Economic Research Unit
Contact: +244 222 696 462
E-mail: dfi.gee@bfa.ao

FLASH NOTE

Nº 13.2023 | October 9th, 2023

Angolan economy stagnated in Q2 2023

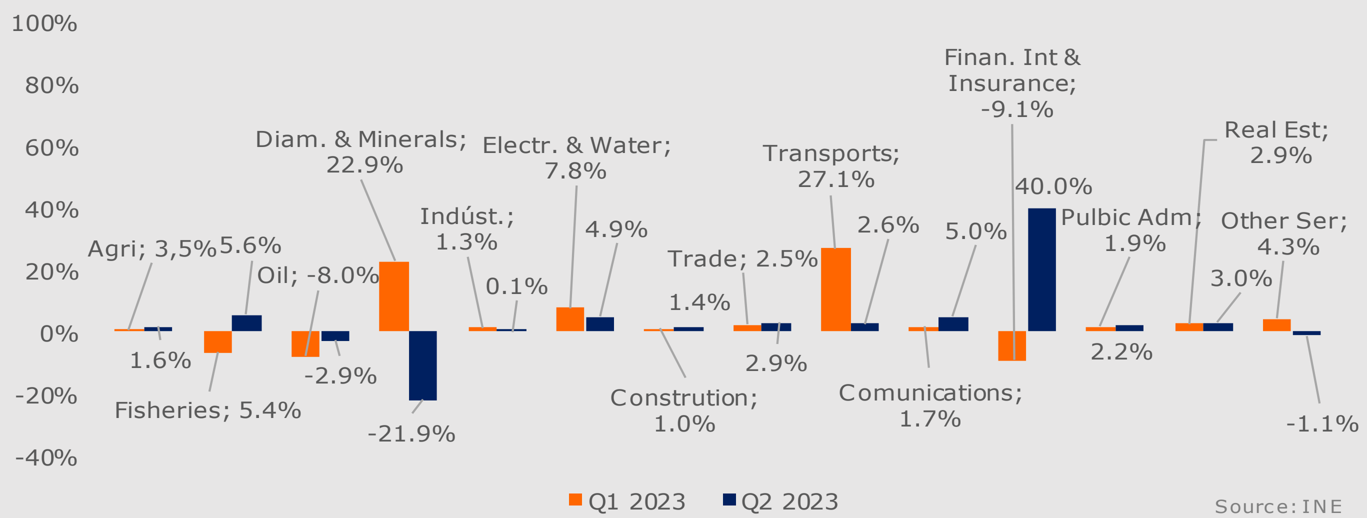
Non-oil sector grew again, but slowed down as predicted

A. DESCRIPTION

1| In the second quarter of 2023, the Angolan economy stagnated when compared to the same period in 2022. By contracting 2.9% yoy in Q2 2023, the oil sector removed 0.8 percentage points (pp) from the general GDP growth rate and added the third consecutive break. The non-oil economy grew 1.2% yoy, slowing down 1.9pp compared to Q1 2023 and added around 0.9pp to the economy's overall growth rate.

The performance of the general level of non-oil activity was once again positive, despite the drop in two sectors

Year-on-year change in percentage



Source: INE

2| The performance of the general level of non-oil activity was once again positive, despite the drop in two sectors. The Financial Intermediation & Insurance (40.0% yoy), Fishing (5.6% yoy) and Communications (5.0% yoy) sectors showed higher growth levels than the others, while the Services and Diamonds and Minerals contracted about 1.1% yoy and 21.9% yoy, respectively.

B. ANALYSIS

1| Growth in the non-oil economy fell by 1.9 pp, with activity growing 1.2% yoy in Q2 2023, as a result of a timid evolution in the Trade, Agriculture and Other Services sectors, which together represent 31% of GDP. We were expecting a slowdown in non-oil economic activity, but to a lesser degree than the current figures from the National Statistics Institute (INE), so the 1.2% yoy growth in Q2 did not meet our expectations, between 2.2%-2.8% yoy.

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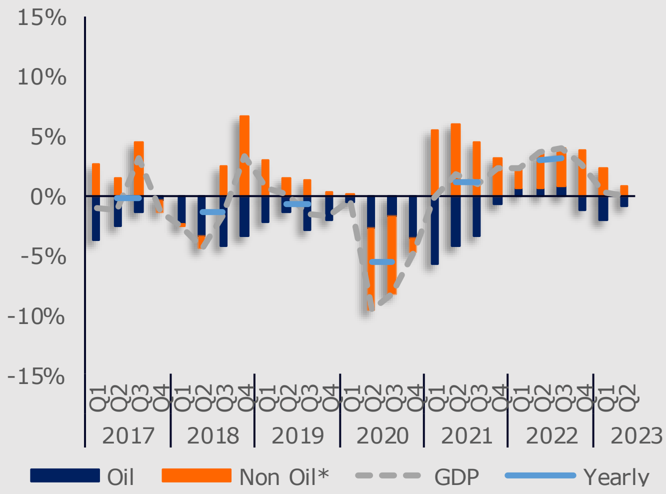
The Other Services sector contracted 1.1% in Q2 2023, after growing uninterruptedly for five quarters. According to the national accounts released by INE, the negative variation in the sector is justified by the fact that there was a decrease in the activity of accommodation and restaurant services by 12.9%, with these representing around 30% of this total. sector. In our opinion, in the Q3 the sector will feel greater effects from the removal of fuel subsidies, the increase in inflation and exchange rate depreciation, which will, by the way, reduce activity. Therefore, we expect the sector to contract more notably in quarterly terms, but in year-on-year terms it may grow slightly, given the fact that in Q3 2022 the level of activity reached values well below the average of recent years.

Non-oil economy slowed again and is expected to contract in Q3 2023

Yoy variation; Contribution to year-on-year change



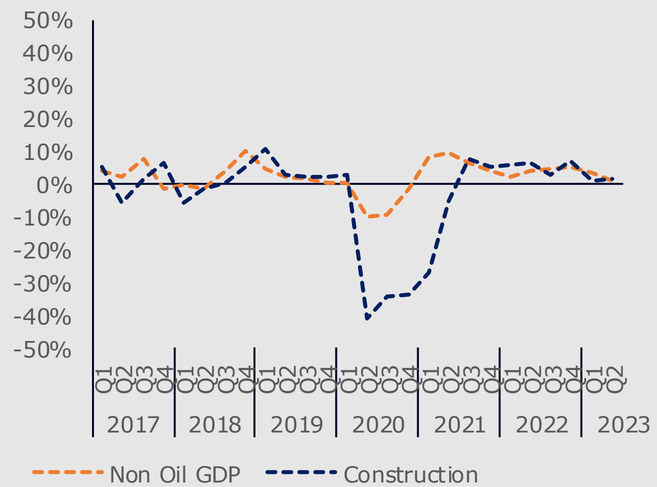
* Proxy: GDP minus Oil GDP

Source: INE

Construction, which is the second largest sector of the non-oil economy, advanced 0.4pp above the levels recorded in Q1, growing 1.4% yoy. This variation was due to the slight increase in the amount of national and imported cement production related to construction materials, which according to INE, represents a weight of approximately 64.2% of the sector. However, Construction should also feel greater impacts from the depreciation of the Kwanza in the Q3. There is evidence that some economic agents in the sector plan to discontinue projects, both in works contracted by the private sector and in public works; In particular, there is a dilemma to be faced now, which boils down to the fact that the prices of construction materials, which are mostly imported, are being indexed to the exchange rate, which is not reflected in the payments agreed by the promoters of the respective projects. Therefore, we expect the Construction sector to contract in Q3 2023.

The construction sector has many challenges to face and is expected to contract in Q3 2023

Real year-on-year variation



Sources: INE; BFA calculations

As we expected, the Diamonds & Minerals sector fell 21.9% in Q2 2023, after growing 23% yoy in Q1 2023. According to INE, this drop was mainly due to the reduction in production from the extraction of diamonds and salt in the order of 22.1% and 52.9%, respectively. Diamond exports in August fell by 80% compared to the same period last year. Since January of this year, we have observed a strong downward trend in exports. The numbers for July and August 2023 are significantly lower than those for the same period last year. Therefore, according to our calculations, for exports in Q3 2023 not to contract, the volume of exports in September would have to grow by at least 122%, which seems unlikely based on recent performance. These numbers are also clear evidence that the Diamonds & Minerals sector could contract abruptly again in Q3 2023. Additionally, there were also statements by

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Endiama officials pointing to a pause in sales to the Indian economy – due to restrictions imposed by the country itself when purchasing diamonds - one of the main external customers for Angolan diamonds.

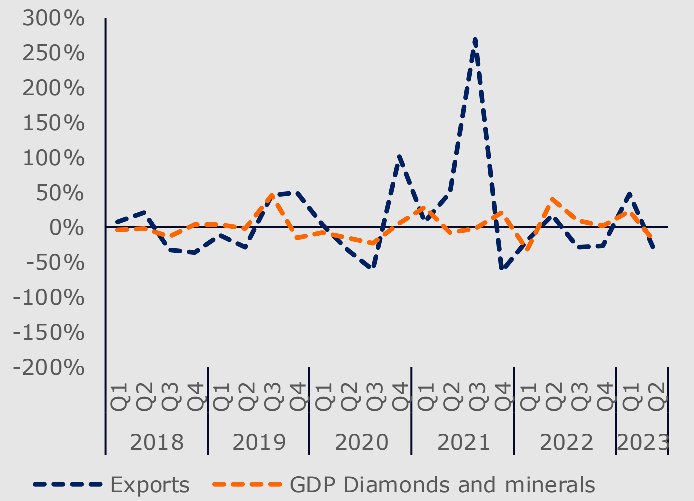
In general, it is clear that the non-oil sectors of the economy slowed down, with some exceptions (Communications, Fisheries, and Financial Intermediation & Insurance).

2| The Q2 2023 data for the oil sector is not very encouraging, as it is the second consecutive quarter of declines. This contraction, around 2.9%, did not meet our expectations, between 4.3%-5.2%, as OPEC's own data already indicated a year-on-year drop in production of 5.3% in Q2 2023. According to INE, the production of extracted quantities of natural gas, LNG and condensate, which represent 10% of the sector, grew year-on-year, which should have contributed to minimizing the decline in the sector as a whole. According to data collected independently by OPEC, oil production in Angola was around 1.12 million barrels per day (mbd) in August. Despite the recovery in production volumes compared to the beginning of the year, the year-on-year variation still shows declines, although less significant at this time. Production between July and August was 1.2 mbd and compared to the same period in 2022, it represents a drop of 1.8%. Therefore, based on our calculations, production in September would need to grow at least 5.4% mom so that the sector does not contract again in the Q3.

3| We believe that non-oil economic activity will contract in Q3 2023. There are several factors that we have been monitoring that contribute to this:

The Diamonds & Minerals sector sank in the Q2 as we expected and should fall again in the Q3

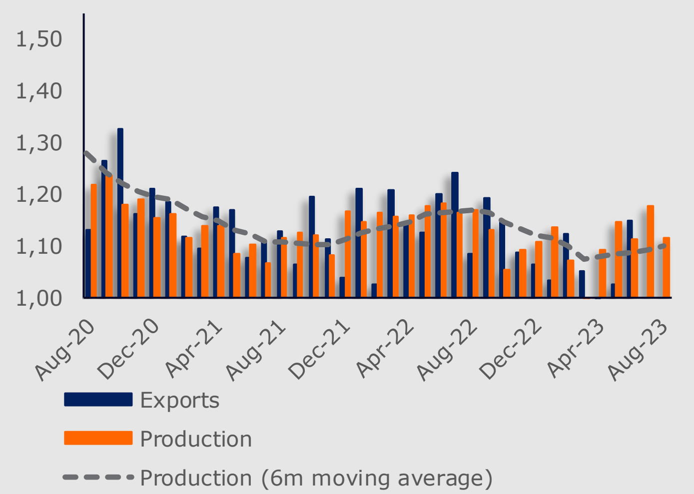
Real year-on-year variation



Sources: INE; BFA calculations

Production is recovering compared to the beginning of the year, but still has yoy declines

Millions of barrels per day



Sources: MINFIN; OPEC

- The sharp exchange rate depreciation that occurred at the end of Q2 2023, which dragged the national currency to historic levels, should continue to have strong impacts on the economy. As the exchange rate began to depreciate in mid-May and throughout the month of June, we expect the impact of the depreciation on economic activity to be stronger in Q3 2023. The same reasoning, we apply to the removal of fuel subsidies announced on the 1st of June, that is, the end of Q2 2023;

- Monthly inflation in August accelerated again, reaching 2.0%, the highest value since December 2021 – compared to August 2022, prices increased 13.5%, the highest rate of annual increase since the end of 2022. Inflation in the "Clothing and Footwear", "Health" and "Hotels and Restaurants" class remains well above the general index and should continue to rise. Furthermore,

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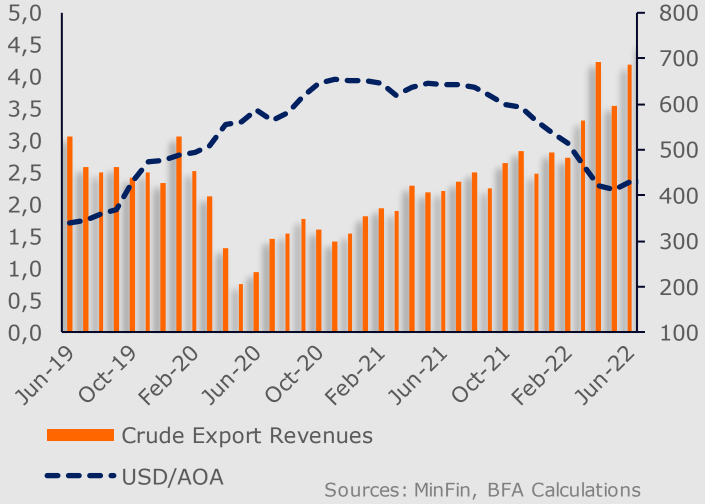
the "Food and non-alcoholic beverages" class, which represents more than 50% of the general index, is rising persistently, in line with general inflation, and for this reason annual inflation should end the year close to or slightly above 20%.

- We note that the Central Bank reversed its monetary policy movement, adopting a more flexible position than the one it had taken since May, which is in contrast with the current inflation trend. At that time, the BNA should already be contracting the monetary base, but on the contrary, it is allowing its expansion and making the money market more liquid. It is possible that the BNA is not changing the instruments for conducting monetary policy because it is still evaluating the effects of past measures, in addition to being optimistic about the temporary nature of inflation. Despite the Central Bank's more conservative position, our inflation forecast of close to 20% leads us to think that in the near future we will have a tighter monetary policy, and we are afraid that the BNA will begin to tighten monetary policy. slightly late, missing opportunities for gains in reducing inflation by a few percentage points, since the time lag between the action of monetary policy and its real impact on the economy is large.

- At a time when economic conditions are tighter and there is a visible drop in confidence and increased risk, net credit to the economy is not expected to grow in real terms. In fact, the credit stock in real terms is growing, but this is not a net growth, but the result of exchange rate depreciation.

Crude export revenues still below last year's average levels

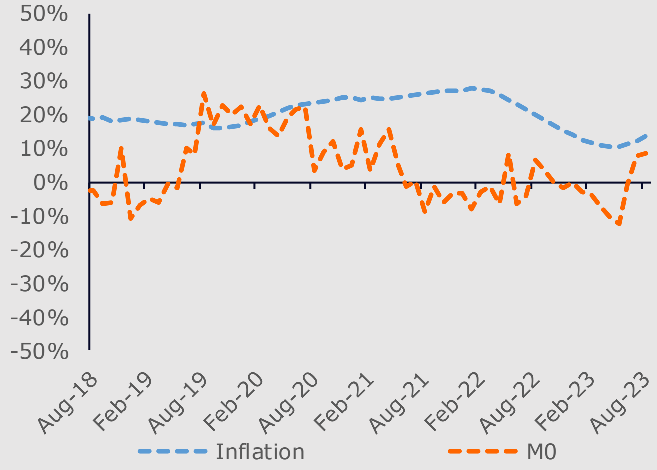
USD Billion; USD/AOA



Sources: MinFin, BFA Calculations

Monetary base continues to rise despite greater inflationary pressures

Yoy variation



Sources: INE; BNA

C. CONCLUSION

1| GDP will continue to grow slowly due to the slowdown in the non-oil economy and also the reduction in the volume of crude oil produced. The oil sector is expected to remain in recession, as no new major investment projects are planned for this year. The non-oil economy is expected to contract in Q3 2023, essentially influenced by exchange rate depreciation and the removal of fuel subsidies. Therefore, our expectation for Q3 2023 is a contraction of 1.9%-2.5% in GDP, supported by a contraction of the non-oil economy between 2.1%-2.7% and a contraction of the oil company around 1.3%-1.9%.

2| The positive evolution of the non-oil sector is essential to guarantee economic growth in 2023, as we have no doubt that the oil sector will contract this year. Our estimates indicate a drop in at least 2 quarters (Q3 and Q4), but this will certainly occur in Q3 2023, more intensely. Overall, we maintain our forecast that there will be stagnation in the non-oil sector and a fall in the oil sector of around 5.0%-5.4%, which will cause GDP to contract in total by close to 1.0%-1.4% yoy.

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