expected to resolve the NPLs sooner though in practice the process of negotiating for the acquisition of the distressed assets has protracted needlessly.

24. ***In view of banks' appetite for government T-bills, we wonder to what extent the private sector is being crowded out?***

- The appetite for T-bills has been associated with lower credit to the private sector, but mainly reflecting portfolio rebalancing by the banks toward safer assets during stressful economic times, as well as lower private sector credit demand given subdued economic growth.

- To the extent that the credit dynamics are influenced by both lower demand (lack of bankable projects) due to slowing economic activity and other supply constraints, including poor asset quality, the evidence for crowing out remains inconclusive.

25. ***In paragraph 22, we note the recent BNA directive to increase commercial banks' minimum regulatory capital requirement threefold by the end of the year. How confident is staff of full compliance in such a short time frame, especially in case of heavily undercapitalized banks?***

- System-wide capitalization has already improved and remained significantly above the minimum requirement of 10 percent. Only a few small private banks may have difficulties to meet the new minimum capital requirement, and this could lead to some consolidation in the sector. As for the state-owned BPC bank, the government's recapitalization plan should also cover the new minimum capital requirement.

26. ***We invite staff to elaborate on the likely impact from the threefold increase in regulatory capital requirement.***

- See answer to question # 25 above.

27. ***We also note the projected growth in credit to the private sector by 27 percent in 2018 (figure 5), which could warrant strengthened supervisory oversight by the central bank. While this follows two years of no credit growth, could staff provide additional information on this increase and indicate how the central bank plans to mitigate potential risks in this area?***

- This nominal increase—the projected increase real terms is very small—is supported by the resumption of economic activity, clearance of domestic payments arrears, and NPL resolution at state-owned banks.

- The BNA's move to a more risk-based supervisory framework would help mitigate some of the risks.

28. ***Could staff comment on further measures to be taken to mitigate the loss of CBRs.***

- The authorities are strengthening the legal, regulatory, and supervisory frameworks for AML/CFT; working to fully comply with FATF standards; and continuously engaging correspondent banks to reopen CBRs.

Structural Reforms

29. ***Finally, we note the extensive list of recommendations that are contained in the report for the authorities to implement. While we broadly agree with the recommendations, could staff set out what they see as the priorities and the appropriate sequencing? And do these align with the priorities in the National Development Plan?***

- Measures to strengthen governance, combat corruption, and improve the business climate should be given high priority and could be implemented simultaneously, as illustrated by the authorities ongoing reforms in these three areas.

- We expect these reforms to feature prominently in the National Development Plan 2018-2022 (not yet publicly available).

30. ***Have any initiatives/projects been undertaken so far to materially quicken the pace of diversification?***

- Both the Law on Competition and the Private Investment Law that have been recently approved by the National Assembly bode well for greater competition in domestic markets and FDI attraction.

- This improved legal framework would complement well the milestones under PRODESI toward greater economic diversification.

- It is also important to note that the process of diversifying the Angolan economy, given its complexity and high dependence on oil, may take many years to yield tangible results.

31. ***One such law passed to attract foreign investment relates to scrapping rules that previously forced foreign investors to partner with local firms. As a large share of the FDI flows to (from) Angola reflect liquidity management by oil companies in the context of lack of local capital markets, in the absence of a sustained increase in oil prices, would this relaxation be able to increase FDI flows into Angola? The staff may comment on how this relaxation would affect the transfer of technology into the domestic sector.***

- The Private Investment Law is expected to facilitate FDI attraction to non-oil sectors, particularly to those considered 'strategic' where the scrapped rule was binding, namely, power and water, hospitality and tourism, transport and logistics, construction, telecommunications and information technologies, and mass media.

- To the extent that FDI increases in sectors that are intensive in technology (e.g., telecommunications and IT) we would expect technology transfer into the domestic non-oil economy.

32. ***We particularly appreciated the SIP's analysis of the potential gain in GDP per capita from addressing weak governance and corruption. Given high inequality in Angola, could staff also discuss the impact of tackling these issues on inclusive growth?***

- The staff has not estimated the direct impact of governance reforms on inequality and poverty in Angola. But the literature has found that weak governance and corruption tend to entrench inequality and poverty, including by lowering spending on education, health and other social services that are important for human capital formation. Against this background, governance reforms are expected to help create more fiscal space that could be used to address the Angola's social challenges. They would also help foster a level-playing field that could lead to greater economic opportunities for the poor.

33. ***We also appreciated staff's comprehensive discussion of the various reforms underway across areas such as establishing a clear legal framework, strengthening fiscal transparency and governance, and improving the business climate. The list is indeed broad and ambitious, and we wonder if staff and the authorities have discussed prioritization and sequencing. The staff's comments are welcome.***

- The staff has not discussed specific issues pertaining prioritization and sequencing in this area. However, many of staff's suggestion in the SIP on "Governance and Economic Performance in Angola" are low-hanging fruits (e.g., taking on entrenched vested interests, combating grand corruption, enforcing existing anti-corruption laws), which feature prominently in the authorities' reform agenda and may be implemented simultaneously. The staff's empirical analysis also suggests that because of potential complementarities across the channels through which governance reforms impact economic performance, there are gains from implementing multiple governance reforms at the same time.

34. ***Additionally, while some of the measures are technical in nature, others will require tackling vested interests and reconciling competing mandates between government agencies. For example, there appears to be overlap between the newly created anti-corruption agency within the Ministry of Interior and the existing DNPCC. Could staff discuss any updates on how these two units will operate in practice? Have staff discussed any plans for asset recovery with the authorities?***

- The authorities have yet to disclose details about the operation of these two units.

- The staff has not discussed specific plans for asset recovery.

- These are issues that could be tackled in the context of ongoing and future TA.

35. ***Could staff comment on whether recent public infrastructure investments have been selective enough?***

- Angola's public investment management framework has several deficiencies, as highlighted in the SIP on "Governance and Economic Performance in Angola" of the selected issues paper. Project selection is one of those weaknesses.

- The recent transfer of the portfolio of public investment projects to the Ministry of Finance is a welcome first step towards better coordination across ministries and improved project selection.

36. ***Regarding gross financing needs (GFN), staff mentions that the substantial financing needs in 2018 are expected to be met by domestic and external sources,***

including bilateral creditors. Does staff expect any financing difficulties after 2018?

- The staff does not expect financing difficulties in the medium term under the baseline scenario in which the authorities implement (gradual) fiscal consolidation and structural reforms. This would lead to lower GFN and improved market access.

37. ***Could the staff provide more details about the creation of the specialized corruption-unit which was recently announced by the Authorities of Angola?***

- The authorities have yet to unveil details about how this unit would operate in practice and how it would coordinate with the other anti-corruption units under the executive and judiciary branches.

38. ***As in the last Article IV review (presented to the board on January 18, 2017), the staff's report highlights that the authorities will introduce VAT in January 1st, 2019. Could the staff provide further details on concrete steps taken since the last Article IV review to implement this critical reform? According to staff's estimates, what are the additional revenues this reform could result in?***

- The authorities have developed—with help of Fund TA—a detailed VAT implementation plan for 2018-19. As part of this plan, a draft VAT law is currently under discussion and, once finalized, will be submitted to the National Assembly for debate and approval (Fund TA is planned for the coming weeks to help the authorities define key tax parameters); the tax authority (AGT) is currently improving its information systems and expects to conclude this work ahead of the implementation date; AGT is also discussing key VAT issues with stakeholders (e.g., professional associations, CSOs, etc.).

- Preliminary estimates suggest that the VAT could yield up to 1¾ percent of GDP on an annual basis in net terms (i.e., considering the revenue loss due to the elimination of the existing consumption tax).

39. ***Could the staff provide the level of public revenues coming from real estate taxation and further elaborate on the reason why better enforcement is needed?***

- Revenue from real estate taxation remains very small, accounting for only 2½ percent of non-oil tax revenue in 2017.

- There is considerable room for increasing revenue collection through effectively enforcing real estate taxation.

40. ***Regarding the program recently set up for promoting export diversification and import substitution (PRODESI) which targets six sectors, we would like staff to provide more details about the economic policy tools that will be engaged for implementing this program.***

- This program combines policies with wider macroeconomic impact, such measures to improve the business environment and the physical infrastructure, with interventions at the sectoral level including to help develop and strengthen production clusters (e.g., implementing sector-specific regulation, prioritizing industry-specific infrastructure developments, concessions).

- Targeted sectors include food products, textiles, cement, fishing, and tourism.

- Given the limited fiscal space, the program seeks to mobilize financing also from alternative sources such as FDI and domestic and foreign private equity.

Fund Issues

41. ***As the outlook is more favorable, Angola has a unique window of opportunity to strengthen reforms and would benefit, in our view, from a deeper engagement with the Fund, perhaps through a signaling arrangement, that could help the country anchor macroeconomic stabilization, send positive signals to investors, and initiate the needed reforms to improve the allocation of resources and diversify the economy away from the oil sector. Could staff indicate if the authorities have expressed any interest in closer engagement with the Fund?***

- The staff will respond to this question during the Board meeting.

42. ***We encourage the Angolan authorities to maintain an open and frank dialogue with the IMF and to continue to seek Fund advice and support to help maintain reform momentum. Any update from staff on this would be appreciated.***

- The staff will respond to this question during the Board meeting.