



# Um Olhar Sobre a Despesa Pública

Centro de Integridade Pública

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## WHY THE GOVERNMENT'S FISCAL POLICY IS DEFRAUDING THE MOZAMBICAN PEOPLE

Fiscal policies remain expansionary in Mozambique, despite the fact that the Government has lost access to important foreign financing since 2016. Due to irresponsible fiscal policies, which cause very high interest rates, the fiscal measures pursued by the Government only benefit the groups closest to the Government, defrauding the expectations of the people.

The economy (gross domestic product, GDP) has been growing since 2016 at an annual average rate of around 3.8%, some 50% below the historical rates of 7% recorded in the previous decade. Over the medium term (through 2020), economists do not expect an improvement in the growth rate. A watershed event that led to this decline in growth was the public discovery in April 2016 of the famous hidden debts of US\$ 2 billion.

One can separate the economic consequences of the event of discovering the hidden debts into two large blocks.

The first block is characterized by:

- Reduction of foreign currency to the Government as a result of the suspension of budget and balance of payments support (which in 2014 corresponded to 11.5% of total expenses realized), as shown in the table below.

**Table. Budget and Balance of Payments Support, 2012-2017**  
(In billions of Meticals and in percent)

	2012	2013	2014	2015	2016	2017
Budget and balance of payments support	13.6	14.1	26.1	6.8	4.4	0.0
Total expenditures realized	145.2	178.5	227.0	200.5	209.0	242.3
Percentage	9.4	7.9	11.5	3.4	2.1	0.0

- Abysmal drop in government investment expenditures, from 87.0 billion Meticals (MMT) in 2014 to an average of 50 MMT in 2016-2017<sup>1</sup> (both those financed with external resources and those financed from the Government's own resources);
- Rise in expenditures related to public debt;

1 Source: Relatório de Execução do Orçamento do Estado 2017, Ministério da Economia e Finanças.

– Significant fall in foreign direct investment (FDI), affecting private sector projects (in 2017 only US\$ 2.3 billion was raised, while in 2016 the figure was US\$ 3.1 billion and in 2015 US\$ 3.9 billion)<sup>2</sup>.

The second block is characterized by:

- Lack of fiscal measures to compensate for the sudden lack of foreign exchange;
- Growth of credit to the Government (issuing money) and
- Accelerated devaluation of the Metical (until September 2016), resulting in accelerated inflation.

CIP considers that the Government's measures to rebalance the fiscal situation in the face of the fall in foreign exchange have been patently insufficient from April 2016 to date, resulting in serious macroeconomic imbalances. The only factor that saved the national currency from a collapse was the actions by the Bank of Mozambique (BM) in the field of monetary policy, by sharply raising benchmark interest rates. The action of the BM first stabilized and subsequently appreciated the Metical, with highly positive benefits in terms of inflation.

However, the BM's reaction was an emergency response to the Government's irresponsible fiscal policies, as complementary measures to the shortage in foreign exchange were not applied in the fiscal area. The BM's reaction (of raising interest rates) has also had a negative impact on productive activity: high interest rates reduce the possibility for companies to obtain credit and, therefore, economic activity decreases. Interest rates are still much higher than before. Although inflation has returned to manageable levels, the economic environment remains unfavorable.

So let us ponder the effects: companies have to close their doors because they cannot bear the weight of credit at high interest rates, resulting in the loss of jobs and thus decreasing household income. One can also see that the fall in the purchasing power of the population has resulted in a fall in imports, increasing the difficulties for many companies to maintain employment levels (vicious circle).

## **CONCLUDING REMARKS**

In the current context, public attention has turned to high interest rates and, consequently, public opinion has blamed the BM. But based on the situation described above, it is CIP's view that the BM can only lower interest rates to 2016 levels, that is, before the "watershed event" caused by hidden debts. This on the one hand. On the other hand, CIP is of the opinion that if the Government adjusts its expenditures to available resources, it can avoid a fiscal deficit that needs to be financed with domestic debt.

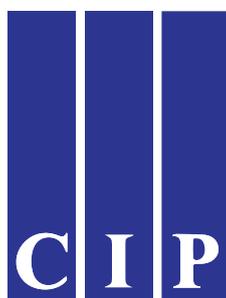
Internal credit to the Government increased from 127.9 MMT in December 2016 to 215.0 MMT in December 2017 - an increase of 67.9%. The rampant growth of domestic credit is a consequence of government action to implement an expenditure policy whose main feature is to finance the deficit - which results in domestic debt - because the Government's own resources are not sufficient to cover the deficit. Under these conditions, the BM cannot reduce benchmark interest rates enough to reach pre-2016 levels without again causing an increase in inflation and acceleration in the depreciation of the Metical. But keeping interests rates high prevents the private sector from getting enough credit for its activities (crowding out), while commercial banks receive high interest rates by buying Treasury bills that the Government is issuing.

The Government must be held accountable for maintaining a high level of spending in the face of scarce resources (many expenses are for non-productive sectors, such as the importation of Mercedes cars for MPs of a country that is "drowning").

Given the Government's lack of own resources, it should adjust the level of expenditures to a level of financing that allows the BM to lower interest rates and thus facilitate more credit for the private sector. The lack of these explanations by the Government is defrauding the Mozambican people.

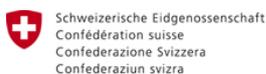
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<sup>2</sup> Source: Bank of Mozambique, Balance of Payments Statistics.



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