

AFRICA RISK CONSULTING

Mozambique Monthly Briefing May 2015

Mozambique Summary 21 May 2015

Prime minister Carlos Agostinho do Rosário introduces the 2015 budget. Equipa Militar de Observadores Internacionais da Cessação das Hostilidades Militares (EMOCHM) (military observation team on the cessation of hostilities) ends its work. United States-based Anadarko Petroleum Corporation picks a contractor consortium to start initial onshore work for its Mozambique liquefied natural gas (LNG) facility. Fitch Ratings maintains Mozambique's B+ rating. Mozambique is at risk of exceeding installed power capacity in the future.

Government introduces 2015 budget

Prime minister **Carlos Agostinho do Rosário** introduced the **2015 Orçamento Geral do Estado** (draft state budget law) to the assembly of the republic (parliament) on 24 April.¹ The budget is predicated on 7.5% GDP growth, and an inflation ceiling of 5.1%.² Increased expenditure means that the government faces a budget deficit of 11.1% of gross domestic product (GDP), which the government will meet through foreign and domestic borrowing.³ The government will finance 25% of its \$6.78 billion expenditure through external resources.⁴ The budget notes that debt repayments will increase from 1% in 2014 to 1.2% in 2015.⁵

The budget prioritises the completion of infrastructure projects already underway as well as the delivery of basic social services. Public spending will increase:

- in the economic and social sectors, from 10.8% to 63.5% of expenditure;
- on infrastructure, from 3.7% to 15.8% of expenditure;
- on agriculture, from 6.2% to 9.1% of expenditure.⁶

Mozambique's 2015 budget contains a number of ambitious targets in the commodities sector. It targets a 7% increase in commodity exports to \$4.2 billion.⁷ The budget forecasts \$1.17 billion worth of aluminium exports in 2015 and \$563m in coal exports.⁸ The budget expects the amount of coal mined in Mozambique to reach approximately 10.1 million tonnes. Meeting this target entails a 62% increase in thermal coal output and a 58.5% increase in coking coal.⁹ Whether this is feasible depends on when the rail line from **Moatize** in **Tete Province** to the **Nacala-a-Velha Port (Nampula Province)** becomes operational.¹⁰ The 2015 budget also forecasts \$371m of natural gas exports.¹¹ It forecasts that natural gas production from the **Pande** and **Temane** fields (**Inhambane Province**) will increase 5.2% and the production of condensate will more than double. The 2015 budget expects imports to increase 5% to \$8.36 billion on the back of large-scale infrastructure projects and an increased demand for fast moving consumer goods.

Rosário warned that delivery of the budget depends upon,

¹ AIM, 27 Apr 2015.

² AIM, 27 Apr 2015.

³ Lusa, 27 Apr 2015.

⁴ Lusa, 27 Apr 2015.

⁵ Lusa, 27 Apr 2015.

⁶ Lusa, 27 Apr 2015.

⁷ AIM, 27 Apr 2015.

⁸ AIM, 27 Apr 2015.

⁹ AIM, 27 Apr 2015.

¹⁰ AIM, 27 Apr 2015.

¹¹ AIM, 27 Apr 2015.

*“...above all, the preservation of peace and the maintenance of political stability. Without peace and stability the Mozambican people cannot expect economic activity to increase, private investment to expand, or more jobs to become available”.*¹²

Military observer mission ends

The **Equipa Militar de Observadores Internacionais da Cessação das Hostilidades Militares (EMOCHM)** (military observation team on the cessation of hostilities) will end its mission after its mandate ends in May. The ruling **Frente de Libertação de Moçambique (Frelimo)** party and the main opposition **Resistência Nacional Moçambicana (Renamo)** invited the EMOCHM to facilitate an agreement for the integration of former Renamo militants into the **Forças Armadas de Defesa de Moçambique (FADM)** (Mozambique defence forces) and the **Polícia da República de Moçambique (PRM)** (national police).

*“The government and Renamo delegations in the negotiations aimed at solving the political crisis affecting Mozambique in the last two years have closed negotiation round number 105 without reaching any consensus over one of the most important and complex matters related to the security and military issues [FADM and PRM integration]. [Former]President Armando Emilio Guebuza’s (2005-2015) inauguration speech raised expectations over this issue, and people believed the new president was going to find a solution soon. However, nothing has changed so far.”*¹³

EMOCHM’s mandate expired on 15 May,

*“... after fruitless mediation efforts. The government accuses Renamo of moving soldiers towards the capital **Maputo** and there were confrontations in the southern province of **Gaza** recently. In April, Renamo announced that it intends to open military headquarters in **Muxungue**, in a clear threat to the government. While the government says it is still pondering the future of the international observer mission, national observers have shown signs of tiring, too. One of the national mediators, pastor **Filipe Couto** is cited saying that now the solution remains in the hands of [President **Filipe Jacinto**] Nyusi [2015-present] and Renamo leader **Afonso Dhlakama**. Besides, the national observers say that the issues discussed should be extended to other interested parties, including other political parties, the parliament and groups of civil society.”*¹⁴

The end of the EMOCHM mandate will delay an eventual agreement between Frelimo government and Renamo over armed forces integration.

*“Some national observers said that the military observers’ mission did not bring any results to the talks, because no list of the names of Renamo armed men was presented to proceed with the integration process, and there is a lack of humility from both delegations to recognise their incapacity to find solutions to the long lasting deadlock.”*¹⁵

The EMOCHM is a team of international military observers mandated to monitor the end of hostilities. The EMOCHM arrived in Maputo in September 2014. The mission officially began in October 2014, for an initial period of 135 days, prolonged for 60 days after the initial period expired.¹⁶ **Botswana** led 23 military officers from Botswana, **Zimbabwe**, **South Africa**, **Kenya**, **Cape Verde**, **Portugal**, **Italy**, the **United Kingdom (UK)** and the **United States (US)**.

Anadarko picks LNG contractors

Anadarko Petroleum Corp, a US-based independent oil and gas exploration and production company, picked **Japan-based Chiyoda Corp**, US-based **CB & I** and Italy-based **Saipem** (collectively known as the **CCS JV**) as the contractors for the initial development of its onshore liquefied natural gas (LNG) facility.¹⁷

¹² AIM, 28 Apr 2015.

¹³ Source, political analyst, Maputo

¹⁴ Source, political analyst, Maputo

¹⁵ www.clubofmozambique.com

¹⁶ www.clubofmozambique.com

¹⁷ www.clubofmozambique.com

Anadarko's announcement is a positive sign that the company is committed to the long-term development of Mozambique's LNG export sector. Anadarko chairman **Al Walker** said,

*"Selecting CCS JV for the development of the onshore Mozambique LNG park is a significant step toward reaching FID [final investment decision] and demonstrates our continued commitment to advancing this important project toward first cargoes ... I am incredibly proud of our co-venture for all of the accomplishments achieved to date, including securing more than eight million metric tonnes per annum (MMtpa) in non-binding long-term off-take agreements, which are now progressing toward binding SPAs [Sales and Purchase Agreements], obtaining letters of intent from lenders for project financing at a very material level, and working with the newly-elected government to keep the project moving forward."*¹⁸

The initial scope of work for the onshore LNG facilities includes two LNG trains, each with a capacity of six MMtpa which is an increase of one MMtpa per train over the original plan; two LNG storage tanks each with capacity of 180,000 cubic metres, condensate storage, multi-berth marine jetty and associated utilities and infrastructure.¹⁹ Italy-based **ENI**

*"... is described as the bigger winner of the competition as besides being the operator of the offshore **Rovuma Basin Area 4**, it also owns Saipem which is part of the consortium ... selected to work for Anadarko. However, the consortium will be led by the Japanese company Chiyoda."*²⁰

Despite this announcement, it still not clear when construction work is going to start. However,

*"Mozambicans seem already prepared to get their share of the business. Mozambican businessmen expect that the Mozambican companies would at least work in the provision of construction materials that will be needed for the project ... However, there were reports [of possible issues] from civil society this week with the land use title granted for the construction of the LNG plant on the **Afungi Peninsula**, in the province of **Cabo Delgado**."*²¹

A foreign journalist working in Mozambique says the land use assessment

*"... needs to be taken seriously since the team of jurists [conducting the assessment] was led by one of the most respected figures in the Mozambican judiciary, retired supreme court judge, **Joao Carlos Trindade**."*²²

Anadarko's agreement with CCS JV is subject to negotiation and entry into a definitive agreement prior to Anadarko and its partners completing the FID.²³ Anadarko operates the **Offshore Area 1** with a 26.5% working interest. Its joint venture partners include government-owned **Empresa Nacional de Hidrocarbonetos EP (ENH)** (15%); **Mitsui E&P Mozambique Area1 Ltd** (20%), **India-based ONGC Videsh Ltd** (16%) and **Bharat Petro Resources Ltd** (10%); **Thailand-based PTT Exploration & Production Plc** (8.5%) and **Oil India Ltd** (4%).²⁴

Fitch maintains Mozambique B+ rating

International ratings agency **Fitch Ratings** kept its rating on Mozambique's long-term debt in foreign and local currency at B+ with a stable outlook, in May.²⁵ Fitch said Mozambique's economic growth was expected to fall this year to 6.8%, after an average of 7.2% over the last five years. The cooling of the Mozambique economy will continue due to the adverse impact of floods in early January on agricultural production and infrastructure.²⁶ Fitch said the prospect of developments in the economy in the medium-term

¹⁸ World Oil, 18 May 2015.

¹⁹ Multiple sources: www.clubofmozambique.com; World Oil, 18 May 2015.

²⁰ Source, business analyst, Maputo

²¹ This was a conclusion of an independent judicial assessment, ordered by the Civil Society Platform on Natural Resources and the Extractive Industry.

²² Source, foreign journalist, Maputo

²³ Source, business analyst, Maputo

²⁴ World Oil, 18 May 2015.

²⁵ www.macaclub.com.mo

²⁶ www.macaclub.com.mo

remained favourable, despite the risks associated with the drop in the price of raw materials and the constraints in terms of infrastructure, with the development of the coal sector suffering from high transport costs and low prices in international markets.²⁷ Investment in Mozambique's natural gas sector is expected to continue;

*"The development of projects related to the exploration of natural gas deposits is expected to continue, and it is estimated it will cost US\$40 billion."*²⁸

Mozambique at risk of exceeding installed power capacity

Fernando Juliao, former head of state-owned electricity producer and distributor **Electricidade de Moçambique (EdM)** from 1980 to 1995, has warned that Mozambique's demand for electricity is in danger of exceeding its installed capacity.²⁹ Juliao said on 4 May that Mozambique will have to create infrastructure,

*"... not only in terms of generating capacity, but also in terms of transmission capacity so that the power reaches the centres of consumption".*³⁰

Currently, Mozambique consumes approximately 700MW of electricity. However, this figure excludes the **MOZAL** aluminium smelter on the outskirts of Maputo. Juliao expects consumption to increase within the next 20 years to 2,500 or 3,000MW. Juliao said this is the equivalent of another **Cahora Bassa** dam. The Cahora Bassa dam on the **Zambezi River** is the largest source of electricity in Mozambique. When operating at full capacity, Cahora Bassa generates 2,075MW. The majority of this power is sold to South Africa, under contracts with the South African government-owned power utility **Eskom**.³¹

Juliao admitted that his forecast for growth depends on industrial projects currently on the drawing board coming to fruition.

*"If some of the industrial projects that are envisaged do not happen, evidently that will change significantly the demand forecast ... the bodies responsible for planning the expansion of the system must pay careful attention to this."*³²

Juliao believes that funding new power production facilities is not a problem and said "any project that is viable mobilises finance".³³ However, that viability was largely dependent on exports,

*"We have to create an environment which allows the market and the investors to feel comfortable, to feel that they are entering a zone of credible investment, that gives them the prospect of a return on their investment, and that when they enter contracts to purchase power, those contracts will be honoured."*³⁴

Implications

The government needs to borrow to meet its 2015 budget obligations. Increased borrowing is manageable as long as Mozambique's debt to GDP ratio does not exceed 40%. Fitch's decision to maintain Mozambique's B rating is a sign that it has confidence in Mozambique's economic outlook and the government's fiscal management plan.

The end of the EMOCHM observer mission is not a signal of a return to a full-scale Renamo insurgency, but will delay an eventual agreement between the Frelimo government and Renamo over armed forces integration.

²⁷ www.macauhub.com.mo

²⁸ www.macauhub.com.mo

²⁹ www.macauhub.com.mo

³⁰ www.macauhub.com.mo

³¹ www.macauhub.com.mo

³² www.macauhub.com.mo

³³ www.macauhub.com.mo

³⁴ www.macauhub.com.mo

Anadarko's decision to award initial LNG contracts signals the company's commitment to the development and Mozambique, which is a positive sign of the long-term stability of the nascent LNG sector.

Mozambique's economic growth potential will strain electricity supplies, unless the government make a stronger commitment to addressing generation and transmission capacity. Electricity is a significant barrier to sustained growth in Mozambique, particularly in the extractive and infrastructure sectors.