

FLASH NOTE

Nº 07.2025 | 23 June 2025

BNA cuts reserve requirements again

Inflation accelerated and core inflation reversed trend, raising alarm about persistence

A. DESCRIPTION

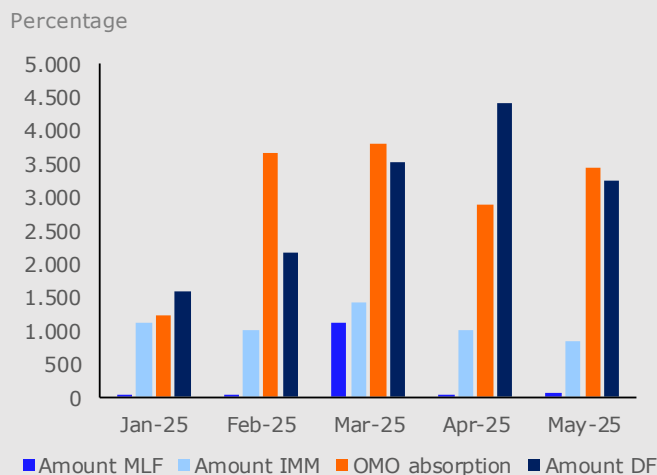
1| The Monetary Policy Committee (MPC) cut the Mandatory Reserve Ratio (MRR) for the third time this year, aiming to stimulate credit to the real economy and support the decline in interbank money market (IMM) interest rates, while once again keeping the policy rates unchanged.

2| Regarding inflation, the year-on-year national inflation rate stood at 19.7% in June, close to the low observed in December 2023. After a period of deceleration since May 2023, monthly inflation edged up slightly to 1.21% (+0.04pp), mainly due to the first-round effects of the administrative adjustment of electricity and water tariffs, although communication prices also increased.

B. ANALYSIS

1| The BNA has adopted an apparently mixed stance, lowering MRR while intensifying the use of liquidity absorption operations. By reducing the MRR by 1pp to 18%, the central bank is set to release approximately AOA 99.8 billion in reserves starting in July - a clearly expansionary measure aimed at enhancing banks' lending capacity and exerting downward pressure on interbank money market (IMM) interest rates. However, this structural easing is occurring in parallel with a sharp increase in short-term liquidity absorption (1-week and 1-month), through open market operations (OMOs) using repos, which totaled AOA 3.4 trillion (t) in May, along with overnight and 7-day absorption facilities, which reached about AOA 3.3t. This combination reflects a calibrated monetary management approach: while injecting liquidity at a structural level, the monetary authority acts tactically to contain short-term pressures on both the exchange rate and inflation.

Liquidity absorption ease and OMAs reach AOA 3.3 trillion and AOA 3.4 trillion, respectively

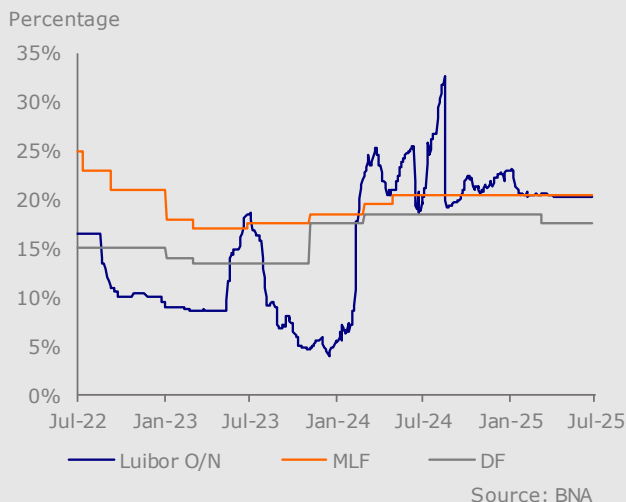


Between January and May, BNA reduced MRR in local currency from 21% to 19% - an accumulated drop of 2 percentage points (pp). This measure, alongside the March cut in the marginal lending facility rate and the reduction of the 7-day repo rate to around 15%, contributed to lower interest rates in the IMM. Since the beginning of the year, the Luibor overnight (O/N) rate has fallen by 249 basis points (bps), while other maturities declined by an average of 189bps - with a notable 251bps drop in the 12-month Luibor. This downward trend is especially important in the current context, as it may be contributing to the robust expansion in private sector credit, which grew by 28.6% year-on-year.

The market has remained highly liquid, yet the Luibor O/N has held steady around 20% over the past three months - most of the YTD decline occurred between January and early February. This rigidity in the O/N Luibor, despite ample liquidity, suggests that other factors are influencing interest rate dynamics, such as still-elevated inflation and the relative attractiveness of alternative instruments, particularly OMOs with maximum rates around 17.5%.

Our recent analysis of lending rates reveals that the average cost of credit remains high, standing at 28.7% in May, well above the 23.6% recorded in the same month of 2024. In this context, we consider the BNA's current stance to be appropriate, as it seeks to stimulate credit while remaining cautious about inflation and exchange rate pressures. The strategy is clear: on one hand, the MRR is being gradually reduced - easing structural constraints on bank lending; on the other, liquidity absorption operations are being intensified at competitive rates, helping to contain short-term excess liquidity and avoid currency pressures. This balanced approach supports real economy financing, promotes a gradual decline in interest rates, and safeguards both price stability and discipline in the money market.

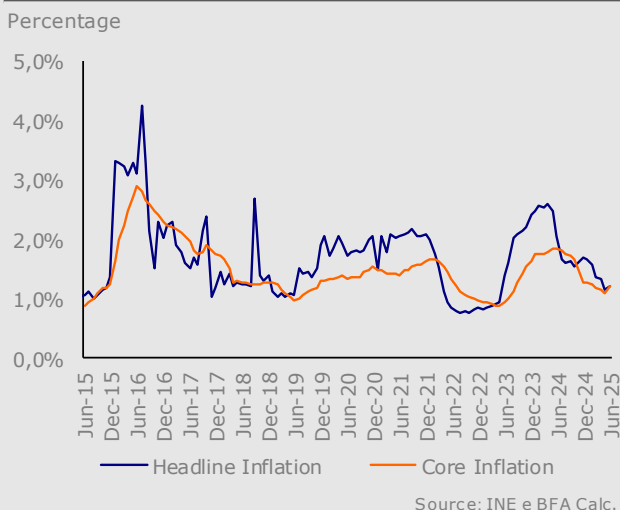
The Luibor O/N remains stable, around 20% since the beginning of the year



2| Inflation accelerated in June after several consecutive months of deceleration, mainly reflecting first-round effects associated with the administrative adjustment of electricity and water tariffs. Added to this shock were price increases in the communications sector, which also contributed to the rise in the overall index.

It is important to highlight that this increase does not yet incorporate the effects of the recent adjustment in the price of diesel, which rose from AOA 300 to AOA 400 per liter, triggering changes in public transportation fares: shared taxis now charge AOA 300 per trip, and urban buses AOA 200. Furthermore, according to Executive Decree No. 187/23 of September 1st, private school tuition fees may increase in the next academic year by up to the May inflation rate, which is expected to put upward pressure on education prices and, consequently, on the general price index.

Inflation gains momentum and the core reverses trend, raising concerns about persistence



The central point, however, lies in the shifting expectations around prices increases in administered and regulated prices are likely to trigger second-round effects, meaning that other sectors may indirectly adjust their prices, contributing to more persistent inflationary pressures. Consistent with this risk, our core inflation indicator - which excludes the most volatile components - edged up slightly in June, breaking the downward trend observed since October 2024. While the increase remains modest, it raises a relevant warning about potential longer-lasting pressures, reinforcing the importance of closely monitoring upcoming data, especially: July, August, and September, which should reflect the increases

in transportation and education; and December, which typically sees seasonal price pressures, especially on consumer goods and food.

Therefore, in this context, we maintain our projection that inflation will close the year at around 21% (even though the current year-on-year figure is still slightly below that level), remaining under pressure in the coming months.

C. CONCLUSION

1| BNA's recent decision to cut MRR again, while simultaneously intensifying liquidity absorption, reveals a mixed and calibrated monetary strategy, which aims to balance credit stimulus with controlling short-term inflationary pressures. However, inflation has accelerated again, influenced by shocks administered to electricity, water, and, in the future, transportation and education. The increase in core inflation reinforces this risk, signaling that price persistence may be greater than previously thought. In this context, monetary policy should remain cautious, with heightened vigilance over upcoming inflation and liquidity data, in an environment where the inflationary trajectory may be longer and more volatile than desired.

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