

**Mozambique:  
Development Financing  
Assessment  
(DFA)**

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**Clarification:** The views expressed in this report are those of the authors and do not necessarily represent those of the institutions to which they are affiliated, including the United Nations Development Program (UNDP) or the Government of Mozambique, the United Nations or its Member States.

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## List of abbreviations

ADP	Public Expenditure Analysis
AOD	Official Development Assistance
AGO	General Budget Support
AFD	Financing for Development Assessment
AfT	Aid for Trade (Aid for Trade)
AIPEX	Investment and Export Promotion Agency
AT	Tax Authority of Mozambique
AR	Assembly of the Republic
BdM	Bank of Mozambique
BM	World Bank
BVM	Stock Exchange of Mozambique
CE	Business Awards
CFMP	Medium Term Fiscal Scenario
CGE	General State Account
COFOG	(Classification of the Functions of Government)
CPI	Investment Promotion Centre
CSS	South-South Cooperation
CUT	Single Treasury Account
DC	MEF Cooperation Directorate
DNCP	National Directorate of Public Accounting (MEF)
DNPE	National Directorate of State Patrimony (MEF)
DNPO	National Directorate of Planning and Budget (MEF)
DPEF	Provincial Directorates of Economy and Finance
DSP	Private Sector Development
EMAN	Strategy for the Improvement of the Business Environment
ENAMMC	National Strategy for Adaptation and Mitigation of Climate Change 2013-2025
ENDE	National Development Strategy 2015-2035
GdM	Government of Mozambique
GFP	Public Finance Management
FC	Fund Common

FCA	Municipal Clearing Fund
FIIA	Investment Fund for Municipal Initiatives
IMF	International Monetary Fund
FNDS	National Fund for Sustainable Development
FOFA	Weaknesses, Opportunities, Forces and Threats
FUNAB	National Environment Fund
GFP	Public Finance Management
GAZEDA	Accelerated Development Zone Support Office
GIRBI	Inter-ministerial Group for the Removal of Investment Barriers
FDI	Foreign Direct Investment
IGEPE	National Institute for the Management of State Participations
IMR	Infant Mortality Rates
IFMIS	Integrated Financial Management Information System (SIIGF)
INPS	National Institute of Social Security
IGEPE	Institute of Management of State Participations
IPEME	Institute for the Promotion of Small and Medium Enterprises
IRPC	Tax on Corporate Income
IRPS	Individual Income Tax
ITIE	Extractive Industry Transparency Initiative
VAT	Value added tax
MEF	Ministry of Economy and Finance
MIC	Ministry of Industry and Commerce
MINDEH	Ministry of Education and Human Development
MINEC	Ministry of Foreign Affairs and Cooperation
MITADER	Ministry of Land, Environment and Rural Development
MMR	Maternal Mortality Rates
MPME	Micro, Small & Medium Business
MZN	Meticais
ODAMoz	ODA Database (MEF)
MDGs	Millennium Development Goals
SDG	Sustainable Development Goals

OE	State Budget
OECD	Organization for Economic Co-operation and Development Organization for Economic Co-operation and Development (OECD)
OFO	Other Official Flows
PAPs	Programmatic Help Partners
PARPA	Action Plan for the Reduction of Absolute Poverty
PEFA	Public Expenditure and Financial Accountability
PEFP	Strategic Plan for Public Finances
PEPIP	Strategic Plan for the Promotion of Private Investment
PES	Economic and Social Plan
PII	Integrated Investment Program
PIM	Public Investment Management (Public Investment Management)
PIMA	Public Investment Management Assessment
PGD	Large Projects
GDP	Gross Domestic Product
PPP	Public-Private Partnership
PQG	Five-Year Government Plan
UNDP	United Nations Development Program
QNIF	National Integrated and Financing Framework
REO	Budget Implementation Report
SADC	Southern Africa Development Community (SADC)
SEE	State Business Sector
SIIGF	Integrated Information System for Financial Management (IFMIS)
SISTAFE	State Financial Administration System
SOE	Subsystem of the State Budget
SPE	Subsystem of State Patrimony
SPO	Subsystem of Planning and Budgeting
STP	Public Treasury Subsystem
SWAp	Sector Wide Approach
UNCTAD	United Nations Conference on Trade and Development
UGB	Beneficiary Management Unit

UGE	Executing Management Unit
USD	US Dollar
VFP	Overview of Public Finances
ZEE	Special Economic Zones
ZFI	Industrial Free Zones

## Executive summary

### 1. Introduction

**Although Mozambique has experienced stable economic growth in the last two decades, its economic and social challenges persist.** The economy grew at an average rate of 7.4% between 2005 and 2015, driven by sound macroeconomic management, large-scale foreign investment and continued support from development partners. However, a significant proportion (46%) of Mozambicans live below the poverty line, and the Human Development Index puts Mozambique in 181st place among the 188 countries analysed. About 70% of the population lives and works in rural areas, mainly in subsistence agriculture. Mozambique has good opportunities to achieve a sustainable reduction of poverty and promote inclusive growth, but for this, the government should implement sound policies in a complex fiscal and economic environment.

**The overall purpose of the AFDs is to help governments develop National and Integrated Funding Frameworks (QNIFs),** which propose a holistic and strategic approach to mobilizing resources (public and private, domestic and external) with a long and medium view consistent manner, to ensure the country's capacity to finance its development strategies. This concept, which was used for the first time in the Addis Ababa Agenda for Action, proposes a framework for governments to be able to develop an adequate perspective of financing for development under the Sustainable Development Goals (SDGs). This type of approach seems opportune to help the government to plan the actions that will be necessary to cross the economic crisis and begin to lay the foundations for solid and inclusive growth.

**The specific objectives of this evaluation are:** (i) to provide an overview of the evolution between 2005 and 2015 of major flows of development finance and their allocation and contribution to national priorities and results; (ii) assess the linkages between finance and results through the relationships between national planning and budgeting processes; (iii) assess the roles and responsibilities of national institutions in managing or influencing the development of individual financial flows; (iv) to analyse the interface between the different flows and the complementarities between the different development financing sources evaluated.

**This report is composed of several chapters, structured as follows:** [Chapter 2](#): describes the socio-economic context and the main development challenges; [Chapter 3](#): looks at how financing can lead to better development outcomes through more integrated planning and budgeting processes; [Chapter 4](#): analyses the quantitative and qualitative aspects of public finance management and the main sources of public funding available in the short and medium term; [Chapter 5](#): Examines the extent to which current efforts to strengthen private sector development are aligned with national priorities and the main sources of private finance; [Chapter 6](#): proposes a prospective framework to analyse the future development of financial flows, analysing the different graduation processes that the country will face in the near future; [Chapter 7](#): outlines the initial findings and key emerging actions of AFD.

### 2. Socio-economic context and main challenges

**The lessons learned in this period provide important clues to focusing on future policies to improve people's well-being and reduce poverty.** The country has several major challenges on the agenda: (i) demographic trends indicate that, in the medium term, more than 300,000 people will enter a labour market per year that is currently unable to absorb such volumes, (ii) most of poverty is concentrated in rural areas, while only 30% of poor households live in urban areas; (iii) although the majority of the population lives on small-scale agriculture, this is not a preference, but a choice of subsistence; (iv)

there is also a large informal urban sector characterized by low productivity; (v) highly capital intensive investment has shown little impact on employment and income generation.

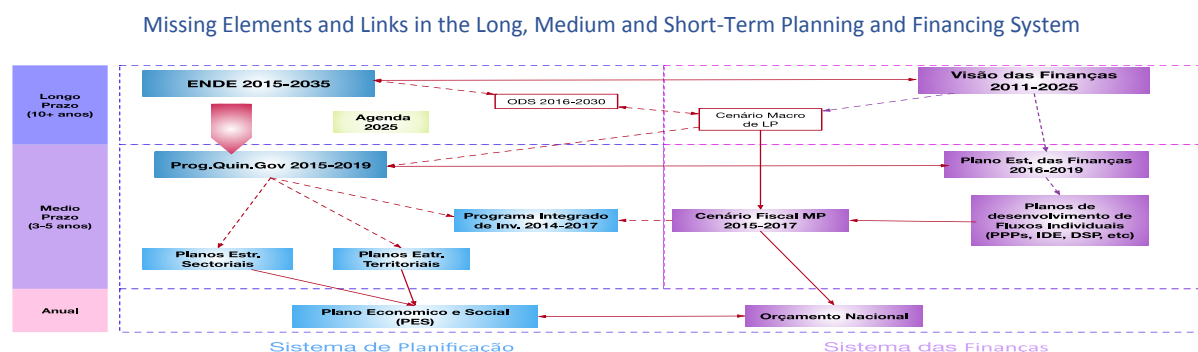
These challenges are clearly analysed in the National Development Strategy 2015-2035, which proposes a structural transformation of the economy, which will have to be more productive and competitive, focusing on industrialization for inclusive and sustainable growth.

**The country is going through a negative situation, the result of a series of factors, external and domestic, that in recent years have had a strong impact on the economy.** Mozambique suffered a fall in the international prices of raw materials that supported its exports. The one that registered in the natural gas delayed the decision on the realization of investments that could have generated important resources. Exceptional climatic factors affected agricultural production, with the resultant contraction of exports and generation of inflation. Faced with these pressures and accelerated metical depreciation, the government took measures to reduce public spending and called for international financial assistance. Complexity was relatively controllable, but the emergence of an unexpected situation in public debt management catalysed a short-term economic crisis that has significantly reduced short-term fiscal space. The current situation of debt (debt distress), makes negotiating the exit of the crisis difficult.

**Despite the short-term impaired situation, the prospects remain promising.** Although the situation is negative, the medium-term context allows for an optimistic outlook. The government is on the right track in seeking a negotiated settlement of the debt situation and continues to implement measures to moderate the short-term crisis. There are expectations that two megaprojects<sup>1</sup> of foreign investment can be confirmed that could bring significant capital flows and have significant multiplier effects on the economy. In addition, the unfavourable situation of international commodity prices began to reverse, which should speed up the interest for more investments. Beginning offshore gas projects to generate export, an expansion of the economy is expected to achieve the highest real GDP growth rates in sub-Saharan Africa.

### 3. National planning and financing systems

AFD has identified concrete opportunities to improve the potential and quality of existing instruments, their horizontal and vertical link, and the need for some new elements. The results of the review of the main elements of long, medium and short-term planning and financing systems are presented in the Figure, highlighting the links that should be redesigned or improved and some additional elements (which are marked in red). AFD proposes the following improvements:



<sup>1</sup> A gas investment by the Italian company ENI Coral in the Rovuma Basin of approximately US \$ 8 billion and the investment of US \$ 12 billion Anadarko, which are expected to be concluded in 2017.

*Development of an integrated long-term vision.* ENDE review to achieve the SDG should improve the technical quality of the results tables and include cost analysis to ensure their viability. The review of the VFP should address the development of public and private finances necessary to enable the implementation of the NSDS;

- *Improve vertical integration between medium and short-term instruments.* On both the plan and the finance side it is important to ensure consistency between the long-term strategic guidelines and the medium-term plans, and the targets of both the PQG and the PEFPs;
- *Improve horizontal matching between plan and medium-term finance instruments.* Such matching is necessary to ensure consistency between the results proposed in the PQGs and in the PEFPs;
- *Improve the quality, prioritization and comprehensiveness of the Integrated Investment Program (IIP).* There is a need to accelerate the reform of public investment management and improve the technical quality of the IIP, its prioritization process, and its inclusion in the focus of reforms to improve the integration of planning and financing systems;
- *Accelerate the introduction of the new system that ensures horizontal integration between PES and OE.* The reforms to introduce the program budget and a results-based financing system are medium- and long-term initiatives that are essential to ensure the quality of public spending and better social development results in the next phase of rapid growth.

**SDGs programming will provide the opportunity to initiate changes to facilitate the integration of the plan and finance system.** Developing an integrated vision for long-term planning and finance is an important precondition for a realistic formulation of SDG. Countries should adjust the SDG targets to find solutions that are affordable to the economic and capacity reality, which is why it is necessary to analyse the costs of the proposed targets. SDGs also require a much more complex plan and finance system as the proposed objectives are highly interlinked to respond to the three dimensions of sustainable development: economic, social and environmental.

#### 4. Public finances and major flows

**Mozambique's public spending is among the highest in the region, but its effectiveness must be given priority.** Macroeconomic performance has ensured rapid economic growth that has ensured good macroeconomic stability, but with poor social development results. The level of public investment in the country is relatively high, but its growth has been highly dependent on donations from development partners. The structure of public spending presents a worrying increase in expenditure on wages and non-wage benefits. Analysis of expenditure allocation and results by sectors indicates the need to deepen and improve budgetary processes, and to focus on the efficiency of public expenditure.

**Increasing efficiency and resource efficiency should be a high-priority area in the management of short-term public finances.** 'Efficiency gains' could considerably increase the available short-term fiscal space. The government should explore several complementary approaches:

- *Improve efficiency in resource allocation.* Improve matching of available resources with priorities and ensure their distribution to the neediest beneficiaries;
- *Improve the impact of public spending on development.* Study the opportunities for more metical development spending, essentially improving the value chain's productivity in providing the most essential public services;



- *Increase tax space by eliminating unnecessary resource losses.* Systematically reduce unnecessary expenses, especially losses of public and investee companies;
- *Increase tax space by reducing subsidies.* Continue the gradual reduction of fuel subsidies, which also negatively affect other sustainable development objectives.

**Initial estimates indicate that the 'efficiency gains' analysed could yield significant results.** The achievement of visible results at the macro level will be achieved through the implementation of a series of measures and interventions that individually produce results at the micro level. However, the more conservative estimates available indicate that the volume of fiscal space that these interventions could release together is highly significant, as the estimated total is 13.5% of GDP, which is half of total public revenue. Therefore, it is recommended to focus attention on the design and financing of a Program to Improve Public Expenditure Efficiency that can achieve a good part of these results within 3-5 years.

Estimates of the fiscal space to be released by the analysed measures that can be quantified

Efficiency Improvement Area	Tax Area that Could Be Released (% of GDP)
	PIB)
Increased revenue collection in richer municipalities	3%
Reduction of the cost / GDP of children enrolment	2.4%
Reduction of the cost / GDP of health services	1.5%
Improvements to the public procurement system	1.3
Public investment	3%
Losses of public companies (reduction of 50%)	1.4%
Losses of investees (reduction of 50%)	0.4%
Reduction of subsidy (reduction of 50%)	0.5%
<b>Total Fiscal Space Estimated</b>	<b>13.5%</b>

### Evaluation of the main public flows

**(i) Public Revenue.** During the period considered, there was a significant increase in total revenues over GDP, and the performance of the Mozambique Tax Authority (TA) has been high. The analysis of the relative weight of large taxpayers in revenue leaves some doubt about the distribution of the tax burden, so it is recommended a review of the cost-benefit ratio of the system to attract external investment based on the provision of large tax benefits, which may not be necessary. There is evidence that revenue could increase at least 3% of GDP by improving control of tax evasion in the production and export of natural resources. For this, the development of the capacity of the Tax Authority is an area of priority. In addition to the above-mentioned improvements, there are other options that have not yet been explored: (i) the possibility of introducing greater progressiveness and pro-poor orientation in the current tax system; and (ii) continue efforts to increase the taxpayer base, with greater incentives for the expansion of the formal sector of the economy.

**(i) External Debt.** Until the crisis, the country was making progress in improving the debt management system, successfully implementing the reforms established in the VFP. The aftermath of the crisis is marked by a deterioration in the country's external position that undermines short-term economic stability. The current profile of public and publicly guaranteed external debt (PPG) is not sustainable. To get out of this situation, the government went the right way: negotiating with creditors a stepped-out way to allow responsible return to capital markets. Future management will require improving the

government's 'control panel' and technical capabilities for quality management in the following areas: (i) management of commercial debt with government guarantees and the risk of contingent liabilities incurred; (ii) management of the blend finance ensuring the viability of the projects financed, especially with South-South cooperation funds; (iii) public investment management and debt sustainability. However, a significant part of the debt problem of public enterprises is not of technical origin, and notes the need for further reforms to ensure the integrity of public management.

**(iii) Official Development Assistance (ODA).** The weight of ODA significantly decreased during the study period; nevertheless, Mozambique continues to be dependent on international cooperation. Over the last ten years, most ODA has been channelled through General Budget Support (AGO), but a few years before the crisis the overall effectiveness of this aid had evolved negatively. Changes in donor behaviour after the outbreak of the crisis determine negative dynamics, with a decline in the use of the AGO in favour of aid by projects. New modalities should be explored to reorient ODA flows to pre-2016 levels and improve the quality of alignment with national priorities. In the short term, the government should improve the quality and use of Management Information Systems (ODAMoz) and strengthen its leadership capacity in the strategic orientation of ODA, ensuring the conditions for efficient and transparent use of resources.

**(iv) South-South Cooperation (CSS).** CSS is a source of funding with great potential in Mozambique, and takes the form of credits to the public sector. During the period under review, China has established itself as a partner that has made more funds available. The available information omits important data and does not allow a good analysis of this flow. The cost-opportunity ratio of these funds should be duly assessed against other options. Good CSS management will require greater government capacity, especially to evaluate the cost-effectiveness of the final work financed together with the cost-benefit assessment of the credit, which is usually done separately. The government should negotiate with suppliers more favourable conditions for the country, such as the elimination of credits that do not allow competitive procurement processes. The government should also consider the benefits of unifying management and integrating information corresponding to CSS with ODA.

#### Other Public Sources

Following is a list of public funds that may be important for the future of the country, but that for reasons beyond the organization of this work could not be properly evaluated.

**(v) Climate Financing.** The limitations and opportunities to improve the management of this flow are being evaluated by a specialized study, and it has not been possible to estimate the quality of expenditure for adaptation and mitigation of climate change. Governance of environmental and sustainable development policies has traditionally been a challenge, and with the creation of MITADER the government has begun a process of reforming the institutional, policy and financing framework. The new strategic framework proposes structural changes and targets that could entail significant costs for public and private investment. MITADER hopes to address outstanding issues of climate finance with the creation of the National Sustainable Development Fund (FNDS). The potential of the FNDS for this purpose is important, but its design should consider national and international issues. In the financial aspects, the MEF should be actively involved in incorporating the lessons learned from the management of other funds and avoiding overlaps with existing funds. Considering the great potential to obtain greater international financing of this flow, strategic coordination of the formulation and management of the timing of climate financing should be better analysed.

**(vi) Non-tax revenue.** Revenues analysed in this evaluation as 'Non-Fiscal' include items accounted for in three different categories in national accounts (Non-tax Revenues + Consigned + Capital). The

evolution of this revenue was much weaker than that observed in the tax revenue, and its growth potential should be analysed. Within the group studied, the observed behaviour of some categories draws attention to the decreasing evolution of capital revenues and own revenues. Specific short- and medium-term targets should be set for this type of revenue to force control and improvements in management quality. Progress in the collection of this type of revenue has points of contact with improving efficiency in public management.

**(vii) Illicit Flows.** Containment of tax evasion and the closing of important legal gaps could bring substantial revenue. International studies of independent monitoring agencies allow estimates of illicit flows to the attention of the authorities to have averaged 8% of GDP in the period under review, which is higher than the average for Sub-Saharan Africa (6.1%). Adulterated commercial invoicing accounts for most of these illicit capital flows. In Mozambique, companies use the practice of adulterated invoicing of imports and exports alike. It was also detected the habitual use by companies established in the country of subsidiary companies based in tax havens to favour these practices. The government should better quantify the level of public finance damage generated by these losses in terms of public revenue and take steps to eliminate them.

**(viii) Revenue on Natural Resources.** The government has much expectation in the revenues that may be generated by future hydrocarbon exports. The possibilities for generating future revenues from the mining sector are also very good. The international comparison indicates that income generation related to the exploitation of mineral resources is very low. One of the reasons is the high level of exemptions granted by the investment promotion system. In addition, there are indications that the tax evasion of this sector is potentially very high. The sustainable production of these resources, as well as the control of revenue generated, should be a concern and a priority. The government is taking individual steps, but a systemic solution is needed that reviews the revenue, the responsibilities of its implementation, and the monitoring and control systems. Returning to the Extractive Industry Transparency Initiative (EITI) would allow for greater transparency and improved social control in the management of revenues generated by extractive industry companies, which would certainly reduce the risk of misappropriation.

**(viii) Other options to be explored.** Mozambique could consider using SWFs to ensure sound management when the expected boom in oil and gas revenues hits. Countries use these funds to ensure the effective use of resources from the extractive sector and to balance current and future needs. The case of the Timor-Leste Fund analysed could be an example to consider. It is also proposed to consider expanding the use of Aid for Trade (Aft), an ODA modality that would lengthen the duration of this funding in the medium term.

## 5. Private Finance and Main Flows

**Private Sector Development (DSD) is a priority in the country's key strategic documents, and the levels of investment achieved describe a history consistent with these priorities.** The ENDE emphasizes the importance of agriculture as the basis of national development and places the manufacturing sector as a driving force for the economy. Future promotion must address significant issues of business structure segmentation. In Mozambique, there are practically no large companies (1.3% of the total) or medium-sized enterprises (1%), and the business sector is dominated by micro-enterprises (78.3%) and small enterprises (19.4%). Most of these companies operate in the car trade and repair sector (55%), or in the hotel and restaurant sector (21%). ENDE priority areas are a small minority: only 10% of the companies are manufacturing and 3% are from agriculture, livestock, hunting, forestry and fishing. There are also important regional asymmetries. The South region

concentrates the largest number of companies (52%) and monopolizes the turnover (80%), generating 61% of the total employment.

**The government has embarked on a long-term effort to remove obstacles to the development of the private sector.** International comparative studies (from the World Bank and the World Trade Organization) coincide in assessing as very weak the conditions for business development and the international competitiveness of Mozambique. The reasons for this poor qualification are manifold, among which: (i) poor access to financing; (ii) inefficient government bureaucracy; (iii) corruption; (iv) inadequately qualified workforce; (v) deficient infrastructure and access to electricity. The design of the next Business Environment Enhancement Strategy (EMAN) incorporates lessons learned from the implementation of the above and strongly focuses on an improved system of dialogue with the private sector. A pending issue of the new EMAN is the development of prioritization procedures - in conjunction with the private sector - of strategic reforms and large-scale investments.

#### Evaluation of the main private flows

**(i) Private Financial Sector.** Domestic credit to the economy grew unevenly, more without credit alignment with some of the sectors considered key to development, such as the industrial and construction sector, agriculture and tourism. The evaluation has shown that there is a competitiveness problem in the cost of credit in the local market, which may be related to a highly concentrated banking system, where the three largest business groups collectively collect 79% of deposits and grant about 77% of credit. Increasing access to credit on competitive terms for priority sectors should be the focus of the next government actions. Since its launch in 1999, BVM has not yet developed into a robust market that can contribute to the deepening of the financial sector and the provision of long-term credit to domestic companies.

**The government has recently initiated policies to strengthen financial inclusion.** Individual financial inclusion policies should solve basic socioeconomic problems and supply inadequacies. Access to credit for MSMEs continues to be far below requirements. The improvement of this access depends on several factors: (i) poor access and availability of information on financing, (ii) low financial literacy of users and weak domain of financing information; (iii) weak structural capacity of MSMEs to become bankable; (iv) inadequacy of the supply of financing for MSMEs. Future measures should aim at strengthening the financial system in a comprehensive way to ensure the growth of a robust system that improves performance and enhances the competence of financial institutions (banks, microcredit institutions and insurance companies). These measures should be complemented with other measures aimed at strengthening the financial markets, the development of the Mozambique Stock Exchange and the dynamism of equity and bond markets.

**(ii) Foreign Direct Investment (FDI).** The FDI has grown significantly during the last decade, especially in megaprojects in the extractive industries. The cost-benefit ratio of promoting this type of investment should be assessed due to evidence indicating that its impact on income generation and poverty reduction was rather limited. Although it is the sector that contributes most to the GDP, and that more workers employ, agriculture absorbed only 10% of FDI. FDI generation has also been concentrated in a few countries, indicating the potential of promotional activities.

**The government is implementing institutional reforms to improve the impact of investment promotion and export policies.** The new AIPEX should improve monitoring systems to monitor the impact of FDI, and assess the potential of the FTZs and EEZs, as well as the usefulness of existing policies. The most critical issue will be how to ensure the quality of FDI - rather than quantity - and its contribution to the country's sustainable economic growth. When developing new policy frameworks

and fiscal incentives, the government should consider well-known limitations in international experience regarding this flow.

### **(iii) Public-Private Partnerships (PPP), Corporate Concessions (CE) and Large-Scale Projects (PGD).**

The growth of this flow has increased over the past decade, and very strongly in recent years. There is no evaluation of the performance of PPPs, CSs and PGDs in Mozambique, but the available evidence suggests that government learning is characterized by mixed experiences. Despite the lack of official information, situations are known where the state had to intervene and take significant losses to rescue distressed PPPs. The problem is not exclusively Mozambican, and international experience indicates that this is a very difficult area of policy in developing countries. There is evidence that the State participates in PPPs through state-owned enterprises operating in the sector. Considering the recent debt situations generated by public companies, this point should receive a lot of attention.

**The government has taken steps to order the legal framework governing these flows and to provide them with coherence.** The law establishes general principles for managing the risks inherent in PPPs, which can generate a false sense of security. The evaluation identified the need to move forward in strengthening government capacity in a number of critical areas: (i) improve strategic decision-making and prioritization of PPPs; (ii) strengthen the centralized capacity of managing PPPs and limit the decisions released at the decentralized level; (iii) define a risk management unit that concentrates highly specialized expertise; (iv) strengthen the capacity of the PPP management units of the sectoral regulatory authorities of government contracting; (v) define the existence of an independent arbitration agency and (vi) strengthen the international promotion of PPPs, linking these activities more directly to actions to promote national investment and FDI.

### **Other Private Sources**

The following is a list of private funds that could be important for the future of the country, but which for reasons beyond the organization of this work could not be properly evaluated.

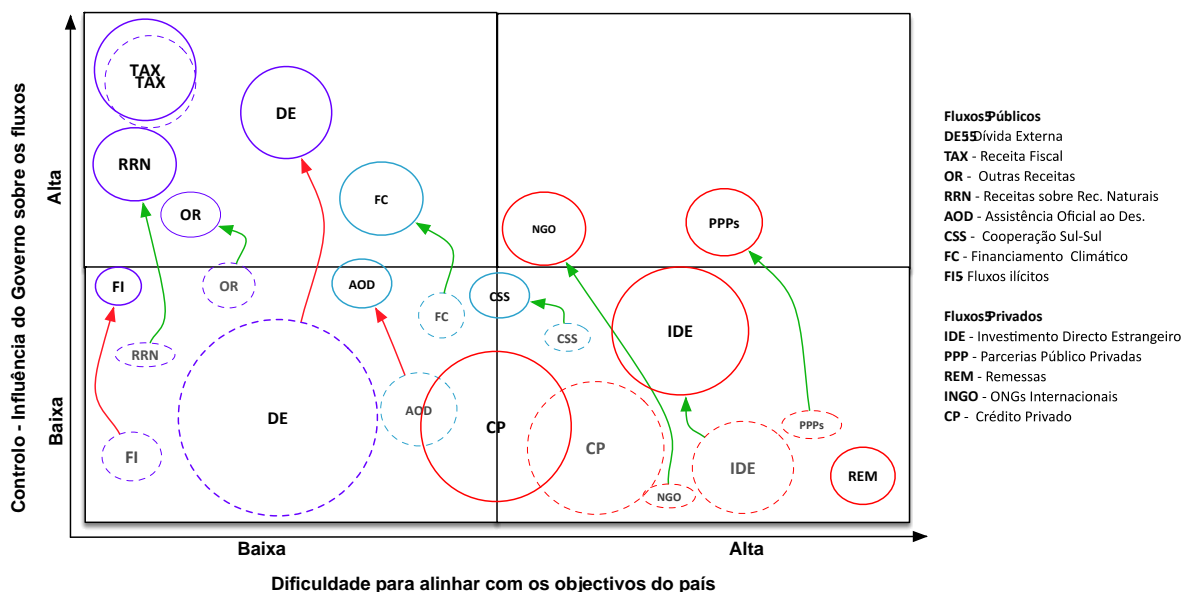
**(iv) Remittances.** A large part of the population (23%) used remittance services, most of them within Mozambique. The use of migrant labour is a historical fact in Mozambican tradition and in the period under review, and flows of private remittances from abroad have been growing. The Banco de Moçambique collects all statistics concerning remittances, but it is not the only institution that collects information. Institutions such as the Ministry of Labour, among others, also collect information on remittances generated by mining workers. The government is unaware of the destination and final use of remittances by receiving families. This knowledge could be used to design policies to improve the impact on these households, facilitating, for example, access to credit to build or improve homes, or to finance small commercial and agricultural businesses.

**(v) International Funding to NGOs.** The role of these organizations is recognized by the government, however, in all sectors analysed, coordination difficulties and information gaps were evident. The lack of data on funds channelled through NGOs (both national and international) is one of the great challenges the government faces to manage this flow well. Private development aid is one of the most important sources of financing for growth in the world, and is still little explored in Mozambique. Experiences at sectoral level make it possible to be optimistic about the possibilities of this type of financing. There are, however, no evaluations to compare the relative efficiency of NGO performance in the provision of public goods and services in Mozambique. The legal framework governing NGO activities in Mozambique is old, incomplete and needs to be reviewed. The revision of Decree 55/98 is a high priority and should reinforce procedures to ensure the government's protection of the annual activities of NGOs, by sector and geographic level. The review could force all NGOs to report directly

to ODAMoz on the type and destination of funding entering the country. The quality of this information could be verified with greater controls through TA. The revision of the Decree could also introduce incentives and other mechanisms to enhance private investment in activities aligned with national targets. The potential volume of this type of financing is very high and can be streamlined quite quickly, without major costs to the government.

## 6. Prospective Analysis of Major Financing Flows

### *Necessary changes in the management of flows*



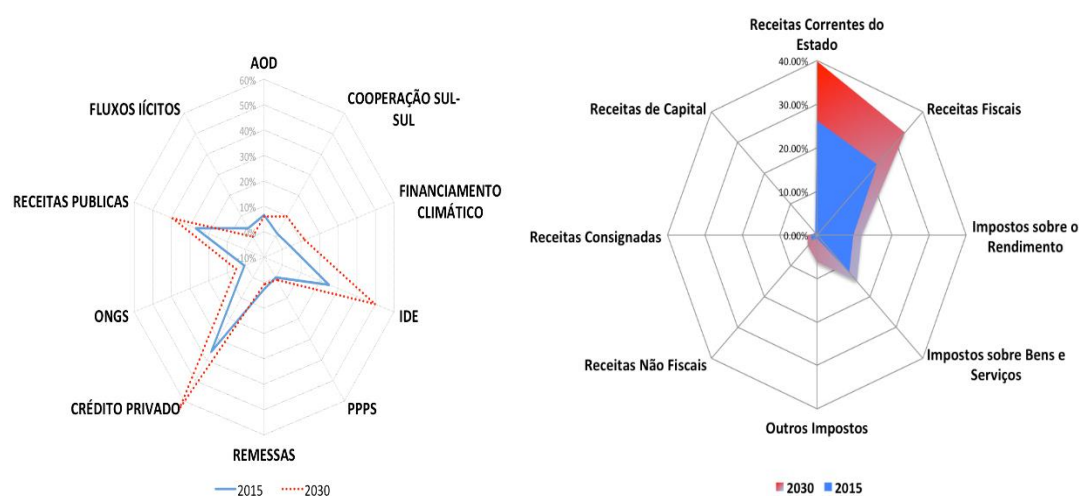
**The analysis indicates the need to improve the control and alignment of the main flows.** The figure below summarizes the results of the prospective analysis and presents the relative position of the flows according to the two variables: (i) the government's ability to control or influence flow evolution; (ii) the level of flow alignment in financing national priorities. The size of the streams presented is not exactly scaled, for graphic display purposes. The figure illustrates what could be the final situation for the flows analysed in Chapter 6. The red arrows indicate the flows that should be reduced in volume, while the green ones indicate those that can increase. The AFD also proposes significant changes in government control capacity (moves up on the chart) and a lot more modest in terms of alignment (left-hand movements in the chart). This is because, to achieve alignment improvements, reforms of the planning and budgeting system need to be implemented.

**The projections of the future evolution of the flows were analysed, considered the new situation of the country and corrected the ENDE original projections.** The purpose of this exercise is to generate a strategic discussion about the need for government to exercise leadership in the management of proactive policies to influence the development of these flows. The example of State revenue projections, analysed in detail in Chapter 6, shows the value that this work could have if it were carried out exhaustively and recurrently.

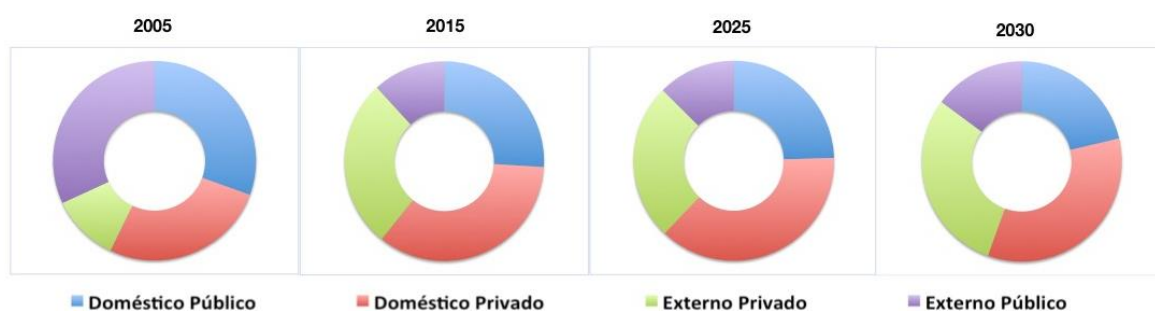
**The result consolidates a structural change in the distribution of the main sources of financing available in the country.** The following figure summarizes the main projections of financing flows and illustrates a framework dominated by projected growth in FDI, Public Revenues and Private Credit. It also indicates the increasing incidence of other flows such as Climate Finance and South-South Cooperation. The figure also gives an idea of the changes in the composition of Current and Capital

Revenues of the State, with a significant growth of other taxes (related quite directly to the exploitation of mineral resources), and of non-fiscal revenues. The internal distribution of the Tax Revenue assumes small changes, favouring the continuation of a moderate growth of income revenues, in relation to those of SDG and services. The last graph shows the progression of the structure of the main sources of financing that support the economy: domestic and foreign; public and private. The trend of structural change is relatively clear: as the country makes progress, it relies less and less on external public funding and consolidates the predominance of private finance and public revenue. The composition changes within each category also mark a clear trend. For example, external public funding increasingly incorporates climate finance and SSC flows, with a progressive reduction of ODA.

Expected evolution of major flows and Public Revenue (% GDP)



Evolution of the Financing Structure



**To achieve these results, the government must implement important changes in the policies that govern the different flows.** The analysis presented in Chapters 4 and 5 of the AFD and summarized in Section 7.3 indicates that in most cases, to achieve these results, the government must implement important reforms in the policy frameworks that govern flows and in institutional coordination mechanisms. It will therefore be necessary to develop five-year strategic plans defining the sequence of interventions needed to achieve these transformations.

**A final aspect to be considered is the desirability of developing an integrated strategic vision to improve the joint impact of the reforms undertaken on individual flows.** Chapter 6 provides a concrete example of the interactions observed by AFD in leveraging the financing of large-scale infrastructures that hinder private sector development. The example examines how to achieve

synergistic benefits through integrated management of policies to improve the management of public investment, prioritization and promotion of PPPs and FDI, adjustments to incentive schemes for private domestic financing and strategic use of ODA to prioritize implementation of these measures.

## 7. Recommended Action Areas and Implementation Roadmap

The main proposition of the AFD is to integrate the actions emerging from the evaluation into a medium-term Economic Transformation Plan (2018-2030). Despite the short-term situation, the prospects are very promising. Managing the transformation will require combining several specific strategies. The interventions that should form part of the plan are complementary and necessary to ensure the quality of the transition in the short and medium term, and propose actions in the three strategic areas summarized in the table. The adoption and implementation of this plan will require high-level political decisions.

Main strategic areas of the Economic Transformation Plan

<i>Área Estratégica</i>	<i>Propósito</i>
<i>Reforms to increase short-term fiscal space</i>	Interventions to reduce losses and increase the volume of some flows that could have great effect in the short term
<i>Structural reforms to improve the quality of management in the medium term</i>	Structural reforms to improve the quality of management in the medium term
<i>Reforms to develop the most important flows in the medium term</i>	Reforms to increase the volume and align funding flows with national priorities in the medium term

### *Strategic Area I: Reforms to increase short-term fiscal space*

**Actions to increase the short- and medium-term fiscal space are complementary and can be implemented quickly.** The evaluation identified several intervention opportunities that could have a major impact, and grouped them into two broad categories:

- *Actions to reduce losses.* Essentially the actions aimed at increasing efficiency and effectiveness in the management of public expenditure in some specific areas identified in Chapter 4;
- *Actions to increase the inflow of new funding.* Improving the management of a selected group of flows that could have significant impact in the short term

**(i) Actions to reduce losses.** Chapter 4 of the AFD proposes a list of interventions that have been identified in other works commissioned by the government. There are likely to be other sources of inefficiency that may also be included in this component of the Economic Transformation Plan, but research into its existence should not be grounds for delaying the start of these reforms. The areas of action identified offer the following opportunities to free up fiscal space as a percentage of GDP:

- *Increase in tax revenues in the richest municipalities (3%).* The target was calculated considering only estimates of higher collection in Maputo and Nampula by increasing property tax and other local taxes;
- *Reduction of costs in the provision of education services (1.4%).* The productivity of decentralized management of delivery of education services is very low. The goal is



conservative as it assumes that only half of the reduction in primary education will be achieved, leaving the improvements from secondary to the next stage;

- *Reduction of costs in the provision of health services (0.7%)*. It will be necessary to revise the forms of essential services (whose unit cost is very high), inefficiencies in the allocation of resources in provinces according to population, and imbalances in the hiring of technical and administrative personnel. The goal is also conservative, since it assumes that only half of the possible improvements will be achieved in the short term;
- *Reform of the public procurement system (1.32%)*. The main area of improvement is the increase in the use of procurement processes that apply competitive methods, since of the 46.4 billion meticaes of the acquisitions of 2014, 52.9% were contracted by direct agreement;
- *Management of public investment (1.5%)*. The efficiency of public investment is 41% lower than the standard comparison values, and the main sources of inefficiency are included in the Public Investment Management Reform Plan, which should be implemented with high priority. The proposed goal assumes that only half of these benefits will be obtained in the short term, and the other half will be achieved in the next phase;
- *Losses and Risks of Public and Participated Companies (0.9%)*. Total losses were estimated at 3.5% of GDP. To reduce it, the system needs to be improved to monitor performance, eliminating fragmentation in supervision and developing critical technical capacity. The short-term goal assumes that only a fraction of this reduction will be achieved during this phase;
- *Reduction of subsidies (0.5%)*. The fuel subsidy is the main element to be considered. The government has already announced its phasing out and has taken the correct decision not to withdraw the subsidies to public passenger carriers. This component is of high social impact and little significant in the volume of this expenditure.

**Reforms concerning efficiency should be viewed as processes of continuous improvement.** The design of the perfect 'form' before beginning the implementation of measures is a path that can be very long. The areas highlighted are well known, and therefore reforms can begin with relatively basic, sufficiently good measures that can be implemented without thorough knowledge. After ensuring short-term results, ongoing medium-term improvement processes can be initiated to carry out the studies that are needed and to improve the measures originally taken.

**The technical component of this type of reform is very important.** Although it is with rudimentary elements of analysis, these measures must be designed with technical knowledge of the processes to be improved. Generic and simplistic measures, such as the general suspension of staffing, or generic cuts in the use of fuel or in the purchase of vehicles, should be avoided. The best way is to negotiate with the responsible ministries a plan with a two-year timetable, with concrete reforms and targets, and to ensure the necessary resources and government support to implement these reforms.

**(ii) Actions to obtain new resources.** The government should consider accelerating The government should consider accelerating the reforms in the following flows, as they could mobilize additional fresh funds with important values (as% of GDP) in the short run.

- *Increase in Revenue from Illicit Flow Reduction (3%)*. For its reduction, the government can begin by improving the control and inspection capacity of the AT and Customs of the export / import companies and limit the use of tax havens by companies established in the country. The short-term target counts only the effect that could be achieved with stricter control over companies exporting natural and mineral resources;
- *Climate Financing (3%)*. The short-term goal assumes that the design of the FNDS is successful and that the fund can progress faster than it has achieved so far. It is important to note that

the intelligent use of climate finance funds for adaptation could replace current infrastructure investment demands even in sectors such as education and health;

- **Official Development Assistance (3.5%).** The crisis has led to an ODA decline of 4% of GDP that can be recovered. The government could combine two approaches: (i) convince partners to invest in the Economic Transformation Plan, as reforms are critical to building trust. (ii) Explore other financing modalities. For some partners, a return to AGO will be difficult, and the government can explore the use of mechanisms to increase aid effectiveness and reduce donor fiduciary risk. There are several options to be explored, such as the use of pooled finance, or other pooled finance mechanisms, but avoiding their proliferation and the consequent fragmentation of funding;
- **International funding to NGOs and Private Institutions (2%).** The estimated target is conservative because this flow can grow more than 5% of GDP in the medium term if the government makes some improvements in the current legislation and begin to proceed with a more strategic and integrated management. The improvements should introduce more strategic and efficient systems of dialogue, and for well-defined purposes at different levels. This can also be a way of rescuing ODA funds that will not return as an AGO, but which, with good management, can reduce public funding in specific areas. A new system of stimulating public-private co-financing and more decisive international promotion actions could also significantly increase these investments.

The data in the table summarizes the gains that could be achieved in the two areas in the short and medium term and should be taken as primary estimates of the possible impact of this type of action. The deadlines correspond to the first two phases of the Economic Transformation Plan analysed below.

*Expected Effects of Short and Medium Term Proposed Interventions*

Effect	Reducing Losses / Increasing Efficiency	Expected Benefit (% GDP)	Additional Resource Volume by Selected Financial Flows	Expected Benefit (% GDP)
Short Term (2018-2021)	Increased collection in richer municipalities (Maputo and Nampula)	3.00%	Increased revenue from raw material exports and reduction of illicit flows	3.00%
	Reduction of fuel subsidy	0.50%	Increase in Climate Financing	3.00%
	Reform in the system of public acquisitions	1.32%	public and private (FNDS)	3.50%
	Improving the efficiency of public investment processes	1.50%	Increase in Official Development Assistance (ODA)	2.00%
	Reduction of the cost of enrolment in primary education (HR reform and salaries)	1.40%	Increase in NGO Financing	
	Reduction of losses of Public and Participated Companies (reduction of 50%)	0.90%		
	Reduction of the cost / GDP of health services	0.70%		
	<b>Total Estimated Short Term</b>	<b>9.32%</b>		<b>11.50%</b>
Medium term (2022-2025)	Collection in richer counties	1.00%	Total Estimated Short Term	2.00%
	Reform in the system of public acquisitions	1.00%	Increased revenue from raw material exports and reduction of illicit flows	6.00%
	Improving the efficiency of public investment processes	1.50%	Increase in Climate Financing	1.00%
	Reduction of losses of Public and Participated Companies (reduction of 50%)	0.90%	public and private (FNDS)	3.00%
	Reduction of the cost of enrolment in primary education (HR reform and salaries)	1.00%	Increase in Official Development Assistance (ODA)	
	Reduction of the cost of enrolment in secondary education (HR reform and salaries)	7.00%	Increase in NGO Financing	
	Reduction of the cost / GDP of health services	0.7 %		
	<b>Total Estimated Medium Term</b>	<b>13.10%</b>	Total Estimated Medium Term	<b>12.00%</b>

*Strategic Area II: Structural reforms to improve management quality*

The Economic Transformation Plan should ensure the short-term start of implementing a list of critical reforms to improve the MEF's capacity in medium-term Public Finance Management. The list of priority reforms reviewed in the AFD includes the following:

- **Management of the Efficiency of Public Expenditure.** The actions examined in the previous section will not happen spontaneously and will depend on a programmatic formulation and the specific assignment of responsibilities for its implementation;
- **Public Investment Management.** Prioritize the implementation of the public investment management improvement plan, which should provide a much-improved version of the IIP to

efficiently prioritize public investment and plan the best use of public-private investment, especially for large infrastructure priority projects. scale;

- *Public Debt Management*. Develop technical capacities to improve the quality of management and provide a new 'dashboard' that allows efficient management of commercial debt with government guarantees, blend finance management systems efficiently using CSS sources, Public Investment Management and Integrated Investment Plan;
- *Reformulation of the ENDE*. Improve the results framework and indicators and aggregate funding estimates to analyse the feasibility of the proposed objectives. This is compatible and can be carried out with the opportunity of programming the response of Mozambique to the SDG;
- *Improvement of the Technical Quality of the Medium and Sectoral Plans*. A capacity-building process needs to be initiated to ensure the homogeneous qualities of these plans that allow the introduction of the program budget;
- *Reformulation of the Public Finance Vision*. (i) Define quantitative targets to develop finances at levels that ensure the viability of the NSDS; (ii) Broaden vision including the development of public and private finance in planning;
- *Implementation of the Program Budget*. Accelerate the introduction of the new program-based budgeting system to allow for the future introduction of a results-oriented management and financing system;
- *Medium Term Financial Flow Development Plans*. The new Finance Vision (VF) should be implemented through more comprehensive five-year Strategic Finance Plans (SPFs), which consider the management of funding from public and private sources.

**These reforms are preconditions for the sustainable management of resources that could be generated during the next phase of rapid growth.** The country should use the way out of the crisis as an opportunity to initiate these actions that will strengthen the medium-term public management system and ensure the sustainable use of resources for the future. To achieve the desired medium-term results, reforms must begin now. In this and other areas of the plan, a financing approach is required to ensure sufficient investment of resources and their medium-term availability, as discussed below.

**The main implementing and beneficiary of these reforms is the MEF.** Most of the actions listed above already exist as initiatives, or included in projects in different areas of the ministry. But in all cases, these initiatives could benefit from strategic prioritization and support from the top leadership of the MEF. The most important result of these reforms is not simply the introduction of new work systems. The reforms seek to strengthen the institutional capacity of different critical areas of the Ministry.

### Strategic Area III: Reforms to develop the most important flows

**The evaluation identified concrete opportunities to develop a wide range of financial flows.** For the better development of each, it will be necessary to transform AFD's proposals into medium-term strategic plans that will allow for the projections of the necessary reforms to improve the quality of policies and the institutional and coordination aspects that govern each flow. The vast majority of the solutions proposed in AFD are in line with existing government initiatives. Table 21 summarizes the complete list of all areas of action that emerged from AFD flow analysis.

**Prioritization of the work to be done will be required.** Attempting to address all these issues at the same time would be a major challenge, considering the other priority actions discussed above. The government should prioritize the emerging agenda and define a realistic list of interventions to be

addressed in the next GFP based on the AFD results and other government priorities. For this purpose, it is recommended to consider the following short-term preparatory actions:

- *Promote an integrated approach of government.* As in previous cases, decision-making on the implementation of some of the recommended actions exceeds the mandate of each government institution and will require a strategic discussion at the highest level;
- *Improve the search for key flows.* The time available, the low collaboration of some agencies and the inconsistencies of the data sources available did not allow to complete the search of some financing flows that may be important. This study will show the potential of some flows that may be important to consider in the Economic Transformation Plan;
- *Better search the interrelationships between key flows.* The analysis presented in Section 6.4 exemplifies the desirability of informing the discussion considering the interrelationships between flows and the level of coherence and coordination that would be required to obtain the maximum benefits;
- *Economic modelling and projections of flows.* To feed the proposed policy discussion above it is desirable to develop more concrete and realistic data that could be elaborated from the analysis of more specifically defined economic scenarios. This requires an economic modelling of the development of key financing flows, simple but one that incorporates the main changes expected in the medium term and projects their economic impacts. The modelling should also incorporate the interconnections;
- *Improve the way evidence is presented and existing information.* To facilitate the process of analysis at this hierarchical level of the relatively complex issues that will be proposed, more work is needed to provide the missing evidence, and to prepare adequate visual materials.

**The MEF's technical and political leadership will be very important during the prioritization process and the formulation of the final work agenda.** The general coordination of the activities referred to above does not correspond to the direct mandate of each MEF directorate and calls for concertation. These needs, which are common to all areas of the Economic Transformation Plan, are discussed in more detail in the next section.

#### Implementation Sequence of AFD Recommendations

**The priorities in the implementation of the Economic Transformation Plan define three differentiated phases.** The different interventions analysed above define a set of priorities that change over time and can be better visualized considering three distinct phases, as summarized in the figure below and analysed here.

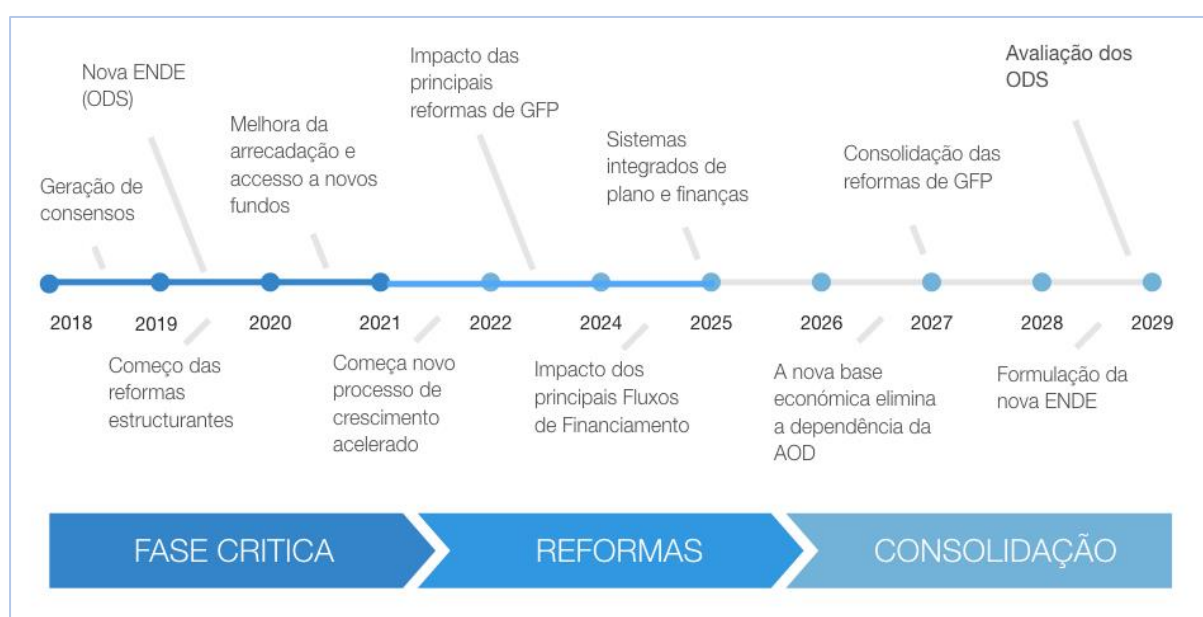
*Critical Phase (2018-2021).* The focus at the beginning of the plan should focus on supporting crisis exit by implementing actions and reforms aimed at freeing up fiscal space and expanding government manoeuvrability during this process. Measures to reduce inefficiencies in public expenditure and to increase the volume of the four selected financial flows should be implemented during this period. One of them (ODA) is of great importance for the implementation of the Economic Transformation Plan. During this phase, the government should move forward in the formulation and implementation of medium-term programmatic support to implement the Plan. It is important to begin the implementation of the structural reforms and strategic plans of the main financial flows at this stage, since only then can they produce results in the next phase.

*Phase of the Structural Reforms (2022-2025).* The second phase of the Plan should focus on achieving substantive outcomes of structural reforms that will enable the government to make the most of funding opportunities in the new phase of accelerated economic growth that should begin with this

phase (2022). These reforms will already lead to appreciable results in the more efficient and effective use of public and private resources. The strategic plans of the main flows should also begin to produce visible results during this period, contributing to an orderly acceleration of the economy.

*Economic Consolidation Phase (2026-2029).* The focus at this stage should be the completion of the implementation of key structural reform measures, and those that have allowed the development of major financial flows. The further improvement of the results obtained should be incorporated as a process of continuous improvement in the long term. Reaching the final goal of the SDG, the government should have already learned important lessons about the good use of political leadership to achieve effective coordination of public policies. The resulting system - most likely more strongly based on public and private domestic financing - will ensure that economic progress progresses faster and has more effects on social and environmental development.

*Main milestones and critical points in the implementation of the Economic Transformation Plan*



*Responsibilities of the Implementation of the Economic Transformation Plan*

**The considerations about the implementation of the Economic Transformation Plan are almost as important as its strategic design.** The biggest challenge to achieve the transformations proposed by the Plan is to generate a consensus at the highest level of the government on its strategic need, and to identify an efficient institutional solution to implement it. The challenge is important because its implementation will exceed the mandate of each government institution and will require a strategic discussion on how to efficiently organize its conduct and political decision-making. The solution will likely require managerial and institutional innovations, since highly cross-sectoral policy coordination is one of the areas where the governance system has shown greatest difficulty in delivering coherent and effective responses.

**The implementation of this plan could be led by the Ministry of Economy and Finance under presidential mandate.** Most of the proposed actions correspond directly to the areas of responsibility of the MEF or institutions under its authority, and all coincide with the fundamental objective of the ministry, which is to ensure macroeconomic stability. This solution could facilitate the implementation of these actions, which could be easily integrated into existing MEF long-term and medium-term financial planning instruments, and the existing Oversight Group - perhaps expanded - could play an important role in the implementation. The alternative of implementing this highly strategic agenda

with disjointed initiatives on behalf of different government actors and supported in a fragmented way by development partners will inevitably create disruptions and challenge the achievement of meaningful results.

**Strengthening the capacity of the MEF will also be necessary to ensure the implementation of the Plan.** Implementation of the Plan will also be an internal challenge for the MEF, as the multiple coordination activities required do not correspond to the direct mandate of any MEF Directorate, and will require informed decisions at the highest level. One solution might be to strengthen the technical capacity at the highest level of the Ministry (Office of the Permanent Secretary or the Minister) to establish appropriate management and monitoring support systems to facilitate the task of the authorities, which is part of the short-term actions (Next Steps) suggested below.

#### *Financing the Economic Transformation Plan*

**The government should seek to ensure sufficient and medium-term funding.** The reforms suggested in the Economic Transformation Plan are large-scale and medium-term, and will require securing funding of USD 40-60 million over the next 10 years. Formulating a project of this magnitude requires investment of time, and technical capacity, and therefore could delay the start of execution. The actions of the first component of the Plan (Short-term Actions) are urgent and cannot be expected to confirm large-scale financing. However, by their nature, these actions are not excessively onerous and could be financed independently to ensure implementation during the first phase of the Plan. This aspect was also included in the Next Steps list.

**It would be advantageous to steer the process of securing large-scale funding for the actions of the Economic Transformation Plan as part of the process of re-establishing AOD.** The reforms seek common objectives, such as increasing the efficiency and transparency of public management, and many of them derive from technical cooperation that has already been funded with ODA resources. There are several successful examples in other countries of using pooled finance mechanisms for medium-term financing of PFM reforms such as the proposals, which could be taken as a reference. Examples are the SWAp-type financing used in Cambodia mentioned in Section 3.3, or the Multi Donor Trust Fund<sup>2</sup> for reforms in Nepal, which have achieved notable successes in both cases.

**The process of consensus building with development partners has already begun.** AFD's calendar of activities includes the holding of three high-level seminars to ensure interest and future participation in the implementation phase of key development partners. In addition, the technical missions carried out at these seminars included direct meetings with partners who are funding the reforms or actions analysed in the AFD, and their suggestions were considered in the evaluation.

#### *8. Next steps: Actions in the pre-implementation phase*

**It would be appropriate for the MEF to consider requesting short-term technical cooperation support to organize AFD's after-action agenda.** Short-term technical assistance to the MEF (2-3 years) could be needed to support the following actions:

- **Preparatory actions for the implementation of the Economic Transformation Plan.** The MEF should lead a process of internal discussion and consensus building of AFD's main results

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<sup>2</sup> Based on a common agenda generated by PEFA, the Multi Donor Trust Fund for Public Financial Management is administered by the World Bank and jointly funded by bilateral cooperation agencies such as Australia (DFAT) and the United Kingdom (DFID), the European Union, and the governments of Denmark, Norway and Switzerland. The fund provides a unique system in which all partners provide their funding using a common programming framework that is designed to support priority reforms defined by the government

within the Ministry, and then another at the highest level of government. To this end, the MEF must carry out the prioritization, research and preparation activities of materials analysed in Section 7.3;

- *Negotiation of financing for the implementation of the Economic Transformation Plan.* From the elements analysed in sections 7.2 and 7.3 of the AFD, it will be necessary to formulate a PFM Reform Framework that allows the shared financing of the reforms proposed in Strategic Areas 2 and 3 of the Plan. This includes negotiating specific pooled finance mechanisms to ensure the medium- and long-term continuity of these actions;
- *Beginning of the implementation of Component 1.* As mentioned earlier, the actions of Strategic Area 1 of the Economic Transformation Plan (Reforms to increase the fiscal space of short and medium term) are urgent and should not wait for the end of the previous ones that can lead time. Therefore, the formulation of this technical cooperation support should also provide for the capacity to finance the implementation of actions to increase efficiency and to develop new short-term funds.

**These actions should be geared towards capacity building at the highest level of the MEF.** This support project should strengthen the technical capacity at the highest level of the Ministry (Office of the Permanent Secretary or Minister). For the execution of the preparatory actions for the implementation of the Plan, appropriate management and monitoring support systems to facilitate the task of the authorities. The MEF can ensure the financing of these actions autonomously.



## 1. Introduction

**1. Mozambique has enjoyed steady economic growth in the past two decades.** The economy grew at an average rate of 7.4% between 2005 and 2015, driven by sound macroeconomic management, large-scale foreign investment and continued support from development partners. With the recent discovery of significant hydrocarbon reserves, the country has embarked on an accelerated process of social, economic and environmental transformation and new opportunities to consolidate the sustainable growth of the national economy. Exploiting these resources will bring with it both notable opportunities and complex challenges that Mozambique needs to address with appropriate policies to fully realize its great economic potential. The country is also undergoing profound environmental changes, mainly due to climate change that can jeopardize the gains of development achieved.

**2. Despite robust economic growth, the challenges to fighting poverty persist.** A significant proportion of Mozambicans live below the poverty line (46%, according to data from the Fourth National Poverty Assessment, 2014-15), and the Human Development Index 2015 puts Mozambique in 181st position among the 188 countries analysed. In addition, recent assessments indicate that inequality has grown significantly in recent years, despite continued economic growth. About 70% of the population lives and works in rural areas, mainly in the agricultural sector or related to it. Mozambique has good opportunities to achieve a sustainable reduction of poverty and promote inclusive growth, but for this, the government should implement sound policies in a complex fiscal and economic environment.

**3. The decision to conduct this Development Financing Assessment (DFA) is timely.** In 2015, the government approved the new National Development Strategy 2015-2035, which is linked to Agenda 2025 and the Government's Five-Year Program 2015-2019, thus completing a comprehensive and integrated framework of national planning instruments. This work needs to be complemented with adequate planning to achieve the necessary financing to achieve these goals. Recent changes in the national and international economic context require rethinking some of the strategies to finance the country's development in the long and medium term. The results of AFD should be useful in guiding the development of new strategies to mobilize all the sources that are necessary to finance the development objectives of the country.

**4. The timing of further evaluations is also beneficial to the implementation of this AFD,** many important studies have recently been completed or are being finalized. In 2014, the government conducted the Public Expenditure Review (PER) and in 2015 completed the Public Finance Management Performance Assessment (PEFA) and a Fiscal Risks Statement, which already suggests a diversification of the sources of risks associated with GDP. The government is also finalizing the first Review of Public and Institutional Expenditure on Climate Finance (CPEIR). These and other works are of great value for the realization and better targeting of AFD for providing very accurate information and a valuable analysis that the AFD will use as inputs for subsequent work.

## 1.2. Evaluation Objectives

**5. The overall purpose of the Financing for Development Assessments (DFA) is to assist governments in developing National Integrated Financing Frameworks (QNIFs)** to achieve their development priorities and results. These frameworks propose a holistic and strategic approach to the development of public and private, domestic and external long-term and medium-term finances. An integrated framework of this kind translates into a system of institutional policies and structures that governments must develop. This concept, coined in the Addis Ababa Agenda for Action, proposes a

framework for governments to be able to develop an appropriate perspective on financing for development under the Sustainable Development Objectives (SDG).

**6. An Integrated National Financing Framework is a tool to help governments mobilize proportional resources in scale and consistency with the results sought.** These systems should provide clarity on the roles that all actors - public and private, domestic and external - could have to contribute to this vision, and indicate which are in the best position. This system also helps determine the responsibilities of different government actors for the mobilization and promotion of resources. In sum, a National and Integrated Financing Framework (NFAP) should help countries to devise a strategy to effectively mobilize the investments they need from all sources and to provide a framework that ensures government-wide coherence in mobilizing resources for areas. Evidence from national funding frameworks points to six pillars of an NFID, as shown in Figure 1.

Figure 1 - Elements of an FNIP for the achievement of national priorities and SDG



Source: UNDP 2017 (to be translated soon)

**7. (i) Leadership and institutional coherence.** High-level leadership is needed to develop a shared vision of this new strategic approach to funding and to align the policies needed to implement them. An NFID will require robust mechanisms to ensure both 'vertical' alignment between general long-term policies and operational policies and a horizontal alignment between operational policies focused on different themes or types of funding. Leadership is therefore essential for joint government action to mobilize funding in an aligned and complementary manner to convene ministries and state agencies at all levels of government to determine their roles and functions in implementing the funding strategy. In most countries, this type of leadership must be exercised from the level of Prime Minister or President of the Republic.

**8. (ii) A clear vision of the results that the country intends to achieve** is at the heart of an NFIS and the basis for long- and medium-term financing plans and targets. Usually this vision is articulated in the national development strategies or plans that define the results of sustainable development that the country intends to achieve. The long-term vision for results provides the foundation for further detailed plans. If national plans form the basis for government efforts, it is also important to understand how they connect with international commitments, especially with the 2030 Sustainable

Development Agenda. This will enable government and stakeholders to monitor progress in view of the international commitments assumed by the country.

**9. (iii) A general funding strategy** with clear estimates of the magnitude and types of funding required to achieve development results is the basis for building an NFID. In most countries medium and long-term vision financing is associated with the availability of short- or medium-term public funding resulting from operational financing policies such as Medium Term Fiscal Scenarios (CFMPs) or five-year plans. The proposed strategic funding approach seeks to fill important gaps in existing systems: (i) ignorance of the order of magnitude of the funding that would need to be mobilized to achieve the desired development objectives, and (ii) lack of clarity on the types of funding which would be more appropriate to carry out the specific investments required. The systems used in most countries are based on the assessment of the resources that are likely to be available projecting current context and recent trends in the future. A different approach is proposed: to strategically analyse how to modify the composition of the existing financing structure and the scale of some key resources to generate a new funding base to achieve development objectives. For most countries, this would be a new feature of the funding framework: a feature that could support and pool existing structures around a common and long-term funding strategy.

**10. (iv) Financing policies for specific flows.** Based on the overall funding strategy, specific policies should be implemented for each funding stream to guide and improve the way resources are mobilized to achieve the desired outcomes, and to be leveraged efficiently. Governments will need to capitalize on contributions from a wide range of resources to address the various challenges of an interconnected agenda for sustainable development. Public finance, development cooperation, philanthropic financing, remittances, for-profit investments and other resources have their own characteristics and can play different and complementary roles in achieving results. This requires differentiated approaches that stimulate the mobilization of resources according to the comparative advantages of each flow and that also allow to take advantage of the synergies between the different types of financing.

**11. Governments have varying degrees of influence over different types of funding.** At the top of the list in Figure 1 are public finances that are entirely government controlled, albeit with the intricacies known to manage competitive interests and coordinate the various levels of administration. The government has direct influence, but not total control to foster partnerships with private investors, and has no direct control over private investment, but it can create conditions and incentives to influence how this funding is developed and used. In all areas of funding, there are many state departments and agencies that are involved in the mobilization or use of funding flows, or that are affected by the way these resources are invested and the results achieved. There are also interactions and synergies between policies in relation to different types of funding that also impact on the same results areas. Governments should develop a holistic view of all the investments that are being made or may be induced, and the impact of these investments on the desired outcomes in the strategic vision, and develop or refine the financial management policies to obtain those contributions.

**12. (v) Integrated monitoring, evaluation and learning structures.** Monitoring, evaluation and learning systems have a direct influence so that funding policies can be managed effectively to achieve the desired results. Given the complexity of the proposed framework, it will be necessary to develop robust frameworks that link government action with the desired results. How data is collected, understood, and used is critical. The quality of information in the learning, monitoring and evaluation systems can only be as good as the data collection systems on which they are based. Access to information to monitor policies presents challenges in many countries as there is no required

information at the required level of quality, or this information is not properly shared. There are generally good opportunities to improve systems by integrating existing data sources that are underutilized, such as administrative data collected by various government agencies

**13. (vi) A conducive environment for accountability and dialogue.** It is unlikely that actors who could provide the broader forms of development financing that countries need to mobilize adequately respond to, or at least have confidence in, the process, relying on established goals, and finding the role that is assigned. The level of ambition for outcomes, coupled with changes in the financing landscape, is leading countries to seek new sources of development finance, including private sector investment and national and international philanthropy. The quality of the efforts and systems that governments implement to engage with these actors in meaningful dialogue - politically and technically - will affect their success to bring them on board in resource mobilization. These actors will be much more willing to participate if they rely on the fiduciary competence and integrity of the authorities expected to work. It is therefore important that countries ensure the independence and professionalism of state oversight institutions: national audit offices, government inspection bodies, competent parliamentary committees and others. It is also important that these institutions are properly funded, focus on the priority sectors and themes, and genuinely independent. This will have substantial implications for the smooth functioning of the planning and accountability mechanisms of country financing.

#### Purpose and objectives of this AFD

**14. AFD serves as a comprehensive tool for mapping present, past and future sources of development finance,** reviewing a wide range of funding flows from internal and external sources, both public and private, as shown in Figure 2. These are specific objectives from this rating:

- Provide an overview of the evolution of major flows of development finance between 2005 and 2015 and their allocation and contribution to national priorities and results;
- Assess the linkages between finance and results through the relationships between national planning and budgeting processes;
- Assess the roles and responsibilities of national institutions in managing or influencing the development of individual financial flows;
- Analyse the interface between the different flows and the complementarities between the different sources of development financing evaluated;

Figure 2 - Main Development Financing Flows to Analyse

<b>External</b>	AOD Donations and Loans Public loan sternal CSS and triangular coop Climate Financing Donations from INGOs (on budget) Vertical Funds (GFATM and GAVI) Other funds (OFOs)	Foreign direct investment Shipments Donations from INGOs (off-budget) External Private Loan
<b>Internal</b>	Tax revenue Non-tax income Public-Private Partnerships Mineral-related taxation Internal Public Loan Sovereign funds	Internal Private Loan Inclusive Business Financing Home Philanthropy and NGOs CSR linked to development
	<b>Public</b>	<b>Private</b>

**15. The purpose of this report is to provide a better understanding of the potential sources of development finance** that need to be mobilized to meet funding needs to achieve the medium- and long-term development objectives and strategies of the country. This evaluation is limited to the analysis of funding at national level and excludes subnational (territorial and district) dimensions. It is hoped that its conclusions and recommendations will serve as a basis for discussions within the Government of Mozambique on these key strategic issues.

**16. This evaluation provides a strategic analysis of the resources potentially available to finance the country's medium-term development.** Identify current and future funding sources available to Mozambique, analyse the resources that have been or can be mobilized to finance national priorities, provide a comprehensive view of funding instruments, and inform policy dialogue to promote efforts to mobilize of resources. The evaluation presents the following chapters, thus structured:

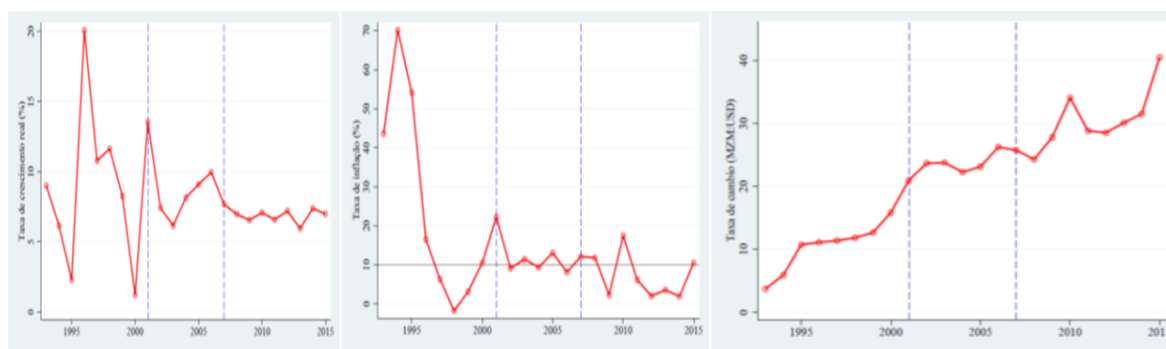
- [Chapter 2](#) - Describes the socio-economic context and key development challenges.
- [Chapter 3](#) - Discusses how financing can lead to better development outcomes through more integrated planning and budgeting processes.
- [Chapter 4](#) - Analyses the quantitative and qualitative aspects of public finance management and the main sources of public funding available in the short and medium term.
- [Chapter 5](#) - Examines the extent to which current efforts to strengthen private sector development are aligned with national priorities and the main sources of private finance.
- [Chapter 6](#) - Proposes a prospective framework to analyse the future development of financial flows, analysing the different graduation processes that the country will face soon.
- [Chapter 7](#) - Outlines AFD's initial findings and key emerging actions.

## 2. Socioeconomic Context

### 2.1 Evolution of the economy and its performance

17. The recent evolution of the Mozambican economy has three distinct phases. More exhaustive studies on the recent evolution of the Mozambican economy<sup>3</sup> suggest that the analysis focus on three periods that exhibit performance characteristics and well-differentiated behaviours, as shown in Figure 3.

Figure 3 - Real growth rate (a), Inflation rate (b) and Exchange rate (MZN / USD) (c) of the economy



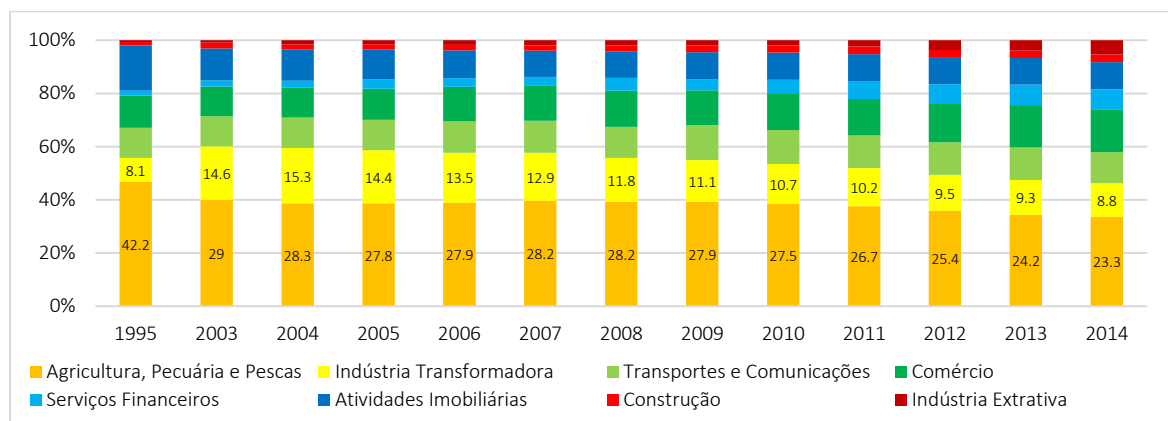
In the first period (1993-2001) the economy was characterized by the post-war reconstruction and recovery effort. There is much variability in growth rates, as well as in the rate of inflation and a stable depreciation in the exchange rate;

<sup>3</sup> See Jones, 2016: Macroeconomic Scenarios and Current Challenges.

- *The second period (2002-2007)* is for standardization and stabilization. There are minor and stable variations in both the growth rate and the inflation rate (10% on average) and an exchange rate against the dollar, which oscillates around the average of 24-25 meticaís;
- *The last period (2008-2015)* and consolidation of stability. The oscillations of the growth rate stabilize, around an annual average of 7%, and inflation rates around 3%. The dynamics of the exchange rate reveals that the greater interaction with the external, the economy also begins to have greater vulnerability to external shocks.

**18. The structure of the Mozambican economy has undergone major changes during this period, but is still essentially defined by the agricultural sector.** Over the past 10 years, the agricultural sector's contribution to GDP has declined from 42.2% in 1995 to 23.3% in 2014; however, approximately 70% of the population lives in rural areas. Figure 4 shows the evolution of other sectors' contributions to the GDP, with the emergence of sectors such as Extractive Industries and Financial Services. Most sectors experienced considerable fluctuations during this period, but they were not propitious to consolidate sustainable development over time. A significant case is Manufacturing, which represented 8.1% of GDP in 1995 and managed to grow above 10% between 2003 and 2011, but quickly fell to 8.8% of GDP in 2014.

Figure 4 - Composition of GDP over time



Source: INE

**19. The agricultural sector also continues to be the main source of employment in the country.** Despite the recent major changes in the economy, they have not been able to change the relative weight of agriculture as the largest employment generator in the country. The data presented in Table 1 show that agriculture accounted for 81.5% of employment in 1990-95 and fell only to 76.1% in 2006-7. The last decade has been marked by the appearance of important megaprojects of foreign investment in areas such as energy, oil, mining and others, with highly capital-intensive investments. The data in Table 1 also indicate that its impact on employment was relatively low. Existing studies state that the labour market is characterized by low unemployment rates, high rates of underemployment and informality, and that government is one of the largest generators of employment, without considering the informal sector<sup>4</sup>.

<sup>4</sup> (Arndt, Jensen and Tarp, Structural Characteristics of the Economy of Mozambique: A SAM-based Analysis 2000) (Tarp, et al. In this paper, we present the results of a study of the impact of the development of Mozambique on the development of sustainable development in Mozambique (Foucault et al., 2011), (Arndt, Hussain et al., 2011), (Arndt, Garcia, et al. ), (Schou and Cardoso 2014).

Table 1: Distribution of the labour force by sector, over time.

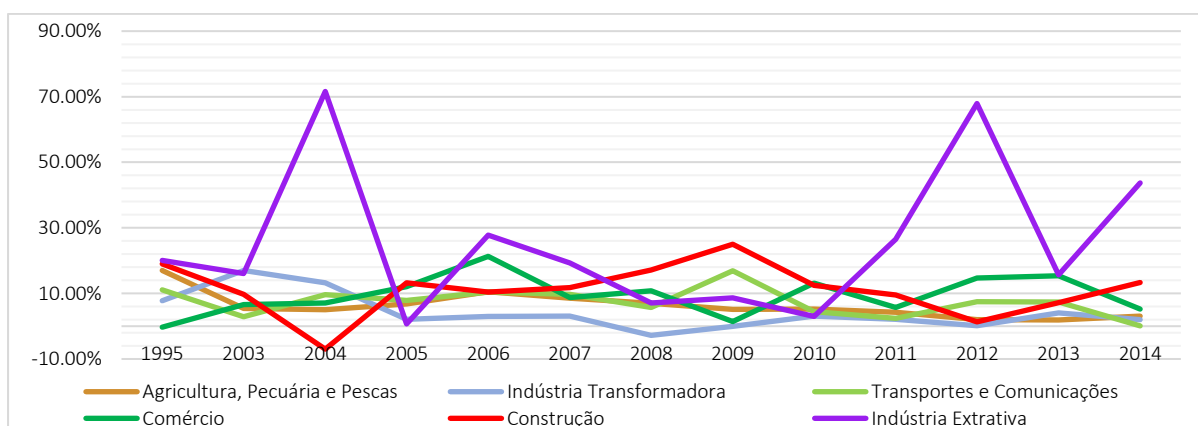
Sectors	1990–95	1996–2000	2001–05	2006–07
Agriculture	81.5	80.8	79.9	76.1
Mining sector	0.9	0.6	0.5	0.6
Manufacture sector	3.8	3.4	3.2	3.2
Energy Sector	0.1	0.1	0.2	0.2
Constructions	1.4	2.0	2.2	2.5
Commerce	4.2	6.5	7.7	7.6
Transport communications and storage	1.2	0.5	0.9	1.1
Others	6.8	6.1	5.5	7.4

Source (Cungura, Fagilde, Garrett, Uaiene, & Headey, 2011) with data based on MPF / UEM / IFPRI and INE

## 20. The productivity evolution of the most strategic sectors of the economy was relatively low.

Figure 5 shows the evolution of the growth rate of production of the main sectors of the Mozambican economy. The most dynamic sector was that of the extractive industries, but still with very erratic growth rates. Labour productivity in the manufacturing sector was stable. However, the contribution to the GDP and the weight in the composition of the exports of the manufacturing sector grew, which is explained by the good performance of megaprojects. Productivity in agriculture was also stable, but low, noting also that agriculture, especially in the last period, lost momentum. The latest survey on manufacturing companies recognizes that the vast majority of Mozambican companies are artisanal and small scale, producing homogeneous products with low levels of technology and selling in the same locality where the company is located. Companies that export - very few that do - have superior performance across a set of indicators<sup>5</sup>.

Figure 5 - Annual growth rate of production by sector



Source: INE.

## 21. The lessons learned from the transformations of the economy in this period provide important clues to focusing on future policies to improve the well-being of the population and reduce poverty.

The country has a major challenge: demographic trends indicate that, in the medium term, more than 300,000 people per year will enter the labour market, which is not currently able to absorb such volumes. A relatively recent study<sup>6</sup> indicates that in 2008, 60 per cent of households whose income was exclusively linked to agricultural activities were considered poor, while only 30 per cent of households whose income was wages and who lived in urban areas were considered poor. The study

<sup>5</sup> (Schou & Cardoso, 2014).

<sup>6</sup> (Jones & Tarp, Jobs and welfare in Mozambique: Country case study for the 2013 World Development Report, 2013).

states that although most people live on small-scale agriculture, it is often a choice because of lack of other opportunities, rather than an active livelihood strategy. There is also a large urban informal sector characterized by low productivity, but dynamic in income generation. The highly capital-intensive investment has had little impact on job creation. These challenges are clearly analysed in the National Development Strategy 2015-2035, which proposes a structural transformation of the economy, which will have to be more productive and competitive, focusing on industrialization for inclusive and sustainable growth.

## 2.1 Main progress of the socio-economic context and social inclusion

**22. By signing the General Peace Agreement in 1992, the parties put an end to some three decades of conflict**, eleven of liberation from Portuguese domination (1975) and fifteen years of civil war. In 1993, Mozambique was the poorest country in the world. In 1994 the first general elections were organized, a moment in which enthusiasm and positive expectations crossed the country. Both former combatants and displaced persons return to rural agricultural areas. Agricultural production grew rapidly due to the rapid expansion of farmland<sup>7</sup>, but the farming techniques used by most farmers were rudimentary, and the inputs of low quality. During the first ten years of peace, the Mozambican economy grew steadily and benefited from substantial development aid (ODA)<sup>8</sup> flows. This growth has made possible the post-war peacebuilding effort, the transition from a planned economy to a market economy, and the adoption of policies for reconstruction and recovery.

**23. In September 2000, the Government of Mozambique ratified the Millennium Declaration** and, through it, the Millennium Development Goals (MDGs), with 189 more nations, in line with its commitment to respect the principles of dignity human, equality and equity, principles that are reviewed in areas considered a priority for the Mozambican State. In 2000, the country benefited from debt forgiveness under the Jubilee Campaign and the Heavily Indebted Poor Countries Initiative (HIPC).

**24. The MDG outcome indicates that the country has made significant progress in some areas but in other areas continues to face significant challenges.** In 2015, the government, with the support of UNDP, developed the Millennium Development Goal Indicators<sup>9</sup> Brochure to recapitulate and present progress made by Mozambique towards the eight MDGs. The main results were as follows:

**25. MDG 1: Eradicate absolute poverty and hunger:** The target for 2015 was to halve the absolute poverty rate of consumption, estimated at 80 per cent in 1990. In the data presented in Table 2, the poverty rate reduced to 46.1%, which initially indicates that Mozambique has taken important steps towards this goal. However, the process of poverty reduction was rather patchy. Between 1996 and 2002, almost 3 million people were above the poverty line, with the percentage of poor people falling from 69.7% to 52.8% of the population. Mozambique was considered by the international community as a success story in terms of growth and poverty reduction<sup>10</sup>. However, the data for 2008 showed that there were no significant changes in poverty levels compared to those measured five years earlier. Three main reasons were associated with stagnation in changes in the incidence of poverty: (i) climate shocks, (ii) declining terms of trade due to rising food and fuel prices and (iii) very low or zero growth rates in productivity which have led to poor growth in food crop production. Finally, in the last

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<sup>7</sup> (Hanlon & Smart, There are more bikes – but is there development? 2008)

<sup>8</sup> Several IMF reports on the country,

<sup>9</sup> (MEF - DNP, 2015).

<sup>10</sup> Arndt, Jones, & Tarp, (Arndt, Jones, & Tarp, *Aid and Development: The Mozambican Case (No. 06–13)*, 2006).



period, the reduction trend returned to progress again, and the national poverty rate reduced to 46.1% in 2014.

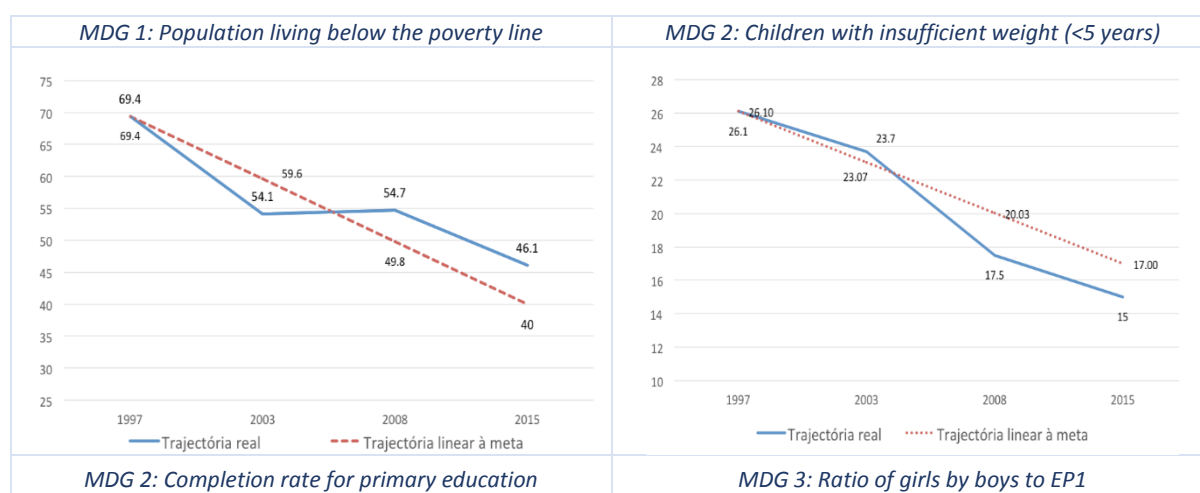
Quadro 1: Índice de pobreza (medida  $P_0$ ) usando a metodologia PLEASE (em percentagem)

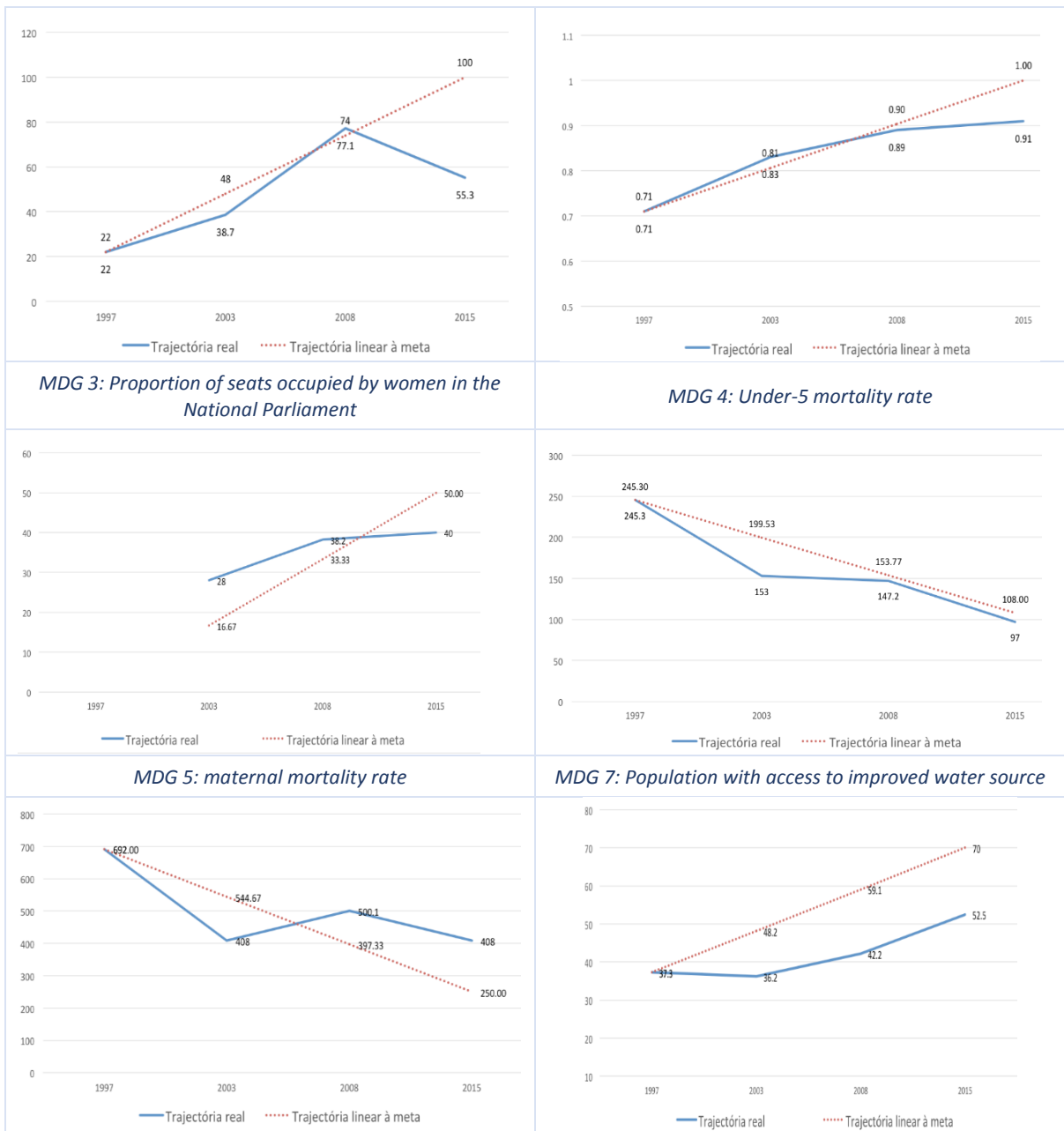
Area	IAF96	IAF02	IOF08	IOF14
National	69.7	52.8	51.7	46.1
Urban	61.8	48.2	46.8	37.4
Rural	71.8	55.0	53.8	50.1
North	67.3	51.9	45.1	55.1
Centre	74.1	49.2	57.0	46.2
South	65.5	59.9	51.2	32.8

Source: (MEF – DEEF, 2016)

**26. However, these developments have not been uniformly distributed among the various socio-economic strata grouped by income levels and between geographical areas.** The data in Table 2 show that these gains did not contribute to a convergence of welfare levels between rural and urban areas or by geographical region. The distance between rural and urban areas is large, and living conditions in the southern provinces are much better than those in the north and centre (partly due to a higher level of urbanization in the South). Of particular note is the performance of the northern provinces where poverty rates have risen recently (with the extreme case of Niassa, where it has almost doubled the number of poor). With regard to Objective 1.b, to ensure full and productive occupation, the situation is more worrying, despite the government's efforts to provide training programs and administrative information summarized in the brochure.

Figure 6 - Progress towards achieving the Millennium Development Goals in Mozambique





Source: Authors' calculations based on official government data

**27. MDG 2: Achieve universal education.** The education system is still far from reaching universal primary education. The gross completion rate of the 7th grade (primary education) in 2014 was on average only 55.3%, but the girls' rate was 52%. The situation is not homogeneous in the country. Data on education reveal a geographical distribution consistent with the results of the poverty and well-being analysis. For example, the completion rate for northern provinces plus Tete and Zambézia is 43% (38.2% for girls) on average, while Maputo province and Maputo City show completion rates above 90% (above 97% for girls).

**28. MDG 3: Promote gender equality and the empowerment of women.** According to the data for 2014, women continue to have more difficulties in completing primary and secondary education. The gender parity index in education registers a regression of 0.97 at 6 years, to 0.94 at 10 years of age, up to 0.66 at 15 years. Mozambique has been making significant progress in terms of women's participation in decision-making and policymaking bodies; 40% of parliament seats are occupied by

women (the target was 50%). The participation of women in subnational and local governments still has low percentages, which are around 20%.

**29. MDG 4: Reduce child mortality:** The goal was to achieve an infant mortality rate of 67 deaths per 1,000 live births. In 2011 the rate was 64 deaths. The target for the infant-juvenile mortality rate was 108 per 1,000 live births, and in 2011 the rate of 97 deaths was reached. These results were achieved thanks to efforts to increase vaccination coverage of children under one year against the main predictable diseases. The rate of children vaccinated against measles (one year old) is 92%, with the target set at 95%.

**30. MDG 5: Improve maternal health:** The goal was to achieve 250 deaths per 100,000 live births. In 2011 this rate settled on 408 deaths. The coverage of institutional deliveries is on average 54.3%, and is particularly low in rural areas (44%). The goal was 66%.

**31. MDG 6: Combat HIV / AIDS, malaria and other diseases:** The prevalence of HIV in young people and adults aged 15-49 is 11.5%. The prevalence in women is higher than the prevalence among men (13.1% and 9.2%, respectively). The disease is one of the major threats to development in Mozambique, constituting a major public health problem. Although there has been a decrease in the malaria lethality rate in recent years, this disease is still one of the main causes of morbidity and mortality. In 2009, its occurrence in children under 5 years of age was 94 cases per 10,000 children. The target for 2015 was 80. The fatality rate associated with tuberculosis in 2009 was based on 504 deaths per 100,000 population. The target for 2015 was 144 deaths.

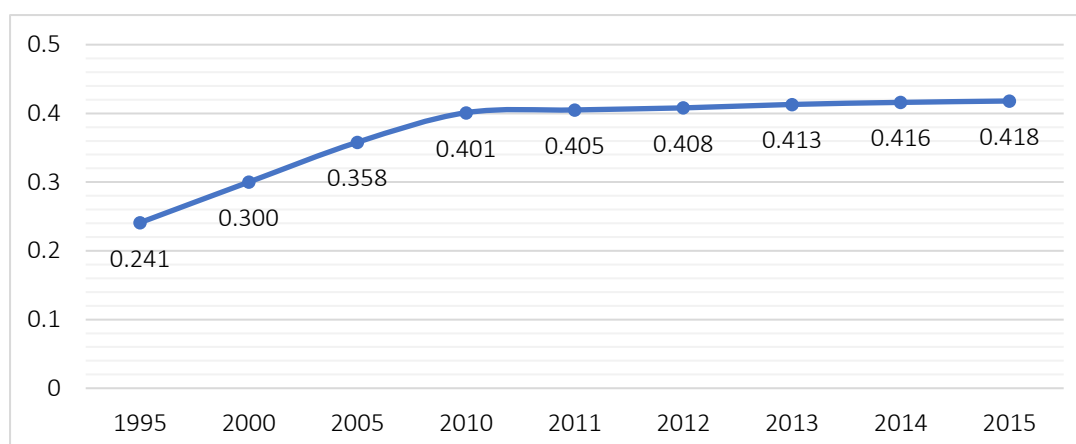
**32. MDG 7: Ensure environmental sustainability:** The percentage of the population using safe sources of drinking water reached 52.5% in 2011. The millennium goal was to reach a level of 70%. In the urban area, the percentage covers 84.6%, while in rural areas only 37.8% of the population uses safe sources of drinking water. In this last area, the main sources of water are the unprotected wells, with 42%, and surface water, such as rivers and lakes. Only 23.8% of the population has sanitary access, that is, it uses an unshared bathroom / improved latrine. In urban areas, the percentage is 47.8% (the target was 80%), however, in rural areas it is only 12.8%. The millennium goal indicated that 80% of the urban population, and 50% of the rural population, should have had access to improved sanitation. Nothing refers to environmental sustainability or any steps taken to ensure it and efforts to improve living conditions on the outskirts of urban areas.

**33. MDG 8: Building a global partnership for development:** Mozambique is one of the countries that most benefits from foreign aid. In Mozambique, the donor community, together with the government, has made significant efforts to implement the principles of the Paris Declaration to increase aid effectiveness. Progress has been made towards this objective, but considerable problems remain, which are discussed in Section 3.3 of this evaluation.

**34. Human Development Index:** The Human Development Index, prepared by UNDP with data provided by governments, ranks 188 countries around the world. Figure 7 shows the evolution of this index between 1995 and 2015, which corresponds to the development history presented earlier: rapid improvements between 1995-2010 and then a certain stagnation. The Human Development Index increased from 0.241 in 1995 to 0.358 in 2005 and stabilized at around 0.40, with a moderate increase to 0.418 in 2015.

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Figure 7 - Human Development Index in Mozambique in the years 1995-2015



Source: UNDP

**35. Despite the progress made, the overall performance of the policies implemented makes it possible to infer that the country could have aspired to achieve better results.** Mozambique has enjoyed strong and sustained economic growth in recent years, but poverty levels have remained high. The country still has a long way to improve the living conditions of citizens. The data in Table 3 shows the countries that occupied the last 15 positions in Human Development in 1990 and 2015. Mozambique was the last country on the list in 1990 and by 2015 still ranks among the 10 least developed countries in the world. Several countries that accompanied Mozambique in the last 15 places in 1990 (Rwanda, Afghanistan, Uganda, Malawi, Gambia, Benin and Myanmar) could move faster and out of the list in 2015. A recent study that groups countries according to level of readiness to achieve the Sustainable Development Goals<sup>11</sup> also puts Mozambique among the last on the list. According to the SDG Index, Mozambique ranks 133 out of 149 countries.

Table 3: Last 15 countries in Human Development in 1990 and 2015

Last 15 Positions in HDI 2015	HDI	Last 15 Positions in HDI 1990	HDI
Ethiopia	0.448	Myanmar	0.353
Mali	0.442	Benin	0.345
Democratic Republic of Congo	0.435	Sudan	0.331
Liberia	0.427	Gambia	0.33
Guinea-Bissau	0.424	Malawi	0.325
Eritrea	0.420	Central African Republic	0.32
Sierra Leone	0.420	Uganda	0.309
Mozambique	0.418	Afghanistan	0.295
South Sudan	0.418	Sierra Leone	0.272
Guinea	0.414	Guinea	0.271
Burundi	0.404	Burundi	0.27
Burkina Faso	0.402	Rwanda	0.244
Chad	0.396	Mali	0.222
Niger	0.353	Niger	0.212

<sup>11</sup> The ODS Index ranks countries in terms of their initial situation with respect to the 17 ODSs, considering 'data' the nearest available data by 2015. The ODS Index allows each country to assess the current status of their progress against similar nations (e.g., income-earning nations or a specific geographic region), ODS targets, and the best possible outcomes in the various countries. indicators. For more information, see: ODS Indexes, Global Sustainable Solutions Network Report, 2016.

Last 15 Positions in HDI 2015	HDI	Last 15 Positions in HDI 1990	HDI
Central African Republic	0.352	Mozambique	0.209

Source: UNDP

### 2.3 Current Situation and Future Prospects.

**36. The country is experiencing a negative situation, due to a series of external and domestic factors that have had a strong impact on the economy in recent years.** Like other African nations, Mozambique suffered from falling international prices of the main raw materials that sustained its exports or could have accelerated others. Figures 8-11 show that between 2011 and 2015 the fall in international prices of high impact raw materials in Mozambique was quite drastic, as for example in the case of aluminium (40%), coal (60%), of sugar (60%) and natural gas (50%). Compared to other nations, the Mozambican economy was more affected by the effect of these prices, due to the country's close export base and its relative dependence on these exports. The fall in the international price of natural gas has delayed the decision on large-scale investments that could have started to generate significant resources for the economy.

Figure 8 - International price of coal 2011-2015

Figura 1 - Preço internacional do alumínio 2011-2015



Figura 10 - Preço internacional do gás natural 2011-2015

Figura 11 - Preço internacional do açúcar 2011-2015



Source: 'UNDP Mozambique Economic Update' with data from Bloomberg and Ycharts

**37. Climatic factors adversely affected agricultural production, with a significant impact on the contraction of exports and the generation of inflation.** A severe regional drought associated with the El Niño phenomenon affected the agricultural production of the southern African countries in 2015/16. The impact in Mozambique was great, especially in the south of the country. Droughts in the south (especially in the provinces of Gaza and Inhambane) and floods in the central and northern parts of the country affected more than 170,000 hectares, corresponding to 3% of the area sown, leading to a significant contraction of agricultural production and exports. Apart from cashew, exports of all agricultural products declined in 2016. In addition to causing losses in the domestic economy and exports, the decline in regional production also generated strong inflationary pressure. Some products

experienced surprising increases: the average retail price for one kilo of corn in grain increased 92% between September 2015 and 2016, while rice increased by 85%. Cooking oil increased by 76% in the same period, and fresh cassava by 87%. Together, these items represent more than 25% of the total food expenses of Mozambican families<sup>12</sup>

**38. The above-mentioned effects have placed Mozambique in economic difficulties that have required exceptional measures.** Faced with declining exports and external investment, inflationary pressures and an accelerated depreciation of the Metical, the government began to take quite drastic measures to reduce public spending, and requested financial assistance from the International Monetary Fund (IMF) for the first time in a decade (since the completion of HIPC). The country has requested a USD 286 million credit from the IMF stand-by mechanism (SCF). The conditions for IMF credit acceptance included a further reduction of the fiscal deficit of 2% and a series of measures which included raising interest rates, further liberalization of the exchange market, reintroduction of mechanisms to automatically adjust prices and import subsidies. The estimated negative impact of these measures was at least 1% of GDP<sup>13</sup>, but the government was prepared to accept and implement these conditions to avoid further economic malaise.

**39. The complexity was relatively controllable, but the emergence of an unexpected situation in the management of public debt catalysed a short-term economic crisis<sup>14</sup>.** In 2016, a set of debts secretly contracted since 2013 by some public companies, of dubious capacity to fulfil the commitments, debts contracted with the endorsement and guarantees of the government. This new situation made the debt unsustainable in the short and medium term and put the fiscal perspective under immense pressure as it affected the BdM's capacity to sustainably manage the levels of international currency reserves. Debts contracted by these public companies increased gross public debt from 62.4% of GDP in 2014 to 130% in 2016 with at least 80% of external debt, considerably increasing the economy's exposure to external shocks ( see the public debt analysis in Section 4.3.2). The revelations of this debt catalysed several short-term negative effects:

*the immediate suspension of PSI (Policy Support Instrument) support by the IMF, which also suspended the possibility of the Government-requested Stand-by loan;*

- the suspension of all disbursements of programmatic assistance and donor support to the budget. These sources financed, on average, 10% of government revenues;
- the acceleration of the pressure on metical depreciation, which depreciated 70% against the US dollar in 2016, after depreciating by 36% during 2015;
- a sharp rise in debt service obligations, adding another 2% of GDP to debt servicing per year;
- The deceleration of the economy produced a fall in public revenues, which went from 42.5% of GDP in 2014 to 31.7% in 2016.

**40. Despite the short-term impaired situation, the prospects remain promising.** Taken together, cuts in budget support, increased debt service and lower revenues have significantly reduced short-term fiscal space. The current categorization of debt (of debt distress) hinders the negotiation of exit from the crisis. Despite the negative conjuncture, the medium-term context allows for an optimistic outlook. The government has begun to seek a negotiated solution to the debt situation and continues to implement measures to moderate the short-term crisis. The government hopes to confirm the

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<sup>12</sup> World Bank, "Mozambique Economic Update (MEU)," May 29, 2017, 1–42.

<sup>13</sup> PNUD Economic and Policy Advisory Team, 'Mozambique: Economic Update', November 2015.

<sup>14</sup> The data presented were extracted from the presentation of S. Exa. the Minister of Economy and Finance to the creditors in October 2016.

completion of two megaprojects of foreign investment that could bring significant flows of foreign capital<sup>15</sup>. These investments could catalyse others, as the country has abundant natural resources, coal and natural gas. In addition, the unfavourable international commodity prices began to reverse last year, which should accelerate the interest for more investments. Beginning offshore gas projects to generate export, expect a significant increase in revenues in the early 2020s and an expansion of the economy that may have the highest real GDP growth rates in sub-Saharan Africa.

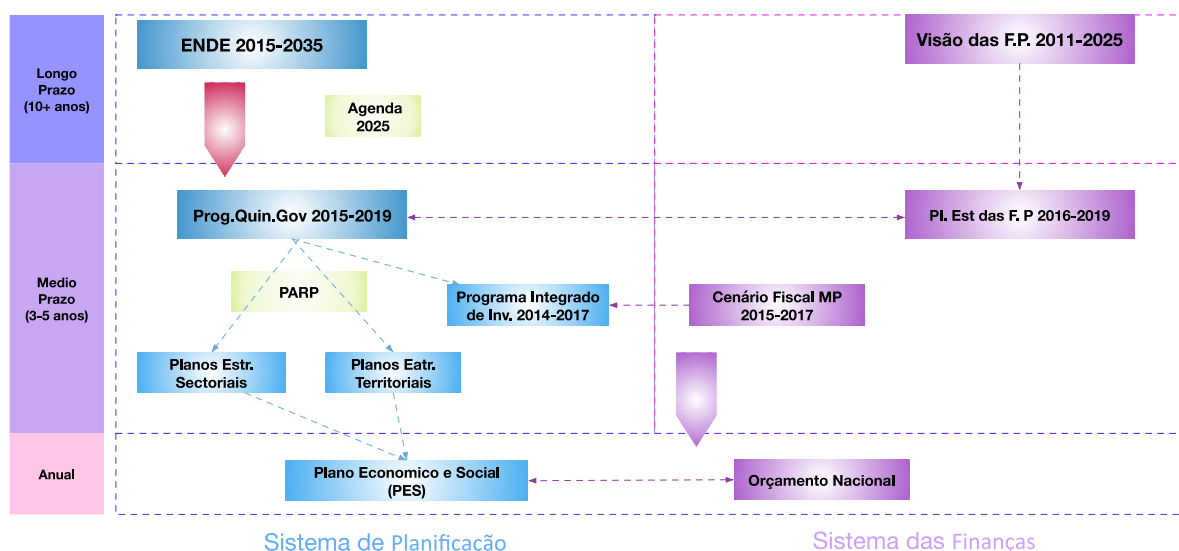
### 3. National systems for planning and financing and linking policies and results

**41. In this chapter the AFD will examine two key pillars for the construction of a National Integrated Funding Framework (QNIF).** The analysis focuses on pillars 2 and 3 set out in Section 1.2 and studies the opportunities and weaknesses for the construction of an integrated financing framework:

- *The national development vision*, defined by a Planning System that articulates national development strategies and plans that establish the results and the impact of sustainable development that the country wants to achieve;
- *The overall funding strategy* and the resulting strategic framework to define long- and medium-term funding targets and the consistency of the main tools used in short-term financing.

**42. The evaluation will initially examine the system's capacity for public finance management.** The main opportunities and strengthening of the system that will be needed to better manage the other sources of funding analysed in the AFD will be reviewed below, such as private (domestic and external) funds and public funds such as Official Development Assistance and South-South Cooperation. Figure 12 shows the main components used by national long-term, medium and short-term public planning and financing systems.

Figure 12 - Main Elements of Long, Medium and Short-Term Planning and Financing Systems



Fonte: Equipa da AFD com base em vários documentos oficiais

<sup>15</sup> The date presented was extracted from the presentation of S. Exa. the Minister of Economy and Finance to the creditors in October 2016.

## 3.1 The National System of Planning for Development

**43. In the period under review, the Government has developed a set of long, medium and short-term planning instruments** in harmony with the broader framework of regional, continental and international commitments, agreements and development strategies<sup>16</sup>. In the late 1990s, the Mozambican Government launched the initiative of all Mozambicans to jointly reflect on the country's future for the next 25 years, and to formulate a national vision and strategies (GoM, 2003). The outcome of this process was the publication of Agenda 2025. Between 2001 and 2014, the Government of Mozambique developed a series of three five-year strategies for poverty reduction<sup>17</sup> following the Heavily Indebted Poor Countries Initiative (HIPC).

### The Long-Term Vision

**44. In 2014, the Government finalized and approved the National Development Strategy 2015-2035 (ENDE).** In addition to the proposals made in Agenda 2025, ENDE proposes a structural transformation of the economy that will have to be more productive and competitive, focusing on industrialization for inclusive and sustainable growth. The National Development Strategy 2015-2035 aims to "raise the living conditions of the population through structural transformation of the economy, expansion and diversification of the productive base."

**45. The main strategy for the transformation of the economy proposed in the ENDE is industrialization,** which seeks to materialize through poles of development. According to ENDE, industrialization must play a fundamental role in boosting the economy by boosting the development of the main sectors of activity (agriculture and fisheries), job creation and the capitalization of Mozambicans. One of the challenges that stands out in the NSDS for its importance is the need to ensure a greater link between mineral resources and other sectors of the economy.

**46. The National Development Strategy defines 4 pillars of action, namely:**

- *Human capital development:* through market-oriented training; institution and expansion of vocational education and improvement of health and social protection standards;
- *Development of production-based infrastructures:* investment in industrial parks; Special Economic Zones (EEZs), aquaparquas; thermal power stations; roads, ports and railways; definition of housing areas and State reserves;
- *Research, innovation and technological development:* creation of specialized research and development centres for agriculture, livestock and fisheries, energy, mineral resources, water resources management and ICTs;
- *Articulation and institutional coordination:* improvement of public institutions, improvement of coordination and intersectoral coordination, reform of legislation and creation of institutions that serve the industrialization strategy - ex. Development Bank.

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<sup>16</sup> The SADC Regional Strategic and Integrated Development Plan, the New Partnership for Africa's Development (NEPAD), the African Peer Review Mechanism (APRM), the African Union Agenda 2063, the Millennium Development Goals (MDGs) and the Post-2015 Global Development Agenda Vision, the Sustainable Development Objectives, Agenda 2030.

<sup>17</sup> Action Plan for the Reduction of Absolute Poverty (PARPA) I and II and the Poverty Reduction Action Plan (PARP). The first covered the period from 2001 to 2005, the second period from 2006 to 2009, and the third period from 2011 to 2014.



**47. To materialize the challenges inherent in the priority development areas, ENDE identifies two main instruments:**

- **Private Sector Development**, which emphasizes the creation of a more favourable business environment and the development of financial instruments that improve conditions and facilitate access to financing of the national private sector, especially small and medium-sized enterprises;
- **Quality Improvement in the Financing of Public Investment**. Policies to increase domestic revenue and for sound management of tax incentives, but also for the use of other sources of financing, such as public-private partnerships (PPPs), considering debt sustainability and in close coordination with monetary policy.

**48. The Strategy provides projections of the value of macroeconomic indicators in 2035.** The ENDE proposes a GDP growth forecast of over 7% for the whole period, and based on figures in 2012, a fiscal ratio growth of almost 12 pp, a reduction to zero of the recourse to internal credit by the government from 2021, a growth of government spending for investment, as a percentage of GDP, by 6 pp. The consequences of these forecasts will be analysed in Chapter 6 of this AFD.

#### *Medium and Short-Term Planning*

**49. The operationalization of the National Development Strategy depends on a series of medium and short-term plans.** The National Planning System includes several planning instruments at national, sectoral and territorial levels:

- **Five-year Government Program (PQG).** The first act of the government after taking office is the presentation for approval of the Assembly of the Republic of the economic and social development priorities of the country established in the PQG, which is based on the Electoral Manifesto covered in the General Elections. In practical terms, the PQG acts as a guide defining most of the medium and short-term planning instruments used during this period;
- **Poverty Reduction Action Plan (PARP).** Until recently, the PARPs were used, in parallel to the PQG, as instruments of dialogue with the Cooperation Partners. Its elimination was decided with the aim of rationalizing the number of planning instruments, making the PQG the government's main medium-term planning document and simultaneously a PRSP. The PARP elements were integrated into the PQG by including in the PQG a matrix of indicators and targets like the strategic matrix that existed in the PARP. The PARP was a technically better drafted document than the PQG and therefore the quality resulting from such integration should be analysed more systematically;
- **Sectoral and Transversal Strategic Plans.** Ministries develop their Sectoral Strategic Plans (Education, Health, etc.) linked to the implementation of the PQG. These plans consider various aspects such as the poverty reduction objectives set out in medium and long-term planning instruments and the existence of various agendas and plans (sometimes not always harmonious) at the sub-sectoral level<sup>18</sup>. There are, moreover, cross-cutting plans, such as the Strategic Plan for the Promotion of Private Investment 2014-2017;
- **Territorial Development Plans.** There are also provincial and district level plans. Districts develop a Strategic Development Plan (SDDS) for a period of five years<sup>19</sup>. Plans should have

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<sup>18</sup> For example, in health there are Strategic Plans of: (i) Pharmaceutical Logistics, (ii) Malaria Control, (iii) Health Human Resources Development, (iv) Tuberculosis Control; (v) acceleration of the fight against HIV / AIDS. All of them with different time horizons and not always horizontally coordinated.

<sup>19</sup> This plan is soon used to prepare the annual operations plan and budget (Economic-Social Plan and District Budget - PESOD).

active local participation and be consistent with national planning strategies. The district's annual operational plans are aggregated into a provincial-level plan. These provincial and district plans are operational in PESOP and PESOD, respectively;

- **Integrated Investment Program (IIP).** This plan defines the list of priority public infrastructure projects, in line with the vision and orientation of the GIP. The IIP tries to prioritize investments in the short and medium term, based on a triennial rolling investment program. The existence of a properly prioritized PII is very useful for informing the medium-term financial planning processes. Such is the case of the CFMP and the Debt Sustainability Analysis;
- **Economic and Social Plan (PES).** It is the document that translates the medium-term priorities into annual activities funded in the national budget. PES provides an operational plan for activities to be carried out based on each program in the PQG. Parliament approved the annual plan (PES) and budget (EO) proposed by the government. The government reports to Parliament on the progress of the implementation of the PES and the implementation of the EO.

### *Vertical Integration in the Planning System*

**50. There are problems of alignment between the strategic orientation of the GPA and the National Development Strategy.** Considering that the NSDS defines long-term national priorities, the PQG should theoretically be based on the NSDS and align national priorities with the action guidelines of the party that won the elections. However, the PQG 2015-2019 does not explicitly refer to the ENDE and defines five strategic priorities and three supporting pillars<sup>20</sup>. The strategic areas of intervention of the PQG focus on: (i) the development of agriculture, (ii) investment in infrastructure, (iii) the energy sector, (iv) tourism. These proposals are not incompatible with the NSDS goals, but do not pursue the same objectives and priorities.

**51. The disconnection between the indicators and targets proposed in the GIP and the ENDE is clear and reflects the lack of vertical integration of long-term and medium-term priorities.** The example of Education presented in Table 4 further illustrates the nature of this disconnect. The PQG is accompanied by a matrix of indicators with defined goals both for the end of the period and for each year, which does not correspond to the indicators and targets established in the NSDS. The PQG targets are more specific and input-oriented than those of the ENDE, but the targets and indicators do not allow establishing how the achievement of the PQG targets will add to the ENDE's overall objectives.

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<sup>20</sup> The PQG defines the government's central objective for the five-year period as "to improve the living conditions of the Mozambican people by increasing employment, productivity and competitiveness, creating wealth and generating a balanced and inclusive development in an environment of peace, security, harmony, solidarity, justice and cohesion among Mozambicans. "To achieve this goal, the Program defines 5 Priorities: (i) to consolidate national unity, peace and sovereignty; (ii) developing human and social capital; (iii) promote employment, productivity and competitiveness; (iv) developing economic and social infrastructures; and (v) ensure the sustainable and transparent management of natural resources and the environment. The Pillars of Support of the PQG are: (i) to consolidate the democratic rule of law, good governance and decentralization; (ii) promote a balanced and sustainable macroeconomic environment; (iii) strengthen international cooperation.

Table 4: NSDS and PQG Indicators and Goals for the Education Sector

Education Sector Indicators	Base	Goal 2035
Completion rate of primary education (7th grade)	47%	80%
Illiteracy rate	46%	27-30%
Net enrolment rate in primary education	46%	75%
Rate of utilization of vocational technical education	27%	70%
Number of students in higher education	3/1000 inhabitant	7/1000 inhabitant
PQG: Education Sector Indicators	Base	Goal 2019
N ° of students with disabilities in special inclusive education	100.000	125.000
Net enrolment rate at age 6 in 1st class	81%	86 %
Gross EP2 Completion Rate	82.30%	92%
Number of school staff in technical and vocational education	42.000	65.000
N ° of students of the 3rd class who reach the basic reading and calculation skills of the 1st cycle of primary education	6.3%	≥12 %
No. of Mozambican researchers and teachers trained at master's and doctoral levels	1.600 (1,200 Masters and 400 Doctors)	3.300 (2,500 Masters and 800 Doctors)
N ° of higher education teachers with psych pedagogical training	3.294 (46%)	.5.878 (70%)

Source: ENDE and PQG

**52. Poor integration of long-term strategies with medium-term plans will be a major obstacle to the effective implementation of SDGs.** Agenda 2030, with its ambition to be transformative, presents significant challenges for governments, for their planning and budgetary capacity. SDGs also introduce an additional degree of complexity in recognizing the integrated and interconnected nature of these challenges and turning them into targets that will then require a better interconnection between sectoral plans.

**53. The sectoral strategic plans have an acceptable correspondence with the GIP and sometimes good integration between the different planning instruments.** The recent review of public expenditures in 2014<sup>21</sup> has shown that in the education sector the goals and objectives in different planning instruments are consistent and well aligned. The six priority programs outlined were consistent with the priorities of the PARP and the sector strategic plan, and the PES correctly defines the activities of each program. MINDEH has made a concrete effort to maintain the same goals and objectives of the program in the different planning cycles. In the health sector, there are several plans, and alignment between them is slowly improving. Although the terminology used in the definition of health programs and targets is slightly different in the Strategic Health Plan compared to plans such as the PQG, the PARP and the PES, the overall objectives are very similar.

**54. The relationship between territorial development plans and sectoral plans at national level is complex and consistency is difficult.** The coherence of this bottom-up planning process is complex, and often harmonization between territorial plans and sectoral strategies is difficult to operationalize. The process of decentralization should be to strengthen local structures and delegate decision-making responsibility, but the framework of accountability in terms of service provision (minimum and uniform) for the whole country, as well as control and supervision of the local government operator.

<sup>21</sup> World Bank, "Mozambique Public Expenditure Review," December 16, 2014, 1–170.

Improving these points could result in a guide that will streamline the harmonization between territorial plans and sectoral policies and their monitoring.

**55. It seems important to continue to rationalize the number of planning tools used and their consistent use.** The overabundance of planning instruments without the definition of policy-makers, and of those who operationalize them, complicates the search for consistency of long-, medium- and short-term objectives and the availability of adequate funding for priority areas. For example, the presence of PARPs (A) and their linkage and consistency with PQGs was not always clear, nor was it clear which was predominant. The integration of the two documents aims at greater consistency, both political and operational, which is expected to bring greater consistency. The link between CFMP and PII can act as an anchor for the development trajectory. The operationalization of CFMPs and IIPs through PESs and EOs, and above all the coherence between the latter two documents, will increase the possibility of linking inputs to expected outputs.

#### *Links with the Sustainable Development Objectives 2016-2030 (SDG)*

**56. The objectives proposed in the ENDE are aligned but not directly related to the SDG.** The NSDS formulation was finalized in 2014 before the SDGs were fully defined and approved. Mozambique actively participated in the Sustainable Development Agenda 2030 and was one of the 53 countries selected by the United Nations to conduct a comprehensive, participatory and inclusive consultation process for the definition of SDG priorities. The national consultations were held under the leadership of the Community Development Fund (FDC) and culminated in a position paper on the post-2015 Development Agenda.

**57. Alignment with the MDGs is most clearly suggested at the level of medium-term planning proposed in the 2015-19 Government's Five-Year Program.** There is a primary link between the SDOs and the Strategic Objectives of the GQP as the PQG seeks to reflect in its priorities the three dimensions of sustainable development: economic, social and environmental. This was the government's first step in integrating Agenda 2030 into the National Planning System to facilitate the process of implementation, monitoring and evaluation of sustainable development commitments.

**58. The process of aligning SDG with the national development vision has begun.** The government has recently established a National Reference Group for locating SDGs and establishing mechanisms to integrate, monitor and report on their implementation. This group includes representatives from government, parliament, civil society, the private sector and cooperation partners. The location of SDGs will undoubtedly be a lengthy process, which will take some time, but due to the coincidence of PGQ with SDG, a significant number of SDG objectives are already being implemented.

**59. Mozambique's response to the DSOs will require a more detailed definition of the NSDS performance frameworks and the economic viability analysis of the proposed new objectives.** The work of the Reference Group will reveal some weaknesses in the NSDS formulation (summarized in Table 8). The NSDS results framework should be substantially improved to incorporate strategic objectives in all areas proposed by the DSOs. In addition, the location of SDG in Mozambique will require a relatively complex analysis of capacity constraints to finance and implement some of the objectives and achieve the specific goals proposed in the SDG. It will surely be necessary to negotiate compromise and compensatory solutions that should be adopted to accommodate capacity and funding constraints. The result of this AFD should be useful in this process.

### **3. 2 Instruments and Functioning of the National System of Public Financing**

**60. In the period under review, the government has developed a set of long, medium and short term financial planning instruments** in line with best international practice, especially in Public Finance Management (PFM). This section will examine the scope of these instruments, including the national budget, in their capacity to achieve effective fiscal policies through results-based public finance management.

### The Long-Term Vision

**61. The Public Finance Vision 2011-2025 (VFP)** proposes a guiding and programming framework for the major actions to be undertaken with the objective of achieving a level of service delivery of excellence in the management and governance of Public Finance. The VFP predicts that it will be evaluated and monitored every five years, coinciding this evaluation with the period of governance. The VFP defines six strategic objectives, namely:

- *The organization and modernization of the system of planning, programming and budgeting by programs and results and their execution*, impelling their decentralization to the Managing Units Beneficiaries of the State Budget
- *The increase in internal revenue and savings*, the adjustment of the expenditure pattern and the careful application of all internal and external resources via OE and CUT
- *The improvement of the prudent management and management of the State's assets and holdings and business sector*, as well as of the public debt and social security and social security, all integrating them into e-SISTAFE
- *The accounting and statistical organization and accounting* of the financial and economic situation of the state institutions, institutions and other entities, regardless of their degree of financial and asset autonomy
- *The adequacy and availability of the statistical and economic-financial information* of the relevant Public Finance to support the management and governance and the improvement of internal and external control and of the monitoring and public rendering of accounts; and
- *The constant modernization of the processes, systems and technological infrastructure of the Public Finance*, based on the professionalization and permanent valorisation of national human resources.

**62. The introduction of the long-term vision has made it possible to consolidate advances in GFP reforms.** According to the evaluation of VFP implementation in its first interim period 2011-2015, progress has been significant in several areas<sup>22</sup>. These improvements include several elements of the budget and plan process: (i) revision of the program framework in force in the PQG over the past 10 years, with a reduction in the number of programs and sub programmes from about 400 to 60 programs; (ii) decentralization and deconcentrating in the elaboration of local level planning and budgeting tools, with community participation, through Local Advisory Councils; (iii) the decentralization of the implementation of State expenditure, covering 128 of the 151 Districts and 1,305 Beneficiary Managing Units (85.57% of the total of the UGB and 74.73% of the total State expenditure); (iv) the preparation and publication on the Internet of Quarterly Reports on Budget Execution (REO) and the annual report of the General State Account (CGE).

**63. VFP is not designed to relate the future development of finance to the financing needs of long-term strategies.** The vision focuses on strategic direction in improving Public Finance Management (PFM) and sets long-term goals for the necessary reforms. In general, the objectives of the VFP are very broadly expressed (maintenance of macroeconomic stability, good state functioning, expenditure

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<sup>22</sup> Analysed in detail in the Public Finance Strategic Plan 2016-2019

management), and therefore lack programmatic relevance. The VFP formulation could be improved to also set specific quantitative targets that public finances should achieve to ensure the availability of funding needed to fund the country's development goals. Even in the PFM field, vision formulation could set quantitative long- and medium-term goals more accurately.

#### *Medium and Short-Term Finance Planning Instruments*

**64. The Strategic Plan for Public Finance 2016-2019 (PEFP).** The PEFP is part of the main guiding instruments of the Country's Development Programs: (ENDE, VFP, and PQG). The PEFP seeks to respond to the areas highlighted in the evaluation of the implementation of the VFP and to the recommendations made in the various Public Finance Management (PFM) assessments and studies carried out over this period. The Plan sets out the actions, indicators and targets to be developed under the PFM by the end of 2019 to achieve the objectives identified as priorities for this period. The plan seeks to unify all existing plans and programs in the PFM area of the MEF, and institutions that oversee and subordinate them. Table 5 summarizes the objectives and main lines of action proposed in the PEFP.

Table 5: Objectives and Main Actions foreseen in the ESDP 2016-2019

Objectives	Proposed actions
A. Stimulating savings and private investment	A.1 Promoting the country as a preferred destination for investment
	A.2 Contribute to the development of national business
B. Increasing State revenue collection	B.1 Increasing State revenue collection
	B.2 Strengthen the mechanisms of intelligence, investigation, inspection and tax audit
C. Ensure careful allocation of resources	C.1 Ensure macroeconomic projections and timely studies in the area of public finances
	C.2 Improve the criteria for selecting, executing and monitoring public investments, ensuring interconnection between different initiatives
D. Ensure greater efficiency in the execution of public expenditure	D.1 Improving financial programming instruments
	D.2 Consolidate single treasury account coverage
	D.3 Improve the scope, quality and deadlines for the presentation of Budget Execution Reports and the State General Account
	D.4 Improve implementation of the plan and budget
E. Improving the management of public assets	E.1 1 Improving the management of public procurement
	E.2 Register the main assets of the State
F. Guarantee the sustainability of public debt	F.1 Guarantee the sustainability of public debt
	Improve the management and supervision of the State business sector
	F.3 Ensure the implementation of measures to protect against fiscal risks
	F.4 Develop and strengthen the State social security area
G. Improve the use of public goods and the dissemination of information on public finances	G.1 Improving the effectiveness of the audit and control function
	G.2 Improving access to information on public finances

Source: PEFP 2016-2019

**65. The Medium-Term Strategy for Public Debt Management (2015-2018).** This strategy (2015-2018) is part of the second pillar of the PQG<sup>23</sup> with the main objective of contributing to sustainable debt sustainability in the medium and long term. The Strategy aims to ensure the mobilization of external and domestic financing to cover the public deficit, considering the lower cost and minimization of risk to the State, and reduction of external dependence. The recent collapse in public debt management -

<sup>23</sup> "Promoting a Balanced and Sustainable Macroeconomic Environment"

which has taken the other government's progress in the PFM field under review (discussed in 4.3.2) - places this strategy in the highest priority area for the implementation of Objective F of the PEFP.

**66. The Medium Term Fiscal Scenario 2015-2017 (CFMP).** The CFMP is the main medium-term<sup>24</sup> budgetary planning tool that forecasts public expenditure as well as the financial resources available at the general and sectoral level. The CFMP is a rolling instrument and subject to an annual update to reflect the current structural and structural changes and has been developed to provide an anchor in medium-term top-down financial planning and budgeting within the framework of the budget cycle. In practice, the CFMP is the instrument used to define the allocation of the Social Economic Plan and the State Budget. As it is a working instrument of the government, it is submitted, appreciated and approved by the Council of Ministers, but it is not submitted to the approval of the Assembly of the Republic.

**67. The Integrated Investment Program (IIP).** A recent PIMA evaluation by the World Bank indicates that the efficiency of public investment in Mozambique is lower than the average of Low Income Countries (LIC)<sup>25</sup>. Although the country has made relatively high public investments - an average of more than 15% of GDP over the past five years - the result is still weak: population access to standard infrastructures (education, health, water, electricity, transport) is lower than in paired countries with comparable levels of investment. The government launched a process of reforms of the public investment management system with the support of the World Bank and the IMF<sup>26</sup>. An important point of these reforms will be the improvement of the technical quality of the IIP, its prioritization process, and the inclusion of the IIP in the focus of the more general reforms that will be implemented to improve the quality of the integration of planning and financing systems.

#### The Annual Budget Process: Key Instruments and Procedures

**68. The budget schedule is well known and respected<sup>27</sup>** Table 6 summarizes the main steps of the national budget process. The preparation of the CFMP initiates the annual budgetary procedure. Planning and budgeting are carried out based on the territorial unit, i.e. at the central, provincial and district levels. The MEF issues a budget limit for the provinces in February, which, in practice, seems to follow historical patterns. The province then distributes budget limits to provincial directorates and districts based on government guidelines. Through the CFMP, budget ceilings are also communicated to ministries and spending agencies at the national level.

Table 6: Budget Schedule

Period	Process / Activity
December (year n-1) – March	Districts conduct an analysis of financial needs
February – May	The MEF prepares macro fiscal and expenditure limits projections and provides technical and methodological assistance to sectors and provinces, as well as preparing and elaborating the Medium Term Fiscal Scenario document (CFMP).

<sup>24</sup> CFMP is the equivalent of a Medium-Term Budget Framework or MTBF.

<sup>25</sup> Public Investment Management Assessment (PIMA), Source WB Public Investment Management Reform Mozambique Mozambique Draft, 2016.

<sup>26</sup> The reforms implemented include the creation of the Committee for Coordination and Selection of the Public Project in 2011; the development of the necessary legal support, making it mandatory for MEF to assess project assessments above USD 50 million before being included in the budget and adopting tools for a more standardized and professional evaluation of investment projects.

<sup>27</sup> (ACE et al., 2016) (World Bank, 2014)

Period	Process / Activity
Until 31 May	The CFMP is approved by the Council of Ministers and the MEF sends the letters (Circulars) and the Methodologies and Guidelines for the elaboration of PES and OE to the Sectors (Ministries) and Provinces (Provincial Governors), accompanied by the disclosure of the global expenditure limits for the CFMP's approved Goods and Services and External Investment lines.
June – July	Planning meetings at the level of the Sectors, Provinces and Districts for the distribution of budgetary limits to the Beneficiary Management Units (UGB) supervised and subordinated. Loading in the e-SISTAFE-MEO of the indicative limits harmonized by each UGB by the DNO-MEF and detailed typing in the MEO for each UGB.
August	DNO consolidates and harmonises budget proposals - possibly with harmonization meetings between the MEF and the Sectors and the MEF and the Provinces.
September	The Budget and PES are sent for approval to the Council of Ministers (until the 15th) and to the Assembly of the Republic (until the 30th) for approval.
Until the 15th December	Approval of PES and Budget

Source: PEFA 2015 (ACE et al., 2016) and PER 2014 (World Bank, 2014), author adaptation.

**69. The annual planning instrument is the Economic and Social Plan (PES), which sets the annual targets for achieving the PQG.** The PES matrix defines the annual implementation strategy for each of the five Priorities and the three Supporting Pillars defined in the PQG. The matrix uses a clear logical structure that defines for each Priority (or Support Pillar) the Strategic Objectives, the Programs for each Strategic Objective and the specific goals and actions for each Program. During the drafting process, the matrix presents a column that defines the budget required to finance these actions. This information does not appear in the final version that later goes to the AR because, theoretically, these definitions have already been incorporated into the State Budget. From the published material it can be verified that the formulation of these programs is of rather irregular quality and that there are significant variations in the coherence of the definition of diverse level objectives and their main goals and indicators.

**70. The process of elaborating the Annual National Budget and the instruments used do not favour the alignment of resources with the financing needs of the PES and the Medium-Term Plans.** A recent study examined the procedures and tools used in defining the annual budget at central, provincial and district level<sup>28</sup>. The evaluation detected several significant negative effects on overall system performance that considerably limit top-down and bottom-up reconciliation of the funding process. A significant shortcoming of the current system is the excessive focus on the formulation of the annual budget and not having a medium-term perspective. The main specific problems observed in the evaluation are:

- The budget is drawn up without proper prioritization of the sectoral programmatic perspective and focuses excessively on the analysis of types of expenditure (salaries, goods and services, investments) and not their strategic need. The information finally published in the OE and PES does not allow to relate the approved funding to the results and development goals;

<sup>28</sup> Stella, D. "Analysis of the Budget Allocation Criteria Used by the Government of Mozambique," UNICEF, February 27, 2017.



- Allocation decisions at sector, provincial and district level) are heavily influenced by projections of past trends rather than by specific strategic needs;
- The process of communication of limits and negotiation of the budget by sector (Education, Health, etc.) is carried out in parallel between the MEF and ministries, provincial and district authorities;
- Sectoral financing is therefore defined at the end of the process as the sum of the direct negotiated at the provincial and district levels, limiting the capacity of ministries to ensure top-down budget coherence with the strategic needs of the sectors;
- The Provincial Departments of Economy and Finance (DPEF) and district and provincial governments are free to reach compromise solutions in the allocation of resources that they deem most convenient without necessarily considering national strategic priorities;
- "Dual-rate" problems were seen with independent consideration of capital financing decisions and their associated running costs. Therefore, streets that are not being serviced quickly, or new schools and hospitals without enough staff are being financed<sup>29</sup>.

**71. The performance of the current system - measured in internationally comparable terms - leaves no doubt that this is a high priority area for future reforms.** The recent PEFA evaluation of public finances in Mozambique analyses in detail the performance of the integration of the plan and budget system. The qualification obtained (D) in the three dimensions analysed corresponds to the lowest performance quality possible. The reasons for this classification are summarized in Table 7. The evaluation ensures that there is considerable scope for developing the quality of the CFMP, which is a critical success factor in the process of improving system performance. The CFMP should allow the MEF and sectoral ministries to have an informed discussion of the funding of programs and projects to achieve the strategic objectives of the Five-Year Government Plan (PQG). The evaluation revealed the need to improve both in the design and use of the instrument and thus increase the capacity of government to guide action itself to achieve the results advocated in the strategies and programs. This analysis emphasizes the importance of the following improvements in the CFMP<sup>30</sup>:

- The CFMP presents aggregated projections and by type of revenue, without indicating the sectors that will generate them, except for megaprojects in the mining areas;
- Only the largest sectors have a sectoral strategy, but given the budgeting process outlined above and the characteristics of the ongoing deconcentrating process in the country, sectoral ministries do not have the full perspective of how sectoral policies are financed;
- Existing medium-term plans are aligned with the GQP, but their full costing is not always verified and an attempt is made to reconcile these cost estimates with the projections contained in the CFMP, which should be the macro planning anchor document;
- There is a lack of consistency in the quality of sectoral CFMPs, especially their integrity and the realism of the projections included therein;
- There is little clarity on the quality of the projections defined in the CFMP and hence on the credibility of the medium-term ceilings set out in the scenario. The comparison made by PEFA between the forecasts and the reality of the annual budget showed that: (i) total expenditure in 2014 was 20% higher than forecast for 2014 in the 2013 CFMP; (ii) capital expenditures deviated by 27% from those planned in the CFMP. More significantly, the OE monitoring documentation does not offer any explanation of these divergences or by the CFMP itself.

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<sup>29</sup> "PEFA Evaluation of Public Finance Management, 2015 - Mozambique, Final Report, Volume II," June 15, 2016, 1-113.

<sup>30</sup> Avaliação PEFA da Gestão de Finanças Públicas , 2015 Moçambique, Relatório Final, Volume II.

Table 7: PEFA Performance Assessment of Plan and Budget

Indicator	Evaluated Dimension	Classification 2015	Justification for Assigned Classification
PI-16: Medium-term perspective on expenditure budgeting	(i) Coverage and content of sectoral strategies	D	Sectoral strategies are not fully funded for most sectors / institutions. When fully funded, there is no clear link between these and the limits of the CFMP.
	(ii) Reconciliation of top-down approaches and vice versa within the medium-term budgetary framework.	D	The total limits published in CFMP 2014-2016 are not comprehensive (only for Goods and Services and Internally Financed Capital Expense items). The reconciliation process is not documented.
	(iii) Links between the medium-term framework and the annual budgets.	D	The second-year ceiling of CFMP at the aggregate level varies significantly. Current expenditure: 105%, capital expenditure: 127%, Internal revenue: 114%, Donations: 77%

Source: Reproduced directly from PEFA 2015

**72. Since 2012, the government has increased the availability of budget information by publishing the citizen budget and improving the coverage of the pre-budget statement.** However, transparency of information to allow greater control of fiscal management by citizens and parliament was also noted in the PEFA assessment as a priority for future reforms. The evaluation gave the least possible qualification (D) to most indicators of transparency of tax information, for example:

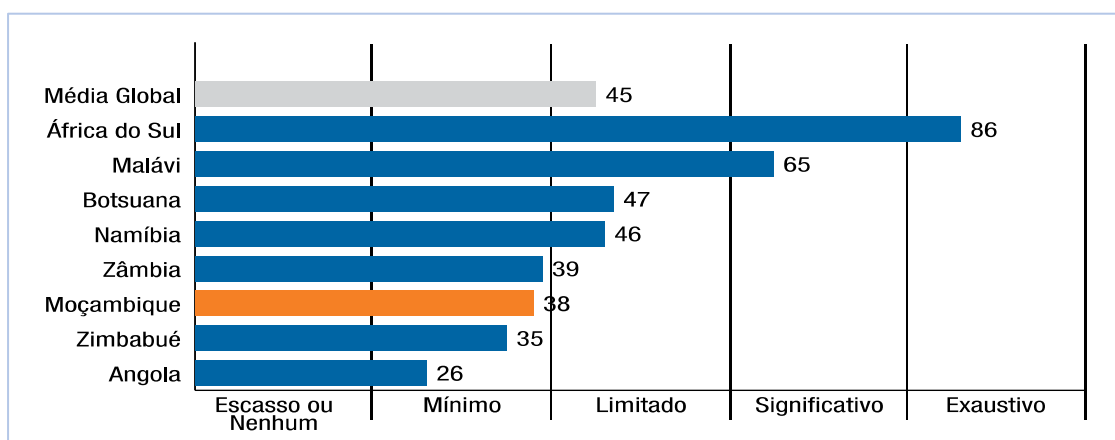
- *PI-5: Scope of Information included in budget documentation.* The budget documentation does not include basic information elements, such as the data on expenditure for the previous year and the estimates for the current year. The proposed budget and the approved budget do not provide a clear definition of what constitutes the fiscal deficit and how it will be financed and should improve the presentation of fiscal deficit / surplus forecasts, following international standards;
- *PI-9: Public access to the main fiscal information.* Reports issued during the year are published late (6-7 weeks after the end of the quarter). The TA audit report on the annual accounts is only available 15 months after the reference period;
- *PI-23: Mechanisms of transparency, competition and complaint in public procurement.* Centralized hiring records through e-SISTAFE provide basic information, but no data on contract performance. Hiring system monitoring (UFSA) produces general contract statistics, but coverage is not complete. Actual procurement processes are not monitored in relation to procurement plans. Most competitively awarded tenders are published, but there is no obligation to publish for those that are not competitively awarded.

**73. Other international transparency measures have placed Mozambique among the lowest performers in the region and in the world.** The Open Budget OBI Index <sup>31</sup> places Mozambique in the 71st place out of a total of 102 countries surveyed by 2015, and at the country level qualifying as minimum transparency. Mozambique's score was 38 points, out of 100 possible, a score lower than the global average of 45 points (Figure 13). The result for 2015 was lower than for 2012; the OBI indicates that the government has reduced the availability of budget information, not publishing the year-end report in a timely manner and for not publishing a biannual review. Furthermore, according to the OBI, the government has not made progress on: (i) publishing a budget proposal of the

<sup>31</sup> The 'Open Budget Index', or OBI in English, is the only independent comparative measure of central government budget transparency.

executive containing only minimal budgetary information; (ii) the publication of an audit report containing only minimum budgetary information.

Figure 13 - Comparison of Budget Transparency in Mozambique with other countries in the region



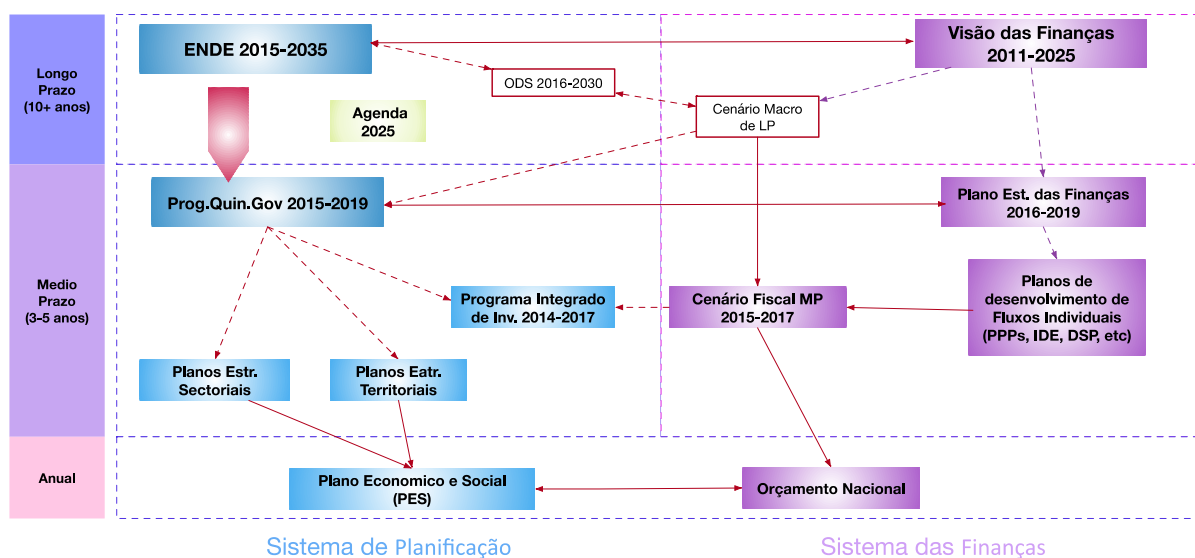
Fonte: Open Budget Index 2015.

### 3.3 The way forward to meet the challenges of sustainable development

**74. The AFD identified concrete opportunities to improve the potential and quality of the existing instruments, their horizontal and vertical link, and the need for some new elements.** The results of the review of the main elements of long, medium and short-term planning and financing systems are presented in Figure 14, highlighting the links that should be redesigned or improved and some additional elements to those previously presented in Figure 12 (marked red in Figure 14). In summary, the AFD proposes to prioritize the following improvements:

- Development of an integrated long-term vision. The NSDS review to achieve the SDG should include cost analysis and the revision of the VFP which should include strategies to finance it;
- Improve horizontal matching between plan and medium-term finance instruments. Action needed to ensure consistency between the results proposed in the GIPs and the PEFPs;
- Improve vertical integration between medium and short-term instruments. On both the plan and the finance side it is important to ensure consistency in policy implementation and the achievement of medium-term results;
- A new system ensuring horizontal integration between PES and OE. Implementation of the reforms to introduce the program budget and a results-based financing system.

Figure 14 - Missing Elements and Links in the Long, Medium and Short-Term Planning and Financing System



Source: AFD team based on various official documents

**75. The starting point should be the design and implementation of improvements to ensure a horizontal link between the instruments used in planning and finance systems.** The main result of the analysis is the poor horizontal matching between the two systems. The resolution of this disconnect is a Strategic Objective of the Public Finance Vision 2011-2025 and of the Public Finance Strategic Plan 2016-2019. In fact, this problem is the first point on the list of weaknesses of the public finance system in the FOFA analysis of the PEFP. The most striking feature of this disconnect is the lack of a direct strategic link between the ENDE and the Public Finance Vision and its medium-term counterparts: the PQG 2015-2019 and the PEFP 2016-2019. The link between short-term mechanisms (PES and EO) as measured by the PEFA evaluation is also very weak and encourages inefficiency in the use of public resources, which in the coming years will always be scarce.

**76. The first point to be addressed is the fact that both ENDE and PQG lack basic estimates of the costs of the suggested policies.** Neither of the two reference instruments of the planning system provides estimates of the amount of investment and resources (public and private) that would need to be mobilized to achieve the desired development results. This type of calculation can be relatively complex, especially for some cross-cutting objectives. However, general basic estimates can be made with a degree of accuracy sufficient to make strategic decisions about their viability, such as the cost of the NSDS goal to increase the number of students in tertiary education from 3/1000 to 7 / 1000 inhabitants (Table 4). Without this type of analysis, it is not possible to establish the economic viability of development plan targets or to estimate reforms in the public and private finance system to respond to these demands.

**77. To achieve consistent cost estimates, the technical quality of the results frameworks of the main planning instruments needs significant improvements.** The quality of the results frameworks of the planning system will require a major overhaul to estimate the costs to achieve the desired results. Many sectors suffer from considerable problems in formulating quality plans, and only in some cases (Education, Health) can they deliver concrete targets to allow reasonable estimates of the expected costs of the projected targets.

**78. SDG programming will provide an opportunity for major changes to be made to facilitate the integration of the plan and finance system.** Developing an integrated vision for long-term planning and finance is an essential prerequisite for a realistic formulation of SDG. One of the major differences between SDG and the MDGs is that the proposed targets must be adjusted to find

solutions that are affordable to the country's economic and capacity reality and therefore the costs of the proposed targets need to be analysed. Another important difference is that the SDG demanded much greater complexities for the plan and finance system, since the proposed objectives are highly interconnected to respond to the three dimensions of sustainable development: economic, social and environmental. The changes SDG programming could introduce include:

- Introduce a results-oriented view, which will require changes in the formulation of the ENDE and the PQG with a better formulation of results by area and by major programs;
- Changes in the formulation of the PQG, where the relationship between the proposed policies and the achievement of SDG should be more clear;
- Analysis of sectorial and macro feasibility of SDG and the capacity of the public and private sector to respond to the demands;
- The need for progress in program planning and budgeting to ensure and monitor the funding of complex cross-cutting programs related to various SDGs;
- Expand the scope of financial analysis and budget to incorporate other flows, whether public or private, as well as domestic and external flows.

### Box 1: Defining a New Strategic View of Finance

The development of a new strategic vision of financing is one of the main pillars for the construction of an Integrated National Financing Framework. For most countries this is a difficult task because they do not have long-term financial planning tools (public or private). In Mozambique, this fundamental instrument can be built on the basis provided by **the Public Finance Vision 2011-2025 (VFP)**, which analyses the long-term issues for the development of Public Finance Management. It is proposed to broaden the existing planning approach with the formulation of a **Finance Vision** that considers two additional dimensions:

- **Establish quantitative targets** for the long-term development of finances to ensure feasibility of the financing needs of long-term plans (NSDS)
- **Broaden the planning framework**, including the development of public and private finances

The development of this expanded vision will require two fundamental exercises: (i) to estimate the associated general costs of a reformulated NSDS to respond to SDG and (ii) to analyse the comparative advantages and possible roles that each financing actor could play (public, private, national or international), in priority areas (sectoral, thematic or geographical). On the basis of these definitions, the new **Finance Vision** should address the following issues:

- **How much is required:** Estimates of costs associated with long-term objectives are necessary to define the scale of resources that need to be mobilized and the specific targets by type of funding.
- **How much should be sought from each source of funding:** General targets covering the resources that could be mobilized from all actors involved (public and private, domestic and external).
- **The level of investment needed by each source, by priority areas:** Based on the perceived comparative advantages of these actors in the context of the country, establish general goals for the investments of specific actors in each sector, thematic area or priority geographic area, as defined in the new ENDE.
- **What the government needs to do:** Promote a framework of incentives and appropriate policies to obtain the contribution of these funding flows and ensure their development on the scale required.

Such a strategic definition would provide a fundamental guideline for the work of government ministries, departments and agencies that can clearly understand their role in meeting funding objectives and interactions between different actors.

Existing practice of systematically operationalizing VFP through Five Year Strategic Public Finance Plans (SPFS) aligned with the PQGs is also a major strategic advantage that the country can use in its favour. The only change is that the new VF should be operationalized through Strategic Finance Plans (PEFs), which are broader than the PEFs because they consider private as well as public finances. The implementation of VF through the PEFs would be an iterative process periodically reviewed based on the actual progress of resource mobilization and cost estimates of the updated plans.

### **79. At the same time, consideration should be given to the recasting of the long-term Finance Vision to achieve an integrated strategy that considers the development of public and private finances.**

The main elements of this reformulation are summarized in Box 1. It is proposed to add two key dimensions in the existing formulation: the programming of long-term structural changes in the financial system to ensure the feasibility of financing the NSDS goals and the integration of financing strategic management of public finances.

### **80. The government could build on the strategic advances already made in formulating the VFP to increase the impact of this instrument.**

The new Finance Vision document (which would no longer be just Public Finance) could provide a strategic framework for the development of funding flows that are considered critical to ensure the viability of long-term development plans. This type of planning marks a substantial shift from current practices of projecting past trends into the future. The idea is for the new VF to analyse the long-term strategic transformation of the existing financial base and,

from these goals, set objectives for the long-term development of flows (public and private, domestic and external). The list of flows analysed in the AFD allows to have a baseline for the main flows to be developed.

**81. The new Finance Vision (VF) should be implemented through new five-year Strategic Finance Plans (SPFs) that are more comprehensive than existing ones.** The existing system (transforming VFP into five-year PEFP) is a great strategic advantage that the country can use in its favour, and will be very useful in ensuring consistency in the implementation of the new Finance Vision. It is proposed to add an additional dimension to the existing formulation by incorporating Medium-term Strategic Plans for the Development of Individual Flows into the PEF (Fig. 14). These plans should set specific quantitative targets for the development of each of the priority funding flows and a coherent policy framework and institutional reforms to expand each individual flow to the maximum of its potential.

**82. These innovations will make it possible to substantively strengthen the role of the strategic phase of the budget in the management of public finances and to improve the quality and realism of the planning objectives.** The reconciliation of top-down and bottom-up competitive priorities is a political decision-making process that requires qualified technical support. Improvements in planning and budgeting should be the priority for the future, and the CFMP should be at the centre of this process, focusing first on developing a credible fiscal strategy and then moving towards improving mid-term budgeting of projects and programs. In addition, the targets for the new five-year PEFPs (which will no longer be public finance alone) should soon be used in the calculation of future Macro Scenarios and the CFMP. In this way, the concept of the opportunity cost of failing to meet the goals to develop the desired financing flows can be introduced into the analysis of finance. The explicit knowledge of the opportunity cost will make it possible to directly visualize the cost-benefit relation of the proposed reforms and their priority, since the cost of not reaching these goals will result in resource limitations to finance the OE.

**83. An additional element will be to prioritize and deepen the implementation of reforms to improve the quality of public investment management.** The government has realized the need to strengthen this management area by introducing the Integrated Investment Plans (IIP) as an auxiliary mechanism in the planning, selection and budgeting of projects to be financed with public resources. The rationality of having an integrated plan is explained in the document itself: (i) to harmonize and systematize sectoral strategic plans with a focus on those recommended in the PQG; (ii) for coordinated growth and impact in economic and social sectors, (iii) ensure that integrated investment projects provide a long-term vision for economic transformation and consensus on priorities, and (iv) ensure that the IIP projects that can be financed through public-private partnerships. To improve the quality of public investment management, it will be necessary to ensure continuity and improve the quality of the IIPs. The PEFA analysis presents some aspects that deserve to be improved so that such an instrument can bring the recommended benefits summarized in Table 8.

**84. Another major priority is to accelerate the introduction of program budgeting and a results-oriented funding system.** The government has begun the process to implement these reforms in 2011, with the introduction of program-based classification of the entire national budget. The implementation of program budgeting is essential to ensure consistency in the programmatic transformation of medium-term plans into short-term plans and their adequate funding. The use of

this tool can be very useful to enable a performance management and to improve the budgetary transparency of the public administration. However, Mozambique still has a long way to go<sup>32</sup>.

**Box 2: Cambodia: PFM Reforms to Program-Based Budgeting and Performance**

*The Government of Cambodia has made solid progress in building a PFM system that is gradually developing the capacity to support medium-term planning and management for results. The Public Finance Management Reform Program (PFMRP) was conceived as a comprehensive, long-term enterprise that defined four sequential phases over a 20-year period. (2005-2025). The PFMRP's long-term approach recognizes the difficulties in achieving meaningful and sustainable results in this field.*

*The program is implemented as a sectoral approach (SWAp) led by the Ministry of Economy and benefited from coordinated support from a broad base of development partners. The PFMRP identified four platforms (Consolidated Action Plans or CAPs), which were built sequentially in this long-term PFM reform process:*

**1. CAP1 (2005-2008) More credible budget.** (I) Comprehensiveness and budget integration; (II) Strengthen macro and revenue forecasting; (III) Streamline spending processes

**2. CAP2 (2009-2015) Effective financial responsibility.** (I) Reform of the classification and codification system for accounting and budgeting; (II) Design of the Financial Management Information System (FMIS) for main processes; (III) Define leadership and standards for the internal audit function

**3. CAP3 (2016-2020) Policy agenda accessible through the policy-budget link.** (I) redesign of the budget cycle and responsibilities (e.g. MTEF); (II) Program-based budgeting and budget analysis; (III) Explore options for fiscal decentralization

**4. CAP4 (2020-2025) Effective accountability of program performance.** (I) Full FMIS design; (II) development of an IT management strategy; (III) Asset registration project

*PFMRP analysts emphasized the importance of doing the reforms in the right sequence. The process began with amendments to the Public Financial System Act in 2008, followed by changes in the budget cycle to allow the introduction of PBB. The use of a Strategic Budget Plan (BSP) was piloted in eight ministries during (2008-2014). The full budgeting and budgeting process is now in place and should be completed by 2018. Only at the end of this phase will it be possible to align the budget with the policy, to establish the main program activities in the budget and to present a better system of indicators performance monitoring and reporting. It is estimated that this will allow the introduction of performance-based budgets in the final phase of the PFMRP.*

**85. International experience indicates that such reforms should be designed with a long-term approach.** Cambodia's example of Box 2 -internationally considered an example of success- indicates that implementation of these reforms may require time. It is usual that reforms are needed in the legislation that must be approved by the parliament. The introduction of other reforms is conditioned by the success of more basic PFM reforms that can also take time. A long-term plan should address the main issues already identified in the PEFA, with a well-studied sequence, and should surely include important intermediate results, such as:

- Complete the introduction of the classification system and codification of budgeting accounting according to international standards (COFOG), and then implement the new system for the elaboration, execution and information of the central government budget;
- Expand the functionality of the state financial administration systems (SISTAFE), integrating it in a coherent way with other systems (plan or audit);
- Redesign important aspects of the budget cycle and responsibilities and introduce new instruments such as the Strategic Budget Plans, which add a multi-year budgetary dimension to short-term program planning;

<sup>32</sup> Reference should be made to the Planning and Budgeting Subsystem (SPO) project as a likely path to solving the constraints mentioned in this area. Based on the SPO, a more integrated system and results-oriented management tools can be developed.



- Develop the capacity of different ministries and government agencies (central and decentralized) to achieve a consistent minimum quality of sectoral plans and their cost estimates. Develop a system of performance indicators and monitoring of performance reports;
- Explore more efficient options to improve the current degree of fiscal decentralization that ensure consistency in the implementation of medium- and long-term plans;
- Redesign Financial Management Information Systems (FMIS) to enable the implementation of major budget processes by programs;

Piloting the introduction of the new system into a selected group of government ministries or agencies for several consecutive periods, gradually increasing the use of the system within the public administration;

Table 8: Summary of key proposals to improve integration between planning and finance

Area	Top Required Enhancements
<b>Reformulation of the Long-Term Plan</b>	<ul style="list-style-type: none"> <li>• Review of the results framework proposed in the NSDS in the SDG formulation process</li> <li>• Redesign the NSDS Indicator Matrix in order to effectively guide the implementation of the pillars of the strategy and its compatibility with the SDG</li> <li>• Improve the scope and consistency of the strategic indicators proposed in the NSDS by ensuring that:               <ul style="list-style-type: none"> <li>• All strategic areas are included in the strategic indicators framework</li> <li>• The results framework provides a definition of quality for the goals and performance indicators at all levels of output (outputs, outcomes, impact)</li> <li>• Consistent definition of indicators at the same level (e.g. between defined targets for infrastructures and private sector development)</li> </ul> </li> <li>• It is necessary to carry out cost estimates of the goals proposed in the NSDS for the SDOs in order to establish the ex-ante feasibility of the main interventions necessary to achieve these objectives and to have concrete targets for the long-term financing strategy</li> </ul>
<b>Integration between Long-Term Plans and Finances</b>	<ul style="list-style-type: none"> <li>• Reformulate the Finance Vision to achieve an integrated strategy that considers the development of public and private finances to ensure the feasibility of financing the ENDE goals</li> <li>• Implement the new Finance Vision (VF), following current procedures, through new five-year Strategic Finance Plans (SPFs) that are more comprehensive than existing ones</li> <li>• Incorporate into the PEF Medium Term Strategic Plans to operationalize the development of individual financing flows that are considered critical in the new VF</li> <li>• Introduce the use of macro scenarios to improve the quality and realism of medium-term planning objectives</li> </ul>
<b>Integration between Long and Medium-Term Plans</b>	<ul style="list-style-type: none"> <li>• Improve the quality of the CFMP by incorporating three-year fiscal projections that include functional and administrative sectoral classification</li> <li>• Extend the focus of the CFMP to cover sector cost estimates and improve budget allocations</li> <li>• Use the targets of the new five-yearly PEFs (which will no longer be just public finance) in calculating the future Macro Scenarios and the CFMP, thereby introducing the opportunity cost concept of not meeting targets to develop the desired funding streams</li> <li>• Improve the linkage of the CFMP with the IIP and consider both the costs of the works and the impact that their operationalization will have on current expenditure.</li> </ul>
<b>Quality of Integrated Investment Plans</b>	<ul style="list-style-type: none"> <li>• Develop an investment plan that incorporates the main infrastructures considered of strategic interest for the development of the private sector, by priority areas</li> <li>• Develop a new IIP model that, in addition to public sources, consider mobilizing private resources and setting targets for PPPs and other public-private financing mechanisms</li> <li>• Incorporate into the IIP the implications that investment projects will have on medium-term operating expenditure and systematically integrate them into the budget</li> <li>• Introduce a system of financial and physical monitoring of the progress of the IIP projects that will report on the evolution of implementation and the reasons for possible deviations from the plan and targets</li> </ul>
<b>Quality of PES and Budget integration</b>	<ul style="list-style-type: none"> <li>• Accelerate the introduction of program budgeting and a results-oriented financing system and plan the sequence to implement actions aimed at:</li> <li>• Redrawing the budget cycle and key responsibilities (new legislation)</li> </ul>

Area	Top Required Enhancements
	<ul style="list-style-type: none"> <li>• Introduce new instruments, such as the Strategic Budget Plans, which add a multi-annual budgetary dimension to short-term program planning</li> <li>• Develop the capacity of different ministries and government agencies to achieve consistent quality of plans and cost estimates.</li> <li>• Develop a system of indicators and monitoring implementation performance</li> <li>• Explore more efficient options to improve the current degree of fiscal decentralization that ensure the coherence of the implementation of the medium and long-term plans</li> <li>• Redesigning Financial Management Information Systems (FMIS) to enable the implementation of major budget processes by program</li> <li>• Piloting the introduction of the new system into a selected group of Ministries for several consecutive, gradually increasing the use of the system in public administration</li> <li>• Expand the functionality of the state financial administration systems (SISTAFE) and make a coherent integration with other systems (plan or audit)</li> </ul>

## 4. Public finances and major flows

### 4.1 Overall analysis of public finances

**86. Mozambique's macroeconomic performance over the last few years has ensured rapid economic growth that has ensured good macroeconomic stability.** Until the sudden deterioration in 2016, the country presented a growth of public expenditure consistent with the evolution of the economy and revenues. The data in Table 9 show the evolution of the main variables of the economy in the last decade, and it can be verified that the total resources of the public revenue almost quadrupled, from 55 to 215 billion meticaís. The fiscal ratio increased from 15.7 percent to 26.3 percent, growing by more than 10 percentage points, and domestic resources increased their share from 50 percent in 2006 to 76.9 percent in 2015, underscoring the government's commitment to pursue fiscal policies that would allow the country to increase domestic revenue and reduce dependency on aid.

*Table 9: Evolution of State revenues in the period 2006-2015*

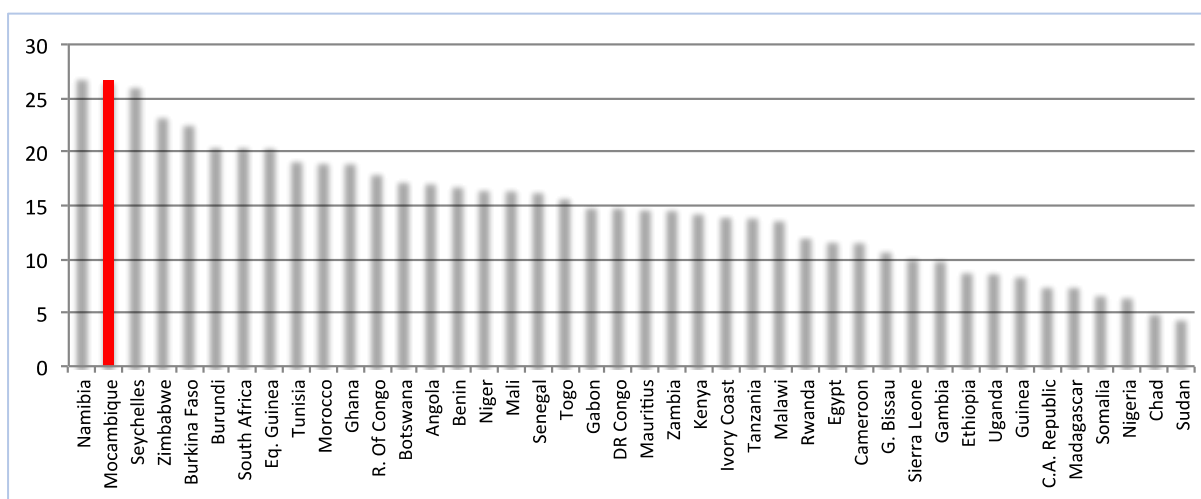
Million of MZN (in nominal terms)	2006		2009		2012		2015	
	MZN	%	MZN	%	MZN	%	MZN	%
Total resources	55,254	100	87,438	100	144,590	100	214,702	100.0
Internal Resources	27,866	50	47,855	55	101,627	70.3	165,025	76.9
Domestic Revenues	27,794	5	47,565	54	98,477	68.1	155,893	72.6
Internal Loans	72	0,13	290	0	3,150	2.18	9,132	4.3
External Resources	27,388	49,6	39,583	45	42,963	29.7	49,677	23.1
Grants	18,188	32,9	25,771	29	27,332	18.9	18,677	8.7
Credit	9,200	16,7	13,812	16	15,631	10.8	31,000	14.4
GDP (Nominal Billions MZN)	178	-	300	-	433	-	592	-
Real GDP Growth Rate	8.5	-	6.4	-	7.2	-	7.5	-
Internal Revenue / GDP	15.7	-	15.8	-	23,.	-	26.3	-

Source: Mozambican Tax Authority, MEF

**87. Mozambique's public spending is one of the highest in comparison to other countries in the region, and therefore its effectiveness should be given priority.** The rapid growth of public spending is also cause for concern. The volume of public expenditure as a percentage of GDP has declined over time, but data for 2015 (Figure 15) indicate that the ratio in Mozambique (26.66%) is the second largest in Africa and significantly higher than the average in the region (15.01%). Therefore, the search for balance in the weight of the State in the economy and the efficiency and effectiveness of this expenditure should be given priority.

**88. The public expenditure structure shows a worrying increase in expenditure on wages and non-wage benefits.** The Public Expenditure Analysis (ADP) of 2014 indicates that even in those times of greater economic stability there was concern about the sustainability of public spending and that public-sector expenditure on wages as a percentage of GDP in Mozambique was also one of the largest in Africa. Providing adequate compensation to staff is a necessary condition for ensuring the quality of public services, but it is not a sufficient condition. The most recently measured reality in the education and health sector ADPs confirms that there is no relationship between wage increases and quality of services and shows that public sector productivity is low compared to the countries in the region. The high weight of wages in the structure of public spending adds significant levels of rigidity to the public budget. It is proposed later to review the efficiency of the decentralized management system, especially regarding human resources management.

Figure 15 - Public Expenditure in Africa (% of GDP)



Source: World Bank

**89. In comparative terms, the level of public investment in Mozambique is relatively high, but its growth has been highly dependent on donations from development partners.** The accelerated growth of the last decade was also boosted by a high and sustained investment of the international cooperation partners. Section 4.3.3 shows that Official Development Aid has decreased its relative weight from 13.1% of GDP in 2005 to 6.8% in 2015, but the country's dependence is still relatively high. This dependence is particularly noticeable in the case of public investment, since in the last decade most of the revenue only covered the financing needs of current expenditure. The expected short-term situation calls for new solutions, as fiscal capacity will be relatively limited and the elimination of donations from development partners is expected to accelerate in favour of increased concessional financing (see Section 4.3.3) considerably reducing the margin and manoeuvre of the government.

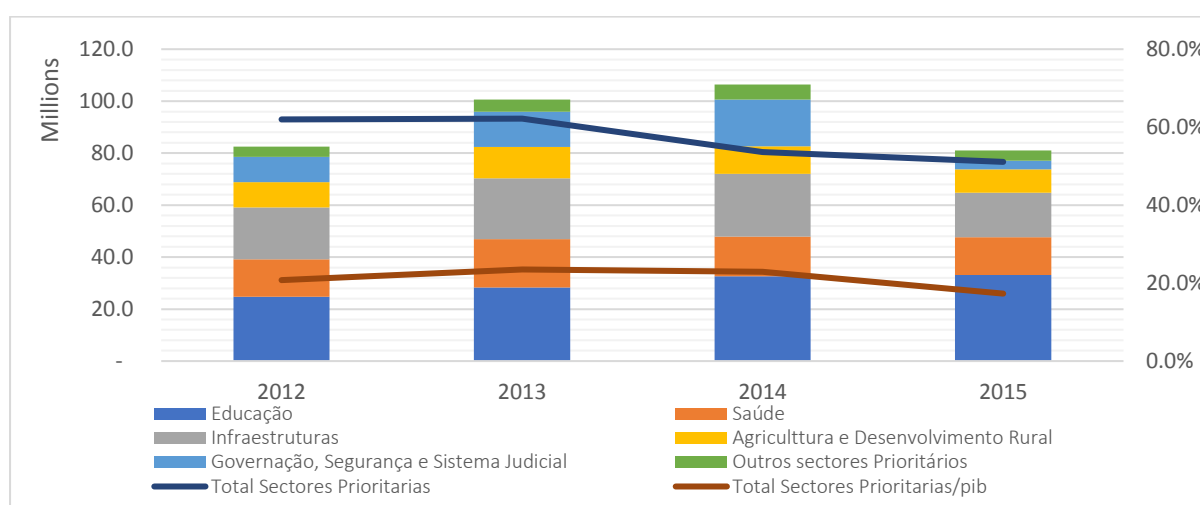
**90. The analysis of expenditure allocation and results by sector shows the need to deepen and improve budgetary processes and to focus on the efficiency of public expenditure.** The recent allocation of public expenditure is summarized in Figure 16, with increasing expenditure alignment (in% of GDP) with the sectors defined by PARP (A) s as priorities<sup>33</sup>. The beginning of budgetary constraints marked a departure from this alignment. Development spending in the structuring

<sup>33</sup> PARP (A) s has defined as a priority a set of sectors including Education, Health, Infrastructure, Agriculture and Rural Development, Justice, Social Action and Employment. In PQG 2015-19 these sectors are called 'Structures'.

sectors hovered over 63 percent to 53 percent in 2014 and 51 percent in 2015. By 2016 the Mozambican government had to revise the budget down for the first time and public spending in the structuring sectors contracted, with significant service interruptions at the end of 2016, as it was also decided not to pay the thirteenth salary to public employees. The current budgeting methodology - described in the previous chapter - results in a substantial difficulty in linking budget allocations with the priority activities. The latest PEFA report explains that there is a disarticulation between the decision-making process of PES targets and the availability of financial resources, and that there is considerable room for improvement in shaping public spending in favour of the poorest. The less poor benefit from public spending, are the majority beneficiaries of higher education and have the greatest access to water and sanitation services. Recent studies<sup>34</sup>

argue that improved and transparent budgetary mechanisms and procedures are needed to ensure minimum standards and the best cost-benefit ratio for all operating and investment expenditure.

Figure 16 - Structural expenditure in MZN million, 2010, and total expenditure as% of GDP



Source DNPO-MEF. Authors' calculations

## 4.2 Efficiency and effectiveness of public expenditure

**91. Increasing the efficiency and effectiveness of resource use should be a high-priority area in the management of short-term public finances.** The perspective presented in Chapter 2 indicates that the financing capacity, and particularly public-sector indebtedness over the next five years, will be limited. Therefore, in addition to seeking new sources of funding, an additional government priority should be the search for more impact on the use of existing resources. Recent studies show that the space for improving efficiency and effectiveness in the use of public resources in Mozambique is broad, and the 'efficiency gains' could be of sufficient magnitude to ensure the continuity of service provision and the most needed investments with the existing fiscal space.

**92. Achieving 'efficiency gains' could dampen a significant drop in the volume of short-term public funding.** The country is facing a period in which, for the first time, projections indicate that the resources available to finance public spending will not grow; and the projections for the worst-case scenario should reduce resources. As early as 2016 the government had to revise the budget low by mid-year. The fall in public resources coupled with the temporary (or perhaps definitive) reduction

<sup>34</sup> Stella, D. "Analysis of the Budget Allocation Criteria Used by the Government of Mozambique," UNICEF, February 27, 2017.

of donations from the General Budget Support (GDO) development partners could have a major impact on the evolution of sectors considered essential (Health, Education, etc.) and processes of poverty reduction and economic recovery.

**93. Increasing the efficiency and effectiveness of public expenditure will require exploring several complementary approaches.** According to the available studies, there are a variety of options that should be researched to achieve efficiency gains in public spending. Unfortunately, many of these options need medium- and long-term reforms to produce tangible benefits. The challenge for the government will be to rapidly implement opportunities that will make a significant impact in the short term. There are at least four main ways to guide this research:

- Improve efficiency in resource allocation. This path proposes to seek a more direct alignment of resource allocation with priorities and to ensure that the scarce resources available are well distributed to the neediest beneficiaries;
- Improve the impact of public spending on development. This course proposes to study opportunities for more development by metical spending, essentially improving the productivity of the value chain in providing the most essential public services;
- Increase tax space by eliminating unnecessary resource losses. This approach proposes the systematic reduction of unnecessary expenditure, especially losses of resources generated by public enterprises;
- Increase tax space by reducing subsidies. In parallel, it is proposed to consider other options to reduce unnecessary expenditure, such as fuel subsidies, which also negatively affect other sustainable development objectives.

**94. Initiatives to address increased resource efficiency will require strong MEF intervention over the next 4-5 years, starting with a damage control perspective.** The more pragmatic conclusion that the government should draw from the current economic crisis is to assume that the goals set in the PQG lack programmatic value - at least until the end of this governance period - and that the current scenario should shift to a control scenario of damages. Therefore, the aim of increasing efficiency is to prevent the crisis from adversely affecting the development objectives already achieved. It is proposed to tackle the crisis with a positive outlook and to take advantage of the situation to improve structural issues in public finance management to make the most of the resources available during the transitional period.

**95. The work to be undertaken will require strong political will, sufficient time and resources that will need to be devoted to tangible results.** As expected, there are no magic solutions and the work will require complex policy decisions, since many of the measures to improve the efficiency of public spending may be unpopular for some sectors of society. Moreover, except for a few very particular cases, it is foreseeable that to achieve visible results at macro level, a series of measures and interventions will be required which will individually produce results only at the micro level. In some cases, it will also be necessary to reprioritize existing medium and long-term initiatives that, with strong leadership and correct orientation, could lead to the generation of tangible results in the short term. The general ideas proposed below should be transformed into a well-defined program with clearly established leaderships, resources and timetables, with a 5-year work horizon.

#### 4.2.1 Opportunities to Improve Resource Allocation Efficiency

96. The acceleration of initiatives to improve the budget system is a priority to improve the allocation of resources. The previous section noted that current methodology and the instruments used for budgeting at central, provincial and district levels do not favour alignment of resources with

funding needs. The difficulties in linking budgetary allocations to objectives and activities required to implement the thematic and sectoral plans at national level are substantial. In a resource scarcity scenario, these problems require urgent attention, for two fundamental reasons: (i) it is necessary to ensure the most efficient allocation of scarce resources; (ii) if budget reductions or cuts are required, the government should avoid applying the same inefficiency criteria used in the current allocation to ensure the least possible negative impact of reductions in the provision of essential services to the population.

**97. The intervention of the MEF should also focus on improving the management of asymmetries in the collection and allocation of resources at the subnational level.** A key role of the MEF is to reduce disparities in resources between the richest and poorest provinces and municipalities, and to ensure that, up to the local level, each municipality can provide the same level of service to its citizens. The Ministry should accelerate reforms of the current system to (i) increase fiscal autonomy by ensuring that richer provinces and municipalities can finance most of their spending needs with their own revenues, and (ii) improve the functioning of the allocations and transfers to ensure equity in the delivery of basic services. The Public Expenditure Analysis (ADP) studies for the central government in 2014, and the most recently completed studies for the Education and Health sectors, coincide in indicating that there are opportunities for significant improvements in two complementary areas:

- *It is possible to free up fiscal space by increasing unrealized revenue in geographic areas where income levels are higher.* The 2014 ADP estimated that the margin for revenue growth in some municipalities is considerable, as for example in the cases of Maputo and Nampula. Revenue could almost triple (from 1.3% to 3% of GDP), mainly by boosting property tax revenues. In Nampula, collections could rise from 0.9% of GDP to 2% of GDP<sup>35</sup>. Only in these two municipalities could a fiscal space of 3% of GDP be liberalized, a volume equivalent to half of total public expenditure on education at national level (from 7.1% of GDP in 2014 and 2015);
- *Further progress is needed in improving the allocation of public expenditure to ensure the equitable financing of the poorest regions.* The overall ADP assessment of 2014 asserts that the richer segments of the population benefit more from public spending in many areas (education, health and water) and that there is significant room to improve equity in allocating spending to the poorest populations. Significant progress has been made in the education sector, but equity in access to education has only improved for primary education and remains severely limited at other levels of education<sup>36</sup>. The 2015 Health ADP notes that the distribution of expenditure by provinces should be improved since it is not equitable in relation to population size or the incidence of poverty.

**98. The increase in revenues collected locally will require significant improvements in central and decentralized fiscal management.** Property taxes and other local taxes are quite complex to manage and the search for a technically perfect solution would require capacity improvements and availability of information at the municipal level that could take a long time to achieve. Equally, sufficient short-term intermediate measures can be sought that point in the right direction and increase collection, although they are not definitive. These short-term measures should also seek to improve the incentive system to increase local revenue. ADP proposes a few measures, such as revising the criteria and formulas used in the Investment Fund for Autonomous Initiatives (FIIA) and

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<sup>35</sup> Mozambique Public Expenditure Analysis, World Bank, 2014.

<sup>36</sup> Analysis of Public Expenditure on Education in Mozambique, World Bank, 2017.

the Municipal Compensation Fund (FCA) to eliminate disincentives to expand tax collection. The new formulas could also include more definite redistribution criteria and better address disparities in revenue collection between rich and poor provinces and municipalities. Predictably, these measures will have political costs, but at a time of economic crisis such as the present, they should be considered.

**99. Improving the transfer system for deconcentrated governments should focus on ensuring equity in the provision of basic services.** For the provinces and districts, own revenues are low and the main sources of revenue are central government transfers. One of the objectives of the transfer system is to ensure a minimum level of essential services. ADP proposes options for improving the system by introducing criteria to prioritize quality and performance and a greater emphasis on efficiency that, at the same time, allow these priorities to be maintained. The level of additional resources available for priority expenditure will require a more careful planning of resource envelope changes and reallocation of funds to priority sectors.

#### 4.2.2 Opportunities to Improve Resource Utilization Efficiency

**100. All existing Public Expenditure Analysis (ADP) studies agree on the need to prioritize the improvement of the value chain's efficiency in the provision of essential public services.**

Mozambique has benefited from several World Bank-funded studies that have analysed the efficiency of public spending in achieving the results recommended in providing services to the population. Available works addressed public expenditure in 2014 and, more recently, specific ADPs were completed in the Health (2015) and Education (2017) sectors. They all agree that significant improvements in the efficiency and effectiveness of delivering essential public services can be achieved.

**101. The analysis of public expenditure in the education sector describes a 'Mozambican paradox' where a significant increase in investment has resulted in decreasing educational outcomes.** 3/4 of the financing of this sector is carried out with public funds, mainly wages. The external donor side is targeted at high priority areas such as building schools, providing teaching materials (including textbooks) and basic school operations (excluding salaries). The study strongly proposes the need to initiate reforms to improve expenditure efficiency with the following arguments<sup>37</sup>:

High unit costs. The international comparison of the unit cost with other countries indicates that the government spends more per enrolled child, especially at the secondary level. Primary education costs are slightly higher than the sub-Saharan African average (13.6% of GDP vs. 11.2%); however, at the secondary level these are notably higher (38% of GDP vs. 24%);

- Higher cost to achieve development goals. In comparative terms, Mozambique could achieve expected (or near-expected) results, using significantly more resources than other countries. A comparison with 172-174 countries, with an average of 12-13 observations between 1990 and 2013, showed that Mozambique is one of the few countries that, when it spends above expectations, does not achieve a change in schooling results to better foreseen;
- Imbalance in cost structure. Most of the increase in public expenditure on primary education was used to finance wages (93%, against 5% for capital investment and 2% for goods and services). Although there are no formulas to define the ideal cost distribution in the sector,

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<sup>37</sup> Analysis of Public Expenditure on Education in Mozambique, World Bank, 2017.

the current distribution cannot be correct, since there are investment minima by area below which quality of service cannot be achieved;

- Increased efficiency and risk of unsustainability of the system. The increase in expenditure on wages was aimed at reducing the pupil-teacher ratio to improve learning conditions, which did not happen. Measurements indicate that the relative efficiency of education has declined in all income indicators since 2006, due to low income performance and rising expenditure. ADP states that recent progress in the sector, focusing on access to education, has been achieved at the cost of a dramatic loss of efficiency in global spending, and that Mozambique is moving rapidly to lower levels of efficiency. The assessment states that continued loss of efficiency, especially at the primary level, has implications for sustainability because it is unlikely that the country will be able to achieve better results and average incomes through higher expenditures.

**102. The analysis of public expenditure in the health sector describes a similar situation and highlights the potential for significant gains in efficiency in public health services.**

The evaluation points out that, although there is a need to increase per capita expenditure, future expenditure will have to be much more efficient. Mozambique's per capita expenditure remains low in relation to the peers and below the average in sub-Saharan Africa. Considering that per capita spending in 2012 was USD 33, and that the cost of delivering a core package for health in 2012 was estimated at USD 86, ADP estimates that Mozambique would have a financing gap of USD 53 per capita. At the same time, Mozambique's Health Performance Index<sup>38</sup> is below average relative to per capita health spending, with countries like Malawi and Ethiopia achieving better results with lower per capita expenditure. The examples presented in the ADP show that 'efficiency gains' could count towards at least USD 4 of the financing gap, estimated by ADM to be USD 53 per capita. These efficiency gains could represent 1.5% of GDP and, to achieve them, ADP considers the following situations:<sup>39</sup>

- Efficiency in the provision of maternal and child health care. Comparison of economic performance to improve maternal mortality (MMR) and infant mortality (IMR) with countries in the region indicates that countries such as Niger obtain IMR like those in Mozambique (60 and 62 per 1,000 live births) at a cost significantly lower (27.2 USD against 40.3). Ethiopia can have a lower MMR than Mozambique even spending less per inhabitant;
- Intermediate results indicators. Comparing performance with reference to malaria prophylaxis for pregnant women shows how Malawi achieves significantly better results than Mozambique (53% of the population affected, versus 36%) while Mozambique spends more per capita (33 USD against 32 USD). A comparison of DPT<sup>40</sup> vaccination costs indicates that to achieve similar percentages of children aged 12-23 months receiving vaccination (74% in Niger versus 76% in Mozambique) Mozambique spends a lot more (33 USD per capita versus 23.9% USD);
- Composition of investment per capita. One reason for these per capita cost differences is the use of community health agents to achieve better results at lower costs, especially in remote or sparsely populated areas. ADP also notes that the lower percentage of technical workers compared to administrative workers also contributes to the low efficiency of expenditure. The finding of possible technical and administrative imbalances indicates a need for a more careful

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<sup>38</sup> The index aggregates performance in several indicators, such as: malnutrition, height for age and weight-for-age in children under five, and acute respiratory infection and diarrhoea in children, low birth weight, maternal mortality rate, contraceptive prevalence and births attended by qualified personnel.

<sup>39</sup> Mozambique Health Public Expenditure Review 2009-2013, Draft, Nov 2015.

<sup>40</sup> DPT: Diphtheria, Pertussis (or whooping cough) and Tetanus



planning of the composition of the workforce and is particularly concerned with the implementation of budgetary constraints that may occur in the short term;

- Unequal resource allocation. One source of inefficiency lies in the unequal workloads in the various provinces. In the current distribution, many provinces get a larger share of the health budget in relation to population size, increasing the costs of providing per capita services nationwide. The distribution of health spending needs to be realigned to reflect the size of the population. A possible reallocation of human resources could correct this imbalance and solve quality problems, as some provinces are overburdened with the minimum workload per worker to provide quality services;
- Reliance on foreign aid and sustainability. Almost two-thirds of total health expenditure is financed from external aid funds, raising questions about the sustainability of the current system and the external aid provided.

**103. Examples of education and health advocate a more systematic review of the efficiency of expenditure in the provision of decentralized services.** It is reasonable to think that the situation described for Education and Health is repeated in other sectors, and that the lack of more concrete examples is because there are no further studies. Decentralization of personnel management reforms at the district level is considered a success from the point of view of provinces and districts. In the education sector, decentralization of payroll is relevant to reducing teacher absenteeism, especially because of increased supervision. In the health sector, decentralization is reducing the level of bureaucracy, allowing the sector to focus more on policy making. However, the two cases analysed in depth show similar situations of high unit costs, inequalities in resource allocation and imbalances in the cost structure, with deviations tending to increase the administrative costs of operating the services. Experiences at the sectoral level suggest the need to systematically review the efficiency of expenditure to finance the provision of services. A focus on continuing to finance 'more of the same' by accepting the inefficiency of the current operating cost structure will not lead to sustainable results in the medium term.

**104. One way forward would be to revise the system for budgeting operating expenditure to finance the provision of essential services.** Without a thorough knowledge of how to improve management by each service area, significant improvements could be achieved by introducing a standardized budgeting system to estimate public service costs. The government could develop basic formulas with standard operating costs to facilitate (mechanize) the budgeting of the operating functions (Wages and Goods and Services) and make it equitable, transparent and more efficient. This standardization should be based on both the services currently provided and the ideal standard, to indicate the distance between reality and the ideal goal. To do this, it is necessary to review the cost parametric used in the different sectors and to compare them with good practices at an international level. The use of instruments such as Public Expenditure Tracking Surveys<sup>41</sup> at the national level, by sector, could be very useful. The introduction of a standardized system would also facilitate the simpler and more objective supervisory functions of internal organs and parliament.

**105. In a resource scarcity scenario, the strategic review of investment expenditure is a priority to increase the efficiency of public expenditure.** The government must use the capital expenditure instrument intelligently to reduce the territorial imbalances of all types of infrastructure. The choice and future allocation of this type of investment should become strategic and clearly indicate the objectives to be achieved (or problems to be solved) to increase the transparency of decision-making.

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<sup>41</sup> Public Expenditure Tracking Surveys ou PETS.

The investment package must be developed with a view to responding to sectoral priorities and sector-specific programs. The programming of government investment - at central and provincial level - should be done from a perspective of allocation of scarce resources among many competitive priorities and, therefore, a shift from the currently used generic budget ceiling systems. The CFMP and the part devoted to financing and capital spending would have to be strengthened, focused and rigorously examined. The IIP and PPP programming should move in line with these objectives.

**106. The reform of the procurement system could also significantly increase the efficiency of public spending.** The PEFA assessment indicates that this is one of the most fragile aspects of public expenditure control, since 67.6% of procurement processes in 2014 did not apply competitive methods. Therefore, 52.9% of the total value of public procurement in 2014 was contracted by direct agreement, which represented a volume of 24.6 billion meticaís out of a total of 46.4 billion. These proportions are very low, especially compared to other countries in the region, which can make purchases through much more competitive procedures. An additional problem identified in the PEFA is that, with the decentralization of responsibility for contracting processes at the level of management units, UFSA cannot exercise full control over these critical areas. Other adverse effects observed include frequent changes and changes in budget appropriations during the implementation process that make procurement planning less effective<sup>42</sup>. The recently completed Public Expenditure Analysis studies for education and health indicate that there are significant inefficiencies in the two procurement sectors that significantly affect the quality of expenditure. Future improvements should also be targeted to include acquisitions made by public companies. If the benefits of developing an efficient, transparent and competitive procurement system produced savings of 15 per cent of the total value of expenditure, it could increase fiscal space by around 1.32 per cent of GDP.

**107. Finally, there are opportunities for significant improvements in the efficiency of public investment processes.** The Public Investment Management Reform Plan, which is being prepared with the help of the World Bank, establishes that the efficiency of public investment in Mozambique is lower than the average of the Low-Income Countries (PBR). Despite high levels of investment, population access to the standard infrastructure of education, health, water, electricity, or transportation is lower than in peer countries with a comparable stock of public capital per capita<sup>43</sup>. According to the standard international BdM scores the efficiency of public investment is 41% lower than it could be, and places Mozambique far from the most efficient countries with comparable levels of public capital per capita. This is also a potentially high source of savings, considering that the average public investment in Mozambique over the last 5 years is more than 15% of GDP. Achieving a moderate increase in the efficiency of investment processes, additional resources could be made available at around 3% of GDP.

#### 4.2.3 Opportunities to Increase the Fiscal Space Eliminating Losses from Public Enterprises

108. The Mozambican Government owns fourteen Public Companies (EP) and holds shares in more than one hundred private companies. The fourteen public companies are 100% owned by the State and governed by Law 6/2012 (of Public Companies) and operate mainly in the services sector (communications, transport infrastructure, electricity or irrigation). According to the information published in 2015 by the National Institute of State Participation Management (IGEPE), the government holds shareholdings - usually in majority - in at least 114 Undertakings which are governed by private law and the same legislation as private companies. It is estimated that, in addition,

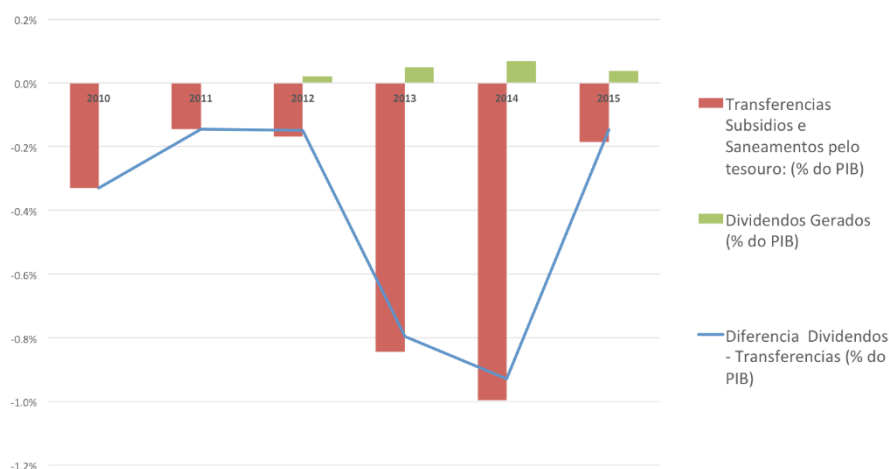
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<sup>42</sup> PEFA Evaluation of Public Finance Management, 2015, Mozambique, Final Report, Volume II.

<sup>43</sup> World Bank, Public Investment Management Reform Plan - Mozambique, Working Draft, Sept 2016.

the State holds a stake in at least 112 private companies, but through indirect participation or subsidiary agreements<sup>44</sup>.

Figure 17 - Net Transfers to Public Enterprises as% of GDP



Source DNT-MEF. Authors' calculations

**109. The information needed to analyse the performance and financial situation of public undertakings is difficult to access.** There is no in-depth information on the level of contingent liabilities that Mozambique accumulates from the management of public and investee companies. Most companies present their audited financial statements to the central government on an annual basis, directly to the National Treasury Directorate of the MEF or to IGEPE, except for public enterprises created by other public companies, which inform the 'parent company', but not IGEPE or MEF. In the case of companies whose supervision is managed by IGEPE, little information is available on the balance sheet of public companies, since the General State Account (CGE) only includes cash balances of these public companies, but it does not include information on their balance sheet<sup>45</sup>, which makes it difficult to analyse the budgetary risks they represent. Some of these companies (Electricidade de Moçambique, Empresa Nacional de Hidrocarbonetos, Caminhos de Ferro de Moçambique) make their financial statements available online. In 2014, only the liabilities of these three companies accounted for 10% of GDP.

**110. The performance of public enterprises in Mozambique has been poor, and the losses generated consume considerable fiscal space.** These Public Companies generate cash flows that are recorded by the Treasury. They generate revenues - which in the budget are accounted for as Capital Revenue - and receive transfers through the budget in two ways: business subsidies and subsidies to prices (according to the program contract). There is one more form of financing that originates in the Budget: the reorganization of the credits that the companies have with the Treasury in the scope of the Retrocession Agreements<sup>46</sup>. Figure 17 shows transfers and revenues generated by the 14 public companies, as well as the net difference of these flows, which results in an annual expenditure that is reflected in the budget. The contract-program, obligations and efficiencies of these companies must

<sup>44</sup> World Bank, Mozambique Economic Update (MEU) 2016.

<sup>45</sup> PEFA Evaluation of Public Finance Management, 2015, Mozambique, Final Report, Volume II.

<sup>46</sup> During the interview with DNT staff, it was learned that companies benefiting from retrocession agreements, by providing the Treasury with information on the follow-up of repayments, is not disaggregated by a retrocession agreement. It is the DNT that reorganizes the data to match the contracts. This is an indicator of the great possibilities to improve the management of the contracts and of the debt contracted by the companies.

be evaluated and fulfilled, clearly reflecting the services they have to offer to the population. The difference between revenue generated and treasury transfers in the period considered (2010-2015) was always negative. The fiscal space consumed by the losses of these companies in this period totalled 2.74% of GDP, equivalent to USD 375.5 million.

Figure 18 - Net transfers to the selected group of companies in% of GDP



Source DNT-MEF. Authors' calculations.

**111. All the above also applies to investee companies, with the additional difficulty that the number of companies is ten times greater.** For this evaluation it was not possible to have a complete picture of the income and losses of the investee companies. Figure 18 shows the revenues and expenses of a selected group of investees with information provided by IGEPE. For the purposes of this study, the 11 participated companies were selected, where the value of the State's shareholdings (through Treasury and IGEPE) is the largest. This covers more than 80% of the value of the shares<sup>47</sup>. As in the previous case, the difference between revenue and transfers of the treasury over the period considered (2010-2015) was always negative, with total cumulative losses of 0.76% of GDP (equivalent to 75.5 million USD).

**112. The use of the loan by public and joint ventures is a major contributor to the considerable fiscal risk to the economy.** Mozambique has used public companies to expand its investment program to contract non-concessional debts, state guarantees and other financing such as public-private partnerships (PPPs). The financing of public companies is usually made through loans to the Government of Mozambique, which is then given by the MEF to public companies (Retrocession Agreements). The 2014 ADP has determined that in 2012, public enterprise loans with the MEF accounted for 7.5% of GDP<sup>48</sup>.

**113. The government lacks a unified framework to monitor performance and oversee the contingent risk of these companies.** The PEFA assessment for 2016 suggests that budgetary risks (guarantees,

<sup>47</sup> Revenues were generated mainly by the Cahora Bassa Hydroelectric Plant (0.3% of GDP between 2012 and 2014). Participations in a commercial bank (Millennium BIM) generated revenues corresponding to 0.3% of GDP in 2012 and 2013. The transfers in 2010 were the result of the reorganization of a debt that TDM had to the Treasury following a Retrocession Agreement. The other transfers are addressed to Petromoc as fuel subsidies.

<sup>48</sup> World Bank, 'Public Expenditure Analysis', Mozambique, World Bank, 2014.

PPPs, long-term contracts for the construction of infrastructures and liabilities by state-owned and state-owned enterprises) were growing rapidly. The large public debt crisis generated by three such companies, the poor overall performance of companies and the fragile economic outlook underline the importance of prioritizing efforts to strengthen the management of fiscal risks in the activities of public and investee companies. In the event of bankruptcies, the liabilities of these companies are ultimately financed by the State, since most of them are providing essential public services, it is unlikely that the government will fail them<sup>49</sup>.

**114. To improve the management of its actions, the Government of Mozambique is preparing a law on the State Business Sector.** The main purposes of the new legislation are to eliminate the lack of clarity on the nature of the public company, the express determination of the applicable law, define the shareholder role of the State; define the State-Owned Company and indicate the way it is created; define and clarify assumptions for the creation of the public company; indicate the General Assembly as a deliberative body on the strategic issues of activity of the public company. The draft law establishes that EPs are created by decree of the Council of Ministers and to carry out economic activities and (or) provide strategic public services structuring the national economy and establishes that the Companies are incorporated under the terms of the Commercial Code in which the State or any other public entity holds a social participation. The State Business Sector must have a program contract that must guarantee the coverage of operating and investment expenses that, by their nature, should be borne by the State.

**115. The new legislation attempts to eliminate conflicts of interest and regulate other situations to limit the state risk of these operations.** State investments in for-profit companies are dispersed across several sectors without a specific strategy to guide investment decisions. In some cases, public enterprises provide services on the market and exercise a regulatory function, presenting a conflict of interest. Public enterprises generally carry out quasi-fiscal activities by providing services below market prices (which are partially subsidized by the State) or by investments in infrastructure such as electrification, railways or roads whose viability is doubtful. In addition, the portfolio is dispersed and a clear mapping of the entities and their relationships is not available, which makes it difficult to assess the State's exposure to fiscal risk.

**116. The new legislation introduces provisions to improve the control of public undertakings, but leaves important gaps in ensuring competent management.** Currently, the National Treasury Directorate unit in the MEF (responsible for supervising the 14 public companies) provides technical support, but only to a limited extent, and there is no entity with supervisory responsibilities to manage the tax risks of the 114 of the 112 companies in which the State holds an indirect stake. IGEPE's role is focused on representing the interests of the State as a shareholder, rather than having a mandate to manage fiscal risks. The draft law is based on the control of the state of public companies and establishes the powers of the General Assembly, the Board of Directors and the Fiscal Council. But the draft new legislation does not explain how to eliminate existing gaps and the fragmentation of criteria in the supervision of the management of public companies as well as of the investees.

**117. The government should consider additional recommendations to eliminate fragmentation in the oversight of public enterprises and the development of critical technical capacity to improve management.** In addition to the measures included in the Draft Law, the World Bank proposes to consolidate a single Technical Supervisory Unit with a mandate to cover both public and private companies<sup>50</sup>. This type of solution responds to good regional practice and deserves consideration to

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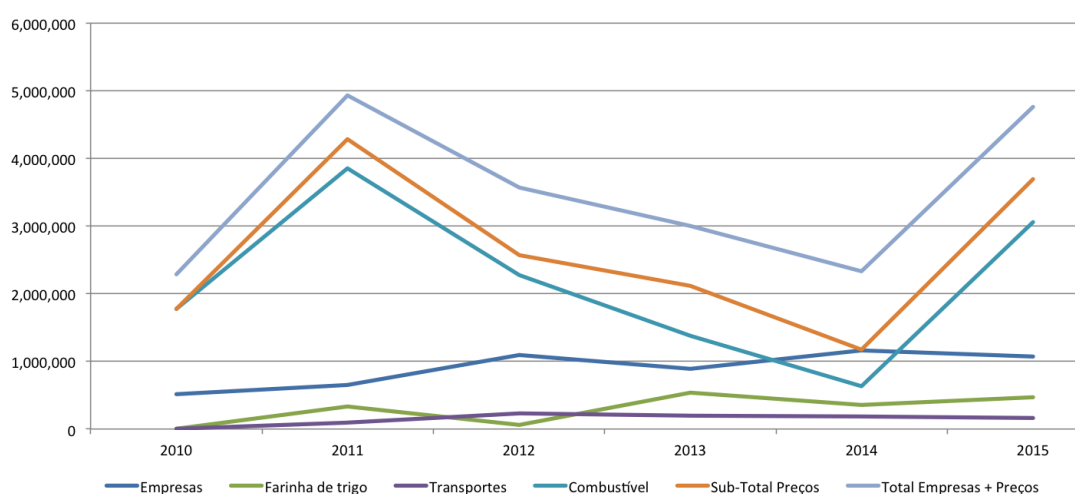
<sup>49</sup> PEFA Evaluation of Public Finance Management, 2015, Mozambique, Final Report, Volume II.

<sup>50</sup> World Bank, Mozambique Economic Update (MEU) 2017.

eliminate defects in the implementation of existing legislation<sup>51</sup>. The technical capacity of this unit should be strengthened to develop comprehensive criteria for fiscal risk assessment and accountability of government assets and liabilities in accordance with international standards. The unit should develop a consistent financial information base to support decision-making and strengthen its public disclosure by presenting consolidated information on government investment in public enterprises and their financial position to be included in the State's annual accounts. The World Bank proposes that the degree of supervision and control exercised by the unit be guided by the financial viability of an entity and its potential exposure to fiscal risk. Enhanced supervisory arrangements would be applied to entities experiencing financial vulnerabilities, while greater autonomy can be attributed to entities that are well executed.

#### 4.2.4 Opportunities to Increase the Fiscal Space Reducing Subsidies

Figure 19 - Subsidies for public enterprises and prices (in MZN x 1000)



Source DNT-MEF. Authors' calculations.

**118. The review of expenditure on subsidies could also release considerable fiscal space.** The Mozambican government has a set of subsidies that include public enterprises or prices, such as wheat flour, fuel and public transport. Figure 19 summarizes the evolution of the total volume of government subsidy expenditures (excluding the retrocession arrangements) and the main individual components of price subsidies. The fuel price subsidies for petrol stations include the subsidy to Petromoc. Table 10 shows the relative values of these subsidies as a percentage of the State Budget and GDP. The average expenditure of subsidies between 2010 and 2015 was 3.48 billion meticaïs per year, which is equivalent to almost 1% of GDP per year, or 2.5% of the State Budget. These are significant figures, especially when seeking to accumulate savings from different individual sources.

**119. The fuel subsidy is the main element to be considered in efforts to rationalize this type of expenditure.** The total volume of subsidies in the period considered was 13 billion meticaïs, which represents an annual average of 2.16 billion meticaïs. This annual expenditure is equivalent to 1.67% of the total expenditure of the State's Annual Budget. Due to these subsidies, fuel prices in Mozambique have been artificially below the actual market price and those practiced in neighbouring

<sup>51</sup> The law prescribes that the CGE summarizes the information presented by the public companies to the MEF, but in practice, this information is not sent on a regular basis. The National Social Security Institute does not inform the MEF or IGEPE, and the IMF 2014 report informs that it has not had audited accounts of these companies since 2009. IGEPE produces a consolidated report on the position of the affiliated companies, but this information is not consolidated by the MEF in an annual report on aggregate tax risk.

countries. The subsidy was introduced to compensate gas companies for the difference between regulated prices for the sale of goods and the import prices of these products. International experience indicates that, in addition to being too expensive, fuel subsidy does not effectively protect the poorest, it is often misdirected and disproportionately benefiting wealthier families<sup>52</sup>. The fossil fuel subsidy also offers wrong incentives to the market: despite negative environmental impacts, subsidies artificially increase consumption incentives rather than economising.

**120. The government's announcement of phase-out of this subsidy in 2017 is an important step in the right direction.** The government announced March 2017 measure to phase out the subsidy is a decision that will surely have political costs due to rising fuel prices, but it is an important step in the process of eliminating unnecessary expenses. The government also took the decision not to withdraw the subsidies to public passenger carriers. This is also a sound decision since the transport component is very marginal in the total volume of this expenditure and, in this way, the government can significantly reduce the social impact of the measures taken.

Table 10: Summary of subsidies to public enterprises and prices as% of GDP and SO

Subsidies ( % do PIB)	2010	2011	2012	2013	2014	2015
Companies	0.15	0.18	0.27	0.21	0.25	0.23
Prices						
Wheat flour	0.00	0.09	0.01	0.12	0.08	0.10
Transports	0.00	0.03	0.06	0.05	0.04	0.04
Fuel	0.51	1.07	0.57	0.32	0.14	0.65
<b>Sub-Total Prices</b>	0.51	1.19	0.64	0.49	0.25	0.79
<b>Total companies + Prices</b>	<b>0.66</b>	<b>1.37</b>	<b>0.91</b>	<b>0.70</b>	<b>0.50</b>	<b>1.02</b>
Subsidies ( % do SB)	2010	2011	2012	2013	2014	2015
Companies	0.49	0.54	0.83	0.56	0.60	0.67
Prices						
Wheat flour	0.00	0.28	0.05	0.34	0.18	0.30
Transports	0.00	0.08	0.17	0.12	0.09	0.10
Fuel	1.68	3.24	1.73	0.87	0.33	1.92
<b>Sub-Total Prices</b>	1.68	3.60	1.95	1.33	0.60	2.33
<b>Total Companies + Prices</b>	<b>2.17</b>	<b>4.14</b>	<b>2.78</b>	<b>1.89</b>	<b>1.20</b>	<b>3.00</b>

Source: DNT-MEF. Authors' calculations.

Estimates of the different sources of 'efficiency gains' previously analysed should be correctly calculated, as these reforms could achieve significant results. Previously provided estimates are simply guiding, based on existing studies and very general comparisons, and should be rigorously reviewed to set goals by area of improvement. However, in all cases, it was chosen to present conservative estimates, which should be well below the achievable targets in each intervention area. As anticipated, the achievement of visible results at the macro level only happens through the implementation of a series of measures and interventions that individually produce results at the micro level. Table 11 provides a summary of the minimum 'efficiency' estimates that could be achieved in each area. The volume of fiscal space that these interventions could jointly release is highly significant since the estimated total amount is 13.5% of GDP, which represents half of total public revenue in its best year (2015). For this reason, it is recommended to focus attention on the design

<sup>52</sup> IMF and BOM data indicate that only 1/8 of fossil fuel subsidies across the developing world benefit the poorest 20% of the population and that subsidies benefit 20% of the richest class, which consumes 2/3 of total subsidies. For more information, see Stratta, N "Strengthening Coherence between the Effective Development Cooperation and Financing for Development Agendas in Asia-Pacific" A Background Paper for the Regional Workshop 26-27, March 2015: Makati City, the Philippines.

and financing of a Public Expenditure Efficiency Improvement Program, which could achieve a good part of these results within 3-5 years.

Table 11: Estimates of the fiscal space to be released by the analysed measures that can be quantified

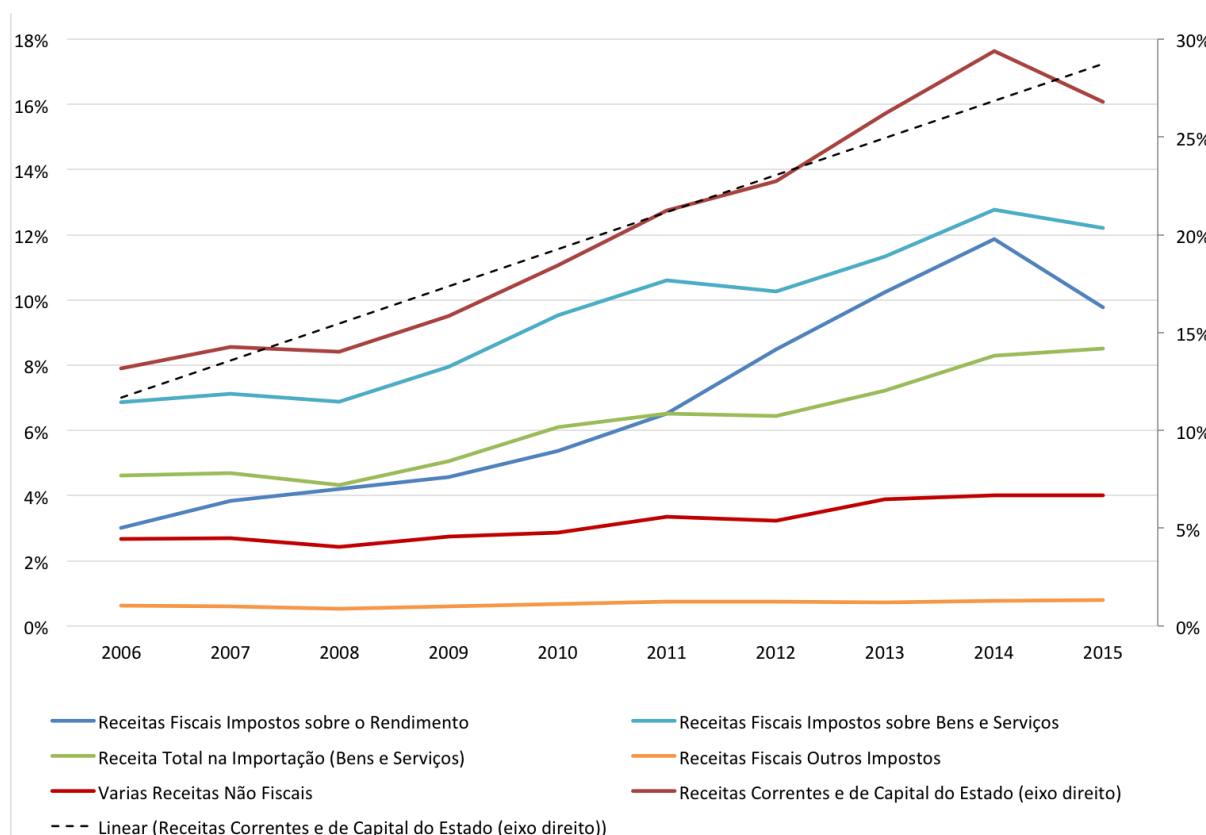
Area of Efficiency Improvement	Tax Space That Could Be Released (% of GDP)
Increased revenue collection in richer cities	3%
Reducing the cost / GDP of children's enrolment	2.4%
Reduction of the cost / GDP of health services	1.5%
Improvements to the public procurement system	1.3
Public Investment	3%
Losses of public companies (reduction of 50%)	1.4%
Losses of investee companies (reduction of 50%)	0.4%
Subsidy reduction (reduction of 50%)	0.5%
<b>Estimated Total Tax Space</b>	<b>13.5%</b>

Source: Authors' calculations.

## 4.3 Evaluation of the main public flows

### 4.3.1 Public Revenue

Figure 20 - State revenue as% of GDP (by type) - Right axis: Total Revenue trend line (as a% of GDP)



Source: Mozambican Tax Authority, MEF, Authors' Calculation

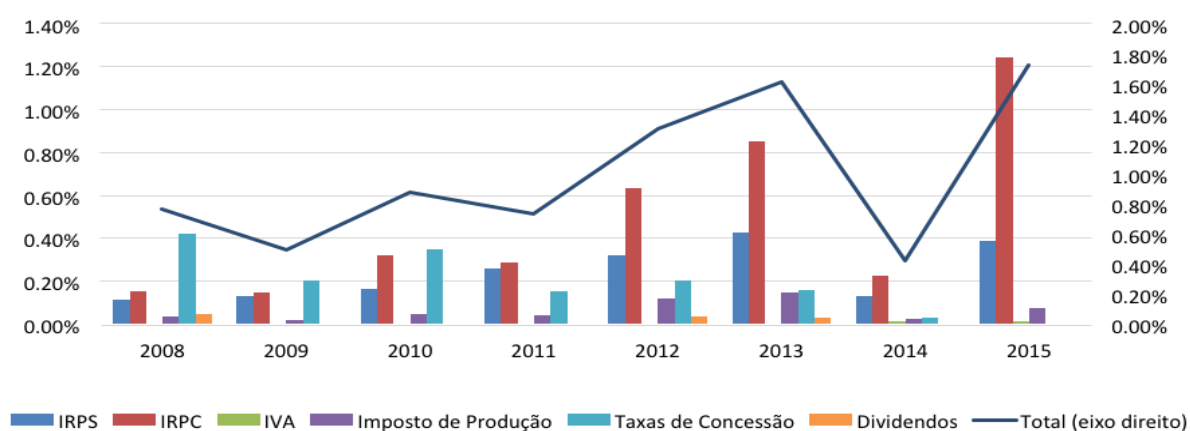


**121. During the period considered in the AFD, there was a significant increase in total revenues over GDP.** During the period under review, the Mozambican economy grew, on average, at rates above 7%. This growth was accompanied by a sustained increase in the contribution of domestic revenues to total government funding, which grew strongly from 50% of GDP in 2006 to 76.9% in 2015. The contribution of revenues to total public expenditure also increased significantly in this period, from 57.4% in 2006 to 82.3% in 2015<sup>53</sup>. Progress in revenue growth was a critical breakthrough in long-term sustainability as it was accompanied by the gradual decrease in external donation contributions in the budget and an increase in the external credit component.

#### Primary sources of revenue and trend analysis

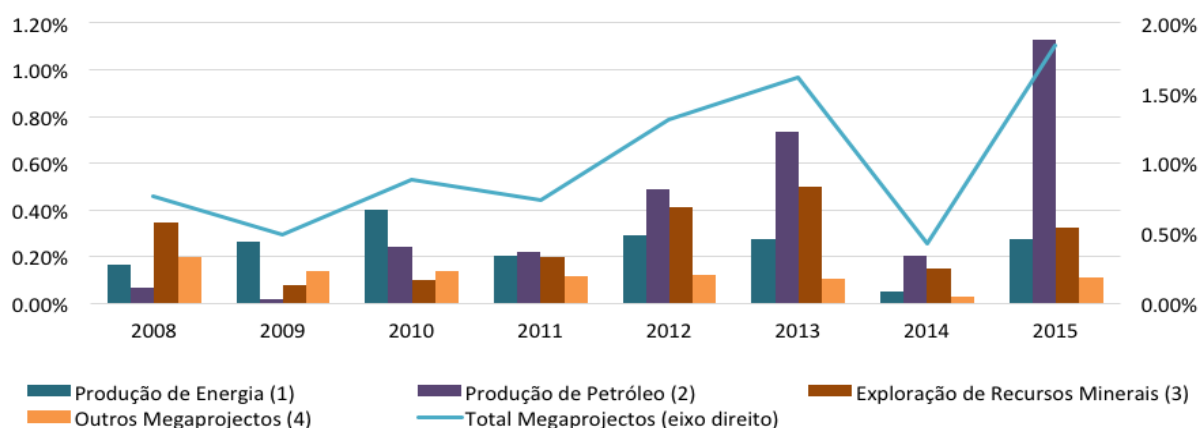
122. Three main sources contributed to revenue growth in this period: VAT, IRPS and IRPC. Figure 20 shows the contribution of the main components of revenue collection and its evolution. It can be observed that the growth of the State revenue is linked to the growth of three fundamental sources: taxes on Goods and Services (especially VAT), taxes on Income (IRPS and IRPC) and revenues from Imports of Goods and Services. Statistical data in Annex II highlight the following trends: (i) Value Added Tax (VAT), which was one of the fastest growing, since in 2006 it contributed to 4.4% of GDP, and in 2015 it reached 8.7%; (ii) the Personal Income Tax (IRPS), which had a similar evolution, doubling its value from 1.8% of GDP in 2006 to 3.6% in 2015; (iii) Corporate Income Tax (IRPC), which grew even more significantly: from 1.1% of GDP in 2006 to 6.1% of GDP in 2015. During the period also the composition of revenue changed, showing that the relative weight of income taxes began to be higher than that of revenue on goods and services as of 2011.

See complete statistical series on these dates in Annex II.



<sup>53</sup> See complete statistical series on these data in Annex II.

Figure 22 - Tax contribution of megaprojects by area of activity (% of GDP)



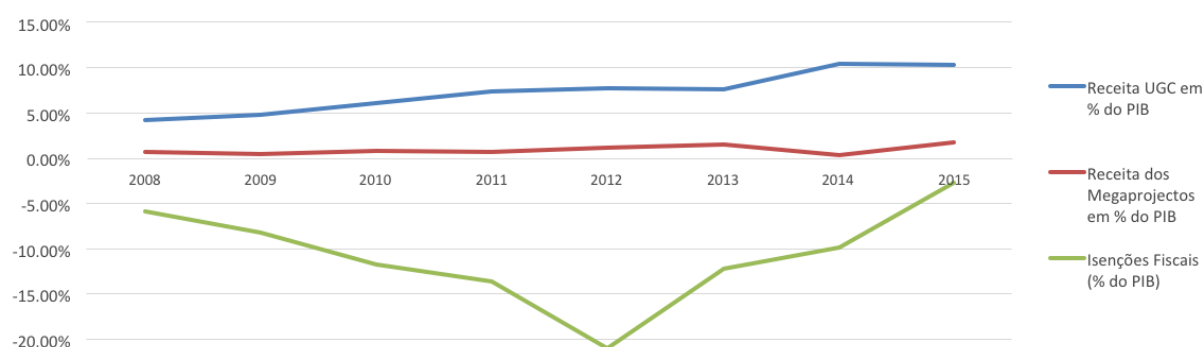
Source: Mozambican Tax Authority, MEF, Authors' Calculation

**123. The growth of corporate and individual income tax (IRPC and IRPS) is a promising element.** The widening of the tax base in terms of taxes on property and income can allow progressive direct taxation modulated on income levels and possibly on a sectoral basis, replacing the indirect tax on consumption, which is less fair. In this process, we highlight the creation of the Simplified Tax for Small Taxpayers (ISPC), which was introduced in 2009 as a measure to favour the transition to the formal economy of agents active in the informal economy, but which has not yet performed its contribution as a percentage of GDP (0.03%) continuous little relevant.

**124. The overall contribution of megaprojects to the increase in tax revenue observed during the period was significant in some areas.** Figure 21 shows the contribution of megaprojects by type of revenue. In 2015, the total contribution of megaprojects to the IRPC was 1.24% of GDP, which represents 21% of the total value of IRPC. The contribution of megaprojects to IRPC was only 0.15% of GDP in 2006. For IRPS, the contribution of these projects is lower: 0.39% of GDP in 2015, which represents only 10.1% of the total amount collected by this tax in the same year. Figure 22 shows the total revenue of megaprojects by main activity sectors: Energy, Oil, Mining and Others. The same figure also shows that the relative contribution of the Mining projects is decreasing in relative terms and relatively small in the total volume.

**125. The analysis of the relative weight of large taxpayers in revenue leaves some doubt about the distribution of the tax burden.** Figure 23 shows the fiscal contribution of large taxpayers and megaprojects as a percentage of GDP. In Mozambique, taxpayers are classified by volume of contribution and not by volume of enterprise or business. This means that some megaprojects - which receive extensive tax benefits - do not appear in the category of large taxpayers. In the group of large taxpayers, the most important is the financial sector. The figure also shows the volume of tax exemptions granted in the same period in accordance with the investment law. The relative weight of the exemptions granted is significant, reaching more than 20% of GDP in 2012. The OECD argues that the efficiency and effectiveness of these exemptions should be further investigated. Since the cost is so high, it would be appropriate to assess whether the social and economic benefits of the projects balanced the loss of fiscal resources.

Figure 23 - Contributions from large taxpayers and megaprojects; Volume of exemptions granted (% of GDP)



Source: Mozambican Tax Authority, MEF Authors' calculations

**126. The system for attracting foreign investment is based on the provision of important tax benefits whose usefulness should be carefully analysed.** The Foreign Direct Investment (FDI) promotion system is heavily based on the provision of significant tax benefits to attract investment. The system offers important exceptions for the realization of megaprojects in the extractive industries and for investments in the Special Economic Zones (ZEE) and Industrial Free Zones (ZFI). These benefits fundamentally seek to compensate Mozambique's low international competitiveness analysed in Chapter 5 of this AFD. The FDI analysis presented in the same chapter recommends a review of the cost-effectiveness of the results obtained with the tax benefits granted and the performance of these incentives by comparing them with possible alternative schemes.

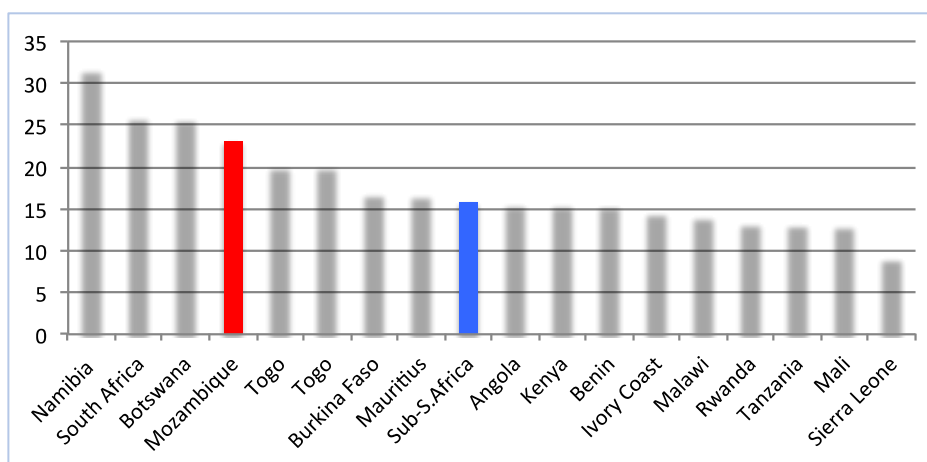
**127. There is potential for future revenue growth based on taxes on the production of oil and mineral resources.** In 2013 and 2014, the government began receiving funds in large amounts of unexpected IRPCs due to capital gains from the sale of shares in the investments in natural gas exploration in the Rovuma Basin, which contributed to the performance of TA in recent years. External factors related to international commodity prices analysed in Section 2.3 have negatively affected the expected expansion of taxes on oil and mining production, but remain an element to be considered in projecting the future development of revenue.

Performance of the expansion strategy of primary revenue sources

**128. The performance of the Mozambican Tax Authority (TA) in the period analysed has been very high.** In 2006, at the beginning of the period under review in this evaluation, the government created the TA, integrating the Customs and Internal Tax Directorates. This is a semi-autonomous entity under the Ministry of Economy and Finance. A group of development partners has been supporting the process of institutional reform and ongoing modernization of the tax administration in Mozambique through a Common Fund (CF) in support of tax reforms. TA has been successful in increasing annual revenue collection in Mozambique and is considered in the PEFA assessment as one of the most efficient tax administrations in Sub-Saharan Africa<sup>54</sup>. The data in Figure 24 indicate the relative position of Mozambique compared to countries in the region, and that the value of fiscal revenue as% of GDP (23.12%) is well above the average in Sub-Saharan Africa (15.83%).

<sup>54</sup> PEFA Evaluation of Public Finance Management, 2015, Mozambique, Final Report, Volume II.

Figure 24 - Fiscal Revenue as% of GDP in Sub-Saharan African Countries (2013)



Source: World Bank

#### Next Steps: Areas that need more attention

**129. TA can still achieve significant improvements in the performance of its core activities.** The diagnosis of the tax administration carried out following the TADAT methodology in 2015 points to several operational domains of TA that require significant improvements. The diagnosis identifies three main areas for focusing on the institution's capacity development in the short term: (i) improving the availability and use of procedural manuals and the harmonized and systematic application of rules; (ii) develop a new AT organizational structure with a clear functional specification that eliminates current fragmentation; (iii) to develop adequate procedures for aggregating and managing data in the different operational areas, and to implement them systematically, eliminating delays in the e-Taxation project and lack of maintenance of the Interim Revenue Collection System<sup>55</sup>.

**130. The development of the Tax Authority's capacity is a priority area to maintain revenue dynamics in the short term.** In the scenario of scarcity of resources previously analysed, the short-term priority is to implement measures to improve and maintain the existing capacity of revenue collection. The PEFA evaluation and the recent evaluation of support for Tax Reform prioritize the improvement of TA capacity and suggest that the good performance of public revenue in this period<sup>56</sup> is masking important institutional weaknesses that must be strengthened<sup>57</sup>. The PEFP establishes for the period 2016-2019 the following priorities to improve the performance of the Tax Administration: (i) terminate the registration of taxpayers still incomplete and with inaccurate information; (ii) develop an overall risk-taking strategy; (iii) to develop automatic data crossing systems to support supervision; (iv) design measures to improve the delivery of tax returns by taxable persons; and (v) introduce systems that allow the payment of taxes using electronic means. The evaluations indicate other areas that could also merit attention, for example:

<sup>55</sup> TADAT (2015) Performance Assessment Report, Republic of Mozambique, Pilot Assessment VII, Lemgruber Andrea et alii, June 2015.

<sup>56</sup> The Tax Authority was able to achieve the PQG objective of increasing revenue by 0.5% faster than GDP growth, which is considered a great success for Mozambique.

<sup>57</sup> (Gerster & Stella, 2015).

- Combine the geographical expansion of AT collection points with the economic potential of expansion regions and priorities according to a geographical expansion plan;
- Develop adequate systems for forecasting and forecasting the inspection and audit processes, setting clear targets and necessary resources;
- Develop economic projections to estimate the impact of the changes introduced by the legislation and the revision of regulations made to increase compliance with tax obligations, especially the improvement of (simpler) tax collection processes;
- Improve control systems and debt collection, an area where performance is not satisfactory, according to the PEFA assessment analysis.

**131. Availability limitations and information processing criteria affect the quality of the analysis and the projections of tax revenues.** The Management Information System on taxpayers in use is a limitation for the analysis of tax revenues. The data are disaggregated by type of tax, but little breakdown can be made with respect to sectors and in terms of size of taxpayers. This limits the possibility of basing the revenue forecasts to be collected on the expected performances of various economic sectors or the possibility of formulating a tax policy that offers incentives to specific strategic sectors. There are areas where the criteria used create confusion. For example, the classification of the taxpayer type (large, normal, small) is not based on the size of the business, but on the supposed contribution. This implies that the so-called megaprojects may not be part of the large taxpayer group because of the tax exemptions granted to them, or because they are in the initial stage of the investment and therefore are not generating taxable profit.

**132. While increasing the capacity and quality of TA management is a priority, it is difficult to draw conclusions on sustainability.** The model that allowed sustained growth in revenue over the last decade could be reaching saturation level. The data in Figure 24 show that, in comparative terms, Mozambique is already at the level of the most developed economies in the region, with little room for expansion of the revenue ratio as% of GDP. In addition, there is a fiscal concentration problem: in 2011, about 80% of tax revenues, excluding import and export taxes, were collected in the Maputo area, and by 2014 the situation had not changed<sup>58</sup>. This degree of concentration of fiscal pressure also raises concerns about the growth of future tax collection and its sustainability. A more homogenous growth of the economy (by regions and sectors) would significantly improve the distribution of the tax burden, but probably very little the level of the fiscal ratio.

**133. In addition to the above improvements, there are other ways of expanding tax collection that have not yet been explored,** such as: (i) the possibility of introducing greater progressiveness and 'poor' orientation in the current tax system; (ii) continue efforts to increase the taxpayer base, with greater incentives for the expansion of the formal sector of the economy; (iii) progressively reduce illicit flows and tax evasion (see Section 4.4.4)

#### 4.3.2 External Debt

**134. Until the crisis, Mozambique was making significant progress on the road to developing an external debt management system.** The country had done a long-term job to develop a robust public debt management process adapted to the dynamics of the Mozambican economy. VFP places improved control and sustainability of public debt, both domestic and external, as one of the main achievements of the Public Finance Management reforms in the decade 2000-2009 and establishes as Strategic Objective 3: Improving prudent management and management assets and holdings and the

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<sup>58</sup> (Gerster & Stella, 2015).

state's business sector, as well as public debt and social security and social security, all of which are part of SISTAFE. To this end, the VFP defined the following priority actions:

- Establishment of the Debt Management Committee;
- Establishment and operationalization of the Project Selection and Coordination Committee;
- Annual and semi-annual preparation of the debt sustainability analysis framework;
- Definition and implementation of capital market development measures;
- Annual review of the state of the debt portfolio and the capital market, internal and external.

**135. The reforms established in the VFP were being implemented successfully and allowed for relative optimism about future progress in debt management.** The Public Finance Strategic Plan 2016-2019 provides a satisfactory review of the implementation of these actions between 2012 and 2015, noting that the result of the sustainability analysis revealed that all indicators were below their respective limits. The PEFP highlighted the following progress:<sup>59</sup>

- Approval and publication of the Medium-Term Strategy for Public Debt Management 2015-2018, which defines the guidelines for contracting the debt, as well as the mechanisms to be adopted to improve its management and annual publication of reports;
- The improvement of public debt management and planning instruments, considering the observance of good international practices, with a view to promoting fiscal transparency and good governance, (publication of quarterly and annual reports on public debt, sustainability analysis, as well as preparation of Internal Indebtedness Plans.
- sustainability, as well as elaboration of Internal Indebtedness Plans.

**136. The PEFP work plan was already focused on resolving technical issues related to emerging debt management issues.** The proposed PEF (Public Debt Sustainability) Objective F planning already recognizes the negative impact of debt generated by state-owned enterprises using concessional credits and with sovereign guarantees for funds mobilized in capital markets<sup>60</sup>, and defines the following priority activities:

- *Restructure Public Debt* with a focus on commercial debt, with the aim of extending its maturity period and renegotiating better terms;
- *Improve the Public Debt Database*, especially the system for recording, monitoring, reconciling and analysing sustainability and producing reports;
- *Improve Debt Procurement Procedures and Criteria*, improvements in the legal framework for the issuance of guarantees by the government, and measures to improve transparency in public debt management including the publication of management and risk reports;
- *Strengthen the capacity of the Fiscal Risk Unit* which deals with the fiscal risks stemming from the ESS, including PPPs;
- *Revise the Public Companies Law* to extend its coverage, strengthening aspects of supervision and reporting to companies in which the State has holdings.

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<sup>59</sup> Present value of external debt on GDP (40%), Exports (150%) and Revenues (250%); and Debt Service on Exports (20%) and Revenues (30%). See more Strategic Public Finance Plan 2016-2019.

<sup>60</sup> The country registered a rise in external indebtedness because of its mobilization to finance the development of infrastructure and security in the country. Even though concessional loans were privileged, the State also issued sovereign guarantees for funds mobilized in the capital market with a view to respond to the risks to which the country is exposed, including, among others, piracy, looting of fish and protection of fishing vessels, research and exploitation of natural resources, logistics and naval maintenance', PEFP, pp. 47.

**137. Despite some dangerous deviations in the use of public debt from state-owned enterprises, the situation appeared to be under control.** The PEFP recognizes that the stock of debt had risen from 36.9% of GDP in 2012 to an uncomfortable 63.8% in 2015, mainly due to the increase in concessional loans for financing infrastructure projects and the debt generated by the PEs. The PEFP proposes (i) to improve the financial protection of PEs in order to prevent fiscal risk in their actions, (ii) to make it obligatory to submit proposals for the indebtedness of PEs for authorization purposes to the Minister of Finance; (iii) publish, on a yearly basis, reports on the financial performance of PEs, and extend to state-owned companies and state-owned enterprises in private companies, including publication of information on direct and indirect financial support, including State debt relief to companies of the public sector. Faced with a decline in exports and foreign investment, inflationary pressures and an accelerated depreciation of the metical, the government began to take drastic measures to reduce public spending, and requested a USD 286 million credit from the IMF Stand-by Facility (SCF). If implemented successfully, this package of measures could have contributed to solving the problem in the short term, but the appearance in 2016 of more information on debts secretly contracted by some public companies as early as 2013 (summarized in Box 3) triggered an economic crisis difficult to control.

**Box 3: The dimensions of the debt problem of state-owned or state-owned enterprises<sup>61</sup>**

A parliamentary inquiry has examined the debt contracted by three different private companies of \$ 2 billion with agreements offering government guarantees on loans that were issued without Parliament's authorization. The debt crisis was generated by three state-owned companies:

- **EMATUM** - Mozambican Tuna Fishing Company. Established in August 2013, it had the function of coastal protection and tuna fishing. The loan was issued in Eurobonds for a total of USD 850 million.
- **Proindicus**. Company established in March 2013 to establish an integrated system of aviation, space, marine, lacustrine, fluvial and terrestrial security. The loan was issued by Credit Swiss of Eurobonds in the amount of 622 million USD. The funds were intended to provide integrated security services (air, sea and land) to gas companies, ships and other maritime traffic, as well as to provide search and rescue services.
- **MAM** - Mozambique Assets Management. Company established in April 2014 for the construction and maintenance of ships. The loan was an issue managed by the VTB (Russian State Bank) of 535 million USD. The purpose of the loan was to build / install shipyards in the ports of Pemba and Maputo to provide maintenance and logistics services to Proindicus and other major operators.

In August 2013 the French press reported on the purchase of fishing boats by the Mozambican Government<sup>62</sup> to a French shipyard. The news has an impact on Mozambique and, in September 2013, the government admits issuing guarantees for EMATUM and assumes part of the debt (initially 350 million USD, then 500 million). To remedy the illegality, the government included in the 2014 budget law a guarantee issue of USD 500 million, leaving USD 350 million of debt in EMATUM. By 2015 EMATUM's debt package has to be renegotiated and, to that end, the government has to publicly disclose the existence of all debts. This is how in 2016 the debt of EMATUM is assumed by the government, and other debts come to light. The parliamentary inquiry revealed several worrying situations:

- **Debt Destination**. Part of the operation financed defence expenditure in an extra-budgetary way. For example, the fisheries component of EMATUM has USD 91 million, but the coastal protection component of USD 750 million has been used for armaments. The arms purchased by Proindicus were handed over to the Ministry of Defence, the Interior Ministry and the company itself.
- **Legality of the procedures used**. Law No. 6/2012 establishes the obligation of the PE to be submitted to the Ministry of Finance for its indebtedness proposals for authorization purposes. In addition, EPs are obliged by the same law to publish their Audited Annual Reports and Accounts, in one of the country's largest circulation newspapers and in the Boletim da República. Although the objectives of Proindicus coincide with those of the

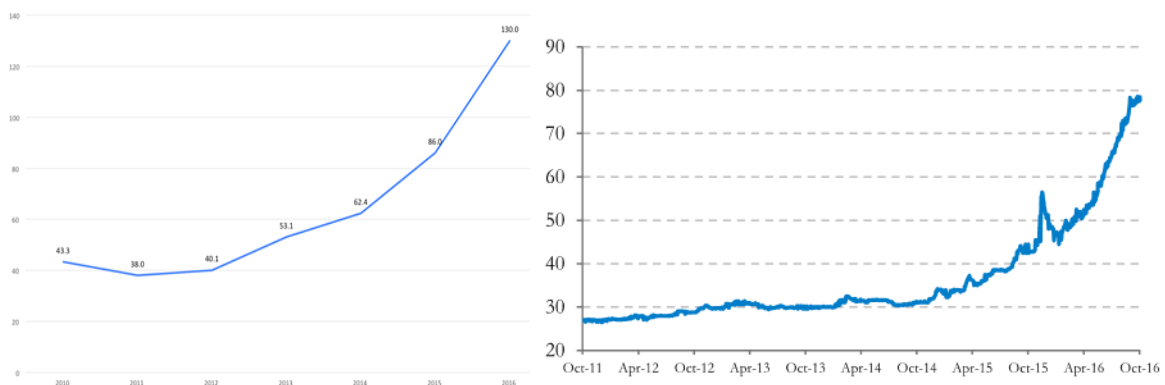
<sup>61</sup> The text of this Box summarizes some of the points discussed more fully in the Report of the Parliamentary Inquiry Commission to Investigate the Public Debt Situation of 30 November 2016 and the publishable information from the international and independent audit report commissioned by the MEF and carried out by the company Kroll at the end of June 2017

<sup>62</sup> The French President and the Mozambican President visited together the Normandy shipyard.

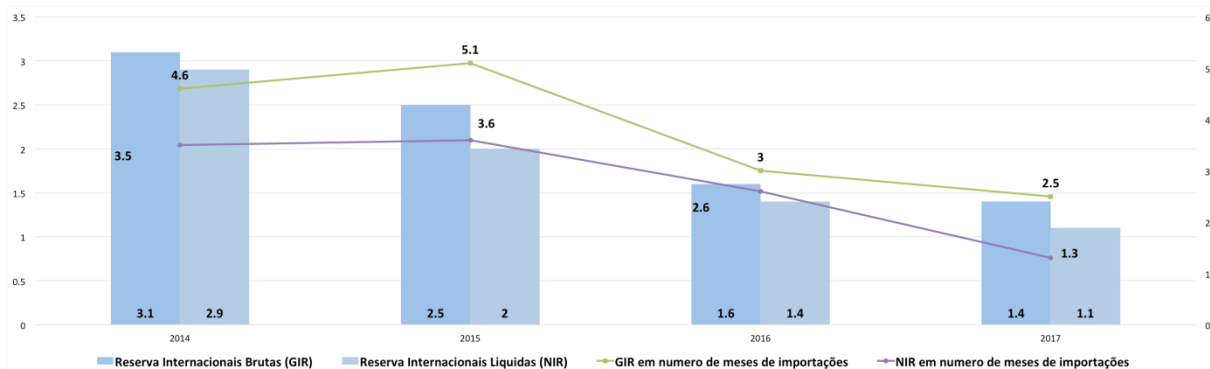
military defence of the State, its operation conflicts with the Law on Defence and Security Policies, which gives the Armed Forces of Defence and Security the exclusivity of the military defence of the State.

- **Viability.** The companies had no credible business plans and the feasibility studies were based on assumptions of dubious sustainability. The investigation argues that both military and fishing materials are inadequate. Military vessels cannot face the high seas, and fishing boats have a restricted range and fish freezing systems not suited to the standards of the most profitable markets.
- **Use of Funds.** Payment was made directly to the supplier as a turn-key project. The companies that were financed "existed only on paper" and had no working capital. The parliamentary inquiry committee was not able to clarify the application of the funds and the payment to the suppliers. The transfer of funds to the supplier was immediate, so much so that the Commission is not sure whether all that was purchased the debt was or will be delivered.

Figure 25 - The effects of the crisis on the debt and the value of the Metical



Status of international reserves



Source: MEF and Bloomberg (MEF Oct. 2016)

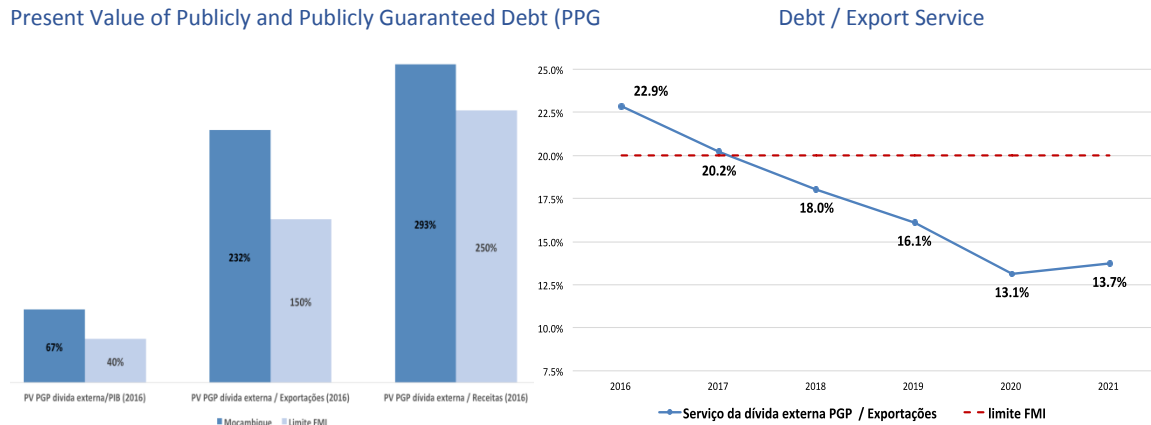
**138. The emerging scenario following the crisis is marked by a deterioration of the country's external position that seriously undermines short-term economic stability.** The revelations of this debt have considerably increased the economy's exposure to external shocks and catalysed many negative effects that have placed Mozambique in a very uncomfortable position. The 2016 data corrected with true hidden debt figures that did not figure in the previous official publications show that gross debt grew significantly to 130% of GDP in 2016 (see Figure 25), a figure thought out only three years ago. The revelations of this debt catalysed a series of negative effects that exacerbated the economic crisis:

- Immediate suspension of PSI (Policy Support Instrument) support by the IMF, which also suspended the execution of the USD 286 million stand-by loan from the mechanism previously requested by the government;

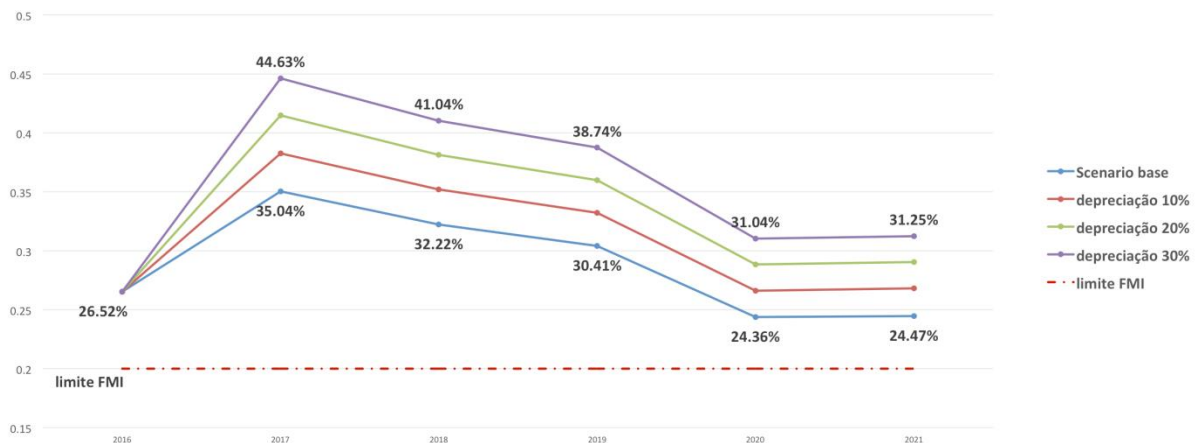


- Suspension of all disbursements of programmatic assistance and donor support to the budget. These sources financed, on average, 10% of government revenues;
- The acceleration of the pressure on metical depreciation, which devalued 70% against the US dollar in 2016, after depreciating 36% during 2015 (Figure 25);
- A sharp increase in debt service obligations, adding another 2% of GDP to debt service per year.

Figure 26 - Status of IMF debt sustainability framework indicators for low-income countries



Rácio do Serviço da Dívida Externa (Pública e Publicamente Garantida - PPG)/Receitas Públicas (%)



Source: Lazard Frères SAS, with MEF data (October 2016)<sup>63</sup>

### Next Steps: Areas that Need More Attention

**139. The current profile of public and publicly guaranteed external debt (PPG) in Mozambique is not sustainable.** Mozambique's public debt and public guarantee structure (PGP) continues to be predominantly concessional, but is subject to exchange rate shocks, being more than 80% denominated in foreign currency. The short-term obligations of the commercial debt service call into question the government's ability to comply with the undertaking. The IMF uses five different indicators to assess the burden of indebtedness and establish levels of security of the country's debt repayment capacity. Figure 26 describes the situation of these five indicators in September 2016 and

<sup>63</sup> The figures were prepared by Lazard Frères SAS ("Lazard"), in connection with her appointment as financial advisor to the Republic of Mozambique, and were presented by H.E. the Minister at the negotiating meeting with creditors in October 2016. The sources of the figures used are official data from the MEF, and the presentation can be found on the Ministry's website. Because the debt situation is very dynamic, the data must be interpreted as a draft that is subject to change.

indicates that all safety limits had been largely exceeded; also indicates that Mozambique is likely to be in violation of most of the IMF thresholds in the medium term. The current categorization of debt is debt distress, which makes it difficult to negotiate the way out of the crisis, since, for example, the IMF cannot have a program in a country in a situation of unsustainable debt, and this, in turn, programs of other bilateral and multilateral donors.

**140. To get out of this situation, the government has followed what appears to be the most correct route.** The government has launched a series of actions aimed at stabilizing the economy and restoring the confidence of the international community. The government has begun to address the two preconditions for the IMF to consider a new program: (i) an effective beginning of the international audit process and independent of the debt of the companies mentioned above; and (ii) put the country's debt in the category of debt distress. With this last purpose, the MEF began a process of negotiation with the creditors where it explained its evaluation of the residual payment capacity of the government for commercial debt service. The presentation made by H.E. the Minister of Economy and Finance (whose graphs are illustrated in this section) seeks to open a process of constructive dialogue with creditors and proposes to consider a debt rescheduling. The MEF offered a rescheduling of the commitments according to the medium-term prospects of the country to be able to assume its responsibilities, and presented a calendar that calculates a growth of the public revenue, especially in the second half of decade 2020-2030. If negotiations - currently underway - are successful, the government could quickly seek an agreement with the IMF to stabilize the economy and restore international confidence.

**141. The alternative path is much less clear.** With minimal room for manoeuvre, the government's alternative would be to declare itself in default and take the same path as other economies, such as Argentina in the last decade. The experience of this country demonstrates that this path may be longer and have high social costs, and that it is surely more difficult than what government is trying to follow. Mozambique's paradox is that it relies on natural resources of such magnitude that, with the confirmation of the decision to hold two megaprojects in the gas sector - which is also under negotiation - the situation of dependence on international financing would change radically. The presentation of H.E. the Minister to creditors pointed out that these two projects<sup>64</sup> could generate an inflow of capital flows of approximately USD 20 billion. Beginning offshore gas projects to generate export, expect a significant increase in revenues in the early 2020s and an expansion of the economy that could achieve the highest real GDP growth rates in sub-Saharan Africa.

**142. Post-crisis external debt management will require a new 'scorecard' and enhanced technical capacities to improve the quality of management.** The way out and resolution of the debt crisis will surely be defined in 2017, and, despite some short-term constraints, the country may resume the path of sustained growth. But the resolution of this crisis should leave lessons learned of great importance to avoid making the same mistakes in the future and priorities to improve the quality of management, at least in the following areas:

- 'Blend finance' management. By 2012, most of the loans granted to Mozambique were provided by traditional donors, which generally ensured the viability of the projects by financing the sustainability of the debt contracted. With the excess liquidity in the international capital market, the government had access to new sources of credit through South-South and commercial cooperation mechanisms. This new situation offered a greater

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<sup>64</sup> A gas investment by the Italian company ENI Coral, in the Rovuma Basin, for approximately USD 8 billion, and the investment of US \$ 12 billion by Anadarko that are expected to be concluded in 2017

freedom of choice, but with higher risks, which the government should manage better in the future;

- Commercial debt management with government guarantees. The debts contracted by EMATUM, MAM and Proindicus were not foreseen in any of the government's programming documents. The sustainability of companies has been dubious from the outset, and the government did not have enough technical elements to carry out an adequate risk assessment. There are many other examples of similar, dubious and debated opportunity ventures co-financed by the government<sup>65</sup>. Therefore, strengthening the management capacity of this type of investment seems to be a priority;
- Public Investment Management and the Integrated Investment Program. This problem appears recurrently in the analysis of several areas of this AFD. The IIP should be the appropriate pre-evaluation mechanism for projects to be financed with budgetary or state resources. The instrument has been described in Section 3.1, as does the need to improve its capacity to function as a project screening mechanism with social, economic and socio-economic impact. The way is to develop an instrument that ensures a prior analysis of the proposals and matches the most appropriate financing opportunities, considering the type and magnitude of the returns. The capacity of the MEF and the government to improve the quality of public investment management will need to be significantly developed.

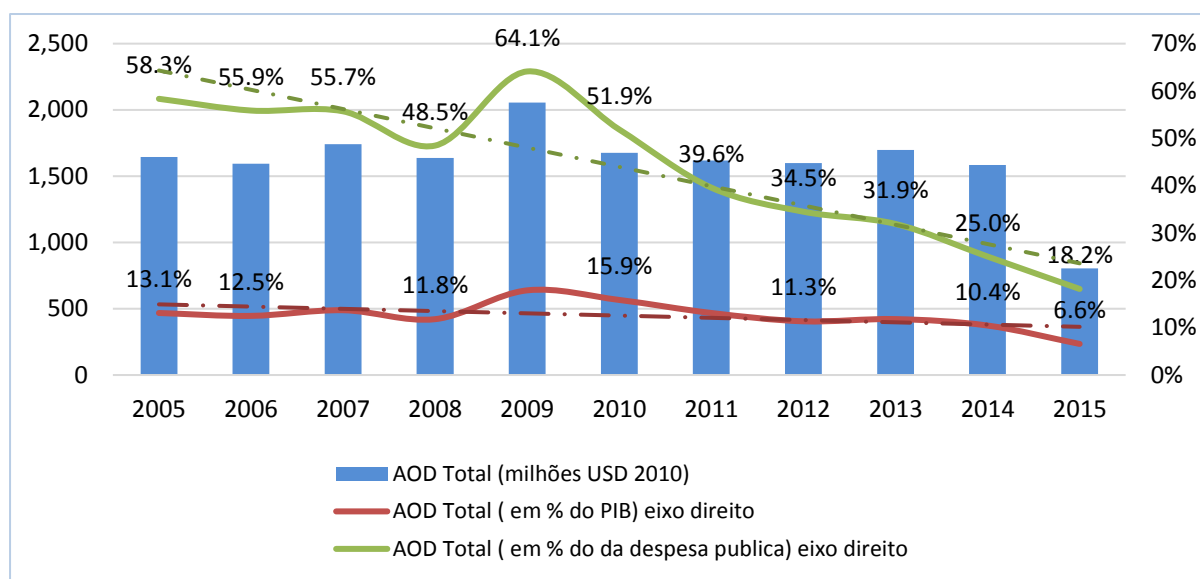
**143. However, a significant part of the public-sector debt problem is not of technical origin and points to the need for further reforms to ensure the integrity of public management.** As discussed earlier, the government is already preparing a new law on the state business sector that aims to regulate the sector to limit the state risk of these operations. Continuing efforts to improve the anti-corruption legal framework and enforcement actions will also be necessary to restore international confidence. This includes reviewing and implementing the non-implemented points of the Anti-Corruption Strategy 2006-2010 and the Governance Action Plan (GAP).

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<sup>65</sup> Como por exemplo: o Estádio Nacional (30 milhões de USD) cuja gestão transformou-se num fardo pelas disponibilidades do Município de Maputo, a Circular de Maputo e a Ponte para cruzar a baía rumo sul (300 Milhões de USD), ainda por completar, o Aeroporto de Nacala financiado através de um crédito outorgado pelo Brasil (80 milhões de USD) e construído pela a Odebrecht, empresa que está no centro do escândalo de corrupção 'lava jato' no Brasil, cuja utilidade continua a ser questionada, tendo em consideração o volume de tráfego aéreo.

### 4.3.3 Official Development Assistance (ODA)

Figura 2 AOD em milhões de USD 2010, em do PIB e em % da despesa total do Governo; 2005-2015



Source: DC-MEF, ODAMoz. Authors' calculations.

**144. The relative weight of Official Development Assistance decreased significantly during the period under study.** Mozambique, during the last two decades, has benefited from robust levels of international aid. Figure 27 summarizes the levels of ODA that entered the country in the period under review. By volume, ODA has been on a steady pace, with USD 1.64 billion in 2005 and USD 1.58 billion in 2014. A significant drop in 2015 (USD 804 billion) and a singularly high point in 2009 (USD 2.1 billion). In relative terms, it can be observed that the weight of ODA to GDP (in red) shows a decrease from 18.1% in 2005 to 6.8% in 2015. The incidence of this flow in total government expenditure (in green), shows a similar reduction since ODA participation increased from 58.3% of expenditure in 2005 to 18.2% in 2015. The evolution of the increase in revenues (in line with GDP growth) analysed in the previous section allowed the gradual decrease of ODA resources in the financing of the State budget.

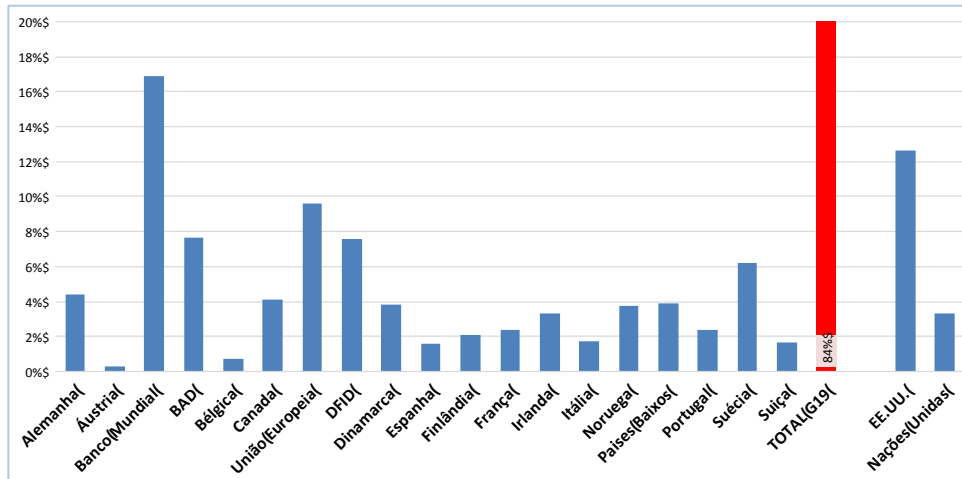
**145. Notwithstanding the reduction of ODA in public spending, Mozambique continues to have a relative dependence on international cooperation.** Although countries consider themselves ODA-dependent when the ODA / GDP ratio exceeds 10 per cent, recent assessments confirm the persistence of some degree of dependency, although the ODA / GDP ratio is already less than these values. The 2014 Public Expenditure Review (ADP) found that, while donor dependence is slowing, the incidence of changes in donor priorities has a significant impact on the consistency of provision of services in key sectors such as health, water and sanitation. agriculture. The recently concluded ADPs in the health and education sectors indicate that ODA dependency in these sectors is still strong<sup>66</sup>:

- In education, ODA finances areas of high priority. ODA is the major source of funding for high priority areas such as building schools, providing teaching materials (including textbooks) and basic school operations (excluding salaries);

<sup>66</sup> Mais informação sobre os resultados destes ADP pode ser encontrada na Secção 4.3.2 desta AFD.

- ODA finances most health care expenditures. Almost two-thirds of total health expenditure is financed from external aid funds, raising questions about the sustainability of the current system and, in particular, the external aid provided.

Figure 28 - Total ODA per donor (of total ODA at constant prices, 2010)

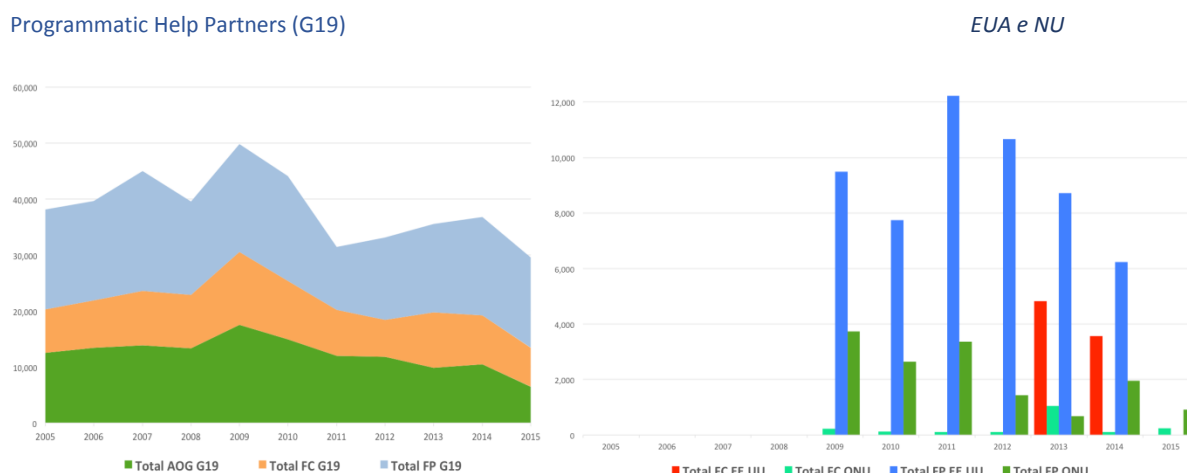


Source: DC-MEF, ODAMoz. Authors' calculations.

**146. Most ODA has historically been channelled through a Program Aid Partners community.** Since 2004, many donors have been using the General Budget Support (GPA) aid modality, and have formed a community of Program Aid Partners (PAPs), also known as G19. Figure 28 shows the contribution weight of each donor as a percentage of the total ODA of the period. The chart is divided into two areas: the PAPs group on the left-hand bars, and, on the right, the largest donors that do not belong to this group (the United States and the United Nations). The red bar (outside the scale of the chart) represents the total ODA channelled by the PAPs, which made up 84% of total development aid. Among these, the World Bank contributed most, with 17% of total aid channelled, followed by the European Union and DFID. On the side of non-G19 countries, the United States is the second largest donor in the country, with 13% of ODA channelled in the period.

**147. Recent trends show a decline in the use of the General Budget Support for aid by projects.** The modalities for channelling ODA can be grouped into three broad categories: (i) General Budget Support (AGO), (ii) Common Funds (FC) and (iii) Project Financing (FP). Figure 29 shows the composition of aid flows disaggregated by modality for G19 (as a whole), the US and UN funds. It is noted that during the first 4 years, program aid (AGM and CF) accounted for more than 50% of flows, with benefits for alignment with national priorities. Over time, as of 2009, the weight of contributions in the AGO (and in the CF, albeit to a lesser extent) has been reducing. The weight of the project component in total ODA has increased. Project aid over the entire period has a large weight, averaging 45% in the first 4 years of the period and 54% on average in the remaining years of the period.

Figure 3 - Overall ODA trends by modality



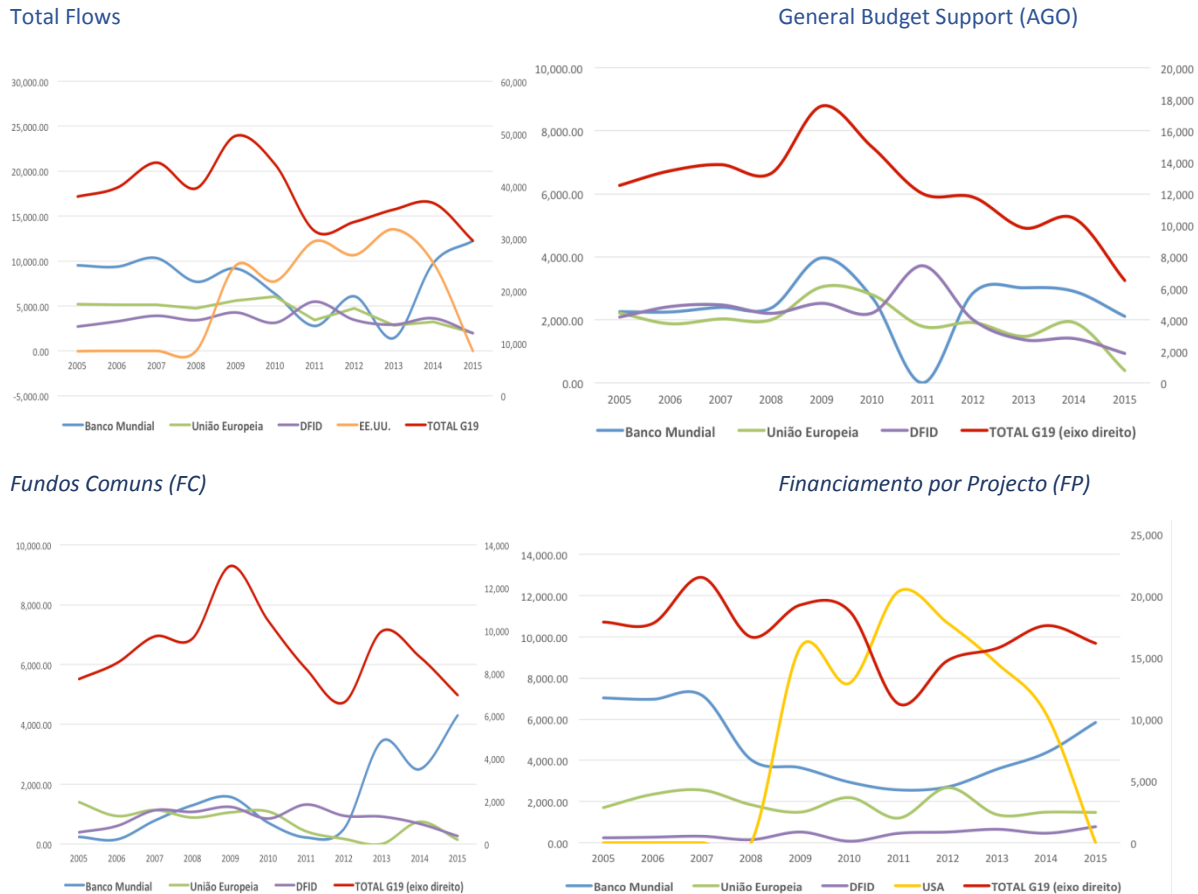
Source:: DC-MEF, ODAMoz. Authors' calculations.

**148. The behaviour of major donors reflects poorly homogeneous dynamics.** Figure 30 shows the total volume of the PAPs and three selected partners with quite different behaviours: (i) at one extreme, the World Bank, (ii) at the other end DFID, and (iii) the European Union, which is a bit hybrid between the two. It also presents data from the United States, which had different standards. What appears to be evident from the analysis of the data is a substantial reduction in the flows of all of them in recent years, a reduction in volumes channelled as an AGO, while maintaining the levels of contribution in the Common Funds. In the last two years there has also been a change, albeit timid, in the aid modality, with a very evident increase in the case of the BM, of the volumes channelled as aid per project. The US behaviour in the chosen aid modality is project financing, especially with NGOs as implementers. In 2008 a joint effort by the United States Government and Government of Mozambique began to assess performance and better track the volume of aid flows to comply with the principles of aid effectiveness.

**149. For many reasons, the changes that are occurring in donor behaviour determine negative dynamics.** The international financial crisis had obvious negative consequences, and in 2012 and 2013 some of the partners began to reduce ODA levels. As Budget Support and support to the common funds are modalities that can be reduced much more easily, this change was reflected quickly in the levels of disbursements, that had a flexion in that period. But the crisis has had other consequences: levels of international trust between governments are reduced because of the changing public opinion of donor countries regarding ODA and aid modalities with high fiduciary risk. The levels of tolerance of some of the capitals of Western countries decrease considerably. Finally, the crisis in public debt management in Mozambique led to the suspension of the AGM and disbursements in the FCs<sup>67</sup>. By 2016 the PAPs had committed to the AUG 212 million, (which represents 7% of the EO), which were frozen sine die. In general, the projects were not suspended (Figure 30). Donors are now seeking other modalities that will allow them to disburse funds hitherto inoperative for the AGO.

<sup>67</sup> Os desembolsos nos fundos comuns foram suspensos até se ter esclarecido que os mecanismos para gerir a liquidez não permitiam que os fundos desembolsados pudessem ser utilizados para pagar o serviço das dívidas escondidas.

Figura 3 - Tendência dos maiores doadores e do conjunto dos PAPs em milhões de MZN e por modalidade de ajuda



Fonte: DC-MEF, ODAMoz. Cálculos dos autores.

**150. In the last years before the crisis, the overall effectiveness of the PAPs group's aid had evolved negatively.** This group of partners sought to respond as closely as possible to emergencies and disagreements with the Government of Mozambique. The AGO was instrumental in generating consensus and support to comply with the principles of aid effectiveness, however, as of 2009, the performance of partners has declined (ADE, ITAD, COWI, 2014). Figure 31 shows the performance of PAPs' aid effectiveness indicators as measured in Mozambique during the joint annual evaluations. The red line - the scale of which is the one on the left - represents the areas in which the performance indicators were reached, and it decreases rapidly from 2009.

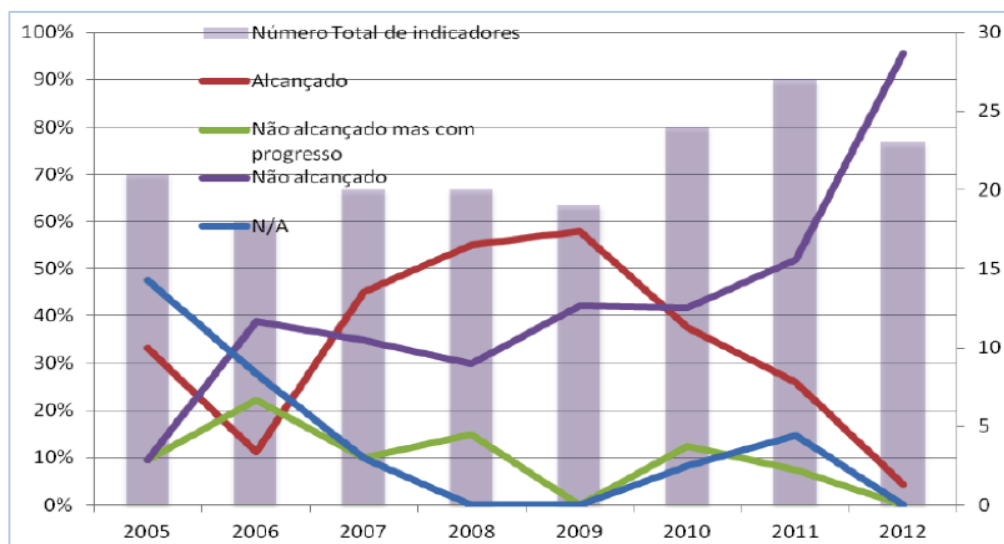
**151. New modalities could be explored to reactivate ODA flows to pre-2016 levels.** Considering the above arguments, it would be appropriate to start thinking of other modalities that are capable of improving the quality and quantity of ODA since confidence is restored. After a study on the fiduciary risk associated with disbursements in the common funds, donors defrosted disbursements with this modality, but it may be necessary to find different modalities to channel the aid that has hitherto been channelled as EFA with more efficient systems than aid by project.

## Distribution of ODA and alignment with country development priorities

**152. For many reasons, the analysis of alignment of ODA with national priorities is very limited.** As discussed in Chapter 3, general long-term government priorities are advocated in the ENDE, and medium-term in the PQGs, PARPs and various types of Sectoral Strategic Plans set up to operationalize the PQG. A number of obstacles prevent the correct alignment of ODA with government priorities:

- The ODAMoz database uses the OECD-DAC classification, which is not aligned with the classification used in the State Budget, so it is not possible to directly verify how ODA finances expenditure defined as priorities in the strategic programming documents;
- Aid channelled as an AGO is considered as external resources when financing the budget; however, in applying the resources, these are considered as quasi-fiscal: such resources are mixed with tax revenues and can finance all kinds of expenditure. It is neither possible nor desirable to trace the application of these resources, and therefore it must be assumed that these are aligned with priorities;
- The flows channelled into the common funds are also delivered to the government, to sectoral ministries, and are administered by the ministries within the priorities defined by the ministries, while meeting the contractual needs set out in the Memoranda of Understanding governing cooperation and dialogue on sectoral policies. These funds, as well as the funds to finance projects, enter the budget and are classified as an external component of the investment;
- It is important to remember the limits that the CED<sup>68</sup> imposes in the State Budget on the analysis of the output and outcome of the funding of policies with external resources, as well as the internal resources analysed in Chapter 3.

Figura 4- Resultados dos indicadores dos PAPs entre 2005 e 2012 no marco das avaliações conjuntas do AGO)



Fonte: Reproduzido de (ADE, ITAD, COWI, 2014), Relatório final, p. 45: Junho de 2014.

**153. On the basis of the information available, it could be ensured that there is a significant concentration of ODA in a few specific sectors.** According to DNCP-MEF data for the period 2012-15 only, 78% of ODA funds financed expenditure in priority sectors such as infrastructure, health and

<sup>68</sup> The CED is also complemented with the Resource Source Classifier (FR) and the Economic Revenue Classifier (REC), but they do not achieve a direct link between inputs and outputs and expected and eventually generated outputs



education sectors, which together received more than 70 % of funds. It is important to consider that the external component of the budget includes both ODA and South-South cooperation funds and external commercial loans.

Table 12: Distribution of ODA compared to budgetary expenditure in priority sectors, 2012-2015

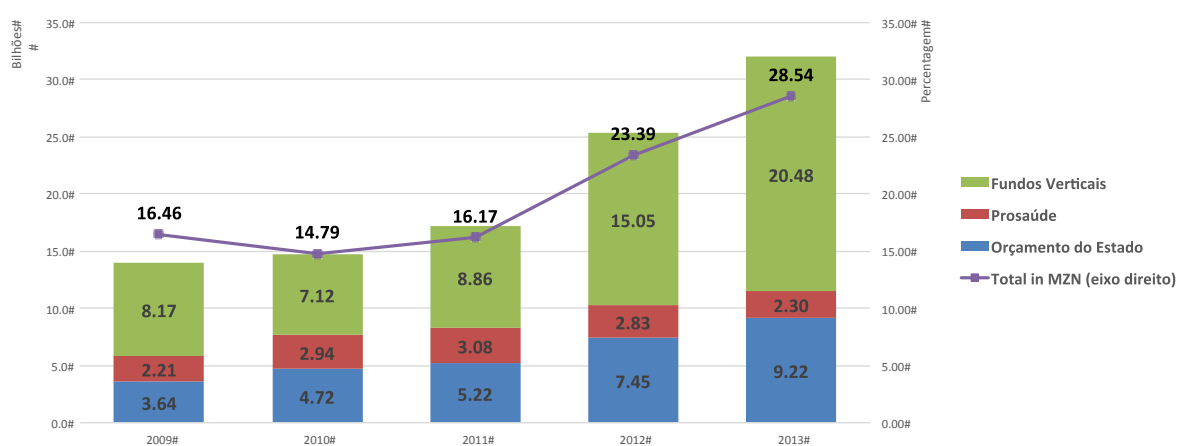
Description	Distribution of the External Component (%) (2012-2015)	Budget expenditure by priority sectors (%) (2012-2015)
<b>Total Priority Sectors</b>	<b>77,8%</b>	<b>56,9%</b>
Education	13,3%	18,2%
Health	21,0%	9,6%
Infrastructures	37,3%	12,9%
Agriculture and Rural Development	4,0%	6,3%
Governance, Security and Judicial System	1,0%	6,8%
Other Priority Sectors	0,6%	2,8%
<i>Other non-Priority Sectors</i>	22,2%	39,3%
<i>Interest and Financial Operations</i>	0,0%	3,9%
<b>Total Expenses (Excl. interest Finan. Op.)</b>	<b>99,4%</b>	<b>96,1%</b>

Source: DNCP-MEF .. Authors' calculations.

### Other Sources of ODA: Vertical Funds

**154. Mozambique also benefits from other ODA funds that are not always visible through the DC-MEF tracking<sup>69</sup>.** This is the case of vertical funds in the health sector, such as the Global Fund to Fight HIV / AIDS, Tuberculosis and Malaria, which are recorded in the health sector budget implementation report but are not captured by the REO by DNCP-MEF. In addition, the amounts associated with procurement of medicines whose procurement is not managed by the Ministry of Health are not tracked by the Budget Execution Report. Similar situations occur with funds from the Global Alliance for Vaccines and Immunization (GAVI)<sup>70</sup>. Cases apart are funds disbursed by different health programs funded by the US Government. These programs that are managed by NGOs are not always captured in budget execution reports.

Figure 32 - Weight of Vertical Funds and ODA in the Health Sector



Fonte: Avaliação da Despesa Pública no Sector de Saúde, 2009-2013

<sup>69</sup> The OECD-DAC definition considers flows out of donor countries. What interests us is the flow received in Mozambique and the way the government traces flows. For this reason, it is considered the database used by DC.-MEF

<sup>70</sup> Global Alliance for Vaccines and Immunisation.

**155. Vertical funding has a growing share of total expenditure on the health sector.** The recent Public Health Assessment (ADP) in the health sector notes that most of the total health expenditure (32 billion MZN or 1 billion USD in 2013) was financed from outside resources outside the Single Treasury Account (CUT). Figure 32 indicates that most of the increase in real health expenditure was generated by the growth of vertical funds, which in 2013 reached 64% of the total, but only 1% of this funding was done at the CUT. The contribution of the Pro-Health Common Fund decreased by up to nine percentage points over the five-year period to 7%, due to the - not very orderly - withdrawal of some fund partners<sup>71</sup>. Public funding in the state budget had a small increase of three percentage points over the five years; but the total ODA contribution is equivalent to 75% of total sector funding.

**156. The management of this type of financing should consider international experience and some of the negative effects that have already been detected in Mozambique.** The information presented in Box 2 allows a quick overview of the known advantages and disadvantages of this type of financing. The recent ADP in the health sector warns of issues related to the sustainability of vertical funding and the need to strengthen the capacity of the health system to deliver services. Vertical funding is creating gaps between disease-specific funding and horizontal funding to strengthen the capacity of health service delivery systems. A mechanism (such as the Pro-Health Common Fund) could help offset these problems and develop these capabilities. But the decline in ProSaúde's resources, and its poor use by the government to fill budget gaps in wage financing, is limiting sustainability. A more comprehensive approach to linking vertical funding with strengthening the health system (called diagonal funding) should compensate for these situations.

**Box 3: Using vertical funds correctly**<sup>72</sup>

International experience indicates that the management of vertical funds in Mozambique could be a subject of greater attention in the short term. Vertical funds are development financing mechanisms confined to single development domains with varied funding sources. The main examples are climate finance funds, such as the Global Environment Facility (GEF), which was created in 1991, and the two vertical health funds, both created in 2000, the Global Alliance for Vaccines and Immunization (GAVI) and the Global Fund for HIV / AIDS, Tuberculosis and Malaria (GFATM). The analysis of vertical funds as a modality of development financing finds positive and negative aspects.

- **Positive aspects.** Vertical funds respond to donor interest in earmarking funds and can be enhanced by allowing donors to fund distinctive and focused programs. The vertical funds have also been praised for offering 'innovative multilateralism'. Although they have a limited number of donors, their governance systems can be inclusive of civil society and the private sector. Such funds also have a reputation for rapid delivery as well as transparency and accountability.
- **Negative aspects.** Significant distortions can result from its size and descending nature. One of the problems identified is that, with the arrival of resources, the funds require human and financial counterpart resources in the beneficiary countries, and draw on these - sometimes scarce - resources from national systems. An additional criticism is the lack of emphasis of this type of financing on capacity building in the beneficiary countries, generating problems of sustainability of the solutions provided.

While the developmental impacts delivered through vertical funds are meaningful and measurable, beneficiary countries will need to take measures to stimulate the opportunities offered by vertical funds, minimizing distortions and ensuring that national institutions and systems are strengthened rather than marginalized programs.

<sup>71</sup> Mozambique Health Public Expenditure Review 2009-2013, Draft, Nov 2015.

<sup>72</sup> See also Browne, S and R. Cordon, "Vertical Funds: Lessons for Multilateralism and the UN", Future United Nations Development System, Briefing 25, January 2015.

**157. The Ministry of Economy and Finance. In Mozambique, the MEF Cooperation Directorate is the institution responsible for coordinating the allocation of ODA and for collecting data on the flows of funds from the cooperation partners.** The information collected is limited to the OECD-DAC partners listed above. DC-MEF has established a timetable for partners to access the ODAMoz database and thus update information regarding disbursements of funds and possible new committed funds. This timetable is aligned with the budget cycle.

**158. The Ministry of Foreign Affairs and Cooperation is the government's main interlocutor in dialogue and relationship with cooperation partners.** In August 2010, the Government of Mozambique, in resolution 34/2010, recognizes the need to establish the objectives, frameworks, lines of action and mechanisms for the implementation of the International Cooperation Policy, as well as the Implementation Strategy, and instructed the Ministry of Foreign Affairs and Cooperation to coordinate measures for implementation. The government promotes regular working meetings with its partners to ensure mutual understanding and a favourable environment for development.

**159. The Policy Coordination Forum is the main dialogue tool for managing ODA with partners.** The Ministry of Foreign Affairs and Cooperation runs this forum, composed of sectoral ministries, provincial governments and cooperation partners. The forum monitors the implementation of cooperation agreements, as well as the implementation of plans and programs and cooperation projects. Coordination of foreign NGOs is done by MINEC, in coordination with sector ministries and provincial and district governments.

**160. The AGO and the Common Funds have their own coordination mechanisms as defined in the Memoranda of Understanding governing partnerships.** These memos regulate the dialogue on sectoral or national policy priorities, the strategic interest target and focus of policy dialogue (sectoral or national), as well as the timetables for evaluating commitments and procedures for disbursing funds.

#### [Access to ODA Data and Information](#)

**161. ODA's main source of information is in the process of being built.** The DC-MEF database (designated ODAMoz) was created to collect ODA flows and to monitor the performance of Cooperation Partners. The DC-MEF coordinates the database updating process, which, in any case, is voluntary and depends on the responsibility of each partner. In some cases, especially in the early years of the period, there are occasional problems of consistency, which, however, do not harm the overall picture. The partners that contribute and feed ODAMoz are those who wish to participate in the exercise of mutual accountability for aid effectiveness and are, in general, traditional OECD donors<sup>73</sup>.

**162. The process of systematising ODA data has yet to resolve significant difficulties.** The first version of ODAMoz was developed by the EU as an instrument for each donor to see the scope of intervention

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<sup>73</sup> The complete list is as follows: Germany, Austria, AfDB, World Bank - WB, Belgium, Canada, European Union - EU, British Cooperation - DfID, Denmark, Spain, France, Ireland, Italy, Norway, Spain, The Netherlands, Portugal, Sweden, Switzerland - which are the members of what was designated G19 in alphabetical order - United States - United States - United Nations - United Nations.

of other donors, to harmonize and avoid overlaps in interventions. This exercise, launched by a donor, was assumed by the Cooperation Department of MPD and after the MEF, which inherited the management of the Database. Over time, minimum donor information sharing objectives have been added to inform the government of both the projections of volumes to be disbursed in a year and the execution of disbursements. The ultimate objective was to inform the budgeting and expenditure implementation process. This last objective was never achieved. The main cause was the inability to ensure that PCs enter data in the precise and consistent format and with the quality needed to feed the EO preparation.

**163. The Budget is also a source of data on expenditure flows, when they finance interventions entered in the budget (on-budget).** That is, flows of funds disbursed by donors and managed by the government through one of its institutions, or funds inscribed in the budget, but managed by another entity. These flows should be a subset of the flows recorded in ODAMoz, but sometimes this is not the case because of different interpretations of the ODAMoz function. In the Budget these funds are classified, at the time of expenditure, as external funds. It is important to consider that the external component of the budget includes both ODA and South-South cooperation funds and external commercial loans, which by 2013 were a minor component.

**164. There are significant compatibility problems for integrating the two sources of information.** Unfortunately, the ODAMoz database is based on the OECD-DAC classification. This classification is not in line with the classification used by the government in its programs or in its Budget. ODAMoz's coding is also not in line with the functional international classification of COFOG expenditure, whose introduction in Mozambique is ongoing and gaining consistency. Therefore, it is always necessary to make some approximations. The State Budget classifies the expenditure in terms of Economic Classification of Expenditure and in terms of Beneficiary and (or) Executors (UGB and / or UGE) Managing Units. These are classified by sector. The expenditure of these institutions is not classified by priority actions (programs), which limits the ability to identify higher or lower priorities within sectoral expenditure. This limits the possibility of input expenditure analysis, almost eliminating the possibility of input-output analysis.

**165. Significant parts of ODA are not consistently recorded.** Mozambique receives funds under concessional and commercial credit and is managed by institutions sometimes linked in some way to governments. The MEF's National Treasury Department is responsible for signing the contracts, and for monitoring the flow of funds, for proper budgeting, both when they represent revenues and when they represent expenses. For the purposes of this study, DNT-MEF provided the information on all credit agreements signed per year. Given the nature of the credit institutions, it is not possible to know whether the DNT-MEF data are also captured in the MEF-DC database. These amounts therefore represent a potential flow, to be disbursed in tranches in the years following the signing of the contract. In addition to funds managed by partners or the government, there are funds that OECD partners provide to international and national NGOs to implement the activities. The government's information on these flows of funds, through the DCF-MEF, is limited, inconsistent and underutilized. This information is reported and analysed in the following paragraphs.

#### Next Steps: Areas that Need More Attention

**166. Strengthen government leadership and strategic direction of ODA. ODA is a potentially important funding stream that must be used strategically.** Instead of earmarking ODA to finance areas such as wages or infrastructure where this type of resource has little comparative advantage, ODA can be instrumental in financing government capacity building in key areas. The government should prioritize the allocation of ODA to develop its capacity to improve management and increase

the volume of other funding streams that can reach very large volumes. In this way, ODA would have a very high multiplier power, since, in relative terms, the investment needed to develop capacities is generally low. In addition, ODA could also be in priority management areas, such as: (i) management of efficiency in the delivery of public services; (ii) the ability to develop and monitor the implementation of quality plans, (iii) financial management. Historically, the allocation of ODA funds was predominantly initiated by donors, based on their own strategies and the donors' perception of their comparative advantages and country priorities.

**167. An additional priority is to take the path of collaboration with development partners and improve the conditions for the efficient and transparent use of resources.** Once the trust problem generated by the external debt crisis is resolved, the priority for the government will be to find efficient and transparent mechanisms to reduce the fiduciary risk of donors and thus be able to reactivate this source of financing. There are various options and modalities for achieving this, but the government should avoid future fragmentation of funding in a multiplicity of projects. There are no evaluations of the effectiveness of the Common Fund instrument, which, if properly formulated, could serve these purposes. In the inevitable case of having to opt for such financing, the government should at least use the most efficient mechanisms and focus on comprehensive and medium- and long-term approaches to ensure the development of key areas. As discussed in Section 4.2.2, an example could be the implementation of medium-term programs to increase efficiency in the provision of services such as education or health, with clearly established goals. As seen earlier, such initiatives could liberate a space which could be reused in the financing of other key areas of the same sectors.

**168. Improving the capacity to monitor the quality of ODA allocation and use should also be considered a priority.** The quality of available information on ODA does not reach the minimum level necessary for effective management of these flows by the central government. The available information is incomplete, inconsistent and outdated. As for information management, DC should seriously consider the final redesign of ODAMoz and move away from the 'ODA database' paradigm to begin to understand it as Management Information Systems, designed and implemented to inform strategic decision making from the government. These decisions should cover the long-term strategic allocation of ODA and the budget process - based on past objectives, performance and performance - and monitoring the actual use of these funds, with clear performance indicators regularly used throughout the year. As will be seen later, ODAMoz should be able to coherently integrate information on ODA, with other flows such as South-South Cooperation, and national and international funding to NGOs. The recently established Directorate for Monitoring and Evaluation of MEF could play a very important role in this process, so strengthening its capacity should also be considered a priority.

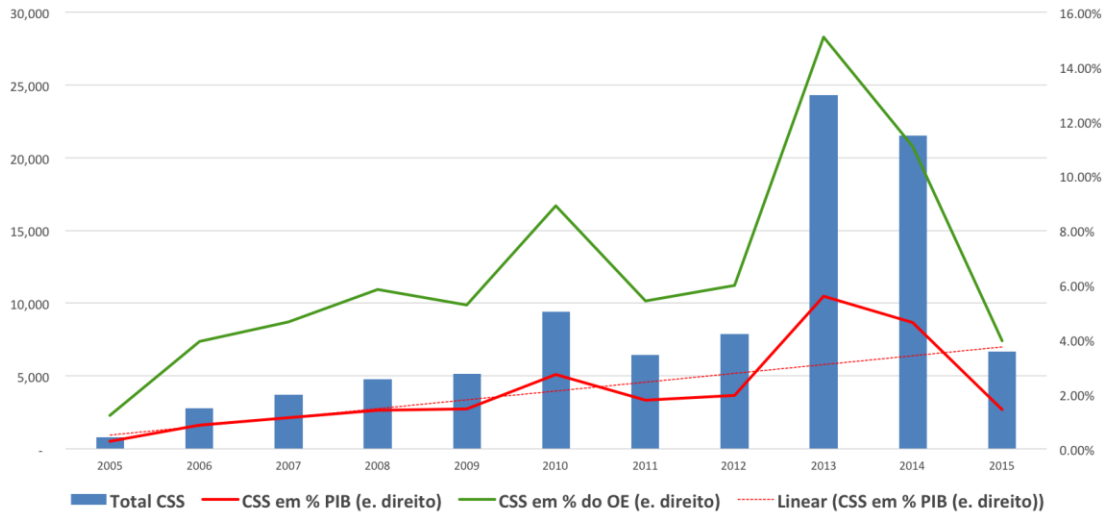
#### 4.3.3 South-South cooperation

**169. South-South cooperation is a dynamic source of funding with great potential in Mozambique.** Figure 33 shows the total value per year (at constant prices 2010) of the contracts subscribed by the Government of Mozambique in the period under analysis and the potential relative weight of these debts<sup>74</sup>. The trend line shows that, clearly, the weight of these contracts in the Mozambican economy has grown over time, from less than 1% of GDP in 2005 to more than 4% in 2014, clearly indicating an increase in the weight of this instrument and the potential of this type of flow. The most likely reason for the decline is that most of these funds are credits and - as the IMF reports at the time indicated -, in those years Mozambique had reached the indebtedness limit that would guarantee debt sustainability.

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<sup>74</sup> Government data is missing data for 2013.

Figure 33 - Evolution of total CSS flows, as% of GDP and as% of OE



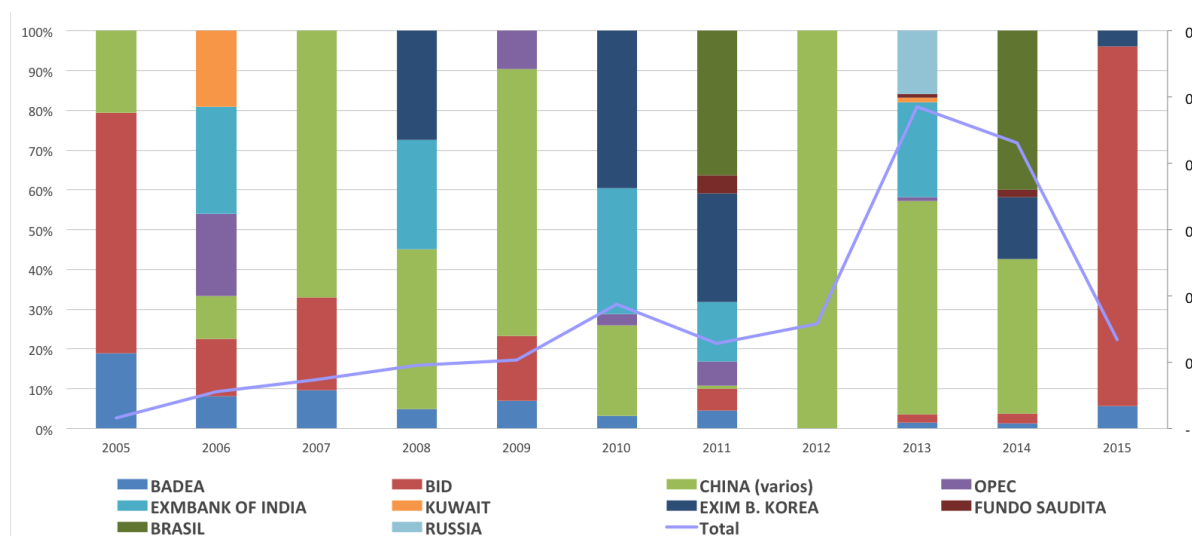
Source: DNT-MEF Authors' calculations.

**170. In Mozambique, SSC takes mostly the form of credits to the public sector.** According to available information, these loans are concessional loans with an average interest rate of 0.9%, an average grace period of 5.7 years, an average maturity of 24.2 years, and a donation component. In CSS contracts, the Granting Institution grants a loan to the Government of Mozambique generally to finance the execution of an infrastructure work. The contracts are signed by MEF-DNT, as the institution responsible for the management of the treasury and public debt. The MEF-DNT provides the data on the execution of the disbursements for proper registration in the public accounting documents, among them the Budget Execution Reports and the State General Account. The MEF-DNT provides a database of all contracts signed between the GoM and the granting institutions of both CSS and other donor institutions such as ADB or BM-IDA.

**171. During the period under review, China has consolidated as a partner that more CSS funds made available.** China's funds, either directly as government or through the Exim Bank of China, totalled more than MZN 39.5 billion through 14 financing contracts for Mozambique in the period under review. The major participations are: (i) Exim Bank of India, with 11.7 billion MZN and 11 projects of various infrastructures, (ii) Brazil, which secured credit of more than 10.788 million MZN for two (iii) Exim Bank of Korea, with almost 10,258 million MZN and ten credit agreements, and (iv) the Islamic Development Bank (IDB), which financed 12 social and transport infrastructure projects, of transmission and distribution of electric energy, in a complex value of 9,408 million MZN. Other donors include the Arab Bank for Economic Development of Africa (BADEA), OPEC, the Saudi Government,

Kuwait. Finally, the governments of Romania, Serbia and Russia rescheduled their debts in 2007, 2011 and 2013 respectively<sup>75</sup>.

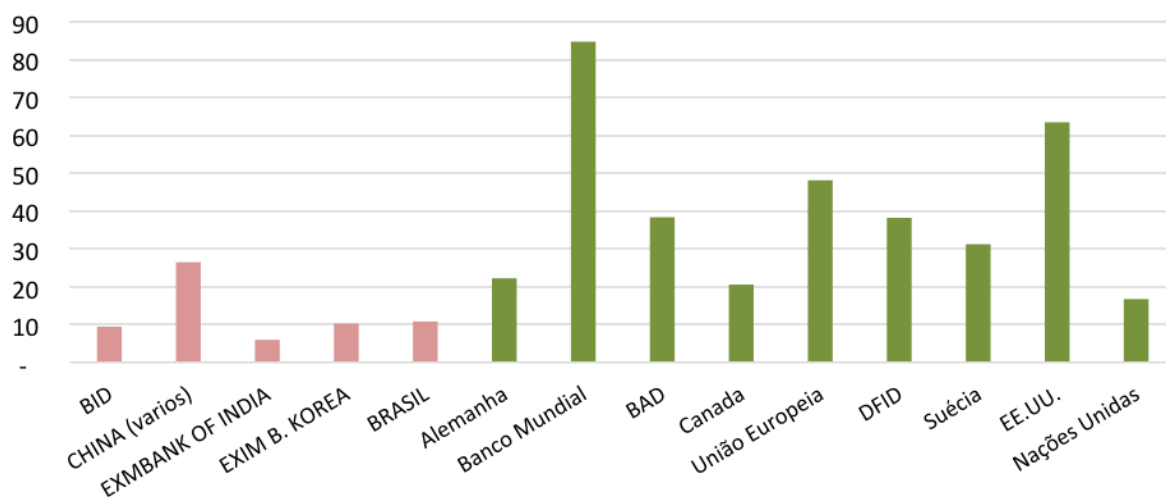
Figure 34 - Relative weight of CSS sources, total credit per year.



Source: DNT-MEF. Authors' calculations

**172. A comparison of the main sources of SSC and ODA makes it possible to observe the complementarity and relative importance of this source of funding.** The data in Figure 35 make it possible to compare the funds made available to selected OECD and non-OECD countries. For the period 2005-2015, China made available funds volumes comparable to those disbursed in the same period by some high-profile OECD partners (such as DFID or Sweden). The Islamic Development Bank (IDB) is about to achieve levels of cooperation equivalent to the total funds available from the United Nations.

Figure 35 - Comparison of available ODA and CSS funds (billion MZN at constant 2010 prices)



<sup>75</sup> The Annex presents a complete list of these financing contracts per year, in millions of MZN at constant 2010 prices, and where possible (unfortunately the information provided is not always uniform), indicates the interest rate applied, maturity, grace period and the eventual component to donation.

## Data Access and CSS Information

**173. The information available permits a very limited analysis.** Data on SSC are generally incomplete and data on these flows, provided by the governments of non-OECD-DAC countries, are therefore likely to present an underestimated picture of actual value. Unfortunately, the information provided in the government databases does not have the same format over the period under review, which weakens the reliability of these data reassumed here. The data on both disbursement and debt service payments are only available in aggregate form, which does not allow the CSS funds to be distinguished from the total debt service paid annually. In addition, the DNT-MEF should regularly update a database for the calculation of debt service in the future. The DC-MEF tracks information from OECD donors who have committed to participating in the exercise to comply with the principles of aid effectiveness. The CSS funds are running out of this crawl.

**174. The information provided by DNT-MEF omits some important data.** The information provided does not indicate to what extent these flows have materialized in Mozambique or are financing agreements for the construction of 'turnkey' infrastructures, where the financier (selects) and pays to the service provider without the beneficiary country receives and can manage the flow of funds. Notable is the case of infrastructure projects financed by the Government of China, where the Treasury records disbursements as the work is carried out, and the Chinese Government pays the executor of the project. The information provided does not specify whether these are projects with technical assistance or capacity building components. Regarding the accounting of CSS flows, they appear in the Budget, registered in the external investment component. Considerations regarding the alignment of ODA with government development priorities, as well as those for the prioritization of infrastructure projects, also apply to CSS.

## Next Steps: Areas that Need More Attention

**175. CSS has significant potential, but the cost-effectiveness of these funds has to be duly assessed.** Considering that these funds are purchased on credit, which will generate future flows to repay debts and interest, their cost-opportunity - that is, the economic and social profitability of the projects financed - has to be duly evaluated. As discussed in Section 4.3.2, in addition to the most questioned cases of debt contracted by public companies, there are many other examples of dubious and debated opportunity ventures funded with CSS funds. One of them was the construction of Nacala Airport, financed through a credit granted by Brazil (USD 80 million), and executed by the company Odebrecht (at the centre of corruption scandals in Brazil and other places in Latin America), and whose utility continues to be questioned, taking into account the volume of air traffic. In many cases, the provision of CSS credits is conditional on the hiring of companies from the country of origin, and in some cases, does not allow competitive bidding processes to be awarded.

**176. Good CSS management will require greater government capacity.** International experience shows that, in general, good management of CSS funds requires an increase in the government's ability to select projects with the highest socio-economic impact. This is already a weakness identified by both the government (VFP, PEFP) and the latest reviews of the Public Finance Management systems in Mozambique (PEFA, PER) already mentioned in Chapter 3. The government needs to develop integrated systems to cost / benefit ratio of the final work at the same time as the cost / benefit ratio of the credit, which are usually done separately. In addition, current and near future solvency conditions indicate that the negotiating space for stipulation of new financing contracts may suffer from some limitations and will require more specialized capacities in various areas of government, for



example, in the analysis and management of CSS credit risk in relation to the implementation of public-private partnerships.

**177. The government should consider the benefits of unifying management and integrating CSS information with ODA.** These are two complementary sources of international cooperation whose management could substantially benefit from the use of unified criteria in programming, alignment with priorities, monitoring implementation and strategic dialogue with development partners. It would also greatly help to improve decision making to consider the integration of CSS information into the final redesign of ODAMoz and ensure quality information with the same compatibility criteria for future integration of information with other government systems, such as Debt Analysis and the State Budget.

#### 4.4 Other Public Sources

178. The following is a list of public funds that could be important for the future of the country but could not be duly evaluated for reasons other than the organization of this work. In most cases, the main reason is that there were not enough data to perform the evaluation. In other cases, the information exists but it was not possible to establish a productive working relationship with the institutions responsible for managing these flows and therefore it was not possible to obtain the minimum elements to analyse the flow perspectives according to the AFD methodology. The information presented here is intended to illustrate the value that might have been duly analysed in future.

##### 4.4.1 Climate Financing.

179. Government policies and programs for adaptation and mitigation of climate change are, by nature, cross-cutting and multidisciplinary. Funding flows to implement policies that address climate change, by their nature, are managed by different institutions. Coordination of activities is the responsibility of the Ministry of Land, Environment and Rural Development (MITADER). Other ministries that stand out for having financed more actions in this scope are the Ministry of Public Works and Housing and the Ministry of Agriculture (which is also responsible for Food Security).

**180. Limitations and opportunities to improve the management of public climate finance are being evaluated by a specialized study.** Since October 2014, the National Council for Sustainable Development (CONDES), with support from the World Bank, has helped the National Environment Fund to carry out the Review of Institutions and Public Expenditure for Climate Change (CPEIR)<sup>76</sup>. The objective of this review is to understand the past and present levels of expenditure for mitigation actions (reduction of greenhouse gas emissions) and adaptation to climate change, and to assess to what extent they are and are in line with the objectives of the policies, while at the same time conducting an institutional analysis of the system established for its fulfilment. These two objectives are shared by AFD. Unfortunately, the CPEIR has not yet been completed, which limits the ability of this AFD to analyse this type of financing. The analysis presented is based on the preliminary results of the CPEIR and offers some very general ideas for improving future access to international funds flows for climate financing.

**181. It is not possible to estimate a baseline for analysing expenditure on adaptation and mitigation of climate change.** The budgetary information does not allow monitoring of these expenditure, which could be done with an appropriate follow-up of the financing of the PES programs or using the full potential of the recently installed system of functional expenditure classification. Therefore, CPEIR will

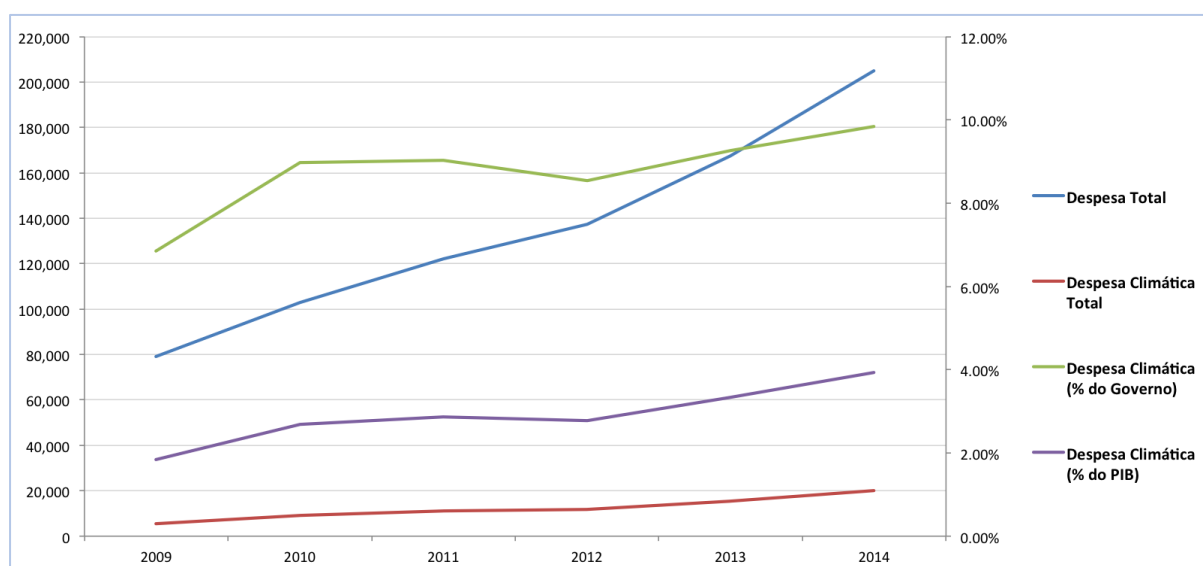
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<sup>76</sup> CPEIR: Climate Change Public Expenditure and Institutional Review.

analyse expenditures classified in the budget as Economic Subject (code 04) and those classified as Environmental Protection (code 05) and will evaluate, for each item of expenditure, whether it was relevant to be considered as an adaptation or mitigation expense climate change. A primary outcome of this analysis for the period 2009-14 is presented in Figure 36.

**182. Analysing the alignment of expenditure with government development priorities in these areas is an even more complex task.** The 2011 Environmental Public Expenditure Assessment (PEER) reveals weak alignment with national plans. The study concludes that the practices of the plan and budget in Mozambique do not allow the easy establishment of a clear link between the policies and the budget allocation and expenditures. In addition, even when policy documents indicate priorities, they do not specify the concrete activities and targets and indicators associated with a given policy objective (GOM-MICOA, 2011). During the preliminary stages of the CPEIR, a specific exercise was required to try to track the financing of the different interventions, and the government's monitoring of actions does not allow confirmation, but it also does not allow denying, if and to what extent, public expenditure was effectively and effectively targeted to government priorities.

Figure 36 - Total and Climatic Expenditures in MZN, and Climate Expenditure as% of total expenditure and GDP (left)<sup>77</sup>



Source II: CPEIR progress report

### Governance and Policy Coordination Framework

**183. The governance framework for environmental policies and sustainable development has traditionally been a challenge in Mozambique.** Regarding policy governance, PEER 2011 recommended improving the performance of the Ministry of Environmental Coordination (MICOA) and the National Council for Sustainable Development (CONDES) and strengthening its institutional capacity, as well as Units / Departments of Environment in ministries selected as very limited in terms of coordination of intragovernmental policies and facilitation of dialogue. ADPA also pointed to the lack of linkage between environmental priorities and the budget allocation and transparency of budget planning and accounting instruments (realignment of COFOG codification in SISTAFE) as well as dependence on funding. It also pointed out that other key players in the sector, such as the National Environment Fund (FUNAB), were not operating according to their potential capacity because they did not benefit from the full potential revenue of the environment to which they could be entitled. After

<sup>77</sup> Climatic expenditure in the functional classification of expenditure (codes 04 0 05). Data in nominal terms.

2015, some of the recommendations have been considered and the new government structure attempts to respond to these challenges, which have been incorporated into the formulation of MITADER and the FNDS.

**184. Taking these considerations into account, the Government has begun a process of reforming the institutional, policy and financing framework for sustainable development.** With the creation of the new Ministry of Land, Environment and Rural Development (MITADER), the government initiated a process of change in the management and redefinition of the competencies of various ministries to better adjust policies and to clarify where to create capacities to institutions and generate knowledge so that the decision-making process is more efficient and technically informed. One of the results of the PEER was that Mozambique did not sufficiently invest in the management of its natural resources: actual expenditure allocated in relation to the cost of environmental degradation and cost to remedy environmental damage. The study estimated that the country loses 17% of GDP annually for causes associated with environmental degradation and unsustainable use of natural resources, and that the estimated cost to remedy such damages would be 9% of GDP. Therefore, if the basis of the ENDE's proposal is that the country's economy is based on natural resources (agriculture, fishing, minerals, etc.), sustainable management of these resources is essential; and only an increase in the allocation of funds in this area can ensure such management.

**185. MITADER has also begun a process of consolidation and reformulation of a strategic framework of policies and plans.** This process seems to be oriented towards the simplification and integration of a very dispersed framework of policies, strategies and plans. From the emerging policy framework, the most prominent elements are: (i) the National Strategy for Adaptation and Mitigation of Climate Change 2013-2025 (ENAMMC); (ii) National Strategy for the Reduction of Emissions from Deforestation and Forest Degradation, Forest Conservation and Increase of Carbon Reserves through Forests (REDD +) 2016-2030; (iii) National Sustainable Development Program (PNDS). These strategies are broadly aligned with the ENDE, which proposes broad principles but few concrete actions in most of the areas involved.

**186. These strategies propose structural changes for the future development of the economy, and set targets that could entail significant costs for public and private investment.** The strategies propose major changes - often structural - in the productive base of the national economy and in the environmental management of resources. Table 13 highlights some of the goals proposed by these strategies that could have a high cost impact. In the case of ENAMMC, the proposed reforms around Mitigation will require very significant investments by the private sector, and certainly of importance on the public investment side (in the form of tax subsidies and other mechanisms to stimulate private investment). In most cases, the strategies do not include estimates of the costs required to carry out these transformations or the sources of funding to mobilize financial resources for their implementation. ENAMCC sets out cost estimates, but only for the first two years of implementation (2013-2014), with an estimated total of USD 142 million for the two years (USD 63.9 million in 2013 and USD 78.1 million in 2014). The strategy does not define the goals by area (only defines the indicators to measure them) and the costs per goal; when compared to the ambition of the proposed interventions, these values appear to be too low and unrealistic. The high-cost targets of the PNDS are clearly defined (see Table 13), but there are no estimates for these costs, which will surely require high public and private investment.

**s. The high-cost targets of the PNDS are clearly defined (see Table 13), but there are no estimates for these costs, which will surely require high public and private investment.**

Table 13: High-investment areas of the Sustainable Development Strategies

Strategy	Area
National Strategy for Adaptation and Mitigation of Climate Change 2013-2025, (ENAMMC)	<p><i>Mitigation and development of low carbon</i></p> <ul style="list-style-type: none"> <li>• <i>Expansion of renewable energies</i></li> <li>• <i>Increase energy efficiency in industry, transport, housing and public buildings</i></li> <li>• <i>Extractive industry emission standards</i></li> <li>• <i>Promoting low carbon urbanization</i></li> <li>• <i>Reduce emissions from industrial processes, including waste and effluents</i></li> <li>• <i>Developing low-carbon farming practices</i></li> <li>• <i>Reduce the rate of deforestation and uncontrolled fires</i></li> <li>• <i>Redefining forest use other land uses, waste</i></li> </ul> <p><i>Adaptation and management of climatic risks</i></p> <ul style="list-style-type: none"> <li>• <i>Use of water resources, agriculture, fisheries, food security and nutrition, social protection, health, biodiversity, forests, urban, tourist and coastal infrastructures</i></li> </ul> <p><i>Cross-cutting issues</i></p> <ul style="list-style-type: none"> <li>• <i>Institutional and legal reform, research and systematic observation, training and technology transfer</i></li> </ul>
<i>National Program for Sustainable Development</i>	<ul style="list-style-type: none"> <li>• <i>Rural poverty reduction to 45%;</i></li> <li>• <i>Provide access to affordable drinking water for 15 million people;</i></li> <li>• <i>Expand the generation of Bioenergy to 4,000 Mw, implementing renewable energy systems;</i></li> <li>• <i>Build 1500Km of tertiary and vicinal roads;</i></li> <li>• <i>Ensure bank coverage in all districts of Mozambique;</i></li> <li>• <i>Ensure access to land by registering 5 million occupations;</i></li> <li>• <i>Raise the elephant population to 17,500;</i></li> <li>• <i>Reduce the emission of gases (CO2) by 72.8 million tons per year;</i></li> </ul>

**187. The design of the main financial aspects of the FNDS should involve a more active involvement of the MEF and consider the lessons learned from the management of other funds.** So far, the FNDS is being developed without the active participation of the MEF or other government partners. However, such an instrument should not be designed in isolation and should not consider its context with a broader framework for financing other government policies, strategies and initiatives that fall outside MITADER's areas of competence (e.g. incentives for private sector development and the promotion of FDI). As discussed in Section 4.3.3, the government has mixed experiences in the management of Common Funds with co-financing from different international sources. There are at least fifteen other funds, which, like the FNDS, are under the financial protection of DNT-MEF and are dedicated to the financing and promotion of development programs and projects. Table 14 summarizes the list of these funds, indicating the purpose and ministry of sectoral tutelage. Collaboration with the MEF should avoid duplicating the design of the FNDS with known problems that reduce the efficiency of funds as financial instruments and their effectiveness in policy implementation. Many of these problems are known informally by both DC and the involved partners working in coordination with DC. This knowledge should be used to guide this new mechanism, which - by the nature of the sources of funding it seeks to access - may be more complex than existing ones. It might be appropriate to consider joint evaluation of the existing funds mentioned in 4.3.3 and to use these results in the final drawing of the FNDS.

**188. The design of the FNDS should include coordination areas with the other national government institutions.** The FNDS has cross-cutting functions which, in order to bring added value, will lead to

close collaboration with each of the institutions in Table 14. The role of the MEF is to avoid overlaps and to provide consistency with other existing mechanisms (e.g. the FUNDAC and the FND, which may have some overlaps with the FNSD's attributions). In order to facilitate collaboration between institutions with different sectoral responsibilities, collaboration with the Prime Minister might be necessary, and already used models of coordination should be used for other mechanisms that needed intersectoral coordination (such as the National Social Action Council or Private Sector Monitoring Council discussed in Chapter 5 of this AFD).

Table 14: Public funds dedicated to the financing of development actions.

Public Funds	Object	Under the Supervision of / subordination
Investment Fund and Water Supply Heritage Fund (FIPAG)	Managing the public investment program in the water supply systems transferred to it.	Ministry of Public Works and Housing
Support Fund for Economic Rehabilitation (FARE)	Financially support the rehabilitation, development and dynamization of the national economy.	Minister of Planning and Development
Artistic Development Fund (FUNDAC)	Support initiatives, programs and projects in the field of artistic training and development and in the context of enhancement of cultural heritage	Ministry of Culture
Fund for Fisheries Development (FFP)	Financial support for private investment in the framework of the objectives of the fisheries policy	Ministry of Fisheries
Small Industry Development Fund (FFP)	Promoting the development of small-scale industry through financial initiatives to create, expand and stimulate small and micro-enterprises	
Marketing Fund	Apoiar financeiramente as actividades relativas ao desenvolvimento da comercialização e produção agrícolas	Minister of Industry and Commerce (subordination)
Fundo de Promoção Desportiva (FPD)	Promote and support projects and programs for the development of sport and stimulate other initiatives related to or contributing to its development	Minister for Youth and Sports
Roads Fund (FE)	Financing the conservation and development of public roads	Minister of Public Works and Housing
Energy Fund (FUNAE)	Develop alternative energy sources that are environmentally beneficial and increase energy availability under more accessible conditions for the public	Minister of Energy (Subordination)
Housing Development Fund (FFH)	Ensure financial support for government housing programs, especially targeted at low-income population groups, skilled labour, and young couples	Ministry of Public Works and Housing
Fundo de Desenvolvimento Agrário (FDA)	Promover o acesso aos serviços providos por instituições financeiras, empresas e associações e mobilização de outros recursos para apoio aos produtores. Promover parcerias entre instituições governamentais e outros intervenientes no sector agrícola.	Minister of Agriculture
National Research Fund (FNI)	Guarantee funding for scientific projects and innovation and technological development projects	Minister of Science and Technology
Universal Access Service Fund (FSAU)	Financing telecommunication programs and projects	National Institute of Communications of Mozambique (management)
Fundo Nacional do Turismo (FUTUR)	Promote the tourism product and ensure the promotion and coordination of initiatives and activities that respect tourism and stimulate those that relate to it or that compete for its appreciation	Minister of Tourism (subordination)

Source DNT-MEF

**189. Similarly, the design of the FNDS should take into account lessons learned at international level especially in areas that affect other national policies and objectives.** In the process of setting up the

FNDS some mistakes have already been made which show a certain lack of knowledge of basic aspects of the operation of these funds and which, for example, have interrupted processes of access to international financing<sup>78</sup>. The design of the FNDS should consider the resolution of some aspects of particular government interest, such as:

- *Financing source*. The design of the SDNDS should consider national experiences and remove known obstacles to administer: (i) non-reimbursable contributions from bilateral donors acting through their development aid agencies; (ii) multilaterally funded financing and mechanisms such as the GCF; (iii) public-private co-financing mechanisms and existing initiatives to promote PPPs and FDI;
- *Multiplicity of Executing Agencies*. The FNDS should function as a financial portal to receive and distribute funds from international funds, other governments, development partners and other climate change<sup>79</sup> financing mechanisms to the entire national government (central, provincial and district) and not exclusively to MITADER. The FNDS should also coordinate funding for actions to be implemented by the private sector for profit (in PPPs or mechanisms such as REDD +) and non-profit (NGOs and universities). In these latter areas, the historical experience of MICOA (which forms the basis of MITADER) was assessed as rather weak;
- *Governance, Transparency and Management*. Such an institution should be designed incorporating mechanisms to ensure integrity in the management of funds and the early (ex-ante) management of the risks of operations that may generate contingent liability. In addition, the design must incorporate transparent mechanisms that allow government accountability to donors, the Assembly of the Republic and citizens in general. The establishment of these systems of transparency and good management, built according to international standards, will convey confidence to cooperation partners, investors and international funds to quickly capitalize on the FNDS;
- *Promotion of private investment*. The fund can be instrumental in revitalizing activities that require private investment. The FNDS should include mechanisms to stimulate the financing of corporate social responsibility initiatives, public-private partnerships, and provide access to global capital markets that could mobilize funding for the private sector. The fund could even claim benefits from the carbon finance and trade market or co-invest with other funds such as the Social Security Fund (e.g. in REDD + projects). But MEF participation is necessary to analyse the risks of these operations prior to their approval.

#### Open questions that AFD could not analyse

190. In the meantime, these reforms are under way and it has not yet been possible to assess the extent to which the institutions' performance can meet the needs of the challenges. Sustainable development and rural development are cross-cutting areas that compete with a multiplicity of sectors and actors. This is one of the biggest challenges for MITADER, which will have to face it better than its predecessor. The CPEIR analysis indicates the existence of technology, knowledge and institutional gaps that limit MITADER's ability to meet its fundamental objectives. From the AFD the main issues that remain open are:

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<sup>78</sup> One issue was the automatic dissolution of FUNAB in the same decree creating the FNDS. It was not taken into account that FUNAB was about to complete the accreditation process to access the Adaptation Fund and that the new fund should restart a process that may take 3 years before accessing these funds.

<sup>79</sup> Such as the Adaptation Fund, the Global Efficiency Fund and EU Renewable Energy Fund, the Green Climate Fund and others.

- It is necessary to carry out cost estimates for the goals established in the ENAMMC and the PNDS and to integrate them in the process of reformulation of the ENDE analysed in Section 3.3;
- An important consequence will be to estimate in more detail private investment costs, especially those that contribute to mitigation (reduction of greenhouse gas emissions, to then include these estimates in the restatement of the NSDS;
- Another consequence is the need to determine the costs of loss and damage caused by the impact of climate change, the cost of inaction (for the whole economy), as well as the cost of adaptation measures and their contributions to the country's economy;
- The establishment of the FNDS does not eliminate the need to provide adequate clarity on provisions on climate finance sources, budget allocation targets and mechanisms for disseminating the delivery of climate finance. The role of the MEF remains important;
- National climate change policies are not very explicit about the financial mechanisms that can support implementation at the local level;
- National development plans are the main policy instrument guiding planning and budgeting, but integration of the climate component in these documents is weak or non-existent (in the ENDE, in the PQG and PES);
- • MITADER's capacity to engage private sector and civil society to co-finance initiatives that contribute to the adaptation or mitigation of climate change needs to be enhanced.

**191 Considering the country's vulnerability to climate change, strategy formulation and opportunity management of climate finance should be better analysed** in a more in-depth and multidisciplinary way, which is particularly necessary in relation to natural resource management (including waters, forests, soils, fisheries, etc.), which are also linked to climate change. It is very important to emphasize the importance of improving its management not only from a conservationist point of view of biodiversity and the environment per se (which could also bring great economic benefits to the country in the tourism sphere), but also from an economic perspective - since most of the population's survival depends on natural resources and ecosystem services - and at the macro level - all the investments made and to be made in the extractive industry, fisheries, agriculture, etc.). Other countries (such as Fiji) have developed well-designed green growth strategies (Green Growth Framework for Fiji: Restoring the Balance in Development that is Sustainable for our Future), which were soon used to define the main parameters and quantitative targets in the formulation of the National Development Strategy<sup>80</sup>. It should be considered a leadership for climate change at the highest level (the PM) for the country to maximize existing opportunities and avoid undesirable setbacks in its development due to the impacts of climate change.

#### 4.4.2 Non-tax Revenues

**192. The total revenue to be analysed in this evaluation as 'Non-tax' includes items accounted for in three different categories in the national accounts.** The first category is what in national accounts is Non-Tax Revenue, i.e.: miscellaneous service fees, other non-tax revenues and own revenues. The second category is Consigned Revenue which comes from the tax on a good or a service and is assigned to an institution to finance its budget. For example, the FNDS receives, for its financing, a quota derived from fees and fines set in the Land, Environment and Rural Development sector which is assigned to the Fund's financing. The third category includes the Capital Revenue, which is generated

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<sup>80</sup> See also UNDP Development Finance Assessment in Fiji, 2016.

by the income of the physical assets and the State's shareholdings. Table 15: unfolds the main subcategories of revenue accounted for within the categories proposed to be analysed.

**193. In the category of Non-Tax Revenues (as defined in the public accounts), Own Revenues are collected by the institutions themselves as payment for some sale of services.** These resources are intended for the management and use of the same institution that collects them. The mechanism of use foresees the delivery of the resources raised to the finances in the territorial directions of taxes. For the institution to have access to these resources, it has previously had to budget expenditure financed with this source of funds. Not having done so previously, these resources are integrated into the state treasury. Each institution that collects funds should make the estimate of own revenues that it will collect the following year. These estimates are often inaccurate, which is reflected in implementation rates, which are erratic. This mechanism provides incentives for non-reporting of these taxes and for use outside the control and tracking systems of public expenditure.

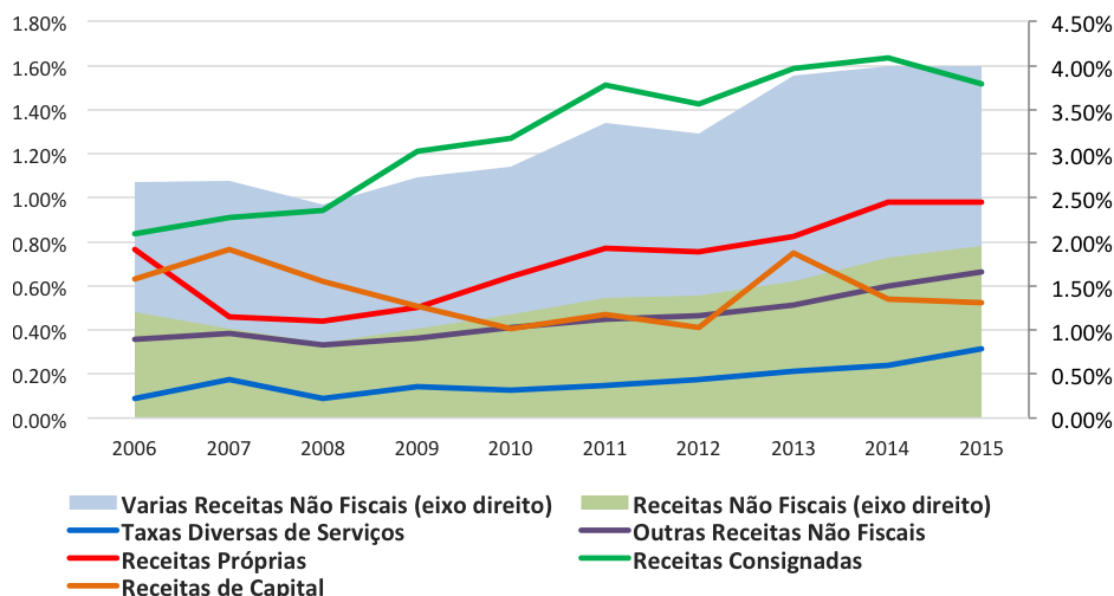
Table 15: Non-tax and recorded revenue.

Various 'Non-tax Revenue'	<b>Non-tax Income (National Accounts)</b>
	Miscellaneous Services Fees
	Other Non-tax Income
	Own Revenues
	<b>Consigned Revenue</b>
	Fuel Rate (Consigned)
	Customs Service Fee
	Chestnut Overestimation Rate
	Madeira Overvaluation Rate
	Other Consigned Revenues
	<b>Capital Revenue</b>

**194. The evolution of Total Non-Fiscal Revenues was much more moderate than that of tax revenue, and its growth potential should be analysed.** Figures 37 and 38 show the historical behaviour of the total of these revenues and their main components. Non-Fiscal Revenue (Non-Fiscal Revenues + Consigned + Capital) increased from 2.68% of GDP in 2006 to 4% of GDP in 2015, representing an increase of approximately 50%; however, tax revenues more than doubled over the same period (from 10.5% of GDP to 22.8%, see Section 4.3.1). Consequently, the contribution of this group of Non-Fiscal Revenues to Total State Revenue fell from 18.9% in 2006 to 14.9% in 2015 (Fig. 39).



Figure 37 - Non-fiscal revenue as% of GDP

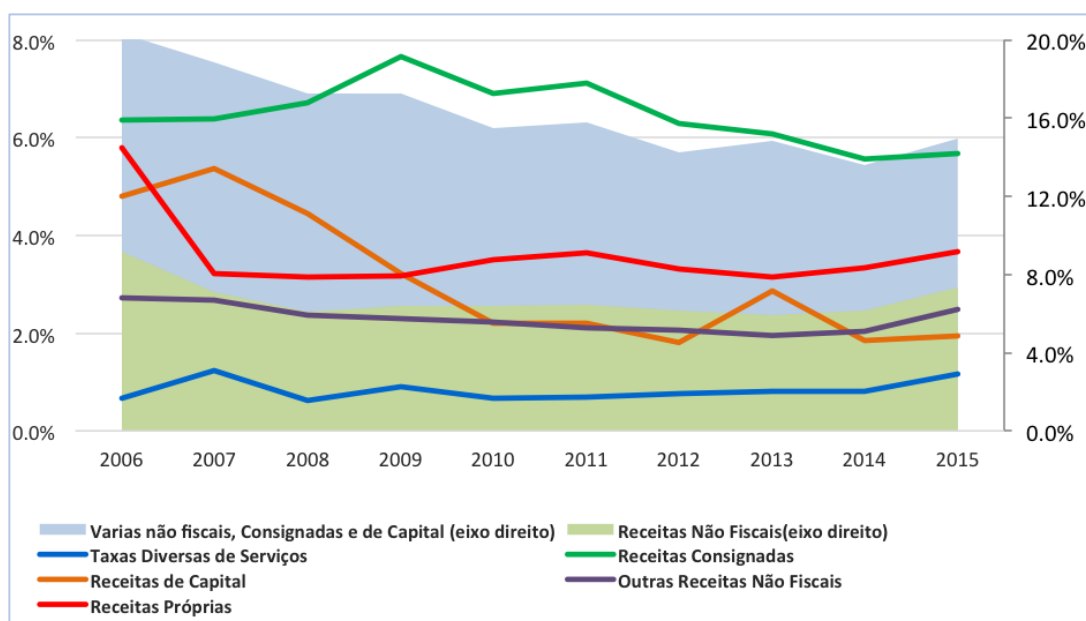


Source AT-MEF

**195. In the group analysed, the observed behaviour of some categories deserves special attention.** Analysing the evolution of Non-Fiscal Revenues (Non-Fiscal Revenues + Consigned + Capital) as a percentage of GDP (Fig. 39), it is worth noting the decreasing evolution of capital revenues (from 4.8% in 2006 to 1.95% in 2015) and own revenues (from 5.8% to 3.34%). Attention is also drawn to the low performance of payroll revenues, service fees and other non-tax revenues.

**196. The growth of this type of revenue is not defined in the PQG as a specific goal.** The PQG sets overall revenue growth targets, but there is no single goal deployed per revenue type. The logical focus of the attention of the Tax Authority and the MEF is the development of tax revenues, ie taxes on income, goods and services and other taxes (including mineral and oil production). Increased attention on non-tax revenues could offer possibilities to maintain the growth of total state revenue, since (as discussed in 4.3 1) it is very likely that tax revenues are about to reach their saturation point in the short term.

Figure 38 - Non-tax revenue as% of Internal Revenue



Fonte AT-MEF

**197. Progress in the collection of this type of revenue has points of contact with improving efficiency in public management.** The analysis in Section 4.2.3 shows that the State could seek improvements in the collection of non-tax revenues if it improves the quality of decentralized management. The Public Expenditure Assessments recently concluded in the education and health sectors coincide in pointing out that this management tends to increase unsustainable spending and pay little attention to the collection of fees. On the other hand, the analysis of the illicit flows presented below indicates that the lack of control by TA and Customs could be leading to significant resource leaks in the collection of assigned revenues.

**198. Specific short- and medium-term targets should be set for this type of revenue to force control and improvements in management quality.** Consideration should be given to reshaping taxation policy and seeking a more evenly distributed burden to prevent (or limit) the misalignment between revenue-generating sectors and actors as well as sectors and actors that generate growth. By setting targets on this type of revenue, the government could automatically trigger management improvement processes like those already in place with the other sources of revenue, which were met with great success.

#### 4.4.4 Illicit flows

**199. The containment of illicit tax evasion and the closing of important legal gaps could bring significant domestic revenues in Mozambique.** The misuse of transfer pricing in international trade and other private enterprise tax evasion practices generate the bulk of current tax revenue losses. Aggressive transfer pricing - the practice of inflating profits in low-tax jurisdictions and reducing profits in high-tax jurisdictions - is a problem that affects both developed and developing countries alike and falls into a grey area, since many practices are not illegal and national and international legal gaps are being abused.

200. This was highlighted in the Addis Ababa Action Agenda, where countries committed themselves to redouble efforts to substantially reduce illicit financial flows by 2030<sup>81</sup>. The statement admits that it is not possible for a single country to eliminate such practices and that broader global efforts are needed. It is estimated that, in 2013, USD 1,100 billion illicitly flowed out of undetected developing countries. These flows of illegal capital are the result of tax evasion, crime, corruption and other illicit activities (Kar & Spanjers, 2015). Governments cannot hold the culprits accountable, since there is no trace of such abuses. This, in turn, results in a significant reduction of resources available to finance development policies in these countries.

**201. International studies estimate that illicit flows left by the authorities of sub-Saharan Africa averaged US \$ 67.5 billion annually, representing 6.1 percent of the region's GDP.** The Global Financial Integrity (GFI) annual report, published in 2015 and referring to data between 2004 and 2013, estimated that developing countries lost an average of USD 785 billion a year, or 4% of GDP. During this period, this flow increased at a rate of 6.5% per year. While the region accounts for only 8.6% of total estimated illicit flows in developing countries, the same figure exceeds the overall average by 2pp of GDP, indicating that, in general, important resources for the financing of public expenditure.

Table 16: Unlawful flows out of the country compared to estimated values for Sub-Saharan Africa<sup>82</sup>

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	Total	Média
Adulterated commercial billing (outbound flow)	0	0	362	103	0	0	640	0	994	235	2.334	233
Estimated unregistered flows	0	0	0	0	0	23	0	44	0	25	92	9
Total Illicit Flows	0	0	362	103	0	23	640	44	994	260	2.426	243
Sub-Saharan Africa	32.550	51.874	56.351	77.012	78.599	85.002	78.038	74.281	66.678	74.593	674.977	67.498

Source: (Kar & Spanjers, 2015).

**202. Adulterated commercial invoicing accounts for most of these illicit capital flows and causes enormous damage to the economy and development of a country.** The adulterated commercial invoice refers to the false and intentional declaration of the value, quantity or composition of the products in the customs documentation and in invoices, generally for evading taxes or money laundering. The change in billing, which covers and includes the price change (mispricing) sometimes used in other studies. There are four basic categories of adulterated commercial invoicing: under-invoicing of imports, over-invoicing of imports, under-invoicing of exports, over-invoicing of exports<sup>83</sup>. Most of the adulterated commercial billing arrangements are made with the knowledge and approval

<sup>81</sup> The declaration states: "redouble efforts to substantially reduce illicit financial flows by 2030" with a view to eventually eliminating them, including combating tax evasion and corruption through enhanced national regulation and enhanced international cooperation. We will also reduce opportunities for tax evasion and will consider introducing anti-abuse clauses into all tax treaties. We will improve the practices of disclosure and transparency in countries of origin and destination, including by seeking to ensure transparency in all financial transactions between governments and companies to the relevant tax authorities. We will ensure that all companies, including multinationals, pay taxes to the governments of countries where economic activity occurs and value is created, in accordance with national and international laws and policies. "

<sup>82</sup> Illegal outgoing flows have two components: those derived from commercial billing adulteration (over-invoicing of imports and under-invoicing of exports) plus the estimation of flows not recorded in the Balance of Payments.

<sup>83</sup> A subfaturação das importações serve para evitar o pagamento de impostos sobre as importações e do IVA; a sobrefaturação das importações serve para legitimar a transferência de divisas para o estrangeiro e reduzir a base impositiva dos rendimentos das empresas; a subfaturação das exportações, como o caso anterior, serve para reduzir os lucros, e, portanto, a base tributável da empresa – os saldos são eventualmente depositados numa conta no estrangeiro; a sobrefaturação das exportações representa entradas de capitais de natureza oculta e que podem levar a uma redução dos rendimentos e da base tributável da empresa e que deveria ser pago ao governo do país importador.

of the seller and the buyer who are involved in the transaction. When the parties involved do not belong to the same company, they come to an agreement on the adulterated value that will appear on the invoice and how they will complete the transaction outside legal limits, often through a deposit into another bank account.

**203. In Mozambique, companies use adulterated invoicing of imports and exports.** The GFI publications explain that in Mozambique the values of under-invoicing of exports and those of over-invoicing of imports are generally comparable, suggesting that companies use both methods to transfer capital out of the country. The same source estimates that between 2004 and 2013, Mozambique lost an average of USD 243 million annually mainly due to the adulterated billing of outflows (see Table 16). This value is calculated by comparing information on the import and export figures reported by Mozambique and its trading partners and analysing the difference of the respective declared amounts. The GFI estimate of total accumulated illicit flows to Mozambique in the period 2004-2013 could be as high as USD 8.6 billion (Table 17).

Table 1: Comparison of estimated illicit flows in Mozambique (2004-2013) and sub-Saharan Africa

Country / Region	Falsification of Invoices of Import		Falsification of Export Invoices		Total Illicit Capital Receipts (b+c)	Total Outflows of Capital (a+d)	Gross Illicit Flows (a+b+c+d)
	Over-invoicing (a)	Under-invoicing (b)	Over-invoicing (c)	Under-invoicing			
Mozambique	1.172	4.383	1.878	1.162	6.260	2.334	8.594
Sub-Saharan Africa	229.748	379.545	352.515	252.643	732.060	482.390	1.214.450

Source: GFI 2015, pág. 42

#### Open questions

**204. It would be interesting to quantify the volume of these losses in terms of public revenue and as a source of funding.** These practices reduce corporate income and hence the value of the base taxable amount for the calculation of taxation. Assuming the nominal corporate tax rate to be 32%, this practice generated an average annual loss of USD 77.8 million, which could be equivalent to 1% of GDP or 3% of the total annual government expenditure. These estimates should be made with more capacity for process analysis, since in some cases there may be no transactions at all and everything is done on paper. With a small additional analysis, the internationally estimated percentages could be applied to known cases where such illicit activities, such as mineral exports, are already suspected, and to calculate with more precision the volume of lost revenue, and possibly recoverable amount with greater supervision of this type of actions.

#### 4.4.5 Revenue on Natural Resources

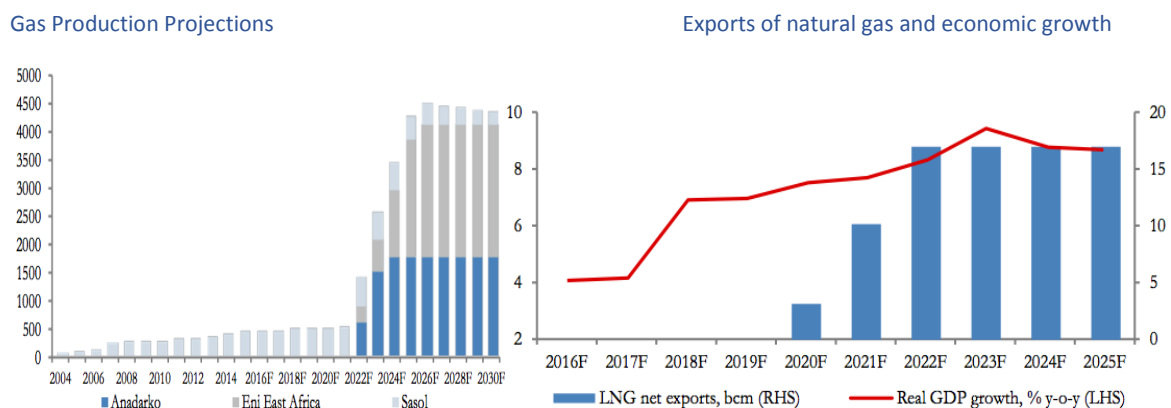
**205. A key part of the growth of future revenue collection may be related to the revenue generated from the exploitation of natural resources.** The exploration, research and production of mineral resources has had a remarkable and incomparable development during the last decade. After a period of low activity, Mozambique has been increasingly affirming in the world market as a preferred destination for multinationals in the natural resources sector.

**206. The government expects the emerging energy sector to generate higher export revenues, more attractive opportunities for foreign investors and a radical increase in GDP.** The prospects for growth in the development of its emerging energy sector are very promising. The government hopes to return to the path of rapid growth once companies holding exploration concessions in the Rovuma basin formalize final decisions on investments. This implies investments by the Italian company ENI of approximately 8 billion USD and Anadarko of 12 billion USD. In relative terms, the size of these

investments is almost the same as GDP, which in 2015 had reached USD 15 billion. Therefore, the multiplier effect of these projects on the economic and social structure can be large scale and have a significant impact on total tax revenue. Figure 39 shows government projections of future revenues that could be generated by expected expansion in natural gas production.

**207. If the future is potentially bright in relation to the production of hydrocarbons, the possibilities of the mining sector leave no doubt.** In addition to hydrocarbons, large-scale coal exports could also have a major impact on the country's current state of development. The Extractive Industries Transparency Initiative (EITI) reports in detail on the great potential wealth that Mozambique could exploit. This potential includes reserves of coal, heavy sands and other minerals such as gold, silver, copper, nickel, chromium, iron, titanium, manganese, fluorite, niobium, tantalum, tin and graphite. It also includes a large variety of gemstones and semi-precious stones such as rubies, tourmalines, beryl's, corindian, pomegranates (pyrope and almandine), quartz (pink, amethyst and agate), phosphates, feldspar amazonite), bauxite, ornamental stones (marble, granite and gabbro's of various shades and colours, dolerites), building materials (limestone, various aggregates, clay, sand, kaolin, bentonite) and diatomite's, among others.

Figura 1 - Os efeitos esperados da exploração do gás natural



Source: MEF and Bloomberg (MEF Oct. 2016)

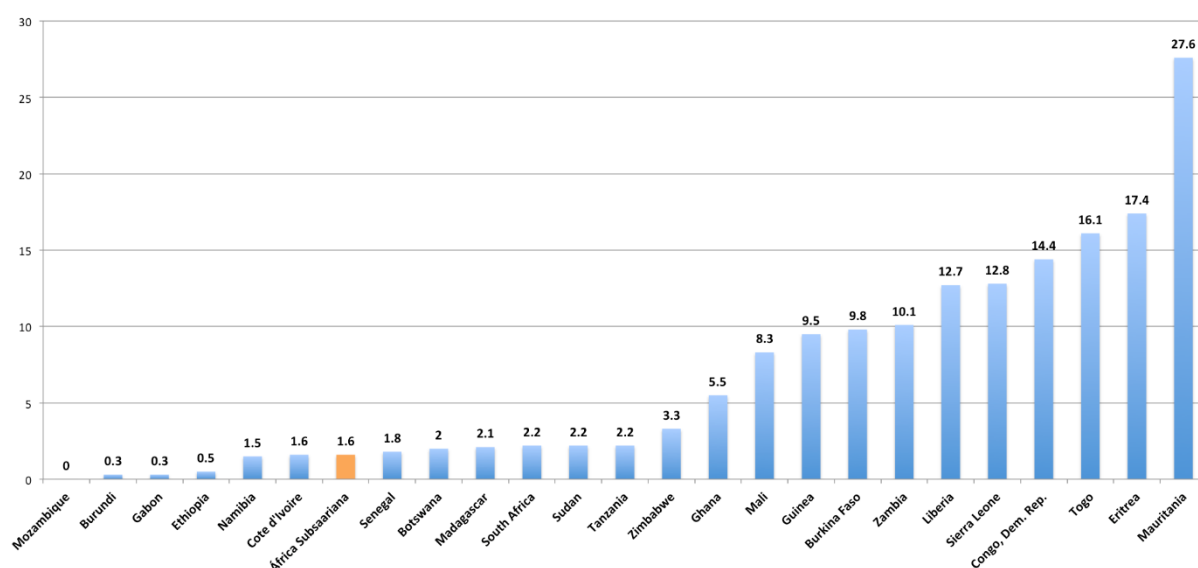
**208. The fiscal space that could lead to entry into the "gas-producing countries" could be very significant.** There is no way to analyse the real potential of this sector as a generator of medium and long-term revenues, but in other developing countries these revenues were very significant and perhaps higher than the amounts originally projected by the government. Other underdeveloped economies, such as Bolivia, which entered a boom in the exploitation of these resources only a decade ago, already earns 2 percent of GDP revenues from natural gas exploration. Likewise, the focus of this AFD is to analyse the whole of this type of revenue and how to improve its potential without closing the country's development possibilities to the development of a single sector.

**209. In view of this, the sustainable production of these resources and the control of the revenue generated by the extractive industry should be a concern and priority for the government.** Sustainable production of these resources could be the engine for generating wealth and accelerating development in the country. Clear management of revenue generated is the starting point for achieving this goal. The analysis presented in Chapter 2 states that the structure of the Mozambican economy has experienced important transformations, but it remains an agriculture-based (subsistence) economy. One of the reasons behind this situation lies in the fact that large-scale mining has been virtually non-existent until recently. Exploration and exploration of mineral resources has shown great momentum only in the last decade, although the raw material crisis has affected the

definitive expansion of this sector in recent years, but prospects of future expansion of the sector generate the need to review the picture policies and management of these resources.

**210. The international comparison indicates that the capacity to generate income related to the exploitation of mineral resources in Mozambique can improve significantly.** In relative terms, the country has achieved weak results in the exploitation of natural resources. The performance of Mozambique in relation to the main indicators measured by the World Bank to analyse income from the exploitation of natural resources (oil, coal, natural gas, mineral and afforestation income) is presented in Annex 2. The results of the comparison in obtaining mineral income presented in Figure 40 show simultaneously the great potential that the country could achieve and the weak performance of the existing policies. According to World Bank statistics, Mozambique earns practically insignificant income from this sector (almost 0% of GDP). On the contrary, the exploitation of these resources in countries with large mineral reserves amounts to up to two percentage points of GDP. The situation in neighbouring countries such as Tanzania (2.2% of GDP), South Africa (2.2%) and Zimbabwe (3.3%) indicates far higher performance than hitherto.

Figure 40 - Income from Mineral Resources Exploration in Mozambique and Africa in 2015 (as% of GDP)



Source: World Bank (see Table 34 in Annex 2 for full data of these indicators)

**211. The government should therefore more systematically analyse the cost-effectiveness of the existing system of promoting investment in capital-intensive projects.** As discussed in Section 4.3.1, the system for attracting foreign investment to the exploitation of natural resources is based on the provision of important tax benefits, the usefulness of which should be carefully analysed. The FDI analysis presented in the next chapter recommends a review of the cost-benefit of the results obtained with the tax benefits granted, and the performance of these incentives, comparing them with possible alternative schemes. There are other (non-fiscal) obstacles to the advancement of these investments, such as access to reliable and competitive power generation, and improved land and sea integrated.

**212. Circumstances exist to suggest that this could be one of the major sources of tax evasion in revenue generation.** Unfortunately, there are no studies that allow estimating the volume of tax evasion in this sector, which is presumed to be the largest generator of illicit flows and tax evasion in the country. Circumstantial evidence of isolated cases always points in the same direction, as, for example:

- Tax evasion claims from companies such as Kenmare Resources, which operates the heavy sands of Moma and uses a complex architecture based on subsidiaries in tax havens (discussed below in Section 5.3.3);
- The plundering of forests and the illegal export of precious woods, often denounced by environmental organizations, was recently demonstrated in the 'Trunk Operation', implemented by the government earlier this year<sup>84</sup>. The government estimates that illegal exports (mainly to China) cost the Mozambican state more than 530 million dollars between 2003 and 2013<sup>85</sup>;
- The duration of the recognition and exploration processes is not systematically analysed by the government, but - in interviews maintained - there seems to be a coincidence of the existence of an excessive duration (of several years) of this process. The government does not conduct a double check to see whether capital imports from these companies correspond to these activities or whether these companies (or their subsidiaries) appear as exporters (with information from TA and Customs).

**213. The government is taking individual steps, but a systemic solution is needed to review revenue, responsibilities for implementation and monitoring and control systems.** Recently, MITADER has enacted new rules for logging, which add to the current ban on the export of raw logs to exports of minimally processed items. Forest exports can only occur from specific port terminals, where they must be observed by accredited forest operators. The government will set new taxes and fees to be paid by the exporters, after consulting the timber market value every three months. The new system will benefit and grant tax privileges to companies that add more value to wood. The measures are well-intentioned, but they do not explain how - despite the existing ban - unprocessed wood continues to leave virtually without fiduciary, port or customs control. The way ahead should provide consistency in the definition of sources of revenue for the exploitation of natural resources and the revision of existing rates, analysing cost-benefit for the State. The ways of strengthening control systems and the design of coordinated measures should also be explored to ensure the best success in the implementation phase.

**214. Income monitoring systems in these sectors should be redesigned to be more effective and transparent.** The government should consider designing a tool to control and verify the correct application of existing law and control of tax evasion in this sector. The decentralized participation of various government actors (ministries, public companies and other provincial and municipal entities) does not ensure consistency or the best possible results. The MEF could design new follow-up and double-checking processes by strengthening the TA and Customs management capacity and integrating existing information.

**215. The additional usefulness of promoting transparency in the management of revenues generated by extractive industry enterprises is to increase social control and reduce the risk of misappropriation, and especially of corruption.** The country's accession to the Extractive Industries Transparency Initiative (EITI) was an important step in this direction. The work has been aimed at improving the various internal instruments already in place to promote good governance, including transparency and corruption prevention, and to ensure that government payments and receipts from the extractive industry are published regularly and in the public domain. But the government seems

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<sup>84</sup> In the operation, government brigades inspected wooden yards throughout central and northern Mozambique and exposed more than 400 cases of illegal logging behaviour.

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to have discontinued this work and the latest report available (corresponding to fiscal year 2013) is from the year 2014.

**216. Despite the interest of the DFA team, it was not possible to get MIREME's collaboration to work together and analyse these flows in more detail.** The MIREME data could have been valuable in projecting and estimating future revenue collections in this sector, as well as in analysing tax evasion situations. It is recommended to carry out some additional research to obtain technically sustained information on: (i) the potential revenue in the event of development of this sector in the short and medium term; (ii) the main factors limiting investment in this sector (inadequate incentives, infrastructures, promotion, etc.), (iv) ways of estimating and limiting tax evasion of companies operating in the sector.

#### 4.4.6 Other Options to Explore

##### Use of Sovereign Funds.

**217. Mozambique could consider using such mechanisms when the expected boom in oil and gas revenues is reached.** The wealth generated by extractive industries in developing countries has the potential to contribute to considerable social progress, but natural resources are particularly difficult to manage effectively. The large and volatile revenues generated by natural resources are notoriously susceptible to income-seeking and corruption, and can significantly impair the institutional structures and processes that govern them. Thus, natural resources have historically become a curse, more than a blessing, for many countries around the world<sup>86</sup>. The case of Mozambique seems to be in tune with these problems and perhaps the mechanism could be considered as an aid in the process of exit from the crisis.

**218. Countries use SWFs to ensure the effective use of extractive resources and to balance current and future needs.** There are good examples in the Asia-Pacific region, such as Timor-Leste and Papua New Guinea, which have each established good mechanism that allocate a certain level of resources to current spending, safeguarding assets for future revenue streams. The issue of transparency is also critical, since transparency supports accountability mechanisms for both generation and use of resources. Some countries are adopting the best practices that benefit from the Extractive Industries Transparency Initiative (EITI) to guide the transparent and accountable management of extractive sector resources.

#### **Box 4: The Case of the Sovereign Fund of Timor-Leste<sup>87</sup>**

In 2005, Timor-Leste established an oil fund to manage government oil sector resources and protect the economy from price and production variations. The Timorese economy is highly dependent on oil. In 2010, oil revenues accounted for 73% of national GDP. The fund receives all revenue from the oil sector and is structured so that transfers to government cannot exceed ESI without approval by parliament. The ESI is calculated based on forecasts of future oil prices (from the US Energy Information Agency) and projections of oil production. In December 2012, the fund's assets totalled \$ 11.8 billion, equivalent to \$ 10,700 per person in Timor-Leste.

In practice, parliament has occasionally approved excess withdrawals above ESI levels. To be able to do so, the government must first carry out an audit on the impact of excessive withdrawals on the future ESI and justify why excess withdrawals are in the country's long-term interest. This has been an area of some debate and at its core are issues regarding appropriate levels of investment and alternative sources of revenue. The ESI model implemented by the Petroleum Fund is based on the Norwegian Sovereign Wealth Fund model. However, investment levels in Timor-Leste, a country with a recent history of conflict and without a long history of public investment, may be justifiably higher than in an advanced economy such as Norway.

<sup>86</sup> Stratta N 2015

<sup>87</sup> Ibid



Transparency has been one of the key features of the Timorese Oil Fund. Timor-Leste is a signatory of EITI and a member of the International Working Group for Sovereign Wealth Funds. Detailed information about the fund's investments is published in annual, quarterly and monthly reports. They are requirements in law for regular reporting and auditing. Timorese experience in managing its oil resources has been widely regarded as a success. The fund has successfully protected the government and the economy from fluctuations in international markets and is also highly regarded in the international rankings for governance and effectiveness of sovereign wealth funds. This is an exceptional achievement considering that it was developed in a post-conflict context and in a country with very low institutional capacity.

**219. The availability of extractive wealth should be used to define 'deadlines' for the country to achieve fundamental results and alternative development models.** The availability of these resources is in most cases limited, and this time limitation should be used as a tangible timeframe for the country to achieve a model of alternative development and sustainability after depletion. Time is a critical variable that is not always used responsibly as it should. The worst-case scenario for any 'raw commodity' country is to indulge in the temporary abundance of resources and exhaust without achieving a sustainable development model and a well-developed society. This is, for example, the main risk for Timor-Leste, since its oil reserves will only last until 2024; despite the prudent management of its resources, public policy progress is slow, the economy is still heavily dependent on oil and progress to achieve the most basic development results desired has been extremely weak.

#### Aid for Trade (AfT) or Aid for Trade

**220. Since 2005, Aid for Trade has played an important role in facilitating the integration of the least developed countries into the multilateral trading system.** It is part of Official Development Assistance (ODA), targeting trade-related programs and projects, with the aim of mobilizing resources to overcome constraints faced by developing countries (WTO). It covers six areas: (i) trade policy and regulation; (ii) commercial development; (iii) trade-related infrastructure; (iv) construction of productive capacity; (v) trade-related adjustment; and (vi) other trade-related needs. Trade policy and regulation, trade development and other trade-related needs are classified as trade-related assistance, and the other three areas are grouped together as productive capacity and infrastructure construction. As aid to trade captures a wide range of trade-related activities, it is not easy to measure.

**221. The Addis Ababa Agenda for Action proposes to streamline Aid for Trade in developing countries, in the least developed countries.** The declaration proposes an improved integrated framework for trade-related technical assistance to the least developed countries. The focus of aid will be on technical assistance and the improvement of trade and transit logistics to enable developing countries to effectively implement policies and regulations to facilitate transport and trade and diversify their base exports. The statement also emphasizes the need to control illegal wildlife trade, illegal unreported and unregulated fishing, illegal logging and mining. Countries have stated that they strengthen global support for efforts to combat hunting and trafficking of protected species, trafficking in hazardous wastes and trafficking in minerals, including strengthening national regulations and increasing the capacity of local communities to seek support. The monitoring, control and surveillance capacity of fishing vessels are also highlighted to effectively prevent, deter and eliminate illegal, unreported and unregulated fishing through institutional capacity building.

**222. There is little information available to analyse the use and potential of this mechanism in Mozambique.** A 2011<sup>88</sup> study placed Mozambique among the top 10 beneficiaries of Aid for Trade commitments for Africa (with Egypt, Ethiopia, Ghana, Kenya, Morocco, Tanzania and Uganda) and

<sup>88</sup> Global Review of Aid for Trade 2011: African Case Stories (UNECA/WTO/OECD/UNECA/AdB)

estimated that the country received AfT commitments in the amount of US \$ 354 million between 2002 and 2005, US \$ 446 million between 2006 and 2009 and US \$ 371 million between 2006 and 2009. During the AFD, detailed information on this flow was not possible. Adopting a focus on AfT could be an option that would lengthen the permanence of ODA investment as donor interest begins to decline.

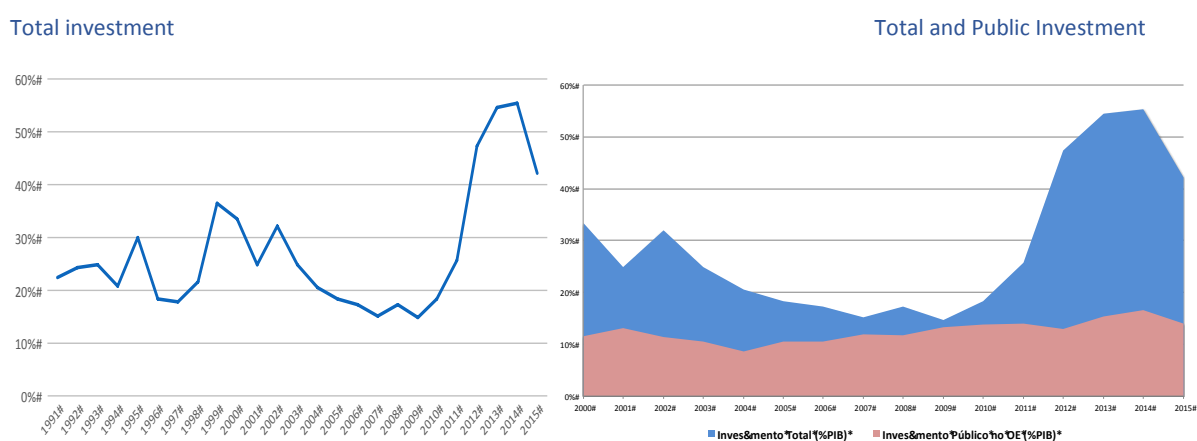
## 5. Private Finance and Main Flows

### 5.1 Private Sector Contributions to Sustainable Development

**223. Private Sector Development (DSD) is identified as a high priority in key country strategic documents.** The ENDE proposes a structural transformation of the economy by investing heavily in the industrialization of the country, and defines the DSP as one of the two main instruments to achieve these objectives, with emphasis on the development of small and medium enterprises. PEFP 2016-2019 places the development of private investment as a top priority in the list of objectives, and defines as priority actions: (i) to promote the country as a preferred destination for investment, and (ii) to contribute to the development of national business (see Chapter 3).

**224. The levels of investment in the country describe a history consistent with these priorities.** Figure 41 shows the growth of total investment, which during the post-war and reconstruction phase fluctuated with investment rates hovering around 25% by 2001. There followed a stabilization period with a reduction in investment weight until 2007 -08, to enter the last period, with a strong expansion of investment, which exceeds 50% of GDP. This latest expansion was mainly due to foreign direct investment targeting major projects to exploit coal deposits and to the (now completed) exploration phase of natural gas in the Rovuma basin, but also targeted to other companies. After 2013, the macroeconomic situation deteriorated, with a resurgence of internal conflict, which undermined the climate of peace, the free movement of people and goods along some roads and railways, which affected the profitability of business and the dynamics of the investment. The figure also shows the variations in private investment in total investment.

Figure 41 - Investment levels as% of GDP



Source:: INE, BDM, DNPO-MEF. Authors' calculations

**225. The National Development Strategy recognizes the importance of agriculture as the basis of national development and that its exploitation results in increased national wealth.** As presented in Chapter 2, the Mozambican economy is essentially an agricultural economy: over the last decade, the average contribution of the agriculture sector to GDP has been around 25%, but it has accounted for about 70% of the population living in rural areas. The NSDS defines two priority actions to facilitate

structural transformations: (i) increased productivity and (ii) increased commercialization of agricultural production. To this end, it is proposed to increase research in the area of agriculture and livestock, and the dissemination of modern methods through technical assistance to stimulate the smaller local producer, as well as increase the supply and reduce the costs of agricultural instruments and inputs, improved access to infrastructure and small-scale irrigation, and river basin management. Finally, the expansion of credit to agriculture, eventually with specific reduced-risk products, and the enhancement of logistics infrastructure to improve access to markets, intermediate - processing and final consumption, completes the strategic vision for the development of the sector.

**226. If Agriculture is the basis of development, ENDE sees the manufacturing sector as the driving force of the economy.** The sector contributes to 8% of GDP. Labour productivity in the manufacturing sector has remained stable over the past 10 years. However, the contribution to GDP and the export composition of the manufacturing sector increased, which is explained by the good performance of megaprojects, which nevertheless absorbed a limited number of workers. As explained in the previous chapter, these megaprojects receive important tax incentives and other subsidies that limit their participation in government revenues.

**227. The ENDE proposes five areas to prioritize the expansion of industrial activities in the country:** (i) agro-industry, therefore, the transformation of agricultural production and production of inputs for that activity, (ii) manufacturing for the productive chain upstream and downstream from exporting mining. (iii) manufacturing to meet domestic market demand for durable and non-durable goods, aiming to replace imports, (iv) manufacturing of construction materials, to meet the expansion of housing and infrastructure construction market (v) the industry to produce electricity. For the activities to be successful, ENDE envisages a set of actions: (i) strengthening the entrepreneurial fabric of MSMEs; (ii) stimulating them to assimilate more complex technologies, (iii) developing human resources capacities, and (iv) eventually stimulating and protecting the industrial sector from becoming competitive in both the domestic and international markets. ENDE also proposes that, by having the intrinsic resources available for the development of a tourism sector, it will need support infrastructures and a set of links with other sectors.

**228. The Mozambican business sector is highly segmented.** According to data presented by IPEME (summarized in Table 18), there are practically no large companies (1.3% of companies) or medium-sized companies (1% of the total) in the Mozambican economic fabric. Most of the business sector is made up of microenterprises (78.3% of the total) and small enterprises (19.4%). MSMEs account for 98.7% of the productive fabric, but employ only 47% of active workers. Small businesses account for 60% of turnover, although they account for only 20% of business actors

Table 18 - Distribution of private sector enterprises by size

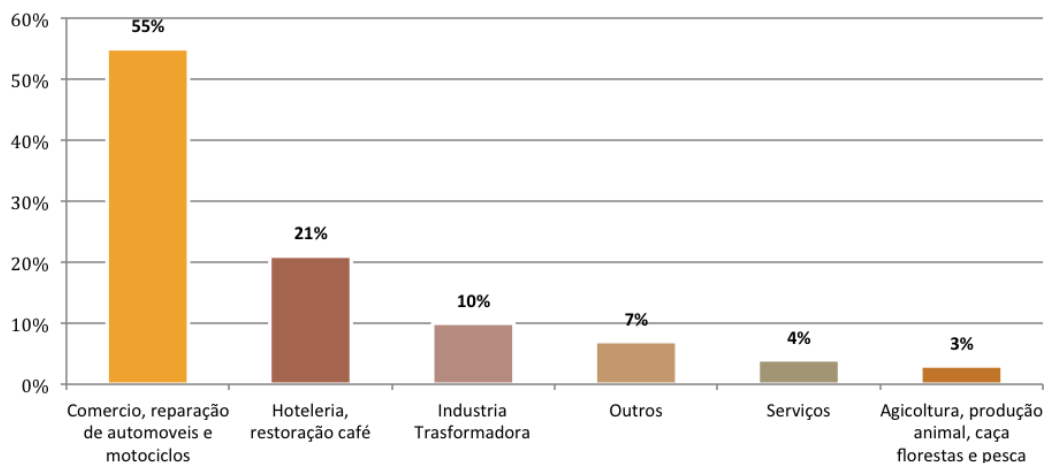
1.	% do total	Number of employees		Volume of business in MZN	
		de	até	de	até
Micro company	78,3%	1	4	-	1.200.000
Small business	19,4%	5	49	1.200.000	14.700.000
Midsize Companies	1,0%	50	100	14.700.000	29.970.000
Big companies	1,3%	100		29.970.000	

Source: IPEME

**229. The distribution of MSME by area of activity indicates a great disparity with the priorities established in the NSDS.** According to data presented in Figure 42, the majority (55%) of these

companies work in the car trade and repair sector and 21% in the tourism, lodging and catering sector. Only 10% of companies are manufacturing and 3% of companies have activities in agriculture, forestry and fishing.

Figure 42 - Distribution of MSME by sector



Fonte: IPEME

**230. The geographical distribution of companies also shows important regional asymmetries.** The IPEME data indicate a clear predominance of the number of companies located in the South (52%), with respect to the centre of the country (36%) and in the north (12%). These asymmetries are also reflected in job creation (61% in the South, 28% in the centre and 11% in the North) and in the distribution of turnover (80% in the South, 14% in the Centre and 6% in the North). The turnover ratio by the number of employees - is about double the centre and north.

**231. Performance studies indicate large variations in company productivity.** According to the latest survey on manufacturing firms (Schou & Cardoso, 2014), the most of companies - artisanal and small scale - produce with low levels of technology and market their products in the same company is located. There is a minority of exporting companies that are expected to perform well across a range of indicators. The links between companies in value chains are essential to achieve multiplier effects, and in Mozambique these links are weak. An analysis of the DySAM<sup>89</sup> multipliers confirms these characteristics. The multipliers to produce staple foods and agricultural products and agricultural activities are higher in value. Those related to manufacturing production and service provision have an intermediate value, while those related to the capital-intensive industry (mining, metallurgical industry, energy sector) have very low values, which indicates minimal links with the rest of the economy.

**232. Prospects for the future remain positive despite short-term uncertainty.** The economic crisis has had major negative effects on private investment, but the outlook in the medium and long term remains good. The government expects to make a significant boost to the multiplier effects of the mega-investments in the Rovuma basin. However, to achieve significant effects, it will be necessary to work to reduce the aforementioned dualities and asymmetries and to strengthen the weaknesses and specialization of today's business fabric.

<sup>89</sup> (Stella, Assessing employment opportunities of the Mozambican economy: A DySAM analysis., 2014).

**233. To achieve the NSDS objectives, it will be necessary to integrate effective policies and measures in several areas.** ENDE points to the need for a harmonious development and a structural change in the economy, an inclusive growth that, among other things, focuses on human capital and training. One of the recurring weaknesses of MSMEs is training, both in business design and strategic vision, as well as in the organization of accounting (to gain access to formal credit), to the training of the workforce. The solution to these aspects combines at least three different types of training and policies that must be coordinated correctly. The newly created Agency for the Promotion of Investments and Exports (APIEX) will have to collaborate closely with IPEME to develop plans to promote the development of MSMEs that guarantee training, but that are monitored for constant measurement of results. These plans must accept the reality of rural-urban and formal-informal economies and the most effective mechanisms for poverty reduction.

**234. Extractive industry is a reality of the country, but it is also one of the areas of greatest potential for economic growth.** The current weight of the extractive industry in GDP is limited, not exceeding 4% in 2014. The capital-intensive nature, dependence on foreign operators, and the (very) limited level of linkage to the rest of the fabric, both economic and social, are a challenge. ENDE points to the development of local transformation from the export of primary products to the export of finished products. To achieve these objectives, however, significant investment in large-scale infrastructures will be required.

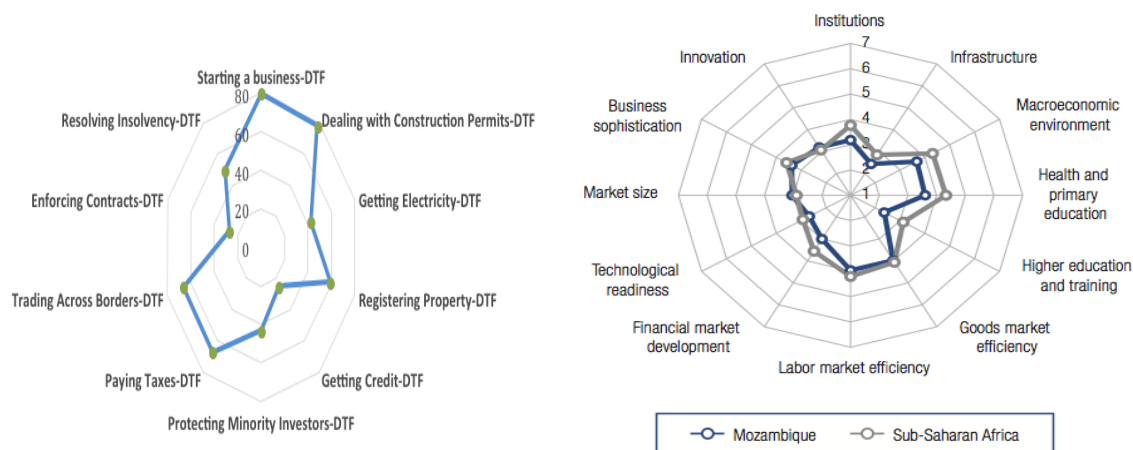
## 5.2 Opportunities and Challenges for Private Sector Development

**235. International comparative studies coincide in assessing the conditions for developing Mozambique's business and international competitiveness as very weak.** International assessments of the conditions for the development of the private sector provide an imperfect measure of a complex and multidimensional concept, but they provide a general picture of the main intervening factors and facilitate comparisons between countries. Mozambique's performance under the Ease of Doing Business framework, developed by the World Bank, places the country in the lowest places in the world ranking (in position 137 among 189 countries evaluated). The analysis of the competitiveness of the World Economic Forum presents a very similar reality: Mozambique places 133 of the 140 countries analysed and, in both cases, Mozambique is below the sub-Saharan Africa average. 236. The reasons for this poor qualification are manifold. Figure 43 summarizes the performance of key indicators measured in the Ease of Doing Business. The major challenges, where over time there have been no substantial changes, are: (i) compliance with contracts (position 185 in 189, SADC only has a worse performance), (ii) access to financing (position 157; in SADC, only Angola and Madagascar have a worse position), (iii) access to electricity (position 168, only four countries in the region perform poorly) and (iv) protection of minority investors (position 132; worse performance). The following: property registration (where it takes 40 days / man to register a property), pay taxes (where 37 different taxes are paid and 200 hours a year are required to pay them), and international trade (where to export are 78 days), are areas in which Mozambique has ample room to improve.

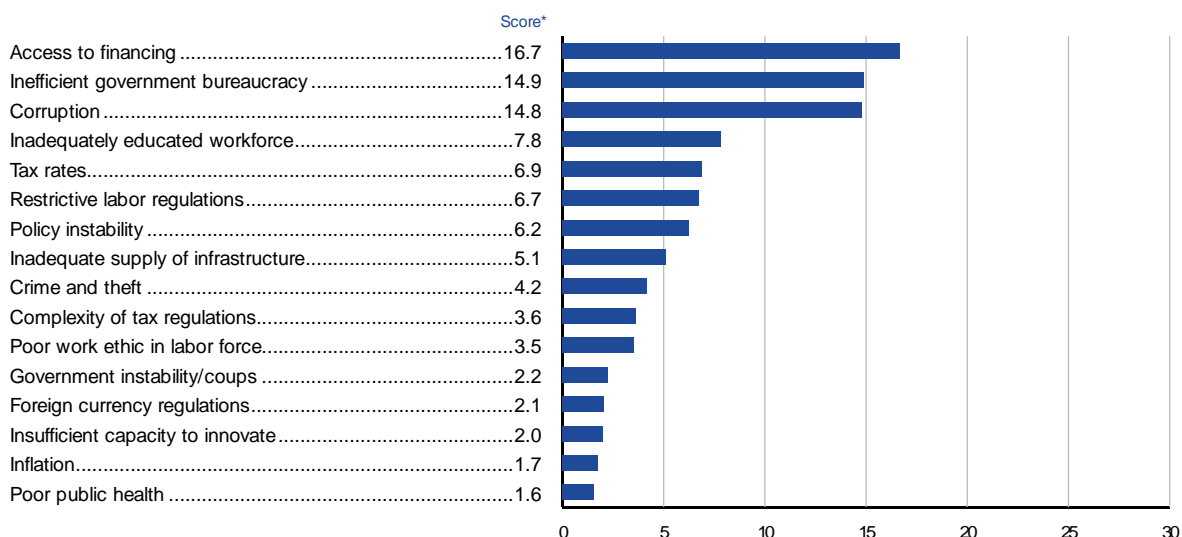
**236. The reasons for this poor qualification are manifold.** Figure 43 summarizes the performance of key indicators measured in the Ease of Doing Business. The major challenges, where over time have not been substantial changes are: (i) compliance with contracts (position 185 in 189, SADC, only Angola has a worse performance), (ii) access to financing (position 157; in SADC, only Angola and Madagascar have a worse position), (iii) access to electricity (position 168, only four countries in the region perform poorly) and (iv) protection of minority investors (position 132; worse performance). The following: property registration (where it takes 40 days / man to register a property), pay taxes

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Figura 5 - Resultados das Medições Internacionais de Competitividade em Moçambique<sup>90</sup>  
 indicators of the Ease of Doing Business 2017 (WB) Mozambique Competitiveness Factors, according to the WEF



Factors that compromise competitiveness in Mozambique (WEF)



**237. The factors affecting competitiveness measured by the WEF are similar and complementary.** The factors that most compromise competitiveness according to the WEF assessment are: (i) access to financing; (ii) inefficient government bureaucracy; (iii) corruption; (iv) inadequately qualified workforce; (vi) tax system; (vii) labour regulations; (viii) political instability; (ix) inadequate infrastructure and (x) crime and robbery (Figure 43). For each of these dimensions, the analysis provides a high level of detail of the elements that justify the punctuation, which are reproduced in the annex<sup>91</sup>. These results are compatible with other international studies, such as the Business Survey conducted by the World Bank, which in the case of Mozambique only provides information from the year 2007.

<sup>90</sup> Further data and results from previous measurements can be found in Annex II.

<sup>91</sup> For example, the assessment of infrastructures offers specific counts for the following dimensions: roads, railways, ports, airports and air transport, availability of air communication, electricity, availability of mobile and fixed telephony.

**238. There are coincidences and some considerable divergences with the diagnosis at national level of the problems that limit the development of the private sector and the consequent prioritization of actions.** The ENDE places the limited financing capacity of the business sector as the focus of action, pointing, among other things, to the creation of the Development Bank to find alternatives to the financing challenges of development priorities. ENDE also places the need for the development of energy and transport infrastructures with dynamic services for the development of the private sector. Other key points of international assessments do not, however, seem to have the same emphasis on national strategies.

**239. The government has begun a long-term effort to address these obstacles.** To this end, in 2008 the government developed the first Business Environment Improvement Strategy (EMAN I 2008-2012), which was soon succeeded by EMAN II (2013-2017), and will soon have a new version (EMAN 2018 -2022). The major challenge to remove these barriers is the multidimensional nature of the problem and the need for multi-sectoral intervention of the solutions that must be applied, which require high levels of central and decentralized government coordination. The implementation of EMAN strategies considers two levels (central and provincial) and organizes the supervision of the central bodies through an Inter-Ministerial Group for the Removal of Investment Barriers (GIRBI), which reports to the Council of Ministers. At the provincial level, the Provincial Governor runs a Provincial Inter-Sectorial Group (GIP), which has the task of ensuring the implementation of the actions and the fulfilment of the goals in its area of responsibility. The focal point of the national government for the implementation of the EMANs is the Ministry of Industry and Trade (MIC), which established the National Directorate of Support to the Private Sector.

**240. In the new EMAN, the government incorporates lessons learned from the implementation of the previous EMANs and strongly focuses on an improved system of working with the private sector.** During the implementation of the previous EMANs, the dialogue with the private sector experimented with different approaches to achieving a productive and efficient format for discussing and promoting reform priorities. The current system establishes a Monitoring Council with the Private Sector, which - together with the MIC - focuses on the definition and monitoring of the annual implementation of a matrix that focuses on 30 priority actions. To this end, the Council works in regular contact with the MIC and meets 3 times a year with the Prime Minister and once a year with the President of the Republic. This system greatly improves previous approaches, which had lists of up to 300 points that blended highly strategic issues with easy-to-solve issues.

**241. A pending issue in the implementation of the new EMAN is the prioritization - along with the private sector - of strategic reforms and large-scale investments.** The agenda set for the functioning of the Monitoring Council with the Private Sector is highly operational, which is an advantage to improve implementation of specific actions. One of the outstanding challenges is to define a similarly productive system of dialogue to prioritize highly strategic issues, such as large-scale infrastructure improvements (ports, roads and waterways, energy, telecommunications). The results of this prioritization should immediately affect the formulation and implementation of other policy instruments, such as the Integrated Investment Plan (IIP), the priorities of the Strategic Plan for the Promotion of Private Investment (PEPIP), the priorities agenda the promotion of PPPs and the strategic planning of sectors, such as education, among others. For example:

Exploitation of the large Moma heavy sand reserves (for the extraction of ilmenite, zirconium and rutile) or the realization of the enormous potential of the exploration and industrialization of graphite demand investments to increase the generation of electricity (at competitive costs) and investments large-scale infrastructures (ports, roads, etc.);

- Although the performance of the education sector is one of the best in the public sector, international competitiveness measurements coincide that poor qualification of the labour force is one of Mozambique's top five constraints.

**242. An added value of the adoption of a National Integrated Financing Framework (IFNF) is to be able to address these interactions in a strategic and systematic way.** Adopting an integrated approach such as that described in Chapter 1 of this AFD will make it possible to directly link macro national priorities to the development of key sector programming and individual funding sources.

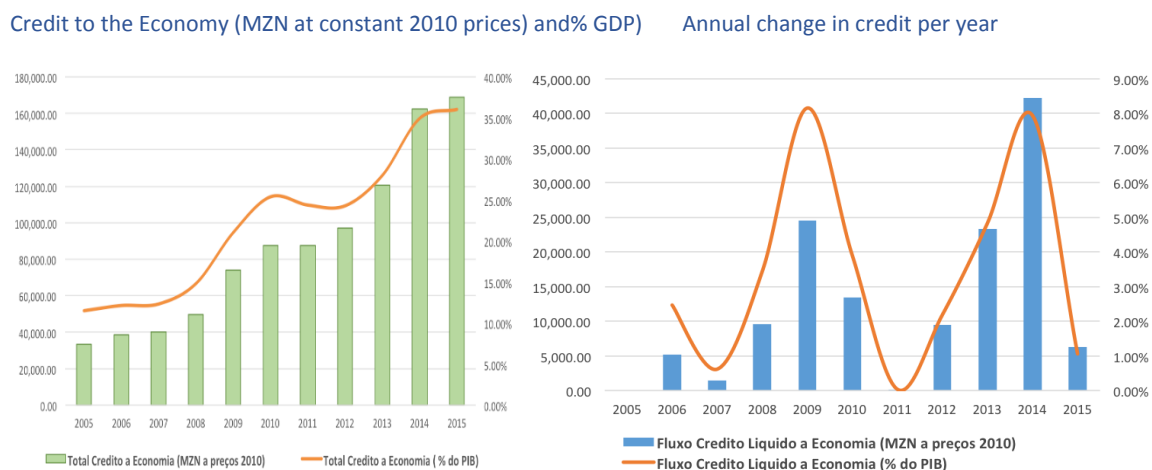
### 5.3 Evaluation of Main Private Flows

#### 5.3.1 Private Financial Sector

**243. Since finance is one of the main obstacles to private sector development, the functioning of the financial sector should be studied in depth.** The financial sector represents the set of structures that should work to harmonize supply and demand for capital. It is important to know better how it was and what the current potential of this system is, and explore how to guide the development of the system to ensure the financing of the priority areas of the country. Unfortunately, there are no systemic analyses that allow an evaluation of the main areas of reform and possible measures to solve the situation. An analysis of the functioning of the financial system should cover the following structures: (i) financial institutions, such as banks and insurance companies; (ii) financial markets, such as equity and bond markets. A comprehensive analysis of the functioning of the financial sector, which goes beyond the purposes of this report, should consider the following aspects:

- **Financial Depth:** analysis of the size of financial institutions with respect to the market;
- **Access:** the degree to which individuals can access and use financial services;
- **Efficiency of intermediaries and financial markets** in the intermediation of resources and facilitation of financial transactions;
- **Stability of financial institutions** and markets.

Figure 44 - General Data of Internal Credit



Source: Banco de Mozambique. Authors' calculations

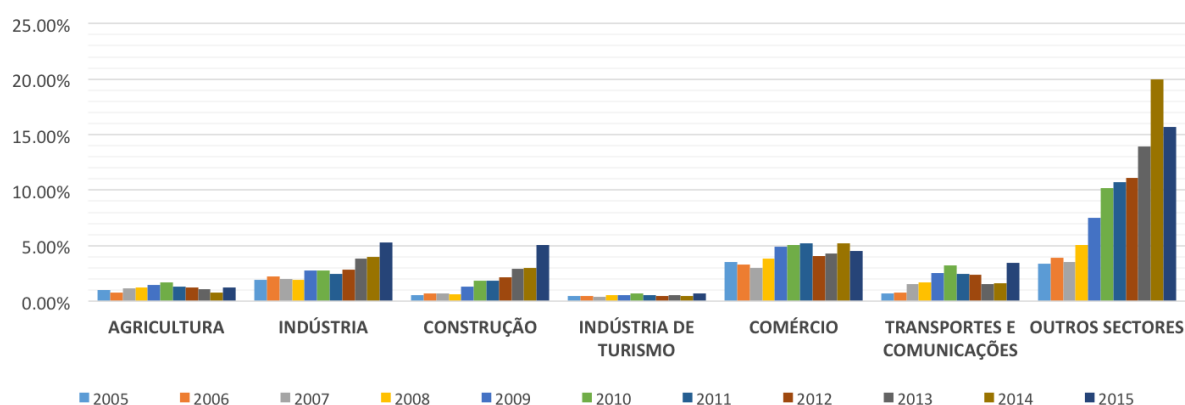
**244. Domestic credit to the economy as a whole grew irregularly in the period under study.** Figure 44 shows the evolution of domestic credit to the economy, which grew by an average of 22% in the period, from 11.5% of GDP in 2005 to 36% in 2015. The annual growth rate was not uniform: there was a strong acceleration between 2007 and 2010, coinciding with the initial period of coal mining projects. Soon after, in 2011, when the crisis of the international economy felt its effects, there was a



sudden slowdown in expansion, to accelerate again in the triennium 2012-14, the prospecting period in the Rovuma basin, and again slowdown in 2015.

**245. Credit alignment with some of the key development sectors, such as the industrial and construction sectors, is limited.** Figure 45 shows the evolution of credit by sector over time. Note that the most dynamic in obtaining credit are a set of unspecified sectors (other sectors), which increased from 3.5% in 2005 to 20% in 2014, down to 15.7% in 2015. The trade sector maintained a stable level of credit (as a percentage of GDP) of around 4,25% of GDP. Loans to industry increased in the period 2005-2015, with two subperiods: 2005-11, where the weight of credit to industry stood at around 2.9%, and the successive period, during which it grew until to reach 5.3% by 2015. The construction sector reached close to the industrial sector in 2015, but grew faster and more steadily from 0.5% of GDP.

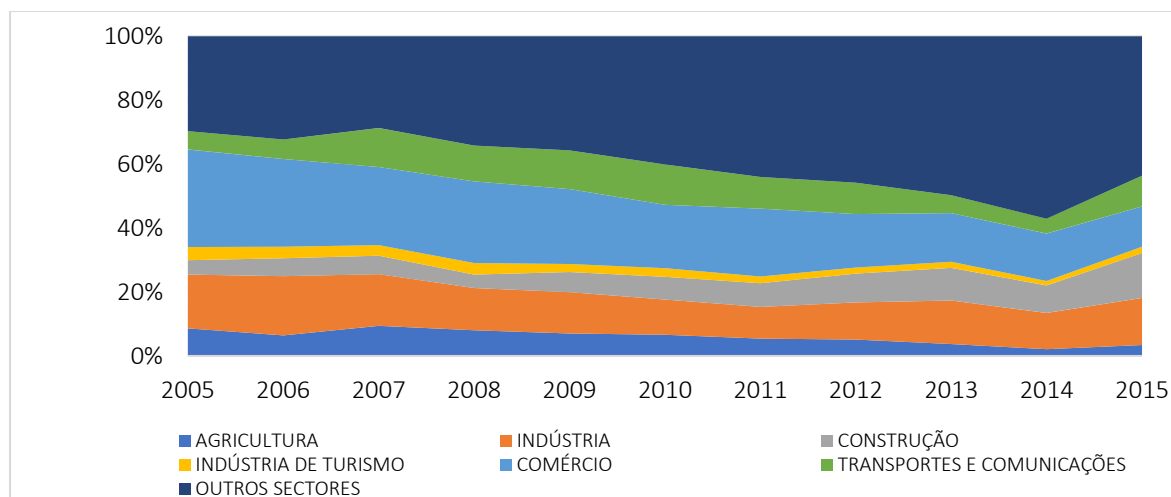
Figure 45 - Distribution of domestic credit by sector and by year (as% of GDP)



Source: Banco de Moçambique. Authors' calculations

**246. Other data seem to demonstrate an apparent disconnection of domestic credit from the poorly performing agricultural and tourism sectors.** The Agriculture sector raises credit on average by 1.2% of GDP, and the tourism sector, which raises annual credit on average by 0.5% of GDP. The two sectors are strategic in the country's development plans. Part (b) of Figure 46 describes a coherent history but points not only to low levels of credit to sectors considered key because of their potential and impact on the economic development of the country, but also shows that during the last 10 years have not been observed changes in credit flows to these sectors.

Figure 46 - Evolution of credit distribution by sector.



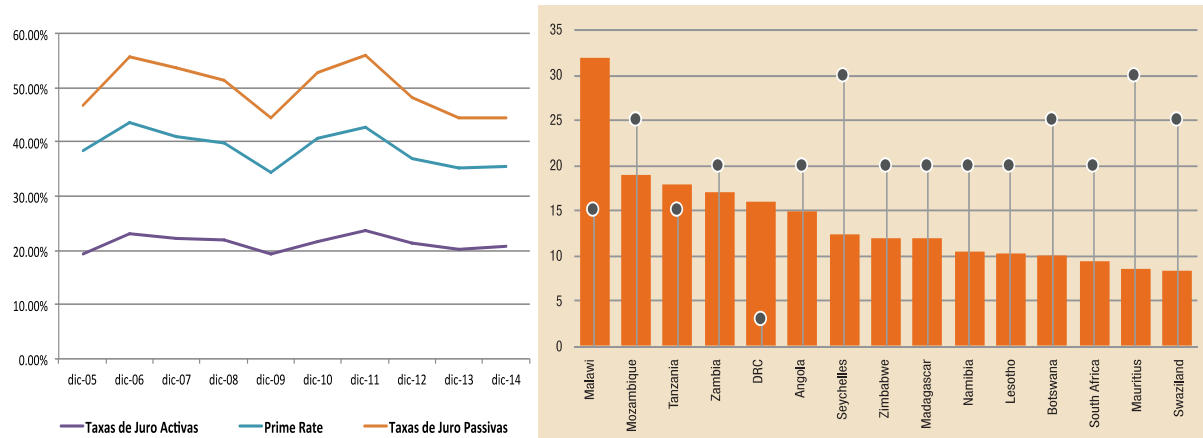
Source: Banco de Moçambique. Authors' calculations.

**247. Unfortunately, there are no more details about the most dynamic sectors in terms of collecting credit.** To address this and other gaps, the Credit for Purposes database will be used. The classification used in this database is - as mentioned below - slightly different. According to the credit database by purpose, the Other Sectors group, which in 2015 represented 43% of the credit to the economy, distributed as follows: loans to individuals (48%), housing loans (4%), and (the remaining 48%). This lack of detail about the fate of a large chunk of credit to the economy limits the ability to perceive which sectors are most capable of collecting credit.

**248. The available data allow us to point out the existence of a competitiveness problem in the cost of credit in the local market.** International assessments give poor qualification both access to and cost of credit<sup>92</sup>. Figure 47 shows the evolution of the interest rates charged by the Mozambican banks for the money they lent to their clients, and the passive rates that the banks pay for the loans they obtain in the market. The difference between these rates is an indicator of the banks' gross profit. The statistical data show that the average value of the active rates in the reference period was 21.4%, while the value of the liabilities was 11.06%. Therefore, the average spread was 9.8%, which could be considered high if compared to the world average in the same period (estimated at 6.14%)<sup>93</sup>. The graph also shows that the interest rate variation was little reactive to prime rate changes. The figure also presents comparative data on mortgage credit that place the country as the second most expensive in the region. These behaviours should merit further analysis, especially in the context of corporate structure, and macroeconomic and monetary policy.

Figure 47 - Competitiveness and Costs of Internal Credit

Figure 47 - Competitiveness and Costs of Internal Credit Interest on mortgage loans (in%) and terms (in years)



Source: Banco de Moçambique. Authors' Calculations and Reprinted from Finmark Annual Report 2016

**249. The participation of Public Companies in the market does not raise significant slices of domestic credit to the economy.** Internal credit finances different institutions of the economy: the Public Administration, its companies (Public Companies), private companies, private individuals and non-profit organizations, and, finally, local administrations and non-monetary financial corporations. The latter two institutions collect negligible credit percentages and, therefore, are omitted. In Figure 48 one can see how the institutions that collect the most internal credit are private companies. The credit flow grew during the period considered, maintaining the dynamics analysed above. The data do not

<sup>92</sup> Segundo A análise de Competitividade do WEF, a acessibilidade ao crédito em Moçambique qualifica-se no lugar 119 de 1140 países (ver Anexo II).

<sup>93</sup> World Bank databases.

report the type of company, the size, the sector, the type of financial product. Domestic credit to private companies starts at 7.3% of GDP and expands to more than 24% of GDP. Throughout the period the credit is less than 5% of GDP. In fact, these companies have access to often concessional external credit.

Figure 48 - Credit to the Economy per year, per institution, as% of GDP.

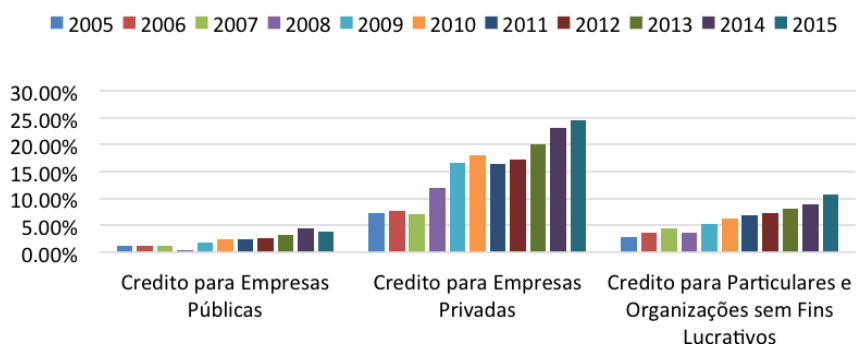
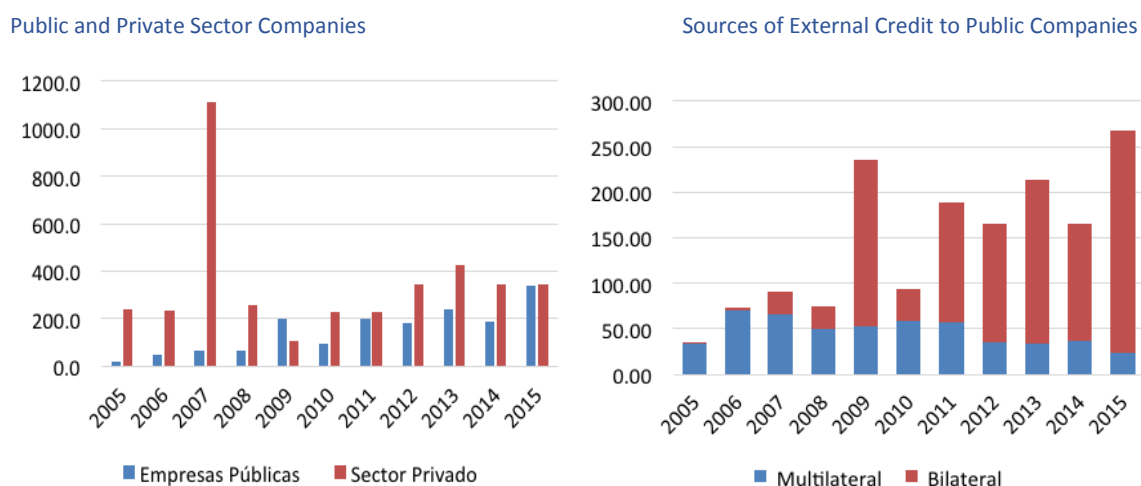


Figure 48 - Credit to the Economy per year, per institution, as% of GDP.

**250. In the last six years, external indebtedness (public and private) has been growing, reflecting the increase in the contracting of external credits to the public sector.** These loans are directed towards projects and companies (retrocession agreements), which have recorded, on average, weights of 49% and 16% in total indebtedness, respectively. The data in Figure 49 show the evolution of external credit to public companies. This credit is granted by multilateral and bilateral international bodies and institutions. Such funds are therefore also accounted for in ODA, OFO and CSS, depending on the nature of the institution. In the database of the BdM, it is possible to distinguish - between credit to the State Administration - credit to public enterprises and credit to the private sector. Public enterprises operate in sectors that the government considers strategic for providing services to the population. In the database these are not classified by sector but considered together.

Figure 49 - External Credit to Public Enterprises (Millions of USD, 2010).



Source: Banco de Moçambique. Authors' calculations

Table: 19 - Structure of Commercial Banks

Description	Total of credit (%)		Total de deposit (%)		Equity / Total Own Funds (%)	
	2007	Sept. 2012	2007	Sept. 2012	2007	Sept. 2012
5 Largest Banks	90	87	94	88	81	82
3 Largest Banks	82	77	83	79	70	75

**251. The Mozambican banking system is expanding, but with a highly concentrated structure.** The data in Table 19 indicate that the market is dominated by three large business groups that collectively collect 79% of deposits and provide about 77% of credit. In terms of loans, major commercial banks are moving into the SME market of the formal sector, but they have shown little interest in conquering the informal sector. The last year revealed a delicate situation in the banking system of Mozambique. The Central Bank had to intervene in the last months of 2016 at Moza Banco (the fourth largest banking institution) because the solvency rate had fallen below zero. The BdM had to replenish USD 100 million in the bank to stabilize it and make it operational. Our Bank, a small bank majority owned by the State, was closed in November 2016 and will be liquidated. The largest shareholders were the National Institute of Social Security (INSS), with 78.6%, and Electricity of Mozambique (EDM) with 12.7%.

#### The Mozambique Stock Exchange

**252. Since its launch in 1999, BVM has not yet developed into a robust market that could contribute to the deepening of the financial sector.** The Mozambique Stock Exchange (BVM) currently has 45 listed securities: 4 issues of shares, 39 bonds (both Treasury and Companies), 2 issues of Commercial Paper. The capital base requirement for listing is USD 1.5 million, less than half of the value proposed, owing to the fragile characteristics of the domestic private sector. The listed securities lists involved the sale of minority holdings in state-owned companies or in the local subsidiaries of multinational companies. With only four shares listed, BVM has not been a financial option for most companies in Mozambique, although the Financial Strategy mentions the creation of a secondary market aimed at MSMEs with less rigorous registration requirements<sup>94</sup>.

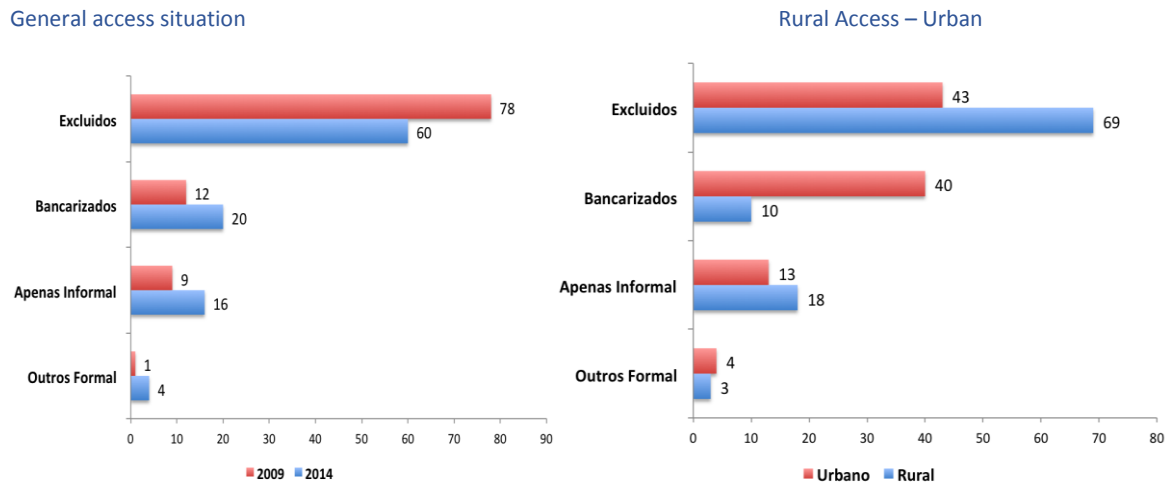
#### Access and Inclusive Financing

**253. Despite recent policy developments, financial inclusion in Mozambique remains low.** A survey on financial inclusion in Mozambique in 2014<sup>95</sup> indicates that although there is a significant increase from the previous measurement in 2009, inclusion data remain weak: (i) 60% of adult Mozambicans are financially excluded (that is, they do not use financial products - formal or informal - to manage their financial lives): (ii) 16% rely only on informal financial products or services; (iii) 4% have or use other formal banking products / services and may use informal financial products but not commercial banking products and (iv) 20% own or use banking products / services. The exclusionary situation is much more pronounced in rural areas, which reaches levels of 69%, while in urban areas the exclusion is 43 % (see Figure 50).

<sup>94</sup> See also: Ayani 2015, Mozambique's Microfinance Sector - a brief overview, SDC.

<sup>95</sup> Consumer Survey FinScope Mozambique 2014.

Figure 50 - Latest financial inclusion data



Source: Finscope 2014

**254. Non-banking reflects basic socio-economic problems and lack of supply to improve access.** The survey responses point to the following as the main causes for non-banking: (i) in 65% of the cases the person does not have enough money to pay for the services; (ii) banks are far away at 20%; (iii) 11% claim that bank accounts are not for people like them, (iv) 8% do not understand the benefits and (v) 7% cannot keep the minimum balance. The use of loans at the individual level was mainly motivated by non-medical emergencies (32%), to start or expand a business (26%), to build or remodel a home (19%) or to finance current expenses (15%).

**255. Access to credit for MSMEs is well below the needs of the sector.** Data from the same survey in 2012 indicated that of the 4.9 million small, medium and micro-enterprises, only 25% had access to credit. As around 75% of MSME owners are financially excluded, they cannot use financial products (or formal or informal) to manage their commercial finances. The survey found that: (i) only 11% are served by formal institutions (banking and other formal non-banks); (ii) 18% of MSME owners use informal mechanisms (e.g. savings groups) to manage commercial finances; (iii) a total of 46% of MSME owners save money (mainly at home), and (iv) only 5% borrow money (mainly from family and friends).

**256. According to IPEME's latest estimates, measures to improve access to SME finance should address a number of structural difficulties,** especially: (i) poor access to and availability of information on financing; (ii) low financial literacy and weak domain of information on user financing; (iii) weak structural capacity of MSMEs to become bankable; (iv) lack of adequate and alternative financing solutions for MSMEs; (v) Lack of alternative or diversified financing solutions for MSMEs; (vi) users' lack of knowledge about the financing solutions of the Stock Exchange and BNI.

### Policy Framework

**257. Legislation and regulations in Mozambique have shown openness and alignment with the objective of financial inclusion.** The Government of the Republic of Mozambique's (GRM) approach to financial services is guided by several well-defined policies, such as its Financial Sector Development Strategy 2013 (ESDF), the Financial Inclusion Strategy (2016) and Rural Finance Policy (2011). At the time of launching the Rural Finance Strategy and the development of the ESDF, the financial sector

was growing. For this reason, actions around financial inclusion has focused on consolidating progress and supporting expansion into rural areas.

**258. The Strategy for the Development of the Financial Sector in Mozambique (EDSFM)** prioritizes 4 strategic actions: (a) to promote financial inclusion, (b) to expand the formal financial system by improving and expanding basic infrastructures, (c) to use PPPs to finance the development of basic infrastructure to support the economic development of rural areas; (d) support the development of the microfinance sector and capture of savings to provide financial services to low-income populations and MSMEs in rural areas and peri-urban areas.

**259. The recently established financial inclusion strategy** aims to expand financial services by increasing the access of the adult population to physical services conveniently and at low cost to the formal financial system. The strategy emphasizes the need for the population to effectively and continuously use a range of financial services

**260. The implementation of these strategies has resulted in some important steps.** Supply-side regulation has prioritized opening doors for innovations and new distribution channels. There is a specific focus on approaches that can reduce the cost of serving rural areas. Demand-side initiatives focused on the promotion of savings and insurance products as well as financial literacy. Financial infrastructure regulations and initiatives would reduce both the costs and the risk of the provision of financial services and allow for greater flexibility through risk-based approaches. Therefore, it can be said that the strategies were relevant to the sector and its objectives<sup>96</sup>.

#### Financial Sector Data

**261. The Bank of Mozambique is the governing body of the financial system, and the body guarantees the country's solvency and financial stability.** It also has the mandate to stimulate the correct and efficient operation of the system, through monetary policy instruments and market regulation. The BdM collects statistics on the functioning of the financial sector and the economy. These statistics form the basis of this analysis. The data provided by the BdM show the annual stock<sup>97</sup> of credit to the economy. The annual stock of credit to the economy incorporates the dynamics of extension of new credits, as well as the payment dynamics of the credit service. With these data, it is also possible to construct the series of annual net credit flows by sector (institution) as well as the variation of the stocks in a year. This gives us the information regarding the speed of expansion (contraction) of the credit.

**262. There are differences between the classification of domestic credit, external credit, and credit by purpose, which complicate the comparison and impede credit analysis.** The internal credit data are broken down by institutional sectors (Public Companies, Private Companies, Non-Monetary Financial Companies, Individuals and Non-Profit Organizations, Local Administration), by purpose and by sectors<sup>98</sup> (agriculture, industry, construction, tourism industry, commerce, transport and communications, other sectors). External credit data are also disaggregated by institutional sectors,

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<sup>96</sup> Source: Study on the Achievements, Challenges and Perspectives of Microfinance in Mozambique, with emphasis on rural finance.

<sup>97</sup> The database is much richer, and the detail is, for the 2011-13 period, up to monthly. For the scope of this study, the annual periodicity is more appropriate.

<sup>98</sup> The total credit by purpose and sector is less than the total credit by institutional sectors, due to the latter being accounting, while the others are obtained by sampling. The important thing is that the first two should represent at least 90% of the credit. Credit totals by sector are, in some years, slightly different from credit per purpose. For the purposes of this analysis, reference is made to the credit data by sector that have the level of detail required by this analysis.

but with a different classification<sup>99</sup>. The incompatibility of these databases does not allow us to analyse with certainty the total credit and its distribution by sectors of national priority

#### Next Steps: Areas that Need More Attention

**263. Increasing access to credit on competitive terms should be the focus of the next actions.** The difficulty of access to credit is one of the main obstacles to the development of the private sector in general. There is a need to deepen existing reforms to make the financial sector inclusive and functional for economic development, especially for those working in rural areas and have a strategy for survival in agriculture.

**264. The expansion of access should also focus on better distribution of credit to sectors considered strategic for the country's development.** The data presented indicate that key sectors for the country's economy are the least favoured in access to credit. This is particularly important for sectors such as agriculture, industry and tourism. Similarly, there is a need to significantly increase financial inclusion and access to credit by micro, small and medium-sized enterprises.

**265. Future measures should aim at strengthening the financial system in a comprehensive way.** Improvements are still needed to ensure the growth of a robust system that improves performance and enhances the competence of financial institutions (banks, microcredit institutions and insurance companies). These measures should be complemented with other measures aimed at strengthening the financial markets and the development of the Mozambique Stock Exchange (BVM) and boosting the equity and bond markets.

**266. There are other policy objectives that must be achieved to improve financial inclusion.** Many of the reasons that limit financial inclusion depend on the success of other public policies. Lack of financial literacy and education are obstacles that do not allow many potential consumers to realize the value of financial products in their financial life by understanding their functioning. Unemployment and low levels of income continue to be an additional constraint for people to be financially included. It is difficult to cut the vicious circle of poverty without access to finance for micro and small entrepreneurs who enable low-income people to develop their economic independence.

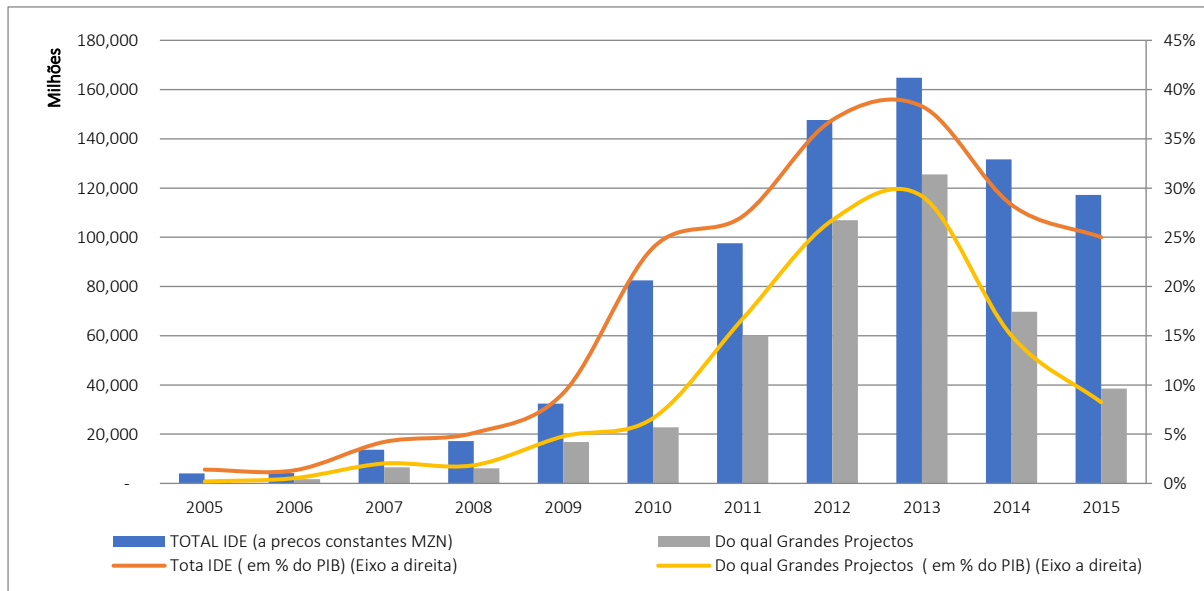
#### 5.3.2 Foreign Direct Investment (FDI)

**267. Foreign direct investment has grown significantly during the last decade** because of the reforms that Mozambique has implemented, which have stabilized the conditions for foreign entrepreneurs to consider investing in the country. Figure 51 shows the behaviour of the flow of foreign direct investment since 2005. It can be seen how the FDI started to grow and become relevant as of 2007 and continue to grow over time. This dynamic was initially boosted by megaproject-related investments, but recent developments indicate greater independence of megaprojects in the total volume of foreign direct investment.

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<sup>99</sup> The areas in this case are: Banco de Moçambique, Public Administration, in turn disaggregated in Credits for Programs and Credits for Projects, and the latter also disaggregated in Multilateral and Bilateral; (Agro-Industrial, Construction, Energy, Finance, Industrial, Fishing, Rail-Port Services, Telecommunications Services, General Services, Hospitality and Tourism, Others, Great Projects).

Figure 51 - Total FDI in the country, and FDI in megaprojects. In MZN 2010, and in% of GDP



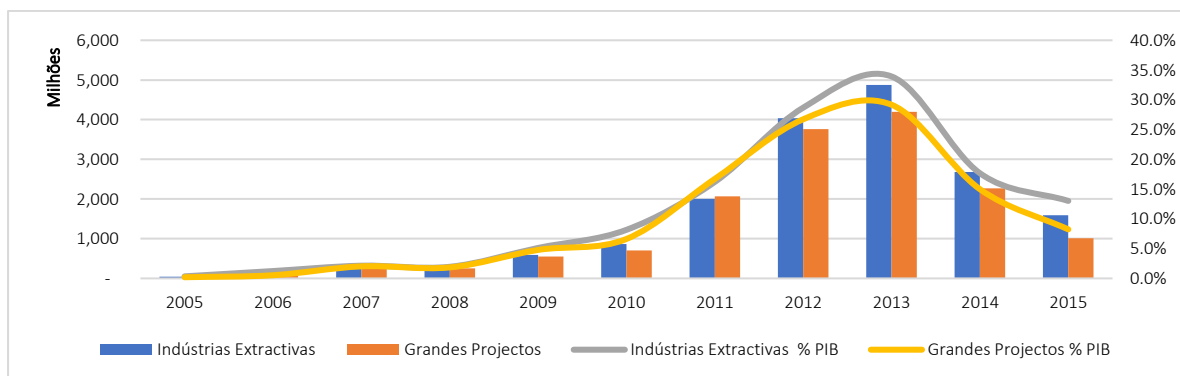
Source: Banco de Moçambique. Authors' calculations.

**268. Foreign direct investment in megaprojects was concentrated in the mineral extractive industries.** Figure 52 shows the behaviour of FDI in the extractive industry and megaprojects, in absolute (USD) and relative (as% of GDP) values, and reveals that, although there is no complete alignment, the two flows have very close behaviour. Foreign investment in extractive industry accounted for 69% of total FDI in the period under review, while investment in megaprojects accounted for 60% of FDI in the same period. It would be interesting to investigate the differences between the two flows: to see what kind of mineral resource exploration does not fall into the megaproject classification, and to study its feasibility, link with the capital market and local markets.

**269. There is evidence that the impact of megaprojects on poverty reduction has been rather limited.** Megaprojects generate significant capital flows, which reflect a positive balance of payments, but the late CPI reports that megaprojects approved between 1992 and 2010 account for 72% of total FDI, but generated only 5% of expected jobs (OECD, 2013). Always with reference to data from the defunct CPI, megaprojects generate 1.7 jobs for every USD million invested, against 77 jobs per million invested from other registered projects. An UNCTAD study in Mozambique indicates that FDI outside megaprojects has generated the most beneficial socio-economic effects. Sectors such as agriculture, industry and tourism have performed better in job creation. (UNCTAD 2012).



Figure 52 - IDE in the Extractive Industry and Large Projects. In USD 2010, and in% of GDP

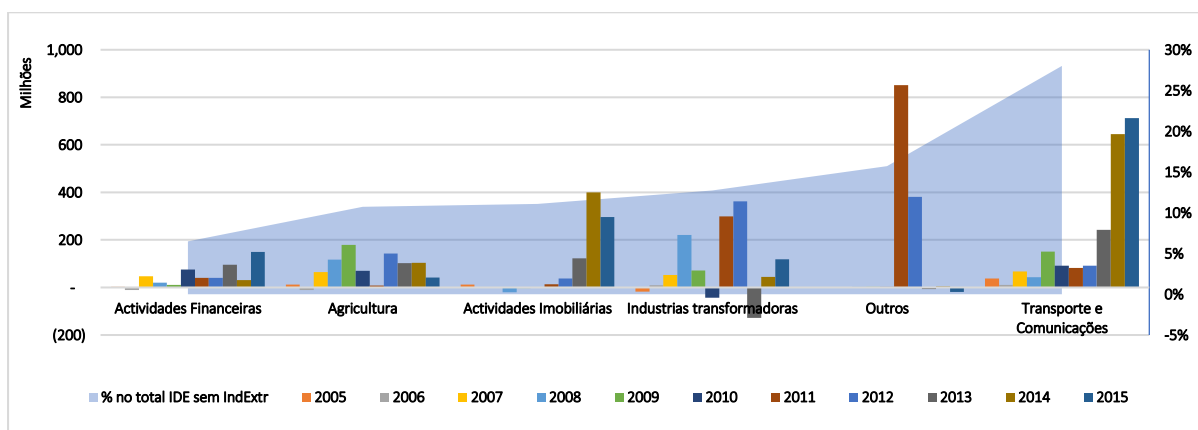


Source: Banco de Moçambique. Authors' calculations.

**270. Excluding megaprojects, the largest FDI growth has been concentrated in six business sectors.**

Figure 53 shows the sectors benefiting from the largest share of FDI without considering the investment oriented to the extractive industry. These sectors are: (i) financial activities, (ii) agriculture, (iii) real estate activities, (iv) manufacturing, (v) transportation and telecommunications and (vi) others. In transparency, the relative weight of these sectors can be seen in total FDI (without extractive industry) in the period. It is observed that Transport and Telecommunications and Real Estate Activities are the ones with the highest incidence in the period and that probably justify the divergence between FDI and investments in megaprojects in recent years.

Figure 53 - SDI by sector (excluding extractive industry) by volume is in% of total FDI (in transparency).

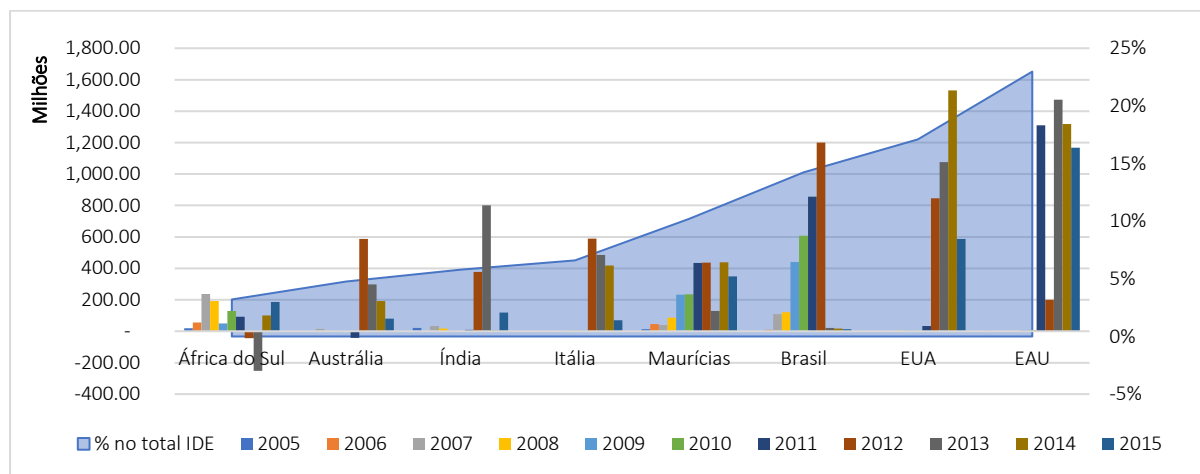


Source: Banco de Moçambique. Authors' calculations.

**271. Although agriculture is the largest contributor to GDP and employs more, agriculture has absorbed only 10% of FDI and most of these investments (90%) have concentrated on export production (OECD, 2013).** We also note that FDI for agriculture is, on average, 0.6% of GDP in the period, so the flow does not stand out as an alternative to the lack of credit and financing of the sector. The UNCTAD study describes FDI outside megaprojects as an 'underestimated factor' (UNCTAD, 2012). These needs and opportunities would merit active recognition in the Investment Promotion Strategies in Mozambique and the Poverty Reduction Strategies (OECD 2013).

**272. The generation of FDI also concentrated on a group of few countries.** According to the BdM database, a group of eight countries accounted for 85% of the FDI. In the period 2005-2015, the United Arab Emirates was the country with the highest investment volume, followed by the USA, Brazil, Mauritius, Italy, India, Australia and South Africa. 2010-2015, this set of 8 countries would continue to be the source of 85% of FDI in Mozambique (Figure 54).

Figure 54 - FDI by countries of origin of flows - USD 2010



Source: Banco de Moçambique. Authors' calculations.

Regulatory environment and alignment of FDI with the country's development priorities<sup>100</sup>.

**273. The current investment promotion law is June 1993.** Current legislation is designed to meet the challenges of a different historical context in the year of the end of hostilities. The spirit of the law, when enacted, was to be functional for the Plan for Reconstruction and Recovery of the Economy, and to open the economy without distinction between domestic and foreign investors. Investors are not required to comply with the law, but only investments that comply with the law - which are therefore investments licensed by the Investment Promotion Centre (CPI) - can access the benefits granted by law. With the development of subsequent regulations in other areas, there are disarticulations between this law and others, such as the law of PPPs or those that regulate investments in each sector, creating difficulties of interpretation and uncertainty in investors.

**274. In 2009, the government established a system of Industrial Free Zones (ZFIs) and Special Economic Zones (EEZs).** To accelerate the promotion of exports, the 2009 regulation of the investment law defined the Free Trade Zones (ZFI) and Special Economic Zones (ZEE) regime<sup>101</sup>. Decree 44/2009 of the same year creates the Investment Council, the ministerial body responsible for designing policies to promote and attract private investment. These Zones provide solutions to improve competitiveness conditions for companies exporters of goods and services on an ongoing basis through improved services and tax benefits, which in the case of EPZs include the following: (i) exemption from payment of customs duties and import VAT of materials and goods; (ii) exemption from IRPC in the first 10 fiscal years<sup>102</sup>; (iii) a 50% reduction in the IRPC rate from the 11th to the 15th

<sup>100</sup> Based on: OECD Investment Policy Reviews: Mozambique, (OECD 2013), Investment Policy Review Mozambique, (UNCTAD 2012), Investment Legislation in Mozambique (CPI), Strategic Plan for the Promotion of Private Investment 2014-2016 - .

<sup>101</sup> EEZ and ZFI existed already but were regulated

<sup>102</sup> Applicable to construction materials, machinery, equipment, accessories, spare parts and other goods intended for the pursuit of the activity licensed in the EPZs

fiscal year; (iv) a 25% reduction in the IRPC rate over the life of the project. Responsibility for the management of EPZs and EEZs was awarded to the Office of Economic Zones of Accelerated Development (GAZEDA). In practice there are only two EEZs in Mozambique: the Nacala Special Economic Zone (Nampula Province) and the Manga-Mungassa Special Economic Zone (Sofala Province).

**275. The government is implementing additional institutional reforms to improve the impact of investment and export promotion policies.** This year the government decided to merge the Investment Promotion Centre (CPI) with the Office of Economic Zones of Accelerated Development (GAZEDA), and established the creation of the Investment and Export Promotion Agency (AIPEX). There are very clear reasons for this decision as the two government agencies work in complementary areas and their individual performance can surely benefit from the merger. This new body is already working on the preparation of a new Strategic Plan for the Promotion of Private Investment (PEPIP) based on four fundamental pillars: (i) improvement of the business environment (together with MIC); (ii) development of institutional capacity for the promotion of investments and exports; (iii) improvement and diversification of the portfolio of investment opportunities; (iv) definition of target markets to focus on the promotion of investments.

[Next Steps: Areas that Need More Attention](#)

**276. The cost-benefit ratio of the current megaproject promotion system should be studied more carefully.** Mega-project investments are very important and necessary, especially in this economic environment. But the government should analyse - with a medium- and long-term approach - the cost-benefit ratio of the promotion system, especially for megaprojects in the extractive industries. The labour market impact of megaprojects is limited due to the scarce links with other sectors of the economy. These investments are a limited source of short-term fiscal revenues, with long-term returns not always predictable (as shown by the crisis in international commodity prices). Another aspect to be taken into account is the weak local capacity to participate in these ventures, given the limited access to credit by the local private sector. The considerations made later in Section 5.3.3 (PPP) on the multiple objectives of the megaproject law, of course apply also in this case.

[Next Steps: Areas that Need More Attention](#)

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**277. obtained from the current system and seems to be an action of importance.** It might be necessary to study in depth the cases of investments that have not been successful in order to better understand the weight of other factors, such as the availability and quality of the available labour force, the relative cost and the reliability of the supply of energy and other essential services. With this knowledge, the government can design a more appropriate mix of promotion measures and policies. This new strategy should adopt an approach based on value chains and programmatic

improvement of the structure and capabilities of the economic fabric in order to mobilize and take advantage of business opportunities associated with these areas.

**278. The opportunity is good for the government to develop a shared vision of the role that private sector development and foreign investment should play in the country's future economic growth.**

The review of NSDS objectives discussed in Section 3.1 in the context of SDOs will provide opportunities to review and focus on strategies to promote industrialization and the expansion of agriculture (micro and macro). These new programming lines - strengthened by a robust strategy for sustainable development and mitigation and adaptation to the effects of climate change - should incorporate the elements of the new PEP strategy, which will surely seek to integrate sectoral policies and strategic investment objectives. A clear vision can serve to reshape public expectations with respect to the volumes and impact of FDI and its real potential. These definitions will also have effects on other policies, such as PPP promotion or Public Investment Management, which should work in an integrated way to achieve the expected results.

**279. The most critical question will perhaps be how to ensure quality - rather than quantity - and the contribution to the development of foreign direct investment flows.**

The government should consider how to arrive at an appropriate balance of the positive and negative effects of promoting private investment. It is necessary to analyse more in detail the benefits of measures to stimulate private investment with the economic, social and environmental return obtained with the public resources affected. In Section 5.2 it was pointed out that the country needs to implement measures to improve the climate for investment. But a greater indifferent 'doing business' can also lead to negative social and environmental effects. International experience indicates that the facilitation of the business climate tends to be confused with greater tolerance in the application of some regulations, especially employment or environmental policies that can have highly problematic consequences in the long term. Finally, higher value-added investments capable of generating high-quality jobs are generally associated with a good level of labour force capacity, and very competitive infrastructure (electricity, transport and telecommunications) conditions that perhaps EEZs and ZFIs could try to compensate.

**280. There are also known limitations of FDI that the government should consider when developing new policy frameworks and fiscal incentives.**

International experience indicates that FDI has some limitations that are independent of the country of destination, for example: (i) FDI hardly reaches least developed countries, unless they are large exporters of natural resources in which case tax exemptions do not are the main motivation for these investments; (ii) it is very difficult to direct FDI to the development of medium and small companies; (iii) FDI is often associated with imposing unlawful withdrawals of resources<sup>103</sup>. The government should take this type of factors into account in the generation of future policies and promotion measures.

**281. The monitoring system for monitoring FDI impacts can be improved. For each project, information about the development of the project and the number of employees is collected.**

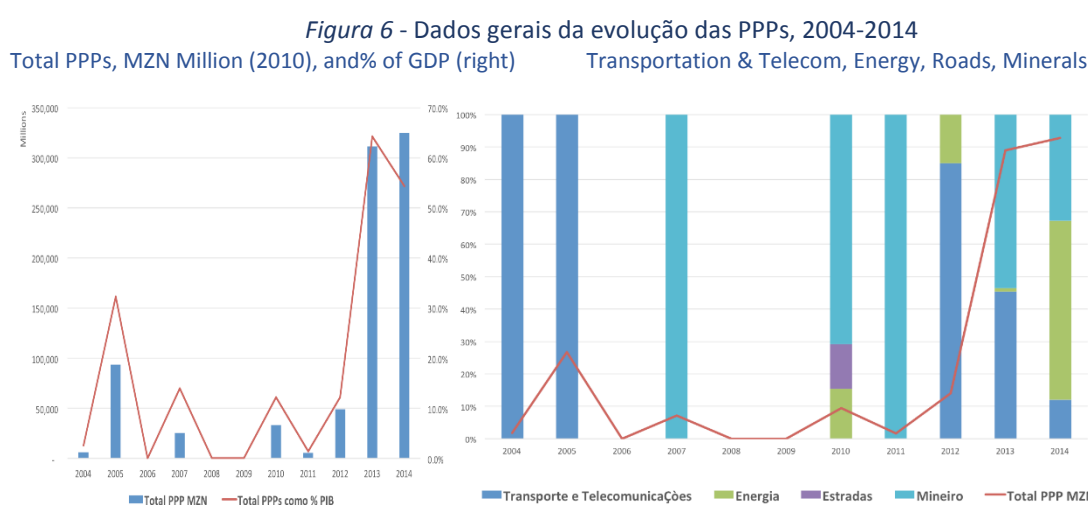
The extinct CPI sent questionnaires to the entrepreneurs, who fulfilled and returned them voluntarily. This information was consolidated in bulletins whose utility was not clear. Socioeconomic effects are also not monitored, as are the fiscal costs of incentives, which are calculated and accounted for by ATM. Monitoring developments, and thus monitoring the effectiveness of investment policy, can be greatly improved and should be a high-priority task.

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<sup>103</sup> Stratta, N. 2015.

### 5.3.3 Public-Private Partnerships (PPP), Enterprise Concessions (CE) and Large-scale Projects (PGD)

**282. The use of PPPs has increased over the past decade, and very strongly in recent years.** Figure 55 shows the total nominal value of PPP contracts per year, by sector, for the period 2004-2014, and the total per area. The first PPP contract in Mozambique was in 1997 to rehabilitate and manage the Mozambican section of N4 Maputo-Pretoria, a 30-year concession, and an invested amount of RZ 6.3 billion at current prices. At the time, Mozambique had no legislation in place, and the agreement was signed based on South African legislation. In 1998 and 2003, PPP contracts were signed for the management of the ports of Beira and Maputo, respectively. These contracts were also drawn up ad hoc, in the absence of a law governing the matter.



Source: DNT-MEF other sources. Authors' calculations

**283. Despite the lack of information, recent experience indicates an acceleration in the use of various types of partnerships in different sectors.** The government is increasingly using PPPs, Business Concessions (CE) and Large-Scale Projects (PGD) in different areas of activity. As of the 2011 legislation, there was a vertiginous increase in the values of the contracts signed, in PPP for transportation and telecommunications and energy production, and in EC for the exploitation of Natural Resources. The following are indicative examples of the potential of this type of partnership by sector:

- **Transport Infrastructure and Ports.** In 2004, the contract was signed for the rehabilitation and management of the Beira Railway System (Sena line for the Moatize Coal and Beira-Machipanda line, bordering Zimbabwe). In 2005, concessions were granted for the management of Nacala and Quelimane ports and concessions for the Nacala and Ressano Garcia lines. In 2013 PPP contracts (and also PGE) were signed for the construction and a port in Macuse and a railway to leach coal from the province of Tete through this corridor. In 2010 the contract was signed for the construction of roads in Zambézia province;
- **Power generation.** In 2007, a contract was signed for the management of the Cahora Bassa Hydroelectric Plant for the Production and Sale of Electricity. In 2010, contracts were signed for the construction of a natural gas plant (extracted in the province of Inhambane). Between 2012 and 2014 contracts were signed for the construction and management of seven power stations, three thermoelectric plants (gas and coal) and four hydroelectric plants;

- Exploration of Natural Resources. In 2010 and 2011, two more fully-owned CEs (IDE) were signed for coal mining in the province of Tete. In 2007, the contract for EC was signed for the purpose of mining Moatize in Tete. Between 2013 and 2014, a further nine CEs were signed (which, according to the law, now have to guarantee access to Mozambicans with few means, which is materializing with the State receiving shares through Mozambican Mining Company, SA ( "EMEM"), the state holding company for mining.

**284. PPPs have the potential to generate savings by mobilizing additional financial resources and benefiting public investment from private sector know-how, but these results are not guaranteed.**

PPPs are advocated to attract private (preferably foreign) funding for public investment and to promote efficiency, bringing market discipline to the selection and implementation of public interest projects. International experience shows that achieving good results depends on several factors, which must be managed by the government: (i) the correct identification of the most efficient bidder, (ii) appropriate risk-sharing arrangements, and (iii) the nature of the contractual relationship established between the public and private partners.

**285. There is no evaluation of the performance of PPPs, CSs and PGDs in Mozambique, but available evidence suggests that government learning has gained mixed experiences.**

In all cases mentioned above it was not possible to obtain information on the performance of these partnerships. There are some studies on particular cases, but without the use of a coherent methodology that allows to analyse in a systematic way the performance of the different functions of the State in the management process of PPPs. It was not possible to analyse any information on the flows that PPPs have generated over time, and what they are expected to generate in the future.

**286. Based on the published information, there are known situations where the State had to intervene and are likely to incur significant losses.**

There are at least two situations of this type: (i) the contract for the provision of the water distribution service in Maputo, Matola and Boane and (ii) the contract for the rehabilitation and management of the Beira Railway System. In the first case, the State was forced to intervene because the distribution of water is an essential service, and the State must assume its provision. In the second intervened, through the Public Company CFM, because the company contracted for the management of the railway did not comply with the terms of the contract. There are other known cases of unexpected negative effects due to the lack of experience on the part of the State in the management of PPPs analysed in Box 3.

**287. The problem is not exclusively Mozambican, and international experience indicates that this is a very difficult area of policy management in developing countries.**

There is abundant international experience indicating that the management of these partnerships can have unforeseen negative consequences for the state in developed or developing countries. This is especially aggravated when the government is forced to intervene to rescue troubled operations and adverse conditions. Box 3 examples can give an idea that business management at the border between the public and private for-profit sectors is one of the most complex areas of public management and demands important capabilities. Effective management of partnerships requires the development of specific capacities to properly manage the different possible modalities.

**288. The expansion of this type of partnership will require the development of specific government capacities to properly manage the different modalities possible.**

Although there are no standard definitions, there are several possible modalities for partnerships with the private sector where the degree and nature of public sector involvement can vary significantly. The different types of contracting define the transfer of risks and benefits between the public and private sectors and the sound management of each requires very specialized capabilities. In its selection, the State should

consider the best cost-benefit ratio taking into account the most convenient type of operation and the capacity constraints themselves to make it sound. The generic categories presented below describe the type of risk management and the associated costs of operation and maintenance:

**Box 5: The difficult task of managing PPPs: Examples in Mozambique and internationally<sup>104</sup>**

- National and international experience indicates that managing PPPs is of great complexity and can become a headache for the government. In Mozambique, there are two cases of public notoriety, where the information found in the press recognizes the need to strengthen the capacity of the government to manage such projects:

Águas de Moçambique (AdM) - In 1999, with the support of the World Bank, the Investment and Water Supply Fund (FIPAG) was created with the objective of attracting private sector capital in the water distribution sector. AdM was created and leased to a consortium with Mozambican investors and two companies with industry experience<sup>105</sup>. The investments were the responsibility of FIPAG, while the AdM had management and revenue collection responsibilities. After the floods of 2000, one of the two companies withdrew from the consortium. In 2003 the other company (AdP) renegotiated the contract in a commercial concession for 15 years. In 2006 water losses were around 58% of the water produced and AdM and FIPAG invested in better management and physical infrastructures. In 2009 losses fell by 50% and were expected to fall by 39% in 2014. In 2010, FIPAG decided to buy AdM. BM's assessments state that most of the problems have been resolved and the WM was in a position to be sustainable. FIPAG had to compensate AdP for lost income. In 2012 FIPAG returned to its initial role as a regulator and the privatization of water distribution was relaunched.

- *Moma Heavy Sands Exploration - In 2002, a contract was awarded for the exploitation of heavy sands in the district of Moma, where some of the largest reserves in the world (estimated at 163 million tons, with a value of 125 billion USD). The mine, which began production in 2007, was one of the first major foreign investments in Mozambique. The concessionaire company is Kenmare Resources (KR), registered in Ireland. An independent study (CIP)<sup>106</sup> notes that the advantages of this exploration for Mozambique were minimal. Due to the government's lack of experience at the time, KR was able to negotiate extremely favourable terms, including non-payment of IRPC for one part of the business group, and halving the tax rate for a period of ten years for the other party, exemption from VAT payment for many of the goods and taxes on export and import. The study also points to KR's use of a complex corporate structure with subsidiaries and representatives in tax havens, enabling tax evasion by sub and over billing, discussed in Section 4.4.4. Another interesting fact is that most credit (80%) of KR was financed by development finance institutions, justified by the company's contribution to employment generation and infrastructure development, which did not happen as expected.*
- *This type of situation is not unique to Mozambique; there is abundant international experience indicating that the management of these partnerships can have unforeseen negative consequences for the state in developed or developing countries. This is particularly aggravated when the government is obliged to intervene to rescue operations in trouble and adverse conditions, such as:*
- *The Fertagus suburban passenger rail service in Portugal. Although the initial contract formally shifted the risk of demand to the concessionaire, the contract stipulated that the Portuguese government should take over the debt if the traffic remained below the lower level of the traffic band for several years. This happened, and the renegotiation of contracts occurred with the government in a relatively weak position.*
- *The Channel Tunnel Rail Link in the UK. In 1996, the government awarded the contract to London & Continental Railways Limited (LCR). LCR planned to finance the construction of the Link, leveraging private funding for future Eurostar UK revenues, and direct donations from the government. When actual demand for the Eurostar rail service proved to be much lower than predicted, the company was forced to abandon its original financing plans, and instead the government had to rescue the company by providing additional unplanned subsidies.*

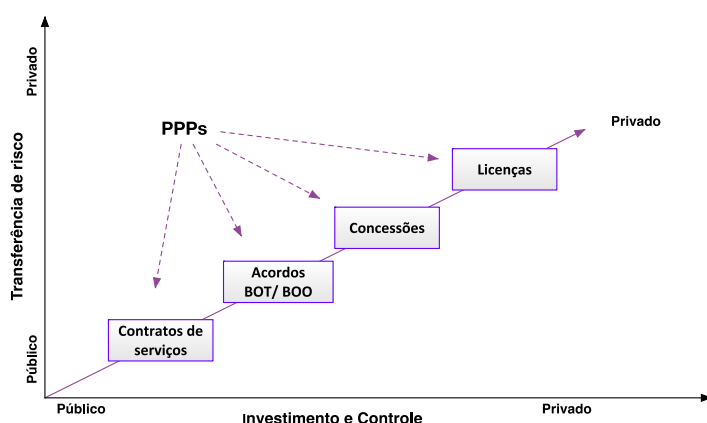
<sup>104</sup> International examples with PPPs extracted from "Public investment management" EDI, 2016 and Oxfam: A. Marriott (2014) 'A Dangerous Diversion: Will the IFC's flagship health PPP bankrupt Lesotho's Ministry of Health?'

<sup>105</sup> Mazi-Mozambique, Seur International, Águas de Portugal (AdP).

<sup>106</sup> "Mining without development: the case of the Kenmare mine in Moma, Mozambique", CIP, European network on Debt and Development (Eurodad), 2013.

- *The Queen Mamohato Memorial Hospital in Lesotho, located in the Maseru capital, was funded by a PPP with the support of the International Finance Corporation (IFC). The promise was that PPP would provide greatly improved health services for the same annual cost as before. Three years later, figures show that the hospital and the three clinics associated with the PPP: (i) cost USD 67 million a year - at least three times as much as the old public hospital would have cost today - and will consume 51% of the total budget of government health; (ii) are diverting urgently needed resources from health services in rural areas, where three quarters of the population live and mortality rates are increasing; (iii) are generating for shareholders a rate of return of 25% on net assets and projected cash proceeds 7.6 times greater than their investment. The cost escalation required a 64% increase in government health spending, with 83% of this increase explained by the PPP.*

Figure 56 - Typical risk distribution and control in the main PPP modalities



Source: Reprinted from ADB 2009

- **Licenses:** Authorize private companies, designated operating or service rights and do not involve revenue or public investment support and therefore do not entail major risks for the State;
- **Concessions:** All revenue risk is assumed by the private sector (from the exploitation of resources or user fees for use of services), and the government takes possession of the assets at the end of the contract;
- **Construction-operation-transfer agreement (BOT)**<sup>107</sup>: The government assumes 100% of the revenue risk under an availability payment to the private company, and assumes ownership of the assets at the end of the contract period;
- **Construction-operation-property agreement (BOO)**<sup>108</sup>: The government assumes 100% of the collection risk under an availability payment to the private company, but does not take ownership of the assets at the end of the contract period;
- **Service contract:** Gets government revenues, but does not demand investment from the private sector, and therefore, the State retains almost 100% of project risks. This type of partnership is used in circumstances where new private sector investments are not needed, but the government wants to improve service delivery with performance-based contracts.

#### Framework for National Development Assistance Policies

**289. The government has initiated a process to order and provide coherence to the legal framework governing PPPs, Enterprise Concessions (CEs) and Large-Scale Projects (PGDs).** With the enactment

<sup>107</sup> Build – Operate – Transfer (BOT).

<sup>108</sup> Build – Own - Operate (BOO).



of law 15/2011, the government initiated a process to order and provide coherence to the current legal framework. The law was passed at the same time as the law on megaprojects and public participation. Under the Mega-Project Law, PPPs should have nine objectives: (i) to be in line with sectoral strategies and development plans; (ii) to contribute to capacity building for the efficient and effective exploitation of national resources; (v) to promote entrepreneurial freedom by removing restrictions that may limit the future viability of the enterprise, (vi) the creation and maintenance of jobs, (vii) contribute to the development of the capital market, (viii) favour partnerships with MSMEs, (ix) promote social responsibility of the venture together with local communities. The new legislation (in preparation) on public enterprises will provide additional support to this policy framework.

**290. According to the governance framework, each PPP, EC and PGD enterprise is subject to the protection of the government institution responsible for the area or sector in which it fits.** The law decentralizes the following essential functions in sector or sub-sectoral regulatory authorities: (i) the selection of projects and (ii) ensuring economic and financial balance between the contracting parties, the protection of users' interests and the maintenance and sustainability of the development. Each sectoral body must ensure alignment with national priorities.

**291. The current decentralization of project selection in line with national priorities and feasibility analysis is a particularly important point that should be reviewed.** The current selection criteria for aligning proposals with government priorities (as set out in the ENDE or in the PQG) are so general that practically everything can be considered a priority<sup>109</sup>. In addition, the decentralized entity must guarantee the interests of the State by ensuring the implementation of due process in the tendering and negotiation phase of PPPs. The necessary technical skills that the contracting unit must have in order to be able to carry out such evaluations and the analysis of the economic and financial balance when contracting partnerships is very specialized. The government should avoid that, due to lack of capacity of the contracting unit, a private entity should take advantage of the provision of a public good, which would determine that during the life of the contract the return of the concession to the State may be below the optimum. This discretion in decision making can have negative consequences for selection - if not undue, at least undesirable - of partnerships.

**292. Each PPP enterprise is subject to financial supervision by the government institution that oversees the Finance area,** namely MEF and DNT which must, for this purpose, define and establish the mechanisms and procedures for interinstitutional coordination with each entity responsible for sectoral supervision. The law establishes that it is the responsibility of the government (MEF) to designate and train the entity responsible for intersectoral coordination and the centralization of the analysis and economic-financial evaluation of PPP, PGD and CE ventures, as well as the monitoring of equitable sharing benefits and risk prevention in these ventures. However, these functions are not specifically defined by law.

**293. A troubling situation is the current freedom of decision of public enterprises on critical issues of state participation in partnerships with the private sector.** There is no concrete evidence but there are known cases, for example: the CFM company participates in the case of ports and railways, EDM in the case of Energy, and ENEM in the case of mining in the EC. Decisions of such partnerships can create risks to the budget through the creation of significant and long-term contingent liabilities, especially when such partnerships are used to circumvent budgetary control. Considering the recent

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<sup>109</sup> All the objectives set out in Law 11/2015 are also principles defined in ENDE and PQG. However, a general indication of all priorities, and hope that each instrument, in the specific case of PPPs, responds to all priorities, may dilute prioritization and make it difficult to select the focus, but also make room for discretion, possible corruption schemes, and potential allocation conflicts.

experiences of creating contingent liabilities for the operation of public companies, the intervention of these companies in an area of high potential risk requires a joint revision of the legislation that regulates PPPs, Corporate Concessions (CEs) and Large-Scale Projects (PGDs) and the new Public Companies Law.

**294. The law establishes general principles for the management of the risks inherent in PPPs, but the government should go further in defining how best to ensure the proper management of these risks.** The law clearly establishes the type of risks that will be considered the responsibility of the state (political, legislative, changes in operating rules, conflicts of interest) and what type of risks should be the responsibility of the private partner. In particular: (i) economic and financial risks inherent to the enterprise (foreign exchange, fiduciary, debt unsustainability, tax evasion, etc.); (ii) design, design, engineering or construction of the project; (iii) commercial, performance management; (iv) impairment of the residual value of the assets; (vi) environmental impact. Although the separation of this type of risk is correct, the law can generate a false sense of security of 'automatic elimination' of risks, since, in the end, if the PPP fails, in many cases, the State cannot avoid assuming the risks. costs. The law also provides for the possibility of the government issuing guarantees for strategic projects of a special socio-economic nature for the country. Based on recent experience with public companies, and following the previous argument, the government must therefore take measures to reduce the possible collateral damage generated by this type of decisions. Therefore, the correct management of risks should be further analysed, adding perhaps a more centralized control layer (see recommendations in this section).

**295. According to the law, the programming of enterprises in PPP should follow the same mechanism of programming of the public expense.** PPP ventures should therefore be part of the IIP, the CFMP and, finally, the EO. In drafting the CFMP and the EO, the government should: (a) enter funds to ensure their co-participation in PPP project investments, and (b) forecast and budget, in terms of aggregate and disaggregated values, compensation or subsidy by the State or concession, access to guarantees or financial facilities for clearly identified PPP enterprises, taking them into account in the analysis of the sustainability of public debt. The law also prescribes that: (i) PPPs, PGDs and ECs should have an appropriate budgetary framework, given their impact expressed in long-term multiyear commitments, with a financial exposure of the public purse, (ii) the General Account of State should report on the implementation and performance of public-private partnerships at the end of each financial year. Finally, the execution and the flows must be properly accounted for in the CGE. Through these documents, the Assembly of the Republic should have all the information to comply with the warrant of control that is for them and for which it is developing capabilities.

**The government has to analyse how to implement the responsibility of indicating and empowering the entity responsible for the analysis and evaluation of the ventures, guaranteeing the equitable sharing of benefits.** DNT-MEF is aware that the PPP unit, which was established in 2010, should develop skills to cope with the weaknesses that a newly created unit naturally has. To this end, the unit is receiving training in project evaluation, it is building a database to accurately collect reliable data on PPP projects to improve management. In addition, it is preparing to take on the role of the law - which is cross-sectoral coordination for project evaluation for approval and monitoring, and finally to ensure and improve alignment with the development strategy and PQG (see recommendations in this section)

**The MEF is working to reorder the area.** Contracts signed before the law comes into force are not always in line with the spirit of it. There is a study group that aims to identify which of the clauses of these contracts can be renegotiated between the parties, and within the contractual rules, to achieve

this superior alignment. In doing this work, the MEF evaluates the time frame of each contract, trying to contextualize it in the current phase of the Mozambican economy to assess the opportunity, costs and benefits of addressing a partner and not sending unclear messages to the market in their set.

#### Access to Data and Information on PPPs, CEs, PGDs

**296. The DNT-MEF database is presented as a list of projects disaggregated by sector and per year,** and as contracts stipulated before and after law 15/2011. In addition, the DNT-MEF organizes the Information on the Economic-Financial Performance of Public-Private Partnerships. This information is presented as the accounting of the flows generated by project, in terms of income, revenues, jobs created, liaison with MSMEs, and CSR funds. Unfortunately, performance is not compared to estimates of ex-ante performance. In addition, this summary was provided only for 2015. Finally, it is unclear whether there is an automatic system for extracting this data or whether the information provided is the result of a manual compilation of scattered information.

**297. The information provided in the database can be improved.** The PPP values available in the database only include the total contract values. As the standard contract is BOT type, it is foreseeable that the volume and nature of the flows will vary according to the stages of the contract. These are long-term contracts, and on average range from 24 to 30 years. It would therefore be desirable to have reliable information on the revenue stream received by the State.

#### Next Steps: Areas that Need More Attention

298. In order to boost the use of PPPs, CEs and PGDs with greater certainty for government, the institutional framework could be further revised and strengthened. Some additional adjustments may be necessary to ensure that the government has the necessary capacity in key areas for managing such partnerships. Following good practice from international experience, it is important to reinforce the following key functions to develop an effective institutional framework for the successful implementation of these partnerships:

- *Support for high-level decision-making.* To ensure efficient prioritization of partnerships and alignment with more urgent needs, many countries set up an institutional figure (National Committee for Infrastructure Development or public-private partnerships) with direct involvement of the Prime Minister. This provides high-level institutional guidance and support for the strategic management of PPPs in various sectors and use of procurement models;
- *Strengthen the centralized PPP management capacity.* It would be appropriate to consider adding a more central control layer (an agency with institutional capacity and sufficient resources) to ensure the actions of coordinating and supervising the issuance of PPP project licenses in a transparent and efficient manner. The present law provides the financial protection of the contracts to the MEF, but decentralizes the responsibility of the decision to the sectoral regulatory authorities of government contracting. The newly installed unit in DNT-MEF could have this function. The unit must have clear responsibilities to act as a single window to coordinate project preparation, transaction and project management within government;
- *Risk Management Unit.* Capacity (and highly specialized expertise) should be centrally concentrated in a centralized agency (MEF) to develop government support criteria and mechanisms, allowing for timely and appropriate decisions on the level of risk, the structure of state participation and risk management arrangements for each PPP project, especially the prevention of contingent and unforeseen risks of management of the partnerships mentioned above;

- *PPP units.* The capacity of the partnership management units of the sectoral government contracting regulatory authorities (public companies and ministries) should be strengthened. These units act in their areas of responsibility as focal points for the development, acquisition, monitoring and management of PPPs, but must have sufficient technical elements to ensure that good practice is applied at all stages of the project (study, tender, management of projects). Project teams should be established to monitor each PPP project with adequate resources from the corresponding PPP unit, using both line staff and consultants;
- *Independent Arbitration Agency.* Consideration should also be given to the existence of an independent agency and expertise around interpretation of concession contracts and to preside over activities such as tariff adjustments, contractual variations and areas of disagreement, if requested by the parties;
- *Promotion of PPPs.* So far government participation has been relatively passive, but the revitalization of PPPs will require proactive investment promotion work. This type of activity has a very clear border with the promotion of FDI and, therefore, this task should be executed by the new Agency for the Promotion of Investments and Exports (AIPEX), with a specific mandate and defined goals.

**299. In addition to establishing or strengthening existing institutions, the government will need to ensure sufficient funding and resources.** These resources need to be provided under management arrangements whereby institutions and staff can be encouraged and accountable for delivering results. Funding agreements within the government will be potentially needed throughout the life cycle of PPP projects (study and feasibility, tendering and project management). Most likely, mechanisms will be needed to finance: (i) the initial cost of involving specialized external PPP staff and consultants; (ii) financing for the feasibility phase: to cover either the cost of land acquisition or other project costs to make them commercially viable; (iii) long-term financing mechanisms to facilitate the participation of the national private sector in PPP projects, among others.

**300. Before accelerating the use of such partnerships, the Mozambican state should establish clear criteria to defend the national long-term interest.** Promoting private financing for natural resource development ventures or developing critical infrastructures is a priority for Mozambique in the short to medium term. The government should maintain a clear strategic position in this process (hence the above recommendation to consider a National Committee for Infrastructure Development or public-private partnerships), considering that the individual interests of market actors (whether private companies or multilateral funding agencies) may or may not be in the best interests of the State. In the examples mentioned above, the need to maintain a clear, independent and transparent process and well-managed processes to ensure investment promotion and proper risk management seems clear.

**301. There are considerable benefits in developing an integrated approach to infrastructure management that can cover various funding streams.** Chapter 6 proposes a solution for integrating existing priorities in public investment management, foreign direct investment management (FDI), PPPs and other key funding areas. The potential benefits of this integration seem to be significant.

#### 5.4 Other Private Sources

**302. The next sections of this section are a list of private funds that could be important for the future of the country but could not be duly evaluated for reasons other than the organization of this work.** In most cases, the main reason is that there were not enough data to perform the evaluation. In other cases, the information exists, but it was not possible to establish a productive working relationship with the institutions responsible for the management of these flows, which is why it was not possible

to obtain the minimum elements to analyse the flow perspectives according to the AFD methodology. The information presented here is intended to illustrate the possible value of analysing these flows in the future.

#### 5.4.1 Shipments

##### **303. Approximately 23% of the population used remittance services, mostly within Mozambique.**

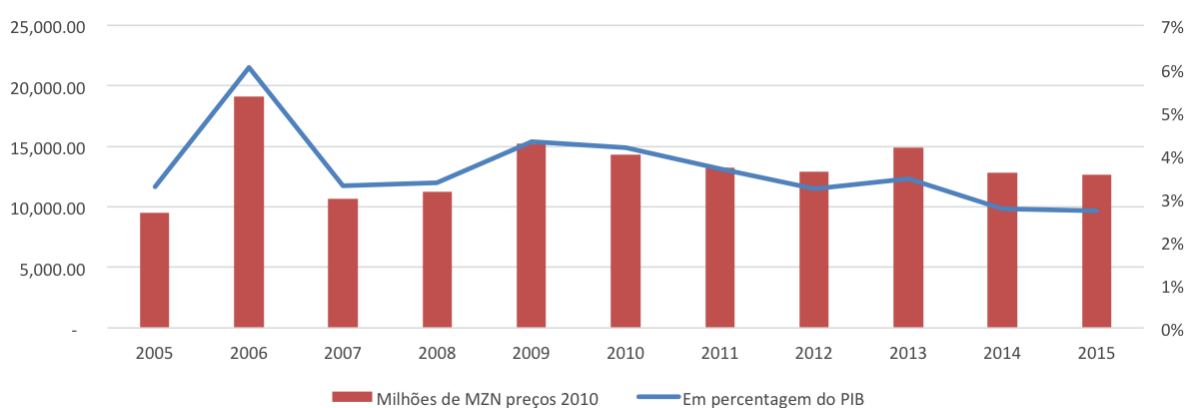
The values of 2016 are much higher than those of 2009, of only 15%. Most people send and receive money within Mozambique, but there are some cross-border transactions. The application of this flow of funds finances: (i) the basic needs of households and (ii) education. Shipments are increasingly sent through banks (2/3), with just over a third of people sending money for friends ..

**304. The use of migrant labour is a historical fact in the Mozambican tradition.** At the end of the nineteenth century, when mining began in South Africa, there were agreements between governments and concession companies of the farms for the employment of Mozambican labour. Over time, the colonial governments of South Africa and Portuguese East Africa had agreements for Mozambican workers to work in the Rand mines. Wenela was the recruiting company of workers, and the provinces of southern Mozambique were the origin of migrant workers. The outskirts of Gauteng continue to require labour for mining companies, workers in the southern provinces of Mozambique (Gaza and Inhambane) continue to migrate under annual contracts and Teba, Lda. is the recruiting company that operates in Mozambique. Mining workers are the ones who generate the most remittances.

##### **305. In the period under review, private remittance flows from abroad have been growing.**

Remittances channelled by individual private individuals in the form of income and remittances from emigrants are one of the channels that have been contributing substantially to the financing of the Mozambican economy. Figure 57 analyses the evolution of remittances over the last decade. In 2005, the cumbersome value of remittance flows was 10.1 billion MZN (2010 prices) or 3% of GDP, with private remittances almost 2 billion MZN (0.7% of GDP) and remittances immigrants 302 million MZN (0.1% GDP). By 2015 the complex value of remittance flows was more than 21 billion MZN (2010 prices) or 5% of GDP, with private remittances almost 1.6 billion MZN (0.4% of GDP) and remittances immigrants 4.3 billion MZN (0.9% of GDP). The peak value of remittances was reached in 2013 with 19.2 billion MZN (4% GDP), with private remittances almost 1.9 billion MZN (0.4% of GDP) and remittances from immigrants 2, 2 billion MZN (0.5% of GDP).

Figure 57 - Total private shipments (according to the definition of BDM)



Fonte: Banco de Moçambique, MITESS, Banco Mundial. Cálculos dos autores

306. During this period, the trend of remittances received from abroad increased until 2012-13, the year of declining remittances due to the instability experienced in the South African mining industry, which, to some extent, contributed to its downsizing, in a which led to a decrease in the workforce. On average, the value of remittances is 0.6% of GDP. (See Figure 58)

### Sources of Remittances

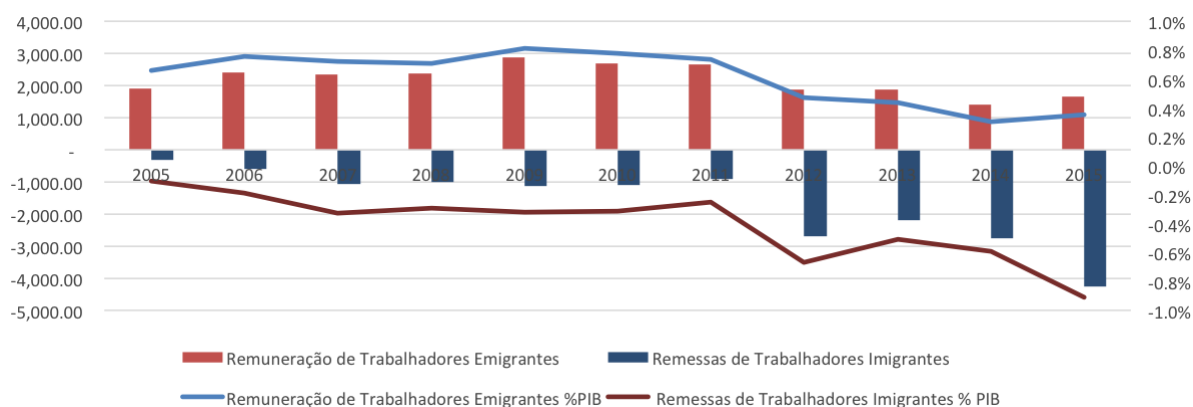
**307. External remittances are mostly generated by organized labour migration in South Africa.** In addition to mine work, recruiting companies seek Mozambican labour to work on farms and other agricultural establishments. Figure 58 shows the number of Mozambican workers employed in SAR, recruited by TEBA. According to interview material, migrant labour is also not considered to increase the skills of workers, for example in farm work, so that, on his return, he can carry out the same activity in Mozambique, but with the new skills learned during the SAR period.

### The Shipment Data

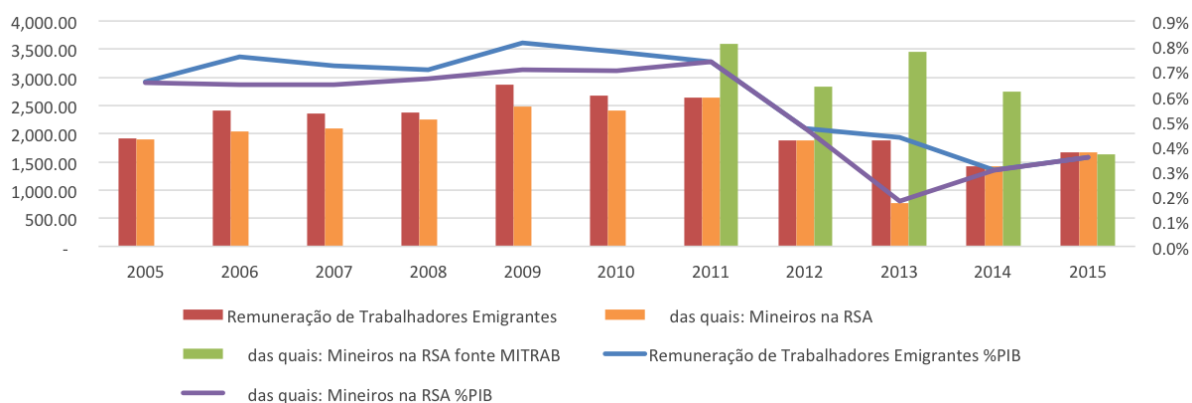
**308. The Banco de Moçambique collects all statistics that refer to private remittances as any other financial transaction inside and outside the country.** When aggregating private remittance data, BdM considers 4 flows: (i) the remuneration of migrant workers (with the detail of the remittances generated by the miners), (ii) the remuneration of the immigrant worker, (iii) (iv) private capital transfers. The first is the flow generated by Mozambican workers who work abroad and transfer funds (savings) to the country. The second is the flow generated by foreign workers who work in Mozambique and who transfer their own savings to the countries of origin. Current transfers (iii) and private capital (iv) are mostly driven by non-profit non-governmental organizations.

Figure 58 - General Data on the Evolution of Remittances, 2005-2015

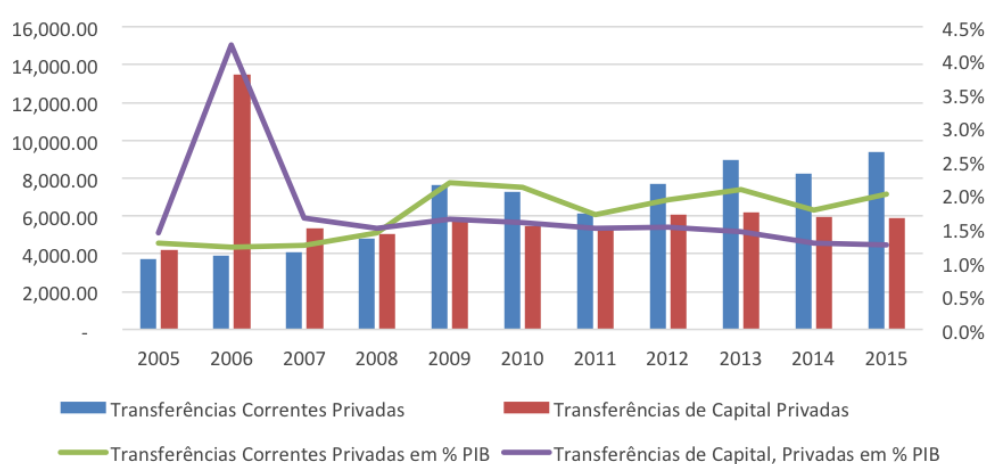
*Remittance flows of migrant and immigrant workers. MZN Millions 2010.*



Remittances of emigrant work, with details of the miners' shipments in RAS, MZN, 2010



Private current and capital transfers



Source: Bank of Mozambique, MITESS, World Bank. Authors' calculations

**309. The Bank of Mozambique is not the only institution that collects information, other institutions use data on remittances for other purposes, as well as Balance of Payments balance statistics.** The Ministry of Labour also collects information on remittances generated by mining workers, and finally, the World Bank tracks data on migration and remittances. MITESS has statistics on the numbers of Mozambican miners hired in RAS, but has no data on the wage paid. TEBA charges a commission for the recruitment work, but there is no data or information about it. The hired labourer at Gauteng has a one-year contract. During the first six months, you receive 100% of the salary in South Africa to cover the expenses to settle. For the remaining six months TEBA pays 40% of the salary in South Africa and 60%, without brokerage of other agents, in the ZAR bank accounts of the miners in Mozambique. Recruitment to South African farms responds to the same schemes.

**310. The government does not collect information about the destination of consignments.** The BdM and the Ministry of Labour do not collect information about how the miners' families apply these funds. Anecdotal indications indicate that this savings is used to build or improve houses to finance small commercial and agricultural businesses.

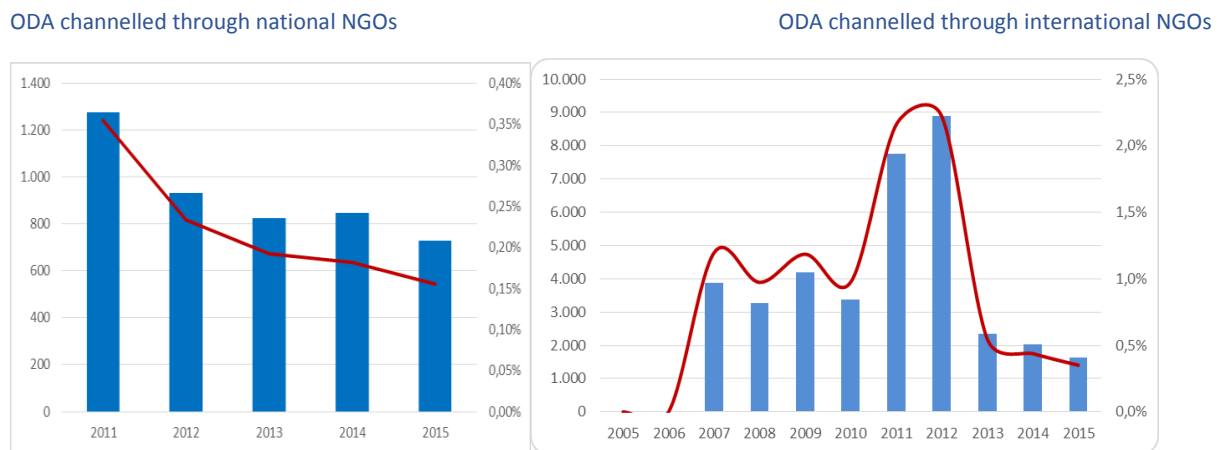
**311. The problem with different data sources is their consistency.** Significant discrepancies are noted between the data taken as references and other sources, namely MITESS and the World Bank and other official sources.

*Alignment of remittances with the country's development priorities*

**312. Further studies on remittance-related issues, such as the study that MITADER is undertaking to analyse the effects of remittances on microfinance, would need to be collected.** A microfinance study recently commissioned by MITADER devotes a section to remittances. There should be further study of isolated promotional measures that could increase the development impact of remittances. A more appropriate mix of current policies and measures could accelerate the exit from poverty of recipient households. For example, working with NGOs (in the area of poverty or rural development) to improve financial literacy of host families and co-finance risk co-lateralization to facilitate access to credit for small and microenterprise start-up or purchase of urban or rural properties.

#### 5.4.2 International Financing to NGOs and Private Institutions

Figure 59 - Evolution of NGO financing, 2004-2014, in millions of MZN, at constant prices 2010.



Source: MEF - DC. Authors' calculations

**313. The role of these organizations is valuable and recognized by the government.** However, in all sectors analysed, coordination difficulties and lack of information regarding the volume of channelled resources were evident. NGOs can have different sources of funding: they can generate own funds, and these funds can have both internal and external sources; can also manage ODA funds. In the latter case, there is information gathered by ODAMoz shown in Figure 59. Donors who contribute to the ODAMoz database also channel funds through both national and international NGOs. Figure 59 shows the volumes channelled by the cooperation partners to national and international NGOs. Volumes (according to ODAMoz data) in the 2011-12 biennium were around 2.6% of GDP, but then declined and became less relevant. In absolute terms, NGO funding in 2015 was US \$ 78 million, of which US \$ 54 million was channelled through international NGOs and US \$ 24 million through national NGOs.

**314. The lack of data on the contributions of funds channelled through NGOs (both national and international) is one of the great challenges that the government faces in order to manage this flow well.** The difficulties are natural in the relationship between governmental institutions and the wide variety of actors, private, non-governmental, national and international, who play a role in building the country's development and offering services to the population.

**315. Private development aid, which is one of the most globally significant sources of funding, is still under-explored in Mozambique.** According to World Bank estimates, the volume of private aid globally is about \$ 60-70 billion a year, equivalent to almost half of the net ODA disbursed annually by all OECD-DAC members. The US is the leading source of philanthropic private flows to the developing world, with \$ 39 billion transferred in 2010. A new generation of individual philanthropists has grown rapidly, with more than 100 billionaires facing Bill Gates' challenge of leaving behind least half of its



wealth for non-profit activities over time. Institutions such as the Bill and Melinda Gates Foundation and social impact investors, such as the Shell Foundation and the Acumen Fund, have gained widespread prominence over the past two decades<sup>110</sup>.

**316. Experiences at sectoral level make it possible to be optimistic about the possibilities of this type of financing.** There are several ministries that work with NGOs and have designed ad-hoc mechanisms to establish a productive relationship. There are many individual cases highlighting the innovation and dynamizing component of these interventions, such as solar electrification projects in schools, hospitals implemented by NGOs (MIREME) or sustainable coal production (NAMA Denmark). However, there is little that is known systematically of this kind of interventions and successful experiences at a specific level that could be replicated. For the purposes of this AFD, three sectors were analysed: Education, Health and Social Action<sup>111</sup>.

**317. However, there are no evaluations to compare the relative efficiency of NGO performance in the provision of public goods and services in Mozambique.** The channelling of ODA through NGOs is usually justified by the search for greater efficiency in the provision of public goods and services to the beneficiaries. In Mozambique there are no specific studies to compare (with clear indicators of performance) the efficiency in the provision of these services<sup>112</sup>. Practices that circumvent the intervention of the national, provincial or district government seek to obtain 'quick wins', sometimes originating in the accountability system of these organizations to their specific donors. There is a danger in the recent NGO funding trend, which requires an excessive focus on delivering 'measurable', and which tends to ignore important non-economic aspects of development, such as community empowerment and rights-based approaches, which can be ignored if NGOs are paid only for delivery of measurable services.

**318. International experience suggests that this type of funding should be better explored.** Experience from other AFDs in the Asia-Pacific region shows that the State achieves significant benefits in using these resources when this type of interventions is coordinated at a strategic level. There is also evidence of significant benefits in terms of efficiency in cases of co-financing of the provision of social services through public-private partnerships (PPPs). In this type of PPPs, the State subcontracts the provision of these services to NGOs, financing all or part of its cost. Experiences from previous AFDs show ways that Mozambique could decide to explore, such as:

- *Cooperation in partnership in Vietnam.* When bilateral partners began to move away from traditional sectoral support, cooperation shifted focus on mutually beneficial relations. This involved a shift to new forms of assistance based on partnerships between public agencies, academics, NGOs and businesses in Vietnam and the donor country. This partnership-based cooperation is new and untested in the world and requires better information flows so that Vietnamese institutions can choose the support that best meets their needs;
- *Impact financing in Cambodia.* The non-profit sector has focused on partnerships with the private sector and has begun to explore the use of Development Impact Bonds (DIBs) and other innovative financing mechanisms described in Box 6. Their potential is accelerated when there is interest and commitment confirmed by government, donors and NGOs, as well as the private for-profit sector.

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<sup>110</sup> World Bank, "Financing for Development Post-2015," February 10, 2015, 1–54.

<sup>111</sup> See Annex III, Experiences from Working with NGOs in Sectors.

<sup>112</sup> For example, costs per vaccinated child, or the printing and distribution of textbooks / manuals (or the time to reach the target population), etc.

**319. The legal framework governing NGO activities in Mozambique is old, incomplete and needs to be revised.** There is no internal regulation regulating the activities of national NGOs in the country, and the governance framework for the operation of international NGOs was defined in 1998 (Decree 55/98). For what matters in this study, we emphasize that such Decree: (i) delegates to the Minister of Foreign Affairs and Cooperation (MINEC) the authority to authorize foreign NGOs, after hearing the central body of guardianship (Article 5).

***Caixa 6: Investimento de impacto, títulos de impacto no desenvolvimento e outras abordagens inovadoras de financiamento de ONGs no Camboja***

**Títulos/Obrigações de Impacto de Desenvolvimento** (ou Development Impact Bonds - DIBs). Compreendem um contrato que concede uma quantia acordada a um contratado do sector privado que entregue um cronograma acordado de bens ou serviços públicos. Os benefícios citados incluem a transferência de risco para o sector privado, bem como incentivos à inovação (especificando os resultados em vez de metodologias que podem permitir que o provedor de serviços explore novas opções de prestação de serviços). O seu uso foi analisado pela AFD no Camboja, onde o mecanismo financiou projectos de água e saneamento implementados pela ONG East Meets West, que recebeu 10,9 milhões de USD da Fundação Gates para usar como modelo público-privado para melhorar o saneamento e a higiene entre os pobres rurais do Vietname e do Camboja, beneficiando 344 mil famílias. Como os DIBs representam fontes adicionais de financiamento para o desenvolvimento, eles podem ser uma importante fonte de novos financiamentos para o desenvolvimento em Moçambique no futuro próximo.

**Investidores de Impacto.** Este tipo de investidores compreende empresas que fornecem financiamento de DIBs relacionados com o desempenho. No Camboja, por exemplo, o Insitor Impact Fund, com investimentos em Khmer Water Supply Holding e Uberis Capital, apoia o desenvolvimento de microempresas. Outro empreendimento deste tipo (ARUN, baseado em Phnom-Penh) é também um investidor de impacto social que apoia empresas sociais, por exemplo, pequenos agricultores e empregos para mulheres, usando capital de indivíduos japoneses e parceiros corporativos. Outros investidores de impacto incluem a Advantage Ventures, que investe em saúde, desenvolvimento rural, educação e energia limpa, e a EcoAsia, que possui um fundo de 100 milhões de USD, que apoia negócios regionais em toda a cadeia de valor agrícola.

Investimentos de impacto social destinam-se intencionalmente a objectivos sociais específicos, juntamente com um retorno financeiro, e medem a consecução de ambos, quebrando a distinção entre 'fazer o bem' e 'fazer bem'. No Camboja, a Fundação Fred Hollows, que fornece cuidados para os olhos, é um exemplo de uma organização que está a usar os modelos de investimento de impacto como parte de seu modelo de financiamento de desenvolvimento. Esta pode ser uma opção para as empresas do sector privado, empresas sociais e organizações sem fins lucrativos colaborarem para mobilizar fundos e promover o impacto no desenvolvimento.

**320. The main objective of the current decree is to regulate the procedures for registering and authorizing the operation of new NGOs.** In the registration process, MINEC requires the submission of a series of information of great potential use, such as) the proposal for the general program of activities and the financial resources available to carry out the intervention; (ii) document of the projects to be executed, (iv) staffing table to be worked in the organization. The project document requested should define project objectives, approach and strategy, coordination, monitoring and evaluation mechanisms, expected results, duration and budget. Unfortunately, this information is not systematically incorporated into a database and is collected only during the authorization process. This responds to a very different social and political reality from the current one, where the participation of NGO financing could become an important source of resources.

## Availability and Sources of Information

**321. ODAMoz does not fully record the volume and type of funding that is being provided to NGOs.** A source of information on donations from international donors is ODAMoz, where funds are channelled through national and international NGOs. But, according to DC-MEC, the government's information on these flows of funds is limited, inconsistent and therefore underutilized. An alternative

source that the government could try to improve is information that donors report to the International Aid Transparency Initiative (IATI)<sup>113</sup>. The information is published on a standard and voluntary basis by donors, and the register currently includes information from 473 international aid organizations and a significant part of the aid flows of the European Union. The available data on Mozambique based on IATI could be very useful if corrected with the partners. The base offers the possibility of analysing the following financing flows: (i) from governments to International NGOs operating in the country; (ii) from governments to national NGOs operating in the country; (iii) governments to Academic and Research Organizations; (iv) from International Foundations to NGOs; (v) from Foundations to Academic and Research Organizations and (vi) from multilateral organizations to NGOs. The published information on Mozambique in the IATI is of great potential value, but it is necessary to work together with the partners to correct some observable systematic errors in the regular publication.

**322. In addition, additional monitoring of the formal economic activity of NGOs could be analysed by the Tax Authority.** Article 9 of the law states that NGOs must register in their respective tax area and are subject to fiscal supervision or auditing, in accordance with the specific tax legislation in force. Therefore, AT can play an important role in monitoring the economic activity of NGOs, which is possible since the existing NUIT coding grants the same generic ordinal number for all NGO activities. economic activities of each NGO operating in the formal market. These data should in fact be used as a double verification system of data submitted annually by NGOs to MINEC.

#### Next Steps: Areas that Need More Attention

323. The revision of Decree 55/98 is a high priority and should reinforce the procedures to ensure the protection of government's annual activities by sector and geographic level. The decree establishes that during the exercise of their activities NGOs must present annual activity reports according to procedures to be defined by MINEC. At present, there are no defined procedures to exercise this guardianship or systems of penalties to ensure the application of the decree. A simple way to accomplish this type of task would be to define the need for an annual report as part of keeping the authorization working, and to design a standard format that could be included in ODAMoz, which NGOs could access, from a distance.

**324. The revision of the Decree could introduce other strategic objectives and mechanisms to enhance private investment in activities aligned with national targets.** A reform of the existing legal framework is necessary to achieve the following objectives:

- Allow MEF to know the scope of NGO activities, and the volume of funding per sector, especially with regard to the activities of NGOs that are not registered in the OE;
- Enable government ministries and agencies (central, provincial and district) to learn more about the activities that NGOs carry out in their areas of competence and to initiate action to work together;
- Establish multi-level dialogue mechanisms to improve the quality of NGO intervention. This could include a strategic level (to stimulate coordinated work in major national priorities (implementation of the NSDS or the DSOs), accompanied by sectoral dialogue mechanisms on specific policies and technical level on shared monitoring;

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<sup>113</sup> The IATI is an initiative launched in 2008 at the Third High Level Forum on Aid Effectiveness held in Accra with the purpose of "publicly disseminating regular, detailed and timely information on the volume, allocation and, where available, the results of development expenditure, to enable more accurate budgeting, accounting and auditing by developing countries. "As part of the initiative, a common standard (IATI Standard) was created that allows donors to publish data in a grassroots data to share that information with structured and consistent data.

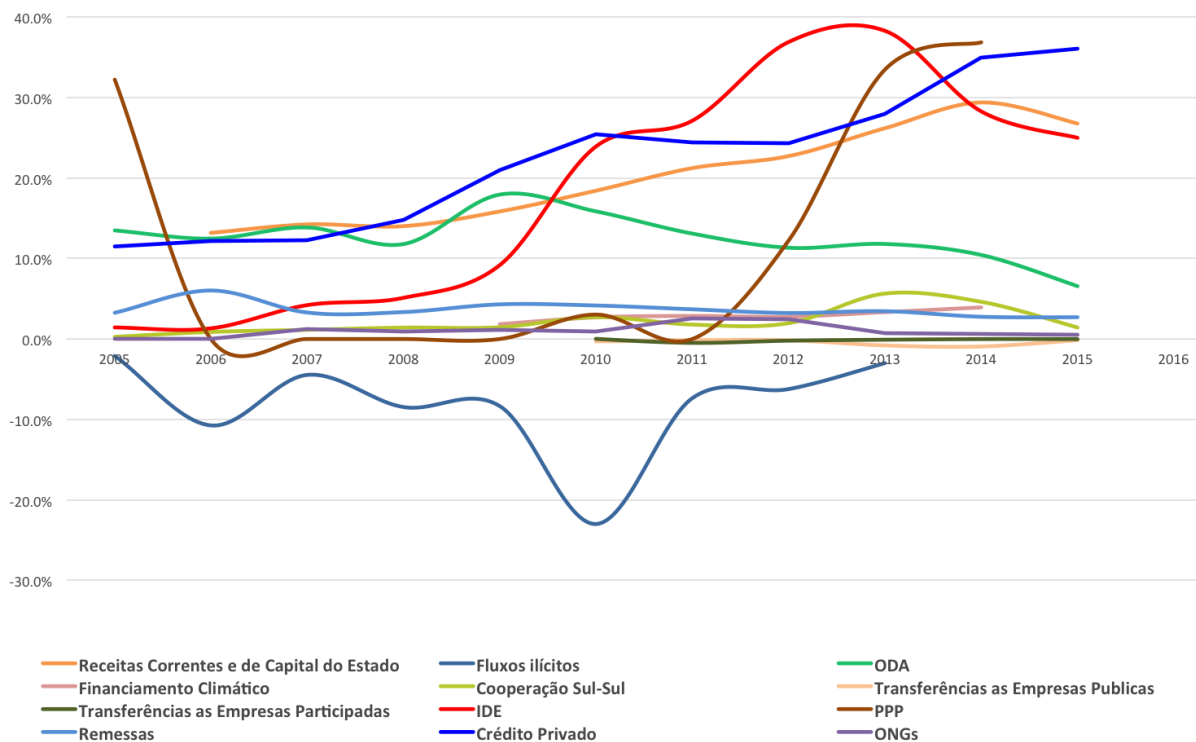
- Establish incentives to stimulate NGO investment and co-financing in public-private partnerships for the provision of services and other actions that can enhance the impact of available public funding and stimulate private investment in critical areas.

**325. The potential volume of this type of funding is very high, and can be streamlined rather quickly and at no great cost to the government.** According to the World Bank's global estimates, this funding should be in the order of 50% of ODA. The volume of ODA in Mozambique was USD 806 million in 2015, representing 6.8% of GDP, while the volume of NGO funding (probably well below the actual volume) was USD 78 million. There could be scope for USD 700 million per year growth, which could represent almost 6% of GDP. These data should be more carefully estimated, since Mozambique being one of the poorest countries in the world could expect to obtain a larger share of the world average. The good news is that the measures needed to stimulate and promote such flows and to ensure alignment with the national objectives mentioned above do not entail major costs or extraordinary capacities.

## 6. Prospective Analysis of Major Financing Flows

### 6.1 Statement of the main cash flows

Figure 60 - Historical evolution of the main financial flows analysed (as% of GDP)



Source: AFD team based on official data

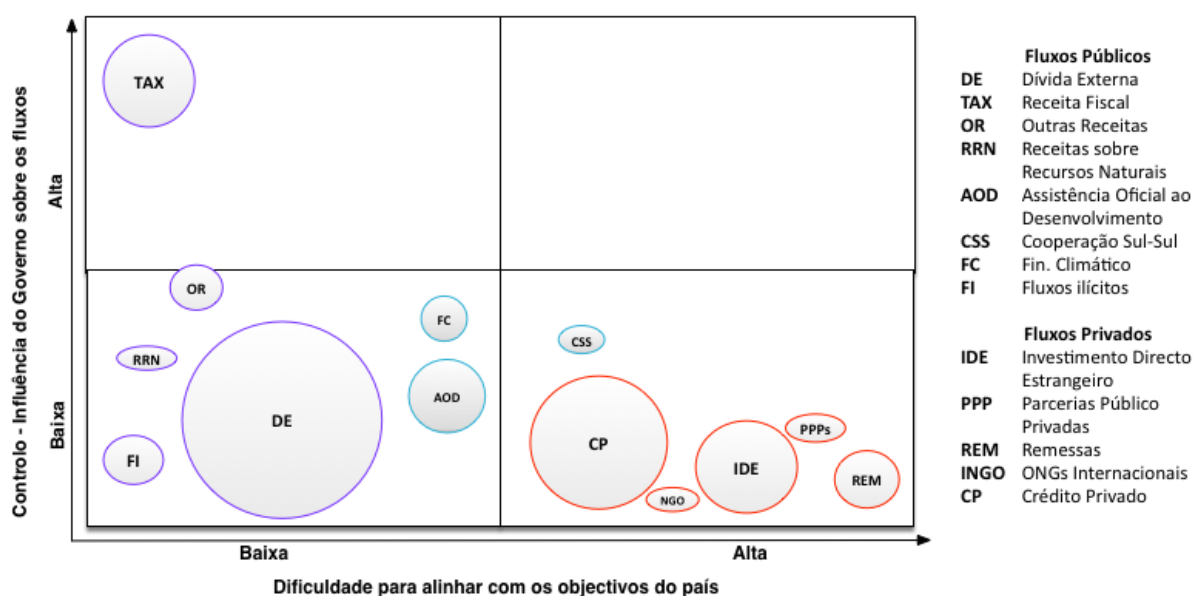
**326. This evaluation provides general guidance for the future mobilization of domestic, external, public and private resources in Mozambique.** The initial estimates should justify the need to carry out more systematically the prospective analysis of the priority financial flows. The historical evolution of major flows summarized in Figure 60 includes the main sources of public and private financing analysed in AFD.

**327. The evaluation also proposes to analyse the current alignment of these flows with the country's priorities and the ability of the government to control or influence its development.** The prospective

analysis evaluates the possible evolution of the selected flows, considering their historical trends and the possible impact of the proposed management reforms. Figure 61 summarizes the results of the flow analysis presented in Chapters 4 and 5 of the AFD and presents the relative position of flows according to two variables: (i) the government's ability to control or influence flow evolution; (ii) the level of flow alignment in financing national priorities.

**328. The initial state indicates the need to improve control and alignment of major flows.** The location of flows in the lower half of the graph indicates government control problems, which is particularly noticeable for public flows that should be controlled directly by the government (violet). Private flows are not under the direct control of the government, and the possibilities to align them to finance public goods are rather limited. But the government can still aspire to better influence its development and performance. To define alignment with national priorities, the analysis considered the economic, social and environmental dimensions of sustainable development. This is important because some private flows that can produce positive economic impacts can also undermine the country's environmental or social priorities. A summary of the main results of the diagnosis of the individual flows is presented below:

Figure 61 - Status of the main analysed flows



Baseline of the main flows (values as% of GDP)

**329. External Debt (130%).** The lack of control of commercial debt management with government guarantees and the weak prevention of debt risk incurred by public and investee companies generated the current situation of debt unsustainability. Government is on the right track, and the quality of government control should improve substantively. Most likely, emergency solutions will have some consequences for debt misalignment with national priorities.

**330. Tax Revenue (22.8%).** The overall performance of the government, and in particular TA, in the collection and control of tax revenue is considered satisfactory. This flow can grow as a percentage of GDP and TA can still achieve significant improvements in the performance of its core activities. The development of its capacity is an area of priority to maintain the dynamics of revenues in the short term.

331. *Other Taxes and Revenue from Natural Resources (0.8%)*. This subgroup of tax revenue can grow strongly, but it requires significant changes from the tax exemption system to exploitation. Tax evasion is considered high and improvements in the current control system could make the collection values approach the values of countries under similar conditions.

332. *Other Non-Tax Income (4%)*. The group of Non-Tax Revenues + Consigned + Capital Revenues performed well below that recorded by tax revenues. The government can generate volume improvements, but it should strengthen centralized control by setting specific responsibilities for its monitoring and also generate quality improvements in decentralized management.

333. *Illegal Flows (3%)*. The government does not collect analytical information on these flows and does not clearly establish the responsibilities for its elimination. The average value of the period studied is over 8% of GDP. The government can substantially reduce this flow by improving the control and inspection of export / import companies and by limiting the use of tax havens in established companies.

334. *Official Development Assistance (6.6%)*. The alignment capacity of these flows is limited by the poor information available and the incompatibilities of their programming with the current plan and budget system. Its reduction is inevitable in the long run, but the government can try to extend the future life of ODA by building trust and gradually introducing other mechanisms such as Aid For Trade.

335. *South-South cooperation (1.4%)*. The level of control of this flow is weak and the government has no formal mechanisms to assess the cost-opportunity ratio of CSS credit with respect to other options. The growth of this flow over the next decade is conditioned by the capacity for debt growth.

336. *Climate Financing (3.9%)*. This flow can grow substantially if government - with the introduction of the FNDS - is able to improve the quality of management, and the diversification of access to public and private sources. The current alignment is weak and, to grow, the DNFN should ensure more transparency in management, and better integration with executing agencies and stakeholders (public and private).

337. *Private Credit (36.1%)*. Alignment of supply with priority sectors such as agriculture, industry, construction and tourism is weak. Similarly, access to credit for individuals and MSMEs is low, especially in rural areas. The government can achieve improvements by implementing measures to encourage the growth of this flow that encourage alignment, competence and cost reduction.

338. *Foreign Direct Investment (25%)*. The flow can grow significantly from 2022 with the expected start of hydrocarbon investments. In addition, the government can improve the promotion of FDI in the EEZs and ZEIs to improve alignment with the ENDE's industrialization goals.

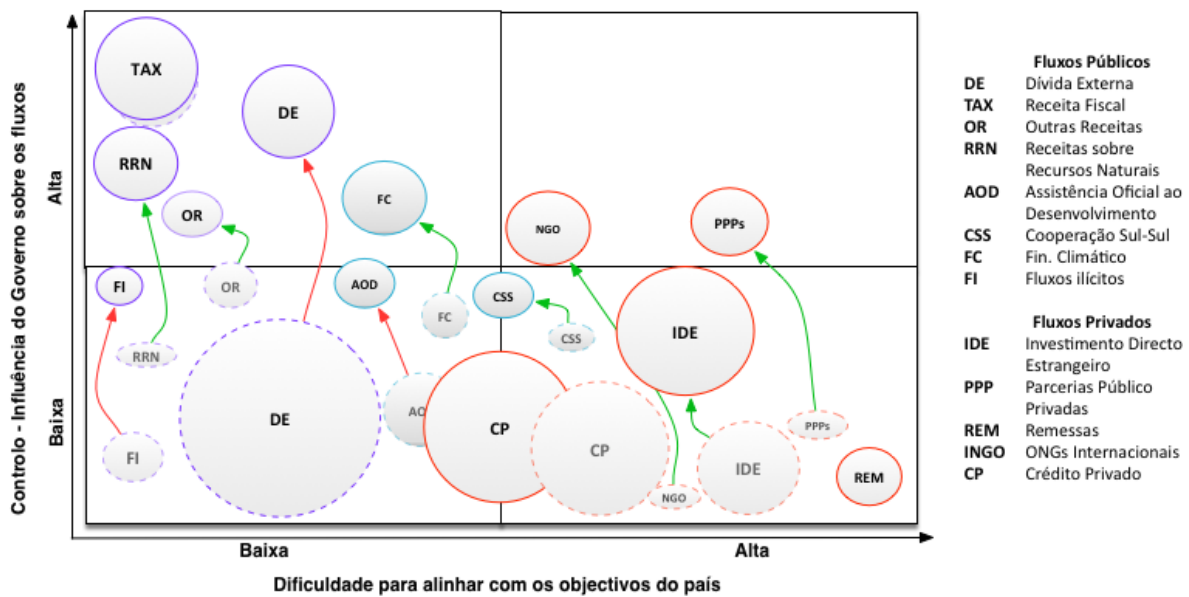
339. *Public Private Partnerships (n / a)* The government has poor control of contingent risk management for the State and does not have data to track the investment made. New management systems and a significant improvement in the quality of the IIP are necessary to ensure growth and alignment of this flow with national priorities.

340. *International NGOs (0.6%)*. The quality of the information in this flow is weak and it is estimated that the actual volume is much larger than that recorded in ODAMoz. The volume of this flow and alignment capacity can be significantly improved through better centralized and decentralized management and the encouragement of co-financing partnerships between NGOs and government agencies.

341. **Remittances (2.7%).** It is estimated that 23% of the population uses remittances (external or internal) and that the volume could grow. The government does not have many elements to control this flow but could pilot experiments to improve the development impact of remittances in the poorest communities. With information available, it is not possible to estimate targets for the growth of this flow. Changes in management improvement can have significant quantitative and alignment and control results. Figure 62 presents an idea of what could be the final situation for the flows analysed. The arrows in red indicate flows that should be reduced in volume while those that are green may increase. The AFD proposes significant changes in government control capacity (moves up on the chart) and a lot more modest in terms of alignment (left-hand movements in the chart). The necessary structural reforms in the plan and budget system are an important precondition for achieving alignment improvements.

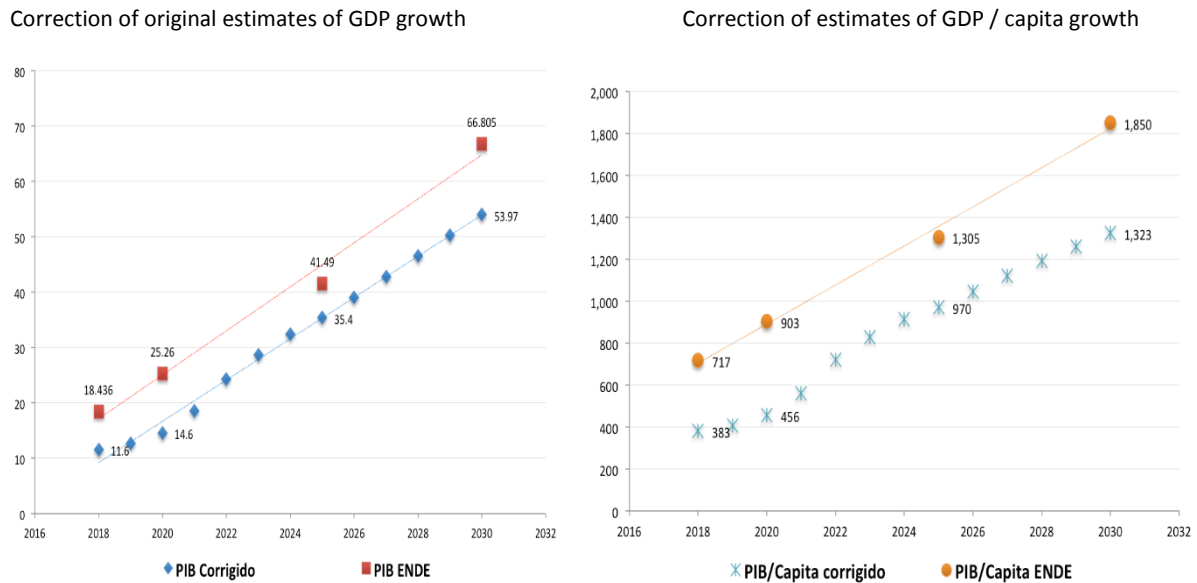
342. **Changes in management improvement can have significant results in terms of both quantity and alignment and control.** Figure 62 presents an idea of what could be the final situation for the flows analysed. The arrows in red indicate the flows that should be reduced in volume while those that are green may increase. The AFD proposes significant changes in government control capacity (moves up on the chart) and a lot more modest in terms of alignment (left-hand movements in the chart). The necessary structural reforms in the plan and budget system are an important precondition for achieving alignment improvements.

Figure 62 - Necessary changes in flow management



## 6.2 Projections of the evolution of the main flows

Figure 63 - Correlated projections of the NSDS taking into account current data



Source: AFD team based on official government data

**343. The projections analysed took into account the new situation in the country and corrected the original ENDE projections.** The present situation has substantially modified some of the original NSDS hypotheses and for this work the most recent scenarios and projections available from the MEF<sup>114</sup> have been used. The main differences can be seen in the graphs in Figure 63. The level of GDP expected in 2018 is well below that projected in the ENDE, and GDP per capita is much lower, since, in addition to GDP expectations having decreased, projections current population growth rates are much higher than originally expected. According to the ENDE, the expected value of GDP per capita for 2018 was USD 717, while, according to the latest available figures, this figure is only USD 383, which greatly modifies the baseline.

**344. The objective of this exercise is to generate a strategic discussion about the need for government to exercise leadership in the management of proactive policies to influence the development of these flows.** The data presented are very primary estimates of the type of growth that could reach these flows. Further examination is needed to model their behaviour and to assess with more developed technical elements the possible effect that changes in policies could have on the volume of flows. Modelling should also consider the interactions between flows and the combined effects of reforms. This work goes beyond AFD's capacity and should be part of the analytical and macroeconomic modelling work that the MEF should be able to do in the future. The example of the state revenue projections presented below exemplifies the value that this work could have if it were carried out exhaustively and recurrently.

### Example: Projections of Current and Capital Revenues of the State

**345. Public revenue can grow significantly over the review period if the government achieves progress in three independent areas.** The proposed guidelines for the development of these flows were grouped into three major categories of relevant potential: i) expectations of growth in total

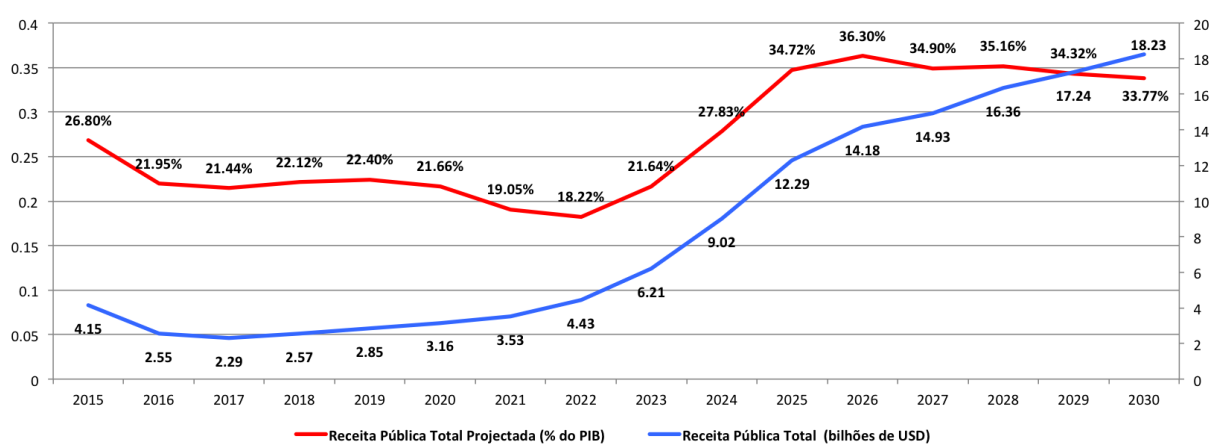
<sup>114</sup> The sources used are the same as those used in the presentation by H.E. the Minister to creditors in 2016, and they are now being used to negotiate with the IMF. They are not definitive data and were used only as an example of what this type of analysis could achieve in the future.



revenues due to future natural gas exploration; li) the expansion of revenues from mineral resources and the control of tax evasion; iii) improvements in non-fiscal revenue collection and decentralized government management.

**346. Expected effects of the expansion of hydrocarbon revenues.** The data presented in Figure 64 correspond to the government's initial forecasts of the effect on public revenue once the companies holding the exploration concessions in the Rovuma basin begin production. The government estimates that revenue growth will begin to accelerate from 2022 onwards. Official projections estimate total revenue expansion to increase from 26.8% of GDP in 2016 to 33.8% of GDP in 2030. This expansion is fundamentally boosted by the collection of fiscal revenues directly generated by the production of hydrocarbons and by the multiplier effect of the large investments expected (of USD 20 billion) in the collection of taxes on income and on goods and services.

Figure 64 - Initial government projections of revenue expansion with the expected effect of gas production



Source: Official government data, Authors' calculations

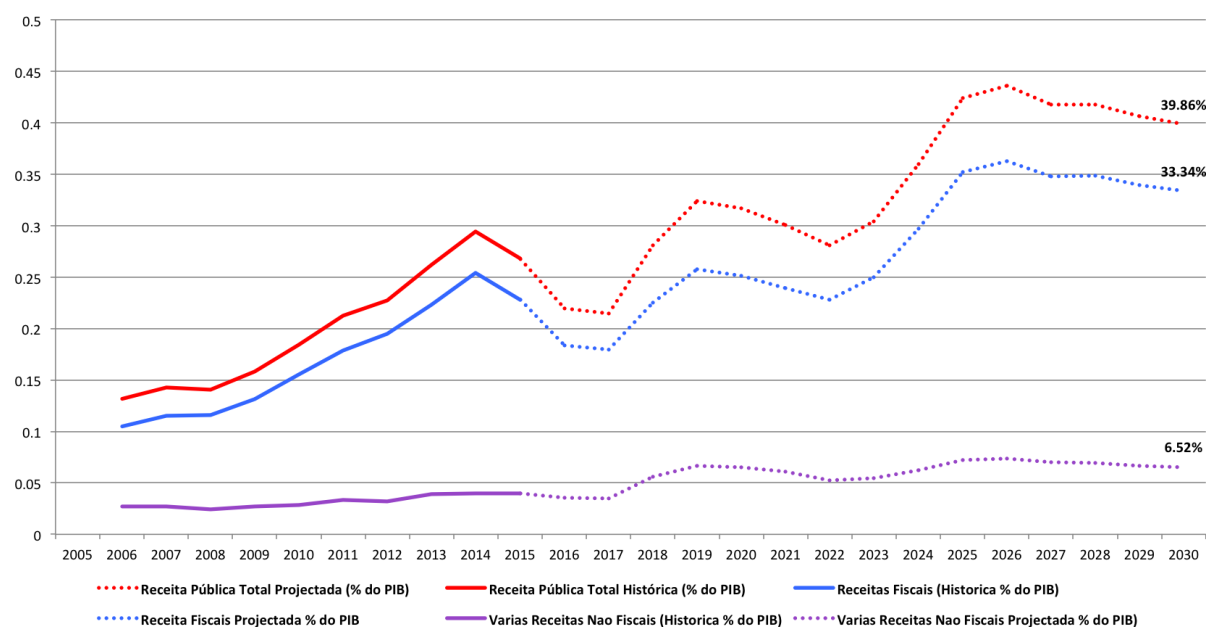
**347. Growth of mineral revenue.** In addition, revenue growth was projected based on the effects of future government interventions to improve mineral revenue. The projection presented in Scenario II (Annex IV) did not consider the possible effects on reforms of the megaproject incentive system. These reforms will undoubtedly be politically laborious to negotiate and may take a long time, and at best would only affect future production. Therefore, the projection has taken a conservative stance and estimated the effects of a gradual reduction of tax evasion in the export of raw materials. It was also estimated conservatively that revenues could reach the level of neighbouring countries by 2024. With this aggregate, the projected value of Total Revenue would increase to reach 36.77% in 2030.

**348. Growth of Other Revenues.** The projection considered the increase in tax collection in the richest municipalities, and the generation of 2.2% to 5% of GDP in five years. It has been considered that this increase will produce a large volume of meticais, which in the short term is also significant as a percentage of GDP. But the expected growth of these revenues in nominal terms will not be able to keep up with the expected accelerated pace of GDP (of more than 7% from the year 2020), and therefore reduce their weight in the medium term. The scenario added very modest gains above the average (of 1% of GDP) of the set of Non-Fiscal Revenue (Non-Fiscal, Consigned and Capital Revenues), which can be generated by improving efficiency in decentralized management.

**349. Using conservative hypotheses, the combined effect of these measures is significant.** The data in Figure 65 are based on the data in Figure 64 and add the effect of obtaining positive results in the three areas. These values are far from the maximum possible. The projection has the following effects: (i) expected oil revenues, (ii) moderate growth in mineral revenue (3%) due to short-term measures,

without considering the effects of a change from exemptions to megaprojects, (iii) the effect of increased revenue in the richest municipalities (3.5%) and very modest results (1%) of improved efficiency in decentralized management. With these assumptions, Total Public Revenue could grow up to 39.86% of GDP in 2030, corresponding to an increase in Revenue Taxes of up to 33.34%, and of Non-Fiscal Revenues up to 6.52% of GDP.

Figure 65 - Combined Effect of the main measures to increase Total Revenue



Source: AFD team based on official government data

### Projections of other flows (values estimated as% of GDP in 2030)

**350. The expected evolution of other flows was projected considering the overall projected scenario and the estimated effects of the main measures that could be implemented.** Using similar hypotheses, projections were made for the main flows where sufficient information exists. Estimates are, in all cases, quite conservative, and do not represent the maximum values that could be reached by each flow. However, obtaining them will require well-organized and systematically implemented interventions. The data in Figure 66 combine the effects that could be obtained from the implementation of the following reforms:

**351. Official Development Assistance (6.0%).** The projection assumes a return to the pre-crisis levels (in 2022), and then a dampening reduction of this flow due to a good government policy of offering alternatives to the AGO and ensuring the permanence of donors.

**352. South-South cooperation (9.8%).** The development of this flow is practically nil in the first three years (to 2020) due to the country's expected limitations of incurring new external debt. The flow begins to grow from 2020 (due to the positive results of the increase in revenue) and accelerates rapidly in recent years with the arrival of the rapid growth phase.

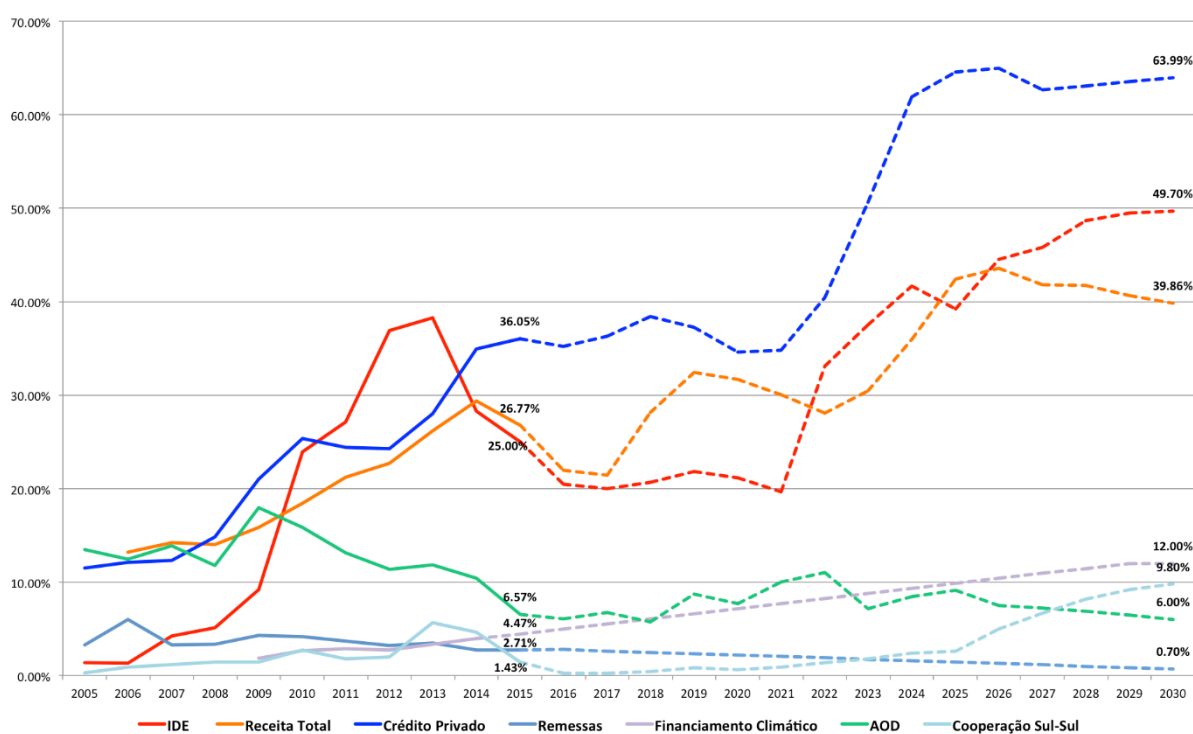
**353. Climate Financing (12%).** The lack of empirical evidence does not allow for a better modelling of this flow, but linear growth has been estimated assuming that the FNDS is successful and is able to attract (public and private) financing gradually to reach a share more suited to the country's potential in the year 2030.

354. *Private Credit (63.99%)*. The growth of this flow begins with a similar evolution to the expected GDP, but acceleration is expected from 2022. This growth is fundamentally due to the evolution of domestic demand, but also includes the expected effect of policies to accelerate access to MPMES and the financial inclusion that is assumed to have a slow impact.

355. *Foreign Direct Investment (49.7%)*. The flow increases significantly from 2022, with the arrival of hydrocarbon investments. The projection assumes a larger growth than expected only from these investments from 2025 due to the success of attracting other mineral exploration investments. It also assumes very weak results in the promotion of FDI in the EEZs and EZE's due to the lack of impact of policies to improve the supply of skilled labour and slow progress in improving the supply of reliable energy at competitive costs .

356. *Remittances (0.7%)*. It is estimated that this flow will begin to decline gradually from 2022 because of two combined effects; (i) the expected increase in the supply of employment, which reduces the need for emigration; (ii) the expected progress of financial inclusion policies.

Figure 66 - Expected evolution of the projected flows



Source: AFD team based on official government data

**357.. In the case of flows that were not projected, the valuation used other methods to estimate future values.** Figure 66 shows the results of the projections. For some flows, the lack of reliable historical information does not allow projection of their evolution, and therefore future values were estimated using international comparative parameters or back-casting from well-defined internal targets. These procedures were applied to the following flows:

358. *External Debt (65%)*. The main assumption for the projection of all flows discussed earlier is that the country can successfully negotiate with creditors and set a reasonable debt rescheduling. This allows the country to resume the path of growth in 3-4 years. Despite the country's accelerated growth process projected from 2022, it was estimated that by 2030 alone the country could reduce

its debt-to-GDP ratio to values equivalent to those of 2014. In order to achieve this result, in all areas of revenue analysed earlier.

359. *Public-Private Partnerships (1%)*. Projected investment levels are higher than the current estimate (0.7%) estimated by the World Bank for investment in Emerging and Developing Markets (EMDEs)<sup>115</sup>. Although this volume will be much larger by 2030, it was estimated that Mozambique should make relatively slow progress in the actual realization of PPPs, because of the priority: to achieve the government's capacity improvements first before accelerating the progress of these flows.

360. *International NGOs (5%)*. The projection considered that the volume of this flow could increase to values like those of other countries (such as Bangladesh, Fiji or Nepal), which, like Mozambique, are in the category of destinations of great interest for this type of donations, but have succeeded in defining a good policy to stimulate this type of financing.

**361. The final result defines a different distribution of the main sources of financing available in the country and of the revenue of the State.** Figure 67 summarizes the main projections of financing flows and illustrates a framework dominated by projected growth in FDI, Public Revenues and Private Credit. It also indicates the increasing incidence of other flows such as Climate Finance and South-South Cooperation. The figure also gives an idea of the future changes in the distribution of Current Revenues and State Capital, with a relatively large increase in other taxes (directly related to the production of mineral resources) and non-tax revenue. The internal distribution of the Tax Revenue assumes small changes, favouring the continuation of a moderate-income growth over income, in relation to that of goods and services.

**362. The projection also marks the consolidation of the transformation process of the structure of the economy.** The last graph in Figure 67 indicates the progression of the structure of the main sources of financing (domestic and external, public and private) that sustain the economy. The trend of structural change is relatively clear: as the country progresses, it relies less and less on external public funding and consolidates the predominance of private domestic finance and public revenue. The changes in composition within each category also mark a clear trend; for example, external public funding does not continue to have the initial downward trend because the planned structure for 2030 incorporates more and more climate finance and SSC flows, with a progressive reduction of ODA.

**363. To achieve these results, the government must implement important changes in the policies governing the different flows.** The analysis presented in Chapters 4 and 5 of the AFD and summarized below in Section 7.3 indicates that, in most cases, to achieve these results the government must implement important reforms in the policy frameworks governing flows and in institutional coordination mechanisms. It will therefore be necessary to develop five-year strategic plans defining the sequence of interventions needed to achieve these transformations.

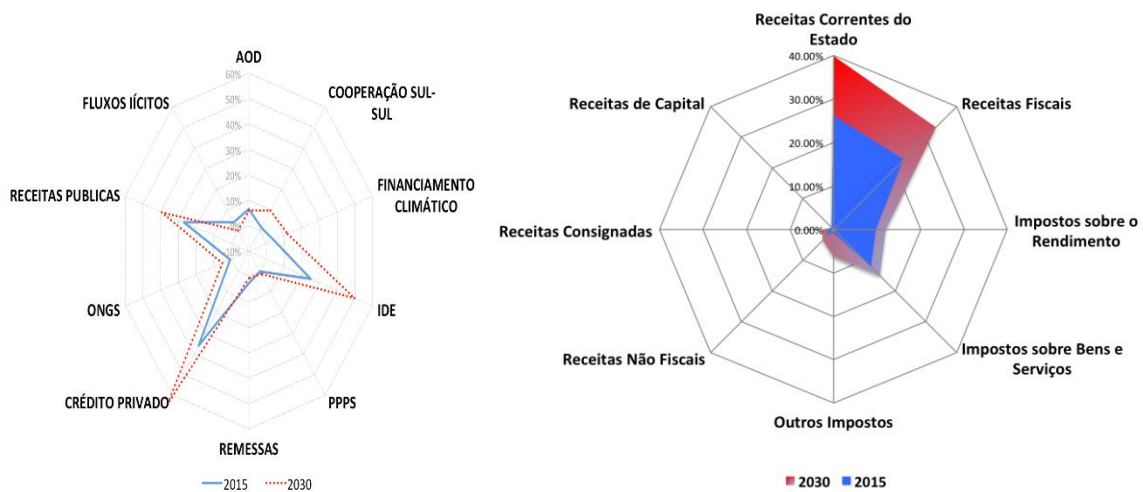
Figure 67 - Expected evolution of major flows and Public Revenue (as% GDP)

Distribution of major flows

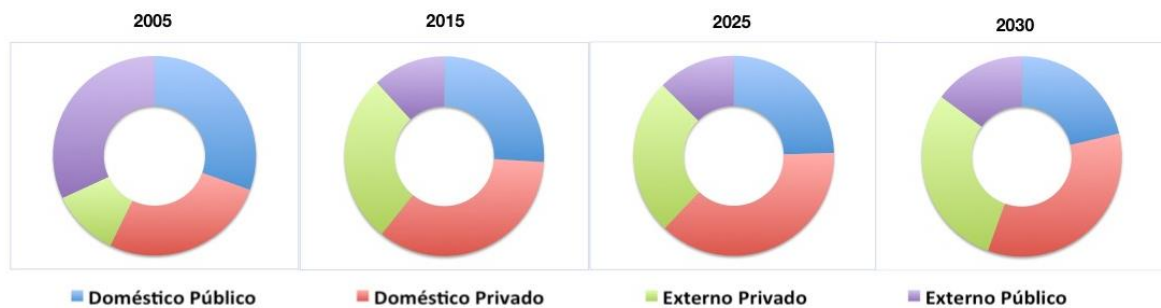
Distribution of State Current Revenues

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<sup>115</sup> EMDEs: Emerging Markets and Developing Economies.



*Evolução da Estrutura de Financiamento*



Source: AFD Team, based on official government data

### 6.3 The advantages of adopting an integrated and comprehensive vision

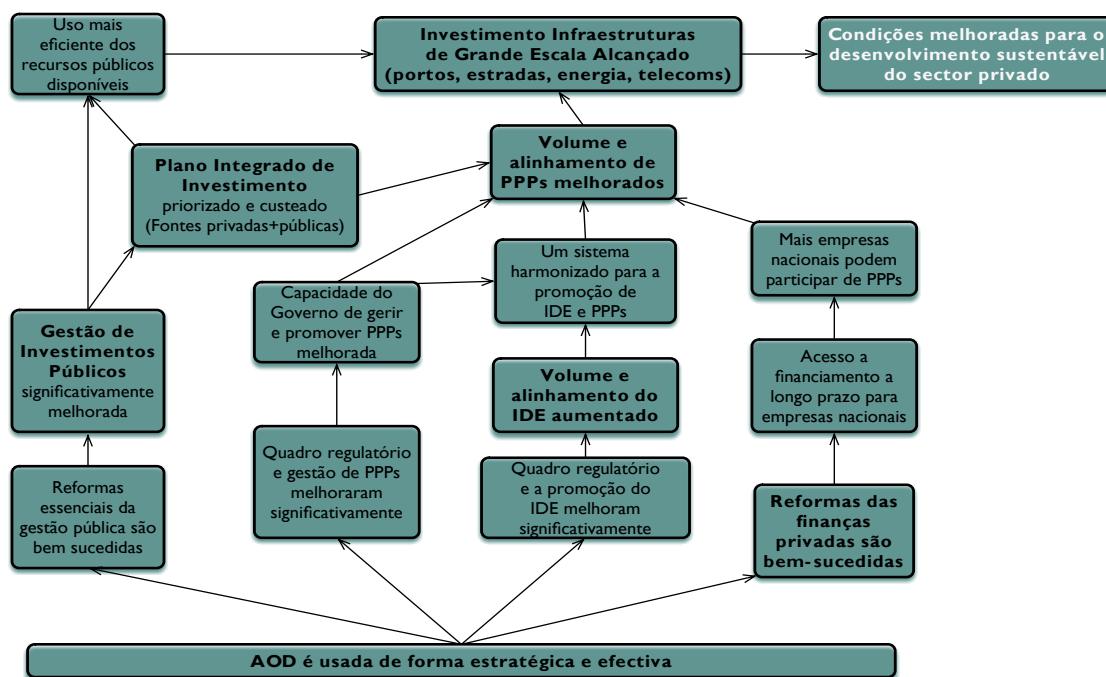
**364. The last aspect is to examine the desirability of developing an integrated strategic vision to improve the joint impact of the reforms undertaken on individual flows.** The government could significantly multiply the effects of policies to improve the management of independent financial flows using an integrated vision. An added value of the proposed approach is the focus on understanding the interconnections between individual flows and how to sequence and plan reforms to improve their combined effect. Most of these interactions are known, but generally, policies do not take this holistic approach into account. The example of continuing to finance large-scale infrastructures should illustrate the benefits of this approach.

#### *Example: Financing of large-scale infrastructures*

**365. Financing large-scale infrastructures to accelerate private sector development can be significantly improved with an integrated approach.** The following example examines the benefits of using this approach. Private sector development depends on several cross-cutting policies, but a critical factor is the need to modernize national infrastructures (roads, ports, communication, energy, telecommunications) that require large-scale investments. The AFD has shown that the government will have a limited financial capacity to respond adequately to this challenge, which is fundamentally due to significant limitations in the capacity of public funding, and policies to prioritize, finance and implement development projects. infrastructure. The current system builds bridges and roads and develops power generation plants. But these works are not located to change the competitive conditions of a particular geographical area, which could accelerate productive investment by geographical areas related to specifically identified value chains. AFD identified the following synergies

that the government could derive from a strategic and holistic approach. Figure 68 summarizes the key interactions identified among the various policy elements analysed.

Figure 68 - Expected evolution of major flows and Public Revenue (as% of GDP)



Source: AFD Team, based on official government data

366. *Public Investment Management (PIM)*<sup>116</sup>. The government has begun reforms to improve the management of public investment with a view to making more efficient use of available resources. These reforms (represented by the orange in Figure 68) should produce significant improvements: (i) the design and use of the Integrated Investment Plan (IIP) (which should be the main planning tool for public investment) and (ii) in more efficient processes to improve the use of available public investment. AFD identified the need to improve the quality of the IIP, especially the feasibility studies of the projects included, the prioritization system and the IIP's ability to select projects that could use all or part of private funding sources.

367. *Reforms and Management of PPPs*. At the same time, the government is carrying out reforms in the management policy of PPPs (represented in blue in the figure). AFD has identified the need to ensure that government is able to manage and promote PPPs to leverage private resources to implement the IIP. The current system of PPPs decentralizes the initiative for government agencies and does not necessarily ensure that these will be undertaken to address these specific needs.

368. *Reforms of Foreign Direct Investment (FDI)*. In addition, the government is implementing a framework of reforms aimed at improving and promoting Foreign Direct Investment (FDI). Considering that most investors for large-scale infrastructure investments are likely to be foreign, investment promotion work must also be synchronized to attract enough investors to meet the IIP priorities. These guidelines will be complemented by the monitoring and evaluation of existing and defined AIPEX priorities.

369. *Development of Private Credit*. To allow national companies to participate in these PPPs, the domestic financial market must provide long-term financing instruments with appropriate and

<sup>116</sup> *Public Investment Management - PIM*.

competitive terms with those that will have access to foreign companies. The reforms in the private financing system (in the yellow) should prioritize the strengthening of the Stock Exchange (streamlining the financing of bonds or bonds), or establish intermediation mechanisms so that companies can access credit windows to the private sector large multilateral banks.

370. **Official Development Assistance (ODA).** The above-mentioned reforms use technical assistance resources that should be provided and prioritized through the national ODA management system (shown in green in the figure). The system should ensure coherent and sufficient availability and support for all policy areas. It may therefore be necessary to deprive other initiatives to ensure the availability of sufficient funds to produce these reforms in a timely manner.

**371. The example examines how to achieve significant synergistic benefits through strategic and integrated management.** A comprehensive overview of the above-mentioned policies could enhance the development of the private sector with the same existing or accessible resources: Significant synergistic results could be obtained if the system is able to function in an integrated way with the following objectives:

- **Prioritization of Public Investment.** The improved IMP emerging from IMP reforms is an important precondition for defining public investment priorities, especially in areas where private finance cannot be achieved. This should reprioritize other competitive needs for the use of these scarce funds;
- **Prioritizing the development of PPPs.** The IIP should also be the main guide for defining the development of PPPs by the central government and the decentralized agencies. This will make it possible to redefine reform priorities that are considered critical (for example, the liberalization of electricity distribution to boost energy generation PPPs);
- **Promotion of FDI.** IPEX should use the IIP to prioritize FDI promotion activities and PPPs in market prospecting. Most likely this definition will determine changes in the focus of the promotion in specifically selected countries (with leading companies in the desired PPP areas);
- **Private Financing.** The Bank of Mozambique and the MEF should jointly define a plan to accelerate access to long-term credit, which may include new regulations for the operation of the Mozambique Stock Exchange to accelerate the issuance of bonds and bonds, negotiation with banks and even the restructuring or recapitalization of banks;
- **ODA financing.** The DC MEF should have an agenda to negotiate with key partners to access sufficient funding to carry out these reforms and support stakeholders in making robust funding proposals that can be implemented in an efficient and synchronized manner.

**372. International experience indicates that this type of approach can lead to appreciable improvements in the impact of various policies.** The work carried out by the AFDs in different countries demonstrated the convenience of this type of infrastructure approach in several of them, such as Indonesia, Cambodia, and the Lao PDR. A similarly recurrent situation is to develop the potential of remittances to improve the impact of sustainable development. AFD studies in countries such as Bangladesh, Nepal, or Fiji have identified the benefits of an integrated management of public policies (protection of migrant rights, destination migration, social security, and capacity-building), with actions to improve the inclusion and financial literacy of the host families, and the use of incentives and subsidies for the expansion of credit for micro and small enterprises and to facilitate the purchase of properties (in coordination with financing of NGOs) and an integrated approach to the efficient use of ODA in poverty reduction programs.

## 7. Recommended Action Areas and Implementation Roadmap

**373. Despite the short-term impaired situation, the future prospects for Mozambique are very promising.** AFD's analysis coincides with the government's general view of creditors last year. Medium- and long-term prospects remain very good and - starting offshore gas projects to generate export and revenue in the early 2020s, the Mozambican economy could expand significantly, producing some of the country's highest real growth rates. GDP in sub-Saharan Africa. The government expects this growth to be up to double digits after 2022, assuming gas projects become operational by 2022-2023.

**374. Managing the transition will require combining several specific strategies.** Taken together, falling commodity prices, cuts in international budget support, the situation of foreign debt distress, the greater weight of debt service and lower revenues significantly reduce the fiscal space and government options to overcome the short-term crisis. The AFD assessment has identified the desirability of supporting this process and analysing the strategic orientations that the government could adopt during this period to accelerate the exit from the crisis and to lay the foundations for the country's next rapid growth process to produce the maximum impact of development.

**375. AFD's main proposal is to integrate the actions emerging from the evaluation into a medium-term Economic Transformation Plan (2018-2030).** The results of the evaluation recommend adopting a strategic approach in the design and implementation of identified actions and reforms. The actions recommended for continuation should not be implemented in a disconnected way or left to the spontaneous initiative of agents in isolation. It is therefore recommended to integrate these proposals into an Economic Transformation Plan, favouring the smoothest possible departure from the economic crisis, and laying the foundations for further growth. A smooth transition will not happen spontaneously, and to assure it, some of the necessary transformations are quite radical, and would require determined government leadership and meaningful institutional reforms over almost a decade. In formulating this plan, the following criteria were applied:

- *Dependence on hydrocarbons.* It is not possible to predict when the conditions will be combined to trigger these investments. Therefore, the plan should not condition its existence on short- and medium-term economic development thinking. It is more advisable to implement actions to create opportunities beyond these resources to prepare the economy for when these mega-investments happen;
- *External Debt Management.* The plan assumes the continuation of the current orientation of trying to responsibly return to the capital markets and the relationship with developed countries;
- *Flow Management.* It is appropriate to prepare the economy to rely more on internal funds, and to develop public management to ensure equitable and sustainable growth;
- *Avoid dispersal.* There are many plans and strategies, usually implemented with a great variation of quality by different agents. This dispersion of initiatives does not allow a clear direction to be seen in strategic actions and sufficient coherence in implementation.

**376. The adoption and implementation of this plan will require high-level political decisions.** Recommended actions will require dedication, coordination and, certainly, a more strategic allocation of scarce resources, such as ODA - to finance priority reforms. A part of the reforms to be implemented are directly in the domain of the MEF and institutions that are responsible. But many of the decisions in this plan are beyond the mandate of a single ministry, and therefore the decision to adopt and effectively implement this agenda will require approval and leadership at the highest level of government. These aspects are discussed more fully at the end of this chapter.



**377. The suggested interventions are complementary and necessary to ensure the quality of the transition in the short and medium term.** The suggested specific interventions, which should form part of the plan - detailed in the continuation in this chapter - propose actions in three strategic and complementary areas summarized in Table 20.

Table 20: Main strategic areas of the Economic Transformation Plan

Strategic Area	Purpose
1. <i>Reforms to increase short-term fiscal space</i>	Interventions to reduce losses and increase the volume of some streams that could have great effect in the short term
2. <i>Structural reforms to improve the quality of management in the medium term</i>	Acceleration of a series of reforms that will have a critical impact in the medium term, but which should start now
3. <i>Reforms to develop the most important flows in the medium term</i>	Reforms to increase the volume and align funding flows with national priorities in the medium term

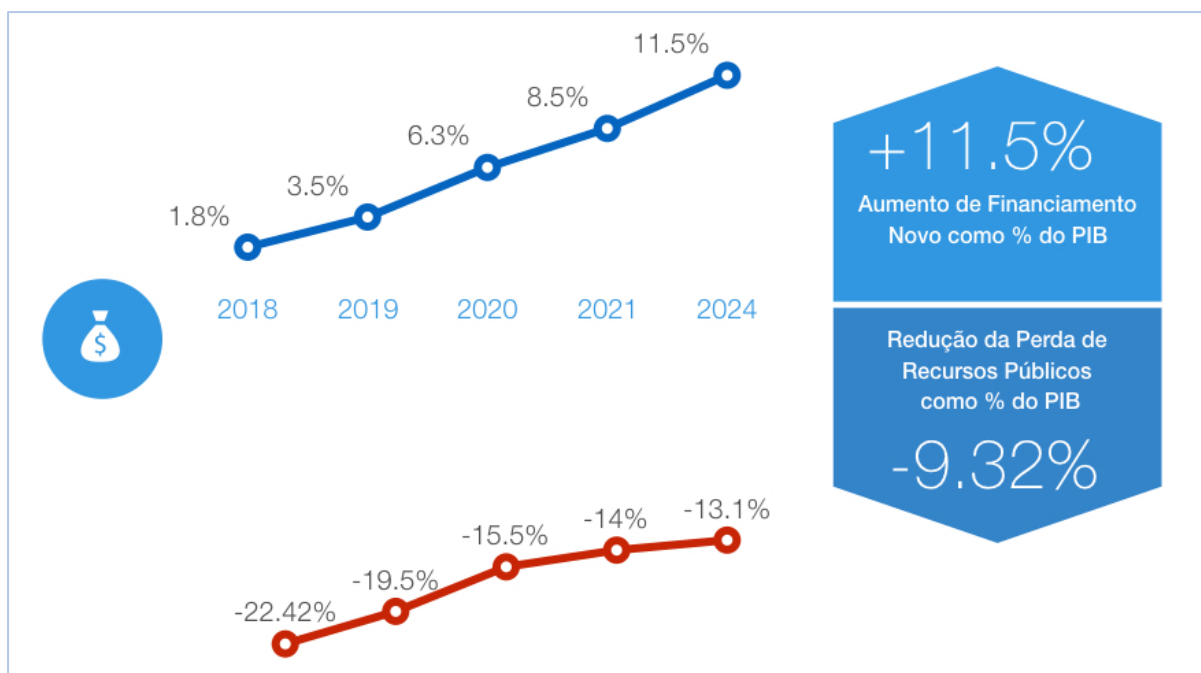
### 7.1 Strategic Area I: Reforms to increase the short- and medium-term fiscal space

378. An important part of the actions suggested in the AFD can have a high impact on the increase of the fiscal space of short and medium term. The evaluation identified a number of intervention opportunities that could have complementary and high impact effects on the generation of fiscal space in the short and medium term. These actions fall into two broad categories:

- *Actions to reduce losses.* Essentially the actions aimed at increasing efficiency and effectiveness in the management of public expenditure in some specific areas identified in Chapter 4;
- *Actions to increase the inflow of new funding.* Improved management of a selected group of streams that could have significant impact in the short term.

**379. These actions are complementary and their implementation can start quickly.** Figure 69 gives an idea of the possible economic impact of the measures identified in the two areas. Reducing losses can generate public expenditure savings of around 9.32% of GDP per year in the short term. Increased flows can mobilize additional resources of up to 11.5% of GDP. The fiscal space that could be added by combining these measures (20.82% of GDP) is considerable, and almost equal to the total public revenue (22% of GDP). These values were calculated based on the values estimated in several studies conducted by the government, and analysed in the AFD. It is likely that these figures are not very accurate, but nevertheless serve to give an idea of the scale of the results of this type of work.

Figure 69 - Expected impact of measures to increase fiscal space



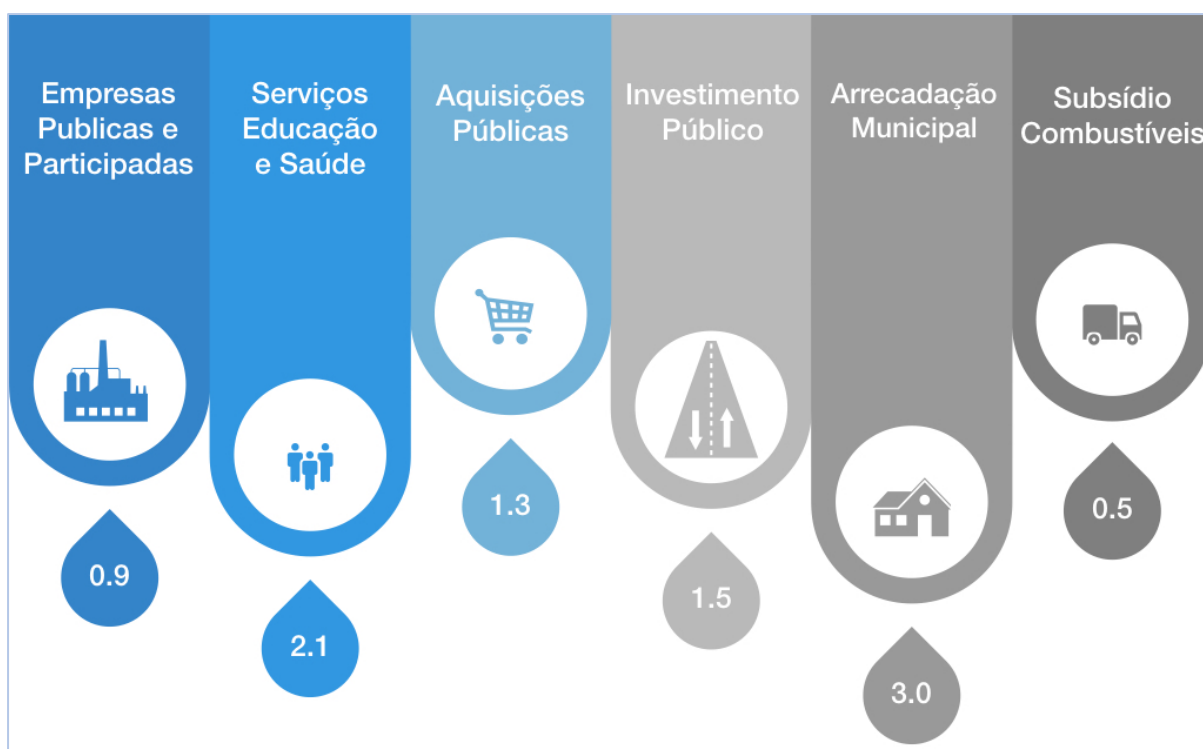
Fonte: AFD Team

**380. The effects analysed below correspond to the Critical Phase of the Economic Transformation Plan (2018-2021), and will also have a significant impact on the next phase (2022-2025).** The definition of this component of the plan responds to the need to support the process of ending the economic crisis by adding options to improve fiscal space and minimize social costs during this phase. The quantitative targets of the measures analysed for the continuation correspond to the estimates of what could be achieved during the initial phase of the Economic Transformation Plan (2018-2021); at the end of the section the goals of the expected impact of the same measures that could be achieved in the next phase (2022-2025) will also be analysed.

#### 7.1.1 Guidelines for actions to reduce short-term losses

**381. Actions to reduce losses focus on the proposals identified to increase the efficiency of public expenditure.** Chapter 4 of this AFD proposes a list of interventions that have been identified in other works commissioned by the government. The search was not exhaustive and therefore the list of actions analysed is only indicative of what could be a work area that should be explored in more detail. There are likely to be other sources of inefficiency already identified that could also be included in this component of the Economic Transformation Plan, but research into its existence should not be grounds for delaying the start of these reforms. The information gathered is sufficient to define an initial action plan for loss reduction and to be able to reap significant benefits. Figure 70 summarizes the main sources of inefficiency analysed in Section 4.2.2 and their estimated benefits.

Figure 70 - Expected impact of measures to reduce losses of public resources



Source: AFD Team

382. *Increase in tax revenues in the richest municipalities (3%).* The analysis indicates that revenue in Maputo alone could almost triple (from 1.3% to 3% of GDP), while in Nampula it is estimated that revenues could increase from 0.9% to 2% of GDP. The tax space that could be released by raising property tax and other local taxes. It was estimated that a comprehensive plan could achieve an equivalent goal in the short term.

383. *Cost reduction in the provision of education services (1.4%).* The productivity of decentralized management of education services is very low. Estimates are that the minimum reduction margin for primary education is 2.4% of GDP, however, at secondary level these are notably higher (14% of GDP). The parametric cost indicates that the focus should be on the best use of the labour force, since most of the expenditure is intended to finance salaries. The short-term goal is conservative, if only a part (1.4%) of the possible reduction of primary education costs will be achieved, leaving the other improvements to the next phase, where only half of the reduction in secondary education costs will be achieved. This is because it is understood that there will be political difficulties in negotiating the best use of human resources.

384. *Cost reduction in the provision of health services (0.7%).* The examples presented in Section 4.2.2 indicate that efficiency gains could account for at least USD 4 of the USD 53 per capita funding deficit detected by ADP for health, which would represent an estimated 1.5% of GDP. To this end, it will be necessary to review the way in which essential services are provided (with a very high unit cost), inefficiencies in the allocation of resources to provinces considering the population, and imbalances in the hiring of technical and administrative personnel. The goal is also conservative, since it assumes that only half of these improvements will be achieved in the short term.

385. *Reform of the public procurement system (1.32%).* The main area of improvement is the increase in the use of procurement processes that will apply competitive methods, since of the 46.4 billion metical of the acquisitions of 2014, 52.9% were of direct contracts. Important reforms are necessary

to develop an efficient, transparent and competitive system, but all can be implemented in the short term and the target is consistent with the estimates made in Section 4.2.2.

**386. Management of public investment (1.5%).** The reduction of the main sources of inefficiency is contemplated in the Public Investment Management Reform Plan, which should be implemented with high priority. The efficiency of public investment is 41% lower than the standard comparison values, and the estimates made in Section 4.2.2 suggest improvements in the order of 3% of GDP, which is consistent with the fact that the average public investment in Mozambique in the last 5 years is more than 15% of GDP. The proposed goal assumes that only half of these benefits will be obtained in the short term, the other half being achieved in the next phase.

**387. Losses and Risks of Public and Subsidized Companies (0.9%).** The performance of companies has been poor and the estimates in Section 4.2.3 calculate the losses in the order of 3.5% of GDP. AFD has assumed that only half of these losses (1.75% of GDP) could be reduced between 2018 and 2025, and only a fraction of this reduction will be achieved in the short term. This will require improvements in the system to monitor performance, eliminating fragmentation in the oversight of public enterprises, and developing critical technical capacity to improve management. The budgetary risks (guarantees, PPPs, long-term contracts for the construction of infrastructures and liabilities by public and investee companies) generated by these companies are fast growing and, although they have no direct impact on current expenditure, they should be controlled.

**388. Reduction of subsidies (0.5%).** The fuel subsidy is the main element to be considered and represents an annual average of 2.16 billion meticaís, equivalent to 1.67% of total expenditure. The government has announced the phasing out of this subsidy in 2017 and has also taken the correct decision not to withdraw subsidies to public passenger carriers, since the transport component is very marginal in the total volume of this expenditure and that this component of the subsidy could have social impact. The target assumes that this process could complete the scheduled reduction of the subsidy in 2021.

**389. Efficiency reforms should be viewed as processes of continuous improvement.** The design of the perfect 'form' before beginning the implementation of measures is a path that can be very long. To have an optimal design of the reforms, specialized, time-consuming and resource-intensive studies, such as conducting Public Expense Tracking Surveys per sector, will be required to analyse specific problems in service delivery. The areas of inefficiency noted are so large that reforms can begin by focusing on the core of the problem, with relatively basic, sufficiently good measures that can be implemented without much in-depth knowledge. In this way, the MEF can ensure short-term results that can be continued as continuous improvement processes, incorporating studies that are necessary and improving the measures originally taken. For example, improving tax collection in richer municipalities can be started with a generalized increase in taxes, which - with more studies - can soon be refined and targeted to more specific targets.

**390. The technical component of this type of reform is very important.** Even if it is with rudimentary elements of analysis, these 'good enough' measures must be designed with technical knowledge of the processes to be improved. Therefore, the use of generic and simplistic measures such as the suspension of all personnel hiring, or generic cuts in the use of fuel or the purchase of vehicles should be avoided. In addition to facing resistance from stakeholders, such measures can generate more damage than benefits in the medium term. For example, negotiating with ministries of education or health, a plan to implement the recommended measures in the recently completed sectoral ADPs, developing a two-year timetable with concrete quantitative reforms and targets, and ensuring the availability the necessary resources and government support to implement these reforms.

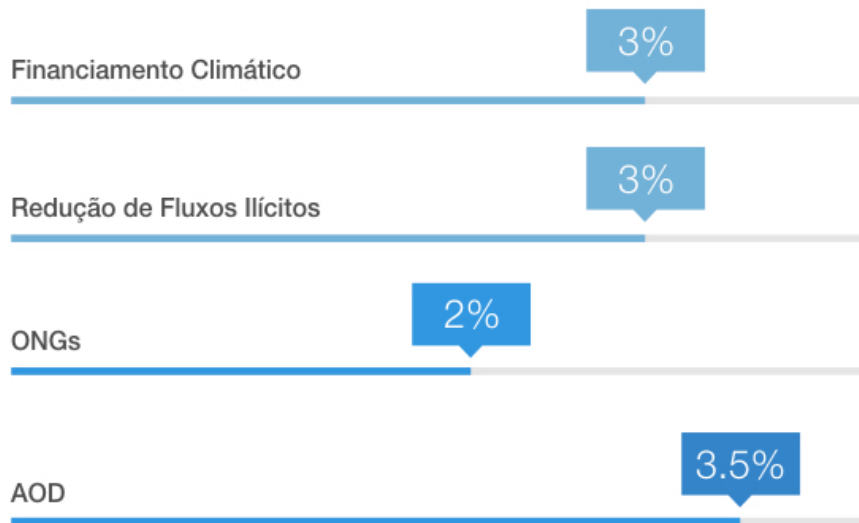
**391. Improvements in inefficiency reforms may be unpopular and may involve measures that may be painful and have political costs.** But these measures should be urgently needed to improve the transition from the crisis. The country also needs to succeed in these reforms to ensure future sustainability in the use of public funding and to achieve visible development results as it reaches the new stage of accelerated economic growth. Rising efficiency demands decided actions with a medium- and long-term vision, but with well-designed measures, the government can achieve significant results in the next two to three years.

#### *7.1.2 Guidelines for increasing the volume of selected funding streams*

392. Although the increase in the volume of financial flows analysed requires a long-term approach, in some cases the government could expect relatively rapid results. The government should consider accelerating the reforms in the following flows, as they could mobilize additional fresh funds with important amounts (as% of GDP) in the short run.

393. **Increase in Revenue from Illicit Flow Reduction (3%).** The average value of these flows in the period studied was over 8% of GDP and its reduction will surely have a visible impact on the increase in public revenue. For this reduction, the government should improve AT's and Customs' control and inspection capacity of export / import companies, and limit the use of tax havens by companies established in the country. The short-term target only accounts for the effect that could be achieved with stricter control over natural resource and mineral resource companies. Tax evasion in these sectors is considered high and the goal is to take tax values close to values in countries with similar conditions.

Figure 71 - Expected impact of measures to reduce losses of public resources



394. *Climate Financing (3%)*. The country has access to much more resources than it is capable of currently processing. The projections in Chapter 6 estimate that it is possible to achieve growth of this flow of up to 12% of GDP by 2030. The short-term target assumes that the design of the FNDS is successful and that the fund is capable of progress faster than obtained so far. It is important to note that the clever use of climate finance funds for adaptation could replace the demands of current infrastructure investments even in sectors such as education and health. The FNDS could also make funds available in other critical areas (such as rural development) that can be used to leverage financing from private companies, NGOs and other international sources.

395. *Official Development Assistance (3.5%)*. The loss of confidence generated by the debts of public companies and other factors analysed in Section 4.3.3 led to a discontinuity in access to these funds, with a decline of 4% of GDP. Before the crisis these values fluctuated above 10% of GDP, but from 2015 they fell to levels close to 6%. The government could seek to recover these investment values over the next 2-3 years by combining two complementary approaches:

- Investment in the Economic Transformation Plan. Convincing an important group of partners to invest in the plan is a way to regain confidence because it proposes common goals and many of the reforms identified stem from technical cooperation funded from ODA resources. Investing in the plan is also a way to begin thawing significant resources, since AFD's initial estimates - without considering some of the areas - put funding needs at the \$ 40-60 million range over the next 10 years;
- Explore other funding modalities. For some partners, the return to the AGM will be difficult, and will probably depend on the results of the structuring reforms prioritized in the plan. The government could explore the use of mechanisms to increase aid effectiveness and reduce donor fiduciary risk. There are several options, such as the use of common funds, or other mechanisms of pooled finance but avoiding their proliferation and the consequent fragmentation of funding.

396. *International Financing to NGOs and Private Institutions (2%)*. The estimated target is conservative, since this flow can grow more than 5% of GDP in the medium term if the government makes some improvements in the current legislation and begin a more strategic and integrated management of these flows. The improvements should introduce more strategic and efficient systems

of dialogue, and for well-defined purposes at different levels. Investment through NGOs can also be a way of rescuing ODA funds that will not go back as an AGO but can, with good management, reduce public funding in specific areas. A new system of stimulating public-private co-financing and more decisive international promotion actions could also significantly increase these investments.

**397. The expected effects in the two areas are of great potential in the short and medium term.** The objective of this proposal is to generate a strategic discussion about the government's need to implement proactive policies to increase the fiscal space in the short and medium term. The data presented are indicative and should be taken as primary estimates of the type of impact that the government might wish to achieve with this type of action. The data in Table 21 summarize the main gains that could be achieved in the two proposed areas of work in the short and medium term. The deadlines in the table correspond to the first two phases of the Economic Transformation Plan analysed below. Short-term goals are certainly much more modest than could be achieved in this period, but the possibility of reducing public spending by an equivalent of 9.32% of GDP and increasing available resources by 11.5% of GDP is very encouraging. The combined effect of these measures is on the same order of magnitude of government tax revenue.

Table 21: Expected Effects of Short and Medium Term Proposed Interventions

Effect	Reducing Losses / Increasing Efficiency	Expected Benefit (% GDP)	Additional Resource Volume by Selected Financial Flows	Expected Benefit (% GDP)
Short term (2018 -2021)	Increased collection in richer municipalities (Maputo and Nampula)	3.00%	Increase in revenue from raw material exports and reduction of illicit flows	3.00%
	Reduction of fuel subsidy	0.50%	Increase in Climate Financing public and private (FNDS)	3.00%
	Reform in the system of public acquisitions	1.32%	Increase in Official Development Assistance (ODA)	3.50%
	Reform in the system of public acquisitions	1.50%	Increase in NGO Financing	2.00%
	Reduction of the cost of enrolment in primary education (RHHH reform and salaries)	1.40%		
	Reduction of losses of public and affiliated companies (reduction of 50%)	0.90%		
	Reduction of the cost / GDP of health services	0.70%		
	<b>Total Estimated Short Term</b>	<b>9.32%</b>	<b>Total Estimated Short Term</b>	<b>11.50%</b>
Medium Term (2022-2025)	Tax Collection	1.00%	Increase in revenue from raw material exports and reduction of illicit flows	2.00%
	Reform in the system of public acquisitions	1.00%	Increase in Climate Financing public and private (FNDS)	6.00%
	Reform in the system of public acquisitions	1.50%	Increase in Official Development Assistance (ODA)	1.00%
	Reduction of losses of public and affiliated companies (reduction of 50%)	0.90%	Increase in NGO Financing	3.00%
	Reduction of the cost of enrolment in primary education (HR reform and salaries)	1.00%		
	Reduction of the cost of enrolment in secondary education (HR reform and salaries)	7.00%		
	Reduction of the cost / GDP of health services	0.7 %		
	<b>Total Estimated Average Term</b>	<b>13.10%</b>	<b>Total Estimated Average Term</b>	<b>12.00%</b>

Source: AFD Team

## 7.2 Strategic Area II: Structural reforms to improve the quality of management

398. The introduction of new instruments used in national planning and financing systems and the redesign of some of the existing ones are priority actions for a better linkage between policies and results. The analysis carried out in Chapter 3 proposes the consideration of a series of improvements that could be constructed taking advantage of existing systems. It also proposes new elements to cover some gaps and operational problems. The integration of these systems will allow a more efficient and effective use of the state budget and forms the basis for the future introduction of management systems based on performance and results.

### **399. The Economic Transformation Plan should ensure the start in the short term of implementing a list of critical reforms to improve the MEF's capacity in medium-term Public Finance Management.**

The list of priority reforms reviewed in the AFD includes the following:

- *Management of the Efficiency of Public Expenditure.* The actions examined in the previous section will not happen spontaneously. They will depend on a programmatic formulation and the specific attribution of responsibilities for its implementation;
- *Public Investment Management.* Prioritize the implementation of the public investment management improvement plan, which should provide a much-improved version of the IIP in order to prioritize public investment efficiently and plan the best use of public-private investment, especially for large infrastructure priority projects. scale;
- *Public Debt Management.* Develop technical capacities to improve the quality of management and provide a new 'dashboard' that allows efficient management of commercial debt with government guarantees, blend finance management systems efficiently using CSS sources, Public Investment Management and Integrated Investment Plan;
- *Implementation of the Program Budget.* Accelerate the introduction of the new program-based budgeting system to allow for the future introduction of a results-oriented management and financing system;
- *Reformulation of the ENDE.* Improve the results framework and indicators and aggregate funding estimates to analyse the feasibility of the proposed objectives. This is compatible and can be accomplished with the opportunity of programming the response of Mozambique to the SDG;
- *Reformulation of the Public Finance Vision.* Define: (i) quantitative targets to develop finances at levels that ensure the sustainability of the NSDS, (ii) broaden the vision including the development of public and private finances in planning;
- *Improvement of the Technical Quality of the Medium and Sectoral Plans.* Initiate a process of capacity-building to ensure the homogeneous qualities of these plans that allow the introduction of the program budget;
- *Medium Term Financial Flow Development Plans.* Implement the new Finance Vision (VF) through five-year Strategic Finance Plans (PFFs) that are more comprehensive than current ones that consider the management of funding from public and private sources.

**400. These reforms are preconditions for sustainable management of the resources that could be generated during the next phase of rapid growth.** The country should use the way out of the crisis as an opportunity to initiate these actions that will strengthen the medium-term public management system and ensure the sustainable use of resources in the future. The working hypothesis is that the country should take advantage of the next fast-growing process (which the government expects to start in 2022), to make a qualitative leap in socio-economic progress and thus lay the foundations for ensuring sustainable economic growth dynamics. Therefore, during this period of economic growth



(which could be at least a decade), Mozambique should be able to significantly improve the level of social and environmental development and avoid repeating what happened in the past when it achieved strong economic progress and low social progress.

**401. In order to achieve the desired results, a financing approach is required to ensure sufficient investment of resources and medium-term availability.** The above-mentioned programs must be properly funded and their long-term funding should be discussed with development partners and ensured. This set of structural reforms is directly aligned with the priorities of several development partners, as these reforms seek to improve the quality of public finance management substantially. It should be noted, however, that these are reforms that require medium-term continuity to produce significant results. Therefore, the MEF should consider the possibility of using pooled finance mechanisms with partners ensure sufficient and long-term resources. AFD's initial estimates put financing needs at USD 30-40 million over the next 10 years. 402. The main implementing and beneficiary of these reforms is the MEF. Most of the actions listed above already exist as initiatives, or even projects in different areas of the ministry. But in all cases, these initiatives could benefit from strategic prioritization and the support of top-level leadership from the MEF. The most important result of these reforms is not simply the introduction of new work systems. The reforms seek to strengthen the institutional capacity of different critical areas of ministry and subordinate agencies:

- *Analytical ability.* The MEF will need to strengthen its ability to understand and analyse technical information and conduct research to inform policy decisions. This capability will often be required in the strategic formulation of fiscal policy aspects, in the formulation of national plans (including infrastructures), and in many more specific policy issues regarding the financial aspects of government activities. The capacity of the Directorate of Economic and Financial Studies and other directorates of the MEF will have to be significantly strengthened to be able to assume this role;
- *Ability to achieve results.* The actions will require improving the quality of MEF reference products and their capacity to stimulate the delivery of results from other players. This includes, for example, achieving a national budget that is in line with the demands of priority policies or tasks such as revenue collection and monitoring of government-wide performance that may also depend on the MEF. The newly established Monitoring and Evaluation Directorate could play a key role, but it should also be significantly strengthened in its current capacity;
- *Coordination capacity.* Coordination is a critical function of the MEF and the implementation of the Economic Transformation Plan will require strengthening the capacity to orchestrate technical and political issues of different actors in pursuit of a common goal. This will entail a wide range of activities that the MEF could coordinate by leveraging its position at the centre of government. The leadership of high-level positions of the ministry is necessary, and therefore it may be necessary to consider strengthening the technical capacity of the Office of the Minister or the Permanent Secretary to support the implementation of these functions;
- *Regulatory capacity:* The Economic Transformation Plan will also need to strengthen the ability to control complex regulatory domains such as public company oversight, debt management, PPPs and financial markets. In a broader sense, the MEF will play an important role in overseeing subnational entities in various aspects of public finances, including managing the efficiency of public expenditure and fiscal aggregates.

### *7.3 Strategic Area III: Reforms to develop the most important flows*

**403. The evaluation identified concrete opportunities to develop a wide range of financial flows.** For the better development of each, it will be necessary to transform AFD's proposals into medium-term strategic plans that will allow for the projections of the necessary reforms to improve the quality of policies and the institutional and coordination aspects that govern each flow. The evaluation analysed the coincidence of these reforms with existing government priorities and plans. The vast majority of the solutions proposed in AFD are aligned with existing government initiatives. Table 22 summarizes the full list of all areas of action that emerged from AFD flow analysis.

Table 22: Summary of key interventions required for the development of flows analysed

Flows		Main Reforms / Actions
1. Externa Debt	1.1	Strengthen systems and management capacity of blend finance using multiple sources of credit (concessional and non-concessional)
	1.2	Reinforce the commercial debt management system with government guarantees and prevention of debt risk incurred by public and investee companies
	1.3	Improve the quality of public investment management and the prioritization of the Integrated Investment Plan using public and private financing
2. Pública Revenue	2.1	Reviewing the cost-benefit ratio of the tax exemption scheme to attract private investment, particularly for megaprojects
	2.2	Improve AT (and Customs) capacity and information systems to control collection at the national level
	2.3	Improve AT (and Customs) capacity and information systems to control collection at the national level
3. Non Tax income	3.1	Set specific targets for the growth of this type of revenue in the PQG and responsibilities for its achievement
	3.2	Implement actions to improve the efficiency of decentralized public management focused on the collection of Set specific targets for the control of these flows and the responsibilities for their achievement
4. Illicit Flows	4.1	Definir metas específicas para o controlo destes fluxos e as responsabilidades pela sua consecução
	4.2	Develop integrated information systems that allow the tracking of the invoicing of export and import companies and the double verification with data of physical control of Customs and the import of the country of destination
	4.3	Piloting control and inspection systems for exporting companies of raw materials
	4.4	Create new regulations to restrict the use of invoicing through tax havens by import / export companies operating in the country
5. Natural Resources Revenues	5.1	Review the policy framework and management of these resources to ensure sustainable production
	5.2	Design specific systems of tax exemptions for exploitation of hydrocarbons, mineral resources and timber (see 2.1)
	5.3	Design integrated government systems to improve the monitoring of income from natural resource exports and control of tax evasion (see 7.3)
	5.4	Improve the transparency and the capacity for social control of the quality of the policies and income of these exports by returning to the EITI reports

Flows		Main Reforms / Actions
6. Official Development Assistance	6.1	Strengthen government leadership in ODA strategic direction to define and fund priorities
	6.2	Design efficient new systems and transparent use of resources to recover lost donations from AGO
	6.3	Improve the quality and scope of ODAMoz and develop systems to monitor the quality of ODA allocation and use
	6.4	Improve the management of vertical flows and promote greater use of this system
	6.5	Explore possibilities to extend the future life of ODA with the introduction of mechanisms such as Aid For Trade
7. South-South Cooperation	7.1	Develop systems to analyse the cost-opportunity ratio of CSS credit by analysing in an integrated way the cost of the final work and credit
	7.2	Review the use of non-competitive procurement procedures
	7.3	Unify CSS credit management systems with external debt and ODA grants integrating all information into ODAMoz
8. Climate Financing	8.1	Implementing the CPEIR considerations in the reform of the budgetary procedure
	8.2	Achieve the active participation of the MEF in the design of the FNDS to ensure coherence and coordination with other funds and the use of the lessons learned from its management
	8.3	Design the SDNDS in order to diversify funding sources and encourage private financing, ensure governance and transparency in management, and good integration with executing agencies (public and private)
9. Sovereign Funds	9.1	Analyse the feasibility of introducing a fund to ensure transparency in the use of extractive sector resources, reducing margins for corruption, and protecting the country from fluctuations in international markets
10. Private Credit	10.1	Design systems to improve alignment of credit supply with priority sectors such as agriculture, industry, construction and tourism
	10.2	New measures to boost competitiveness and eliminate concentration
	10.3	Strengthen the Stock Exchange and its capacity to allow access to long-term financing for the national private sector
	10.4	Strengthen the implementation of the Financial Inclusion Policies and design incentive mechanisms for access to credit to individuals and MSMEs
11. Foreign Direct Investment	11.1	Continue to improve the quality of the facilitation and promotion system initiated by the extinct FDI, which can be enhanced through the creation of APEX, and focus on target markets
	11.2	Strengthen the use and management of EEZs and EPZs (considering the privatization of their management) to accelerate the export-oriented industrial SDI
	11.3	Develop a shared vision (in ENDE) of the role that FDI should play in economic growth and how to improve the quality of FDI
	11.4	Improve the monitoring and follow-up of the impacts of the FDI
12. Public-Private Partnerships	12.1	Review and strengthen the institutional and policy framework for improving centralized and decentralized capacity in PPP management, independent arbitrage and sound management of contingent risks to the State

Flows		Main Reforms / Actions
	12.2	Define priorities for PPPs from the IIP and responding to infrastructure priorities ne for the development of the private sector.
	12.3	Define a system of international promotion of PPP integrated with the activities of promotion of the IDE carried out by the APEX
13. International NGOs	13.1	Review the legal framework governing the activities of NGOs to ensure greater transparency and complete and up-to-date information on their actions in the country
	13.2	Design an integrated system in ODAMoz to monitor the funding of these activities, align them with national priorities and inform decisions in the state budget process
	13.3	Review dialogue systems to encourage and improve the quality and alignment of NGO intervention, revitalizing dialogue at a strategic level and better integrating sectoral, if thematic mechanisms
	13.4	Analyse ways to stimulate and promote the use of new systems such as impact funding or partnership cooperation
14. Remittances	14.1	Develop studies to analyse the use of national and international remittances by households in the poorest communities
	14.2	To design pilot interventions to improve the use of remittances in integrated actions with financial inclusion measures (10.4) and with initiatives of ministries and NGOs for poverty reduction

404. A **prioritization of the work to be done will be required**. Attempting to address all these issues at the same time would be a major challenge considering the other priority actions discussed earlier in this chapter. The government should prioritize the emerging agenda and define a realistic list of interventions to be addressed in the next GFP based on the results of the DFA and other government priorities. For this purpose, it is recommended to consider the following short-term preparatory actions:

- *Promote an integrated approach of government*. As in previous cases, decision-making on the implementation of some of the recommended actions exceeds the mandate of a single government institution and will require a strategic discussion at the highest level;
- *Improve the search for key flows*. The time available, the low collaboration of some agencies and the inconsistencies of the data sources available did not allow to complete the search of some financing flows that may be important. This study will show the potential of some flows that may be important to consider in the Economic Transformation Plan;
- *Better search the interrelationships between key flows*. The analysis presented in Section 6.4 exemplifies the desirability of informing the discussion of the interrelationships between flows and the level of coherence and coordination that would be required to obtain the maximum benefits;
- *Economic modelling and projections of flows*. To feed the proposed policy discussion above it is desirable to develop more concrete and realistic data that could be elaborated from the analysis of more specifically defined economic scenarios. This requires an economic modelling of the development of key financing flows that, while simple, incorporate the main changes expected in the medium term and project their economic impacts. The modelling should also incorporate the interconnections mentioned above;
- *Improve the way evidence is presented and existing information*. To facilitate the process of analysis at this hierarchical level of the relatively complex issues that will be proposed, more work is needed to provide the missing evidence, and to prepare adequate visual materials.

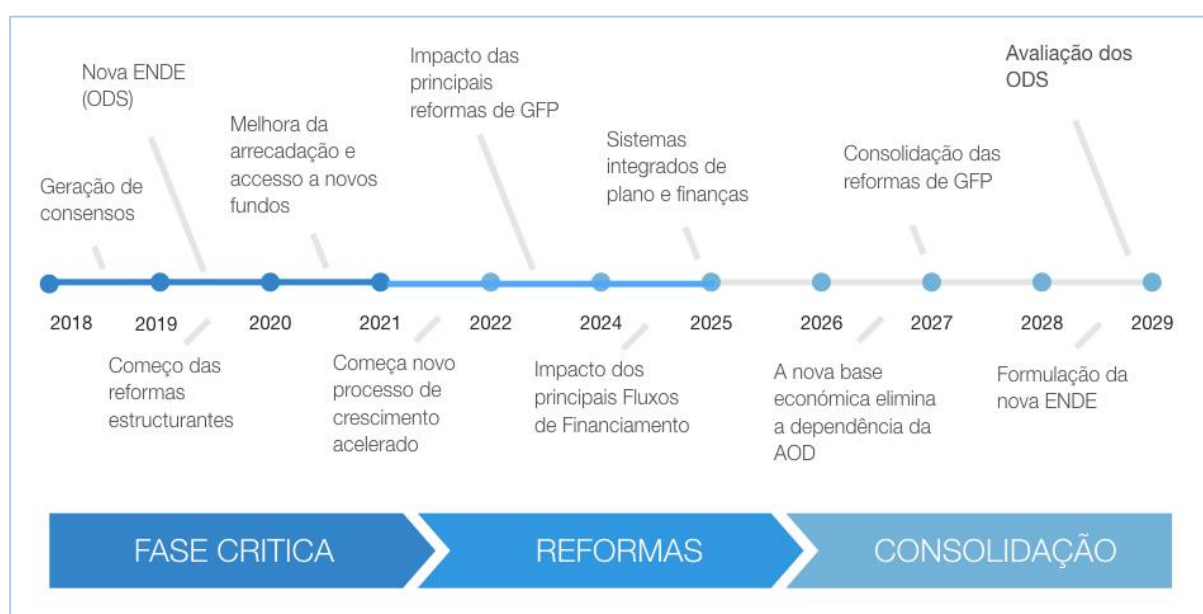
**371. The technical and political leadership of the MEF will be very important during the prioritization process and formulation of the final work agenda.** The general coordination of the activities mentioned above does not correspond to the direct mandate of the individual MEF directorates and demands coordination. These needs are common to all areas of the Economic Transformation Plan and are discussed in more detail in the next section.

#### 7.4 Implementation sequence of AFD Recommendations

##### 7.4.1 Short and Medium-Term Priorities of the Economic Transformation Plan

405. The priorities in the implementation of the Economic Transformation Plan establish three differentiated phases. The different interventions analysed above define a set of priorities that change over time and can be better visualized considering three distinct phases, as summarized in Figure 72 and analysed below.

Figure 72 - Main milestones and critical points in the implementation of the Economic Transformation Plan



406. *Critical Phase (2018-2021).* The focus at the outset of the plan should be on supporting the end of the crisis by implementing actions and reforms aimed at freeing up fiscal space and expanding government manoeuvrability during this process. A key task at this stage is to create a comprehensive approach to government work, integrating leadership at the highest level. During this period measures should be implemented to reduce inefficiencies in public expenditure and to increase the volume of the four selected financial flows. One of them (ODA) is of great importance for the implementation of the Economic Transformation Plan. Therefore, during this period the government must re-establish the confidence of the development partners. Progress should be made in formulating and implementing medium-term programmatic support to implement the Plan, and it is important to ensure the implementation of the structural reform package and the strategic plans of the main financial flows. These reforms must begin during this phase to produce results in the next phase.

407. *Phase of the Structural Reforms (2022-2025).* The second phase of the Plan should focus on achieving substantive outcomes of structural reforms that will enable the government to make the most of funding opportunities in the new phase of accelerated economic growth that should begin with this phase (2022). These reforms will already lead to appreciable results in the more efficient and

effective use of public and private resources. The strategic plans of the main flows should also begin to produce visible results during this period, contributing to an orderly acceleration of the economy.

*408. Economic Consolidation Phase (2026-2029).* The focus at this stage is the completion of the implementation of key structural reform measures, and of the key financial flows to be developed. The further improvement of the results obtained should be incorporated as a process of continuous improvement in the long term. With the arrival of the final SDG target, the government should have already learned important lessons about the good use of political leadership to achieve effective coordination of public policies. The resulting system - most likely more strongly based on public and private domestic financing - will ensure that economic progress progresses faster and has more effects on social and environmental development.

#### *7.4.2 Responsibilities of the Implementation of the Economic Transformation Plan*

**409. Considerations on the implementation of the Economic Transformation Plan are almost as important as its strategic design.** The biggest challenge to achieving the deep transformations and ambitious goals that the Plan proposes is to generate a consensus at the highest level of government on its strategic need and to identify an efficient institutional solution to implement it. The challenge is important because the implementation of this plan will exceed the mandate of a single government institution. The solution will likely require managerial and institutional innovations as highly cross-sectoral policy coordination is one of the areas where the governance system has shown greater difficulty in delivering coherent and effective responses.

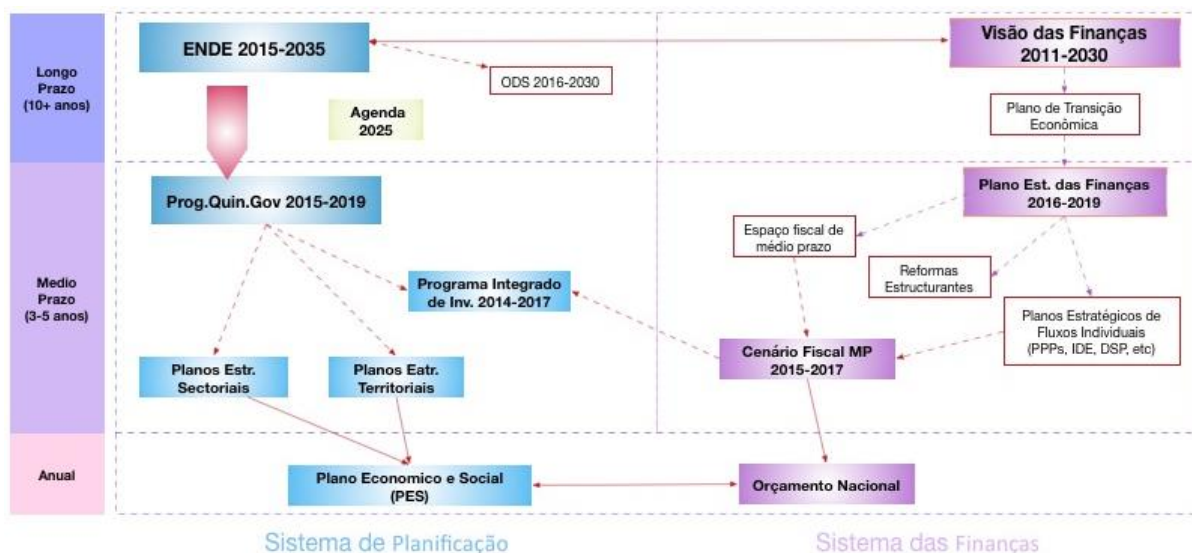
**410. The MEF's technical and political leadership will be very important in generating consensus on the need for this plan and in finding the best solution for its implementation.** Most of the actions of the first strategic area aimed at reducing losses correspond to areas of direct responsibility of the MEF or of institutions supervised by it. The same applies to almost all the actions of the second strategic area, which proposes structural reforms. But most actions aimed at increasing the volume of selected flows and other specific areas of the plan should be implemented by other Ministries and government agencies. It will therefore be necessary to reach a consensus decision within the governance of the best system to ensure consistency in coordination. The alternative of implementing this highly strategic agenda with disjointed initiatives on behalf of different government actors and supported in a fragmented way by development partners will create disruptions and challenge the achievement of significant results. Therefore, the leadership of the MEF is very important in explaining to the government the importance of coordinated and efficient implementation.

**411. One way to facilitate the operation of the Economic Transformation Plan is for the government to grant responsibility for its implementation to the Ministry of Economy and Finance under a Presidential mandate.** The main argument to justify this decision by the government could be that the actions proposed in the plan that correspond directly to areas of responsibility of the MEF (the great majority), coincide with the strategic priorities of the Ministry set out in the VFP and PEFP, the maintenance of macroeconomic stability, the smooth functioning of the State, and the management of expenditure. The other actions of the Plan that are to be implemented by other Ministries and government agencies are designed to contribute to another fundamental objective of the MEF, which is to ensure macroeconomic stability, and are therefore all in the Ministry's best interest. This could be a way of ensuring the levels of strategic coherence and efficiency needed to implement these actions

**412. If the MEF is given responsibility for implementing the Economic Transformation Plan, its integration into the current system of financial planning instruments would be natural and**

**straightforward.** The Economic Transformation Plan would have a natural integration with the improved versions of the long-term Vision of Finance (VF) and the new five-year Finance Strategic Plans proposed in Chapter 3 of the AFD. These expanded instruments are more comprehensive than the existing ones, since they would not be limited to Public Finances alone and would provide a strategic framework for the development of financing flows - public and private - that are considered as priorities to enable the financial needs of the NSDS. In this context, the long-term objectives of the Economic Transformation Plan would be automatically integrated into the new VF, and the three areas of intervention proposed by the Plan would be easily programmable within the new PEF Plan (see Figure 73). The proposed new PEF implementation areas are marked in red. Most structural reforms already exist and are the planned implementation of the PEF and the strategic objectives of the FP; its execution is now given a different prioritization. The idea proposed at the beginning of this chapter is to avoid dispersion. There are already many plans and strategies, and the dispersion of initiatives does not allow a clear direction to be seen in strategic actions and sufficient coherence in their implementation.

Figure 73- Integration of the Economic Transformation Plan with the current instruments of financial planning



Source: AFD team based on various official documents

**413. The extended AFD Oversight Group could play an important role in supporting the implementation of the Economic Transformation Plan** The establishment of an AFD Oversight Group (GS) was designed to generate government ownership of the evaluation process and its results. The GS integrated people from different areas of government: The Prime Minister's Office, MEF Directorates (DNPO, DEEF), Banco de Moçambique and MITADER. The creation of an enlarged group over the current one (an Economic Transformation Plan Supervisory Board) could play an important role in supporting the MEF's actions during the implementation of the Plan. The shared vision of a government reference group that engages policy-decision staff from selected institutions can be of great help. In its constitution, the MEF should also consider the lessons learned from the operation of this group during the AFD and improve the working system to ensure a more consistent participation of the decision makers of these institutions. Perhaps establishing a regular (quarterly) monitoring plan for this group with the Prime Minister could ensure this interest.

**414. To ensure the effective implementation of the Plan, it will also be necessary to strengthen the capacity of the MEF itself.** The implementation of the Plan will also be an internal challenge for the MEF, including for actions that are fully under the responsibility of the Ministry. The multiple

coordination activities required do not correspond to the direct mandate of any MEF Directorate, and will require informed decisions at the highest level. One solution could be to strengthen the technical capacity at the highest level of the Ministry (Office of the Permanent Secretary or the Minister) to establish appropriate management and monitoring support systems to facilitate the task of the authorities. This solution is part of the short-term actions (Next Steps) suggested below.

#### *7.4.3 Financing of the Economic Transformation Plan*

**415. The government should seek to ensure sufficient medium-term financing.** The reforms suggested in the Economic Transformation Plan are medium-term and will require funding of USD 40-60 million over the next 10 years. Formulating a project of this magnitude requires investment of time and technical capacity, and therefore could delay the start of execution. The actions of the first component of the Plan (Short-term Actions) are urgent and cannot be expected to confirm large-scale financing. But by their very nature, they are not excessively onerous, and could be funded independently to ensure implementation during the first phase of the Plan. AFD provided sufficient analysis and information to be able to design a project to support its implementation immediately, which was also included in the list of short-term actions (Next Steps) suggested below.

**416. It could be advantageous to guide the process of securing the financing of the Economic Transformation Plan as part of the ODA restoration process.** As was mentioned above, the Plan could be a vehicle for regaining the trust of the partners and unfreezing the financing of an important group of these. The proposed reforms seek common goals, such as increasing the efficiency and transparency of public management, and many of the actions derive directly from technical initiatives and cooperation that have already been funded with ODA resources. There are several examples of the use of pooled finance mechanisms in other countries to enable the medium-term financing of PFM reforms, which could be taken as a reference model. For example, the SWAP funding used in Cambodia mentioned in Section 3.3, or the Multi Donor Trust Fund<sup>117</sup> for reforms in Nepal, which have achieved notable successes in both cases. Equally, defining an efficient pooled finance mechanism of this type is a task that will require a lot of effort and some patience on the part of the government to successfully conduct any negotiations that are necessary.

**417. The process of consensus-building with development partners has already begun.** AFD's calendar of activities includes the holding of three high-level seminars to ensure interest and future participation in the implementation phase of key development partners. AFD's calendar of activities included three half-day seminars: one at the AFD launch (July 2016), the other at the intermediate stage (April 2017), and a Validation Seminar to be held at the presentation of the final results of AFD. Although AFD interim documents were not shared, the presentations were sufficiently exhaustive to present the analysis results. The seminars were well attended by development partners. In addition, the technical missions undertaken at these seminars included direct meetings with the partners who are funding the reforms or actions analysed in the AFD, and their suggestions were considered in the evaluation. Therefore, the work of generating consensus with development partners should be facilitated by these actions.

#### *7.5 The recommended areas of action and the construction of a QNIF418.*

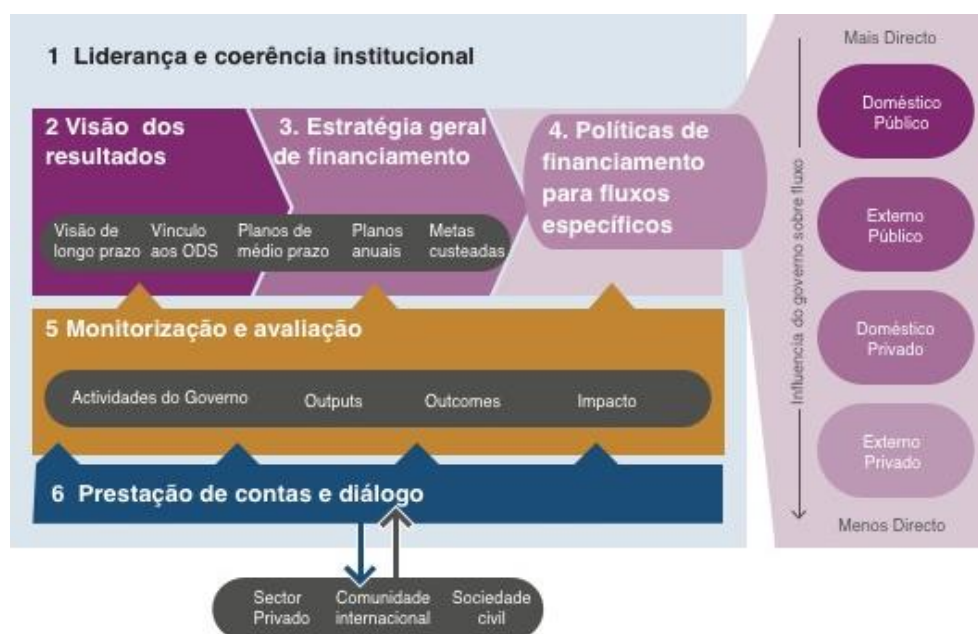
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<sup>117</sup> Based on a common agenda generated by PEFA, the Multi Donor Trust Fund for Public Financial Management is administered by the World Bank and jointly funded by bilateral cooperation agencies such as Australia (DFAT) and the United Kingdom (DFID), the European Union, and the governments of Denmark, Norway and Switzerland. The fund provides a single system where all partners provide their funding using a common programming framework that is designed to support priority government-defined reforms.



The evaluation demonstrated the desirability of adopting an integrated and comprehensive vision of development finance and identified concrete opportunities to start building it. The present Evaluation on Financing for Development in Mozambique has identified the desirability of developing a holistic and integrated view of finance that will: (i) provide clarity on the roles that all actors (public and private, domestic and external) could have to finance (ii) determine the responsibilities of the different government actors that are best placed to ensure the effective mobilization of these resources. It is therefore appropriate to link the improvement proposals analysed in this AFD with the construction of a National and Integrated Financing Framework (NIFF).

Figure 74 - Elements of an FNIP for the achievement of national priorities and SDGs



Source: UNDP 2017

AFD has found concrete opportunities to develop each of the pillars that form the basis of a National Integrated Funding Framework (FNIF). The description of the pillars of an NFIS analysed in Chapter 1 is reproduced in Figure 74. The main results of this NFD propose improvements that are related to the construction of each of these pillars as summarized below:

420. (i) *Leadership and institutional coherence*. Many of the solutions identified in the AFD could have a high impact on the mobilization and better management of public and private resources in the short and medium term. But a good and important part of these solutions is beyond the mandate of an individual Ministry - even MEF - and therefore, the effective implementation of this agenda will require leadership at the highest level of government. The implementation solutions proposed above would allow exploring new ways to develop integrated and comprehensive management.

421. (ii) *The vision of the results that the country intends to achieve*. The AFD has analysed the need to revise the formulation of the long-term vision (ENDE), to improve its results framework and to make cost estimates to achieve these objectives. The review is also needed to define the country's response to the Sustainable Development Agenda for 2030. This will enable the government and stakeholders to monitor progress against the country's international commitments.

422. (iii) *A general financing strategy*. The evaluation determined the need to broaden the formulation of the Public Finance Vision (VFP) to achieve an integrated strategy that considers the development of public and private finances to ensure the feasibility of funding the goals of the new NSDS. He also

highlighted the opportunity to use a strategic strength of the current system and to continue the practice of implementing VFP through five-year Public Finance Strategic Plans (SPFS), which in the future should be broader than existing ones (public and private finance). Well used, this strategic strength would allow developing an approach that would allow the integration of planning and financial systems.

423. *(iv) Financing policies for specific flows.* The evaluation examined fourteen funding streams (public and private) and determined the desirability of defining specific policies for each of them in order to guide and improve the way resources are mobilized to reach the largest possible volume and how to use them in a efficient. The evaluation examined some of the interactions and synergies between policies concerning different types of funding, particularly in the case of large-scale infrastructure financing.

424. *(v) Integrated monitoring, evaluation and learning structures.* It will be necessary to rethink the monitoring systems currently used considering the complexity of the proposed framework. It will be necessary to develop more robust frameworks that allow the government to have a 'scorecard' that can integrate existing information that is underutilized, of improving the quality of information on many of the flows analysed, and especially of collecting information on some flows over which the government has no information.

425. *(vi) A conducive environment for accountability and dialogue.* It will be necessary to re-establish a climate of trust with the actors who could provide the broader forms of development finance that the country needs to mobilize. Transparency and dialogue mechanisms will be needed to restore confidence in the process, so that they trust the established goals and find the role assigned to them attractive.

**426. The recommendations included in the medium-term Economic Transformation Plan (2018-2030) are aligned with this construction.** There are concrete opportunities to start building a National and Integrated Financing Framework (NFAP) from the implementation of the recommendations grouped in the Economic Transformation Plan. This approach will allow an appropriate perspective on financing for development in the context of the Sustainable Development Goal (SDGs).

## 8. Next steps: actions in the pre-implementation phase

### 8.1 Need and characteristics of a short-term support program

**427. It would be appropriate if the MEF considered the possibility of requesting short-term technical cooperation support to organize the AFD post-action agenda.** A result of the analysis of the previous section is that short-term technical assistance to the MEF (2-3 years) might be required to support the following actions:

- *Preparatory actions for the implementation of the Economic Transformation Plan.* The MEF should lead a process of internal discussion and consensus building of AFD's main results within the Ministry, and then at the highest level of government. To this end, the MEF must carry out the prioritization, research and preparation activities of materials analysed in Section 7.3;
- *Negotiation of financing for the implementation of the Economic Transformation Plan.* From the elements discussed in sections 7.2 and 7.3 of the AFD, it will be necessary to formulate a PFM Reform Framework that allows the shared financing of the reforms proposed in Strategic Areas 2 and 3 of the Plan. This includes negotiating specific pooled finance mechanisms to ensure the medium- and long-term continuity of these actions;

- **Beginning of the implementation of Component I.** As mentioned previously, the actions of Strategic Area 1 of the Economic Transformation Plan (Reforms to increase the fiscal space of short and medium term) are urgent and should not wait for the end of previous ones that can take time. Therefore, the formulation of this technical cooperation support should also provide for the capacity to finance the implementation of actions to increase efficiency and to develop new short-term funds.

**428. These technical cooperation actions should be geared towards capacity building at the highest level of the MEF.** As mentioned earlier, this support project should strengthen the technical capacity at the highest level of the Ministry (Office of the Permanent Secretary or Minister). For the implementation of the preparatory actions for the implementation of the Plan, it will be necessary to establish adequate management and monitoring support systems that facilitate the task of the authorities.

## 8.2 Calendar of Results for the Short and Medium Term

Figure 75 - Timetable of results of the actions of the pre-implementation phase



**429. Actions in the first year.** The focus in the coming months is the discussion of AFD results, and the generation of internal and internal consensus. Perhaps most important is the consensus on the urgency to implement the actions of Strategic Area 1 of the Economic Transformation Plan (Reforms to increase the short- and medium-term fiscal space) and start implementation as soon as possible. Consensus generation should also include development partners to encourage the start of negotiations to finance the implementation of the Economic Transformation Plan.

**430. Second Year Actions.** The main focus of these actions is to generate significant progress in the implementation of the reforms to increase the fiscal space in the short and medium term that will liberate fiscal space and increase the manoeuvrability of the Ministry in the management of the exit process. crisis. This year's actions should consolidate the consensus within the government on how to implement the Plan and the development partners to finance their implementation.

**431. Third year actions.** The last year of technical cooperation should focus on supporting the start of implementation of the Economic Transformation Plan and the use of the new financing mechanism

(terms of reference and hiring of key posts) coordinate of the actions previously initiated for its harmonic continuation using this new mechanism.

### 8.3 Financing of short-term support program

**432. The MEF can ensure the financing of these actions autonomously.** The scale of the technical cooperation actions needed to support the Ministry's action are not onerous and are in the order of magnitude of the projects that the Ministry is able to finance autonomously. Therefore, it would be advisable for the Ministry to take advantage of the presentation of the final results of the AFD (Validation Seminar) to initiate contacts with partners who are already supporting technical cooperation projects in the Ministry.

## Attachments

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## Annex II: Revealed experiences of working with NGOs in sectors

### Experiences in the Health Sector

In the health sector since 2002, it has been a question of signing a Code of Conduct between MISAU and NGOs, which covers both national and international ones. Some of the most relevant information on the work done with NGOs is:

- There is a listing of all NGOs working in the sector, but it is not an accessible database for planning or monitoring and accountability purposes. WHO funded the development of a database, but it was no longer fed and existing;
- NGOs participate in the moments of integrated sectoral planning in the provinces. Projects that provide for a transfer of funds to be managed for one of the governing bodies are integrated into the PES. The others are not;
- The Health SWAP has a working group with NGOs that meets twice a year;
- The greatest difficulty is to monitor and verify performance against planned. The provincial bodies, which are those proposed to coordinate the provision of services, do not appropriate the instrument well, giving the mechanism a more bureaucratic function rather than a real effectiveness of the intervention;
- MISAU has developed a performance mechanism that combines, in a single score, the alignment component with the policy (as recommended in PES) and the program performance component;
- NGOs do not report financial information and argue that it is impossible to fill in the information requested in the External Financing Survey (IFE). The IFE is a very basic database (an Excel sheet used in the health sector to collect information from donors).

The sector faces difficulties in aligning the NGO programming cycle (each has its own cycle) with the government programming cycle. Moreover, although differently advocated in Decree 55/98, it has great difficulties in influencing the place of implementation (sometimes the project points to problems and needs already overcome, and sometimes even the approach used by NGOs may not be respectful towards the sensitivities local cultural

"NGOs are a moving sea" and they need to organize themselves in networks to facilitate dialogue.

### Experiences in the Education Sector

Some of the most relevant information on the work done with NGOs is:

- MINEDH has a list of 157 international NGOs operating in the country.
- The Ministry receives annual reports from NGOs, but there is no certainty that they all report.
- The annual report is required to renew the authorization to work in the Country.
- The MINEC, in fact, asks the MINEDH to confirm the information. In turn, MINEDH asks for confirmation from the provincial bodies, but there were cases in which the latter did not know about the intervention.
- There are no mechanisms to verify that the information is reliable. The Ministry asks for opinions to the provincial directions.
- Reports are received in physical form and the information is not systematized for further analysis.
- MINEDH is developing a database to be fed by the provinces and districts to capture the information and cross it with the one presented in the annual reports.

### Experiences in the Social Action Sector.

The Gender, Children and Social Action Sector is reforming its mechanisms for dialogue with the public, including NGOs. The dialogue mechanism is the National Council for Social Action and the Council for the Advancement of Women. The two Councils have an analogous functioning, although they have different vocations.



The National Council for Social Action, which meets every six months, is attended by the Ministers of Health, Education, Labour, Agriculture, Public Works and Economy and Finance. Representatives of Civil Society Organizations (CSOs) and religious institutions also participate. The reform included the (i) Children's Councils, (ii) the Elderly, (iii) Disabled Persons and (iv) the Basic Security Subsystem, in a single Council chaired by the Prime Minister where the GMAS Minister is Vice- chair, with coordination functions.

- The mechanism provides for an executive secretariat (whose tasks are to be defined) and work committees for each area of the Social Action;
- In each province there are councils made up of members who are homologous to nationals. They are chaired by the Permanent Provincial Secretary. They seek to find solutions locally, and if any part is not satisfied, they ask the executive secretariat to be handled by the CAS;
- The Working Committees issue opinions in their area on the implementation of the Council recommendations by the different sectors;
- For each area, minimum service standards were defined. The reports of all stakeholders are globalized and assessed in the Council;
- The typical dynamic is as follows: government requires compliance with the standards of service delivery by the actors that manage the service (usually CSOs and NGOs) and CSOs pressure the government to do more, devote more financial resources to the AS area;
- For the past four years, the Ministry has been demanding and receiving NGO activity reports. These are physical reports and no meta-analysis is done. It is intended to develop a database that records the entire planned intervention of your budget.

The Council for the Advancement of Women works in the same way, but with a specific focus, and there are also provincial councils. The Ministry of Gender, Children and Social Action organizes a National Meeting with cooperation partners, donors, NGOs and religious institutions. There is a Social Assistance Working Group that deals with external financing that goes through the ministry's management. Dialogue with partners and funders is well structured, allowing the integration of funding for specific actions (for example, the information system of INAS - National Institute of Social Assistance - was carried out with contributions from different donors, each of which financed, a specific part). Before the debt crisis it was thought to organize a common fund for the financing of Social Welfare, but it was no longer viable. In the meantime, the Joint United Nations Joint Plan was prepared to finance - through United Nations.

## Annex III: Other Statistical Data

Table 23: Evolution of revenue in the budget (MZN in nominal terms) and as% of GDP

Million MZN in nominal terms	2006	2009	2012	2015
Total Resources	55.254	87.438	144,590	214.702
Internal Resources	27.866	47.855	101,627	165.025
Real Estate Management	27.794	47.565	98,477	155.893
Internal Loans	72	290	3,150	9.132
External Resources	27.388	39.583	42,963	49.677
Donations	18.188	25.771	27,332	18.677
Credits	9.200	13.812	15,631	31.000
% of GDP	2006	2009	2012	2015
GDP (nominal billion MZN)	178	300	433	592
Real GDP Growth Rate	8,5	6,4%	7.2%	7,5%
Internal Revenue / GDP	15,7%	15,8%	23,6%	26,3%
Internal Revenue / Total Expenditure	57,4%	56,4%	24.1%	82,3%

Source: Mozambican Tax Authority, MEF

Table 24: Major components of revenue in the budget (MZN in nominal terms) and as% of GDP

	2006		2009		2012		2015	
	MZN	% GDP	MZN	% GDP	MZN	% GDP	MZN	% GDP
Current and State Capital Revenues	41.843,90	13,2	55.901,01	15,9	90.933,45	22,7	125.472,25	26,8
Current State Revenues	39.837,17	12,5	54.106,50	15,3	89.289,39	22,3	123.021,05	26,3
Tax Revenues	33.331,78	10,5	46.262,64	13,1	77.999,64	19,5	106.723,23	22,8
Taxes on Income	9.561,12	3,0	16.120,77	4,6	33.982,71	8,5	45.847,45	9,8
From Corporate People	3.580,33	1,1	8.283,76	2,3	22.534,41	5,6	28.569,99	6,1
Of Individuals	5.696,81	1,8	7.447,50	2,1	11.089,02	2,8	16.869,50	3,6
Special Tax on the Game	47,45	0,0	55,65	0,0	76,46	0,0	86,62	0,0
Free Zones Liberalization Fee	236,53	0,1	333,86	0,1	282,82	0,1	321,34	0,1
Taxes on Goods and Services	21.812,81	6,9	28.044,84	8,0	41.055,00	10,3	57.153,83	12,2
VAT - Value Added Tax	14.127,81	4,4	19.935,32	5,7	29.622,72	7,4	40.939,97	8,7
National Production Consumption Tax	1.689,35	0,5	2.107,20	0,6	2.811,54	0,7	3.221,96	0,7
Tax on Consumption of Imported Products	1.048,38	0,3	1.143,22	0,3	1.661,21	0,4	2.983,61	0,6
Foreign Trade Taxes	4.947,27	1,6	4.859,10	1,4	6.959,53	1,7	10.008,30	2,1
Other taxes	1.957,85	0,6	2.097,03	0,6	2.961,93	0,7	3.721,95	0,8
Of which Production Tax	142,72	0,0	119,26	0,0	492,74	0,1	622,58	0,1
Tax on Oil Production	0,00	0,0	98,60	0,0	280,78	0,1	293,34	0,1

	2006		2009		2012		2015	
	MZN	% GDP	MZN	% GDP	MZN	% GDP	MZN	% GDP
Mining Tax	0,00	0,0	20,65	0,0	211,96	0,1	329,25	0,1
Of which Royalties and Surface Tax	57,55	0,0	50,10	0,0	83,01	0,0	46,46	0,0
Royalties	0,00	0,0	9,23	0,0	12,88	0,0	6,25	0,0
Surface Tax	0,00	0,0	40,88	0,0	70,13	0,0	40,21	0,0
several	415,43	0,1	205,75	0,1	245,98	0,1	181,21	0,0
Simplified Tax for Small Taxpayers	0,00	0,0	2,52	0,0	74,95	0,0	146,60	0,0
Non-tax Income	3.844,79	1,2	3.563,10	1,0	5.577,58	1,4	9.178,42	2,0
Miscellaneous Services Fees	278,10	0,1	504,24	0,1	692,24	0,2	1.467,28	0,3
Other Non-Tax Income	1.139,56	0,4	1.287,74	0,4	1.869,36	0,5	3.111,72	0,7
Pension Compensation and Survival Pension	905,16	0,8	1.047,26	0,5	1.546,90	0,8	2.727,19	1,0
Own Revenues	2.427,12	0,8	1.771,12	1,2	3.015,98	1,4	4.599,42	1,5
Consigned Revenue	2.660,60	0,6	4.280,76	0,8	5.712,17	0,9	7.119,40	0,9
Miscellaneous Consigned Fees	1.980,23	0,2	2.827,09	0,4	3.775,14	0,5	4.446,34	0,6
Other Consigned Revenues	680,37	0,6	1.453,68	0,5	1.937,04	0,4	2.673,06	0,5
Capital Revenue	2.006,73	0,0	1.794,51	0,2	1.644,06	0,0	2.451,20	1,1
Income from State Assets	38,65		786,58		49,42		61,94	
Other Capital Income	1.968,08		1.007,93		1.594,64		2.389,26	

Source: Mozambican Tax Authority, MEF

Table 25: Revenue from megaprojects (as% of GDP)

Sector	Tax	2008	2009	2012	2015
1. Energy Production	IRPS	0,03	0,04	0,03	0,02
	IRPC	0,01	0,02	0,02	0,13
	VAT	0,00	0,00	0,00	0,01
	Production Tax	0,00	0,00	0,00	0,00
	Concession Fees	0,12	0,20	0,20	0,11
	Dividends	0,00	0,00	0,03	0,00
	Subtotal 1		<b>0,16</b>	<b>0,26</b>	<b>0,29</b>
2. Petroleum Production	IRPS	0,00	0,01	0,02	0,12
	IRPC	0,03	0,00	0,42	0,99
	VAT	0,00	0,00	0,00	0,00
	Production Tax	0,03	0,01	0,05	0,02
	Concession Fees	0,00	0,00	0,00	0,00
	Dividends	0,00	0,00	0,00	0,00
	Subtotal 2		<b>0,06</b>	<b>0,02</b>	<b>0,49</b>

Sector	Tax	2008	2009	2012	2015
3. Exploration of Mineral Resources	IRPS	0,03	0,04	0,22	0,20
	IRPC	0,01	0,03	0,12	0,07
	VAT	0,00	0,00	0,00	0,00
	Production Tax	0,00	0,01	0,07	0,05
	Concession Fees	0,30	0,00	0,00	0,00
	Dividends	0,00	0,00	0,00	0,00
	Subtotal 3	<b>0,34</b>	<b>0,08</b>	<b>0,41</b>	<b>0,32</b>
4. Other Megaprojects	IRPS	0,05	0,04	0,05	0,05
	IRPC	0,10	0,09	0,07	0,06
	VAT	0,00	0,00	0,00	0,00
	Production Tax	0,00	0,00	0,00	0,00
	Concession Fees	0,00	0,00	0,00	0,00
	Dividends	0,05	0,00	0,00	0,00
	Subtotal 4	<b>0,20</b>	<b>0,13</b>	<b>0,12</b>	<b>0,11</b>
<b>Total by Sector of activity</b>		<b>0,77</b>	<b>0,49</b>	<b>1,31</b>	<b>1,84</b>

Source: Mozambique's Tax Authority

Table 26: Weight of exemptions in GDP

Description	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Income Taxes	<b>0,00</b>	<b>0,00</b>	<b>0,00</b>	<b>0,00</b>	<b>0,00</b>	<b>1,35</b>	<b>1,37</b>	<b>0,97</b>	<b>1,25</b>	<b>0,00</b>
(Domestic trade)	0,00	0,00	0,00	0,00	0,00	1,35	1,37	0,97	1,25	0,00
IRPC	0,00	0,00	0,00	0,00	0,00	0,00	0,00	0,00	0,00	0,00
IRPS	<b>3,69</b>	<b>0,10</b>	<b>5,77</b>	<b>8,14</b>	<b>11,61</b>	<b>12,14</b>	<b>19,57</b>	<b>11,10</b>	<b>8,50</b>	<b>2,61</b>
Tax on Goods and Services	1,01	0,02	1,59	2,11	3,14	3,11	5,94	2,77	1,57	0,74
(External Eating)	2,55	0,09	4,04	5,58	8,33	8,98	13,42	8,23	4,19	1,84
Rights	0,13	0,00	0,14	0,36	0,14	0,05	0,20	0,11	0,06	0,03
VAT	0,00	0,00	0,00	0,08	0,00	0,00	0,00	0,00	2,69	0,00
<b>Total</b>	<b>3,69</b>	<b>0,10</b>	<b>5,77</b>	<b>8,14</b>	<b>11,61</b>	<b>13,50</b>	<b>20,94</b>	<b>12,07</b>	<b>9,76</b>	<b>2,61</b>

Source: Mozambique's Tax Authority

Table 27: Production by Sectors (Sector Share in GDP)

	1995	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Agriculture, Livestock and Fisheries	42,2	29,0	28,3	27,8	27,9	28,2	28,2	27,9	27,5	26,7	25,4	24,2	23,3
Extractive Industry	0,6	0,7	1,2	1,1	1,3	1,4	1,4	1,4	1,4	1,7	2,6	2,8	3,7
Manufacturing industry	8,1	14,6	15,3	14,4	13,5	12,9	11,8	11,1	10,7	10,2	9,5	9,3	8,8
Construction	1,2	1,5	1,3	1,4	1,4	1,4	1,6	1,8	1,9	2,0	1,9	1,9	2,0
Transportation and Communications	10,3	8,2	8,4	8,3	8,4	8,5	8,4	9,3	9,1	8,7	8,7	8,7	8,1
Trade	10,9	8,2	8,2	8,4	9,3	9,4	9,8	9,3	9,9	9,8	10,4	11,2	11,0
Financial services	1,7	1,6	1,9	2,5	2,4	2,4	3,4	3,0	3,6	4,8	5,0	5,4	5,4
Real Estate Activities	15,3	8,8	8,7	8,1	7,5	7,0	7,2	7,2	7,3	7,2	7,2	7,1	7,1

Source: INE

Table 28: distribution of labour force by sector over time

Sectors	1990–95	1996–2000	2001–05	2006–07
Agriculture	81.5%	80.8%	79.9%	76.1%
Mining Sector	0.9%	0.6%	0.5%	0.6%
Manufacturing Sector	3.8%	3.4%	3.2%	3.2%
Energy Sector	0.1%	0.1%	0.2%	0.2%
Real Estate Management	1.4%	2.0%	2.2%	2.5%
Trade	4.2%	6.5%	7.7%	7.6%
Transportation, Communications and Storage	1.2%	0.5%	0.9%	1.1%
Others	6.8%	6.1%	5.5%	7.4%

Source (Cungura, Fagilde, Garrett, Uaiene, &amp; Headey, 2011) with data based on MPF / UEM / IFPRI 1998, INE 1999, MPF / UEM / IFPRI 2004; INE 2006, INE 2008.

Table 29: Total FDI compared to developments in MZN 2010 (at constant MZN prices)

	2009	2010	2011	2012	2013	2014	2015
TOTAL OF FDI	32.376	82.532	97.563	147.650	164.747	131.649.	117.171
Of which large projects	16.857	22.845	60.125.	106.930	125.480	69.706	38.573
FDI without megaprojects	15.519	59.688	37.438	40.719	39.267	61.943	78.598

Source: Banco de Moçambique. Authors' calculations.

Table 30: Percentage weight in GDP of the FDI to the beneficiary sectors of 85% of the total (without the extractive industry).

Sector of Activity (CAE INE)	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Transport, Storage and Communications	0,3	0,1	0,5	0,3	1,3	0,9	0,7	0,6	1,7	4,3
Others	0,0	0,0	0,0	0,0	0,0	0,0	6,9	2,7	0,0	0,0
Manufacturing (food, beverages, tobacco, textiles, other)	-0,1	0,1	0,4	1,6	0,6	-0,4	2,4	2,6	-0,9	0,3
Real Estate Activities, Rental and Business Services	0,1	0,0	0,0	-0,1	0,0	0,0	0,1	0,3	0,9	2,6
Agriculture, Livestock, Hunting and Forestry	0,1	-0,1	0,5	0,8	1,6	0,7	0,1	1,0	0,7	0,7
Financial Activities	0,0	-0,1	0,4	0,1	0,1	0,7	0,3	0,3	0,7	0,2

Source: Banco de Moçambique. Authors' calculations.

USD	2012	2013	2014	2015
Germany	856.62	2,998.37	435.00	0.00
AFDB	0.00	0.00	1,240.27	0.00
World Bank	2,951.73	57,394.03	0.00	0.00
Canada	0.00	0.00	0.00	0.00
European Commission	5,714.22	4,425.22	0.00	0.00
DFID	860,54	0.00	0.00	0.00
France	6,508.86	5,288.99	0.00	0.00
Ireland	320.51	0.00	0.00	0.00
Italy	0.00	0.00	949,24	0.00
Norway	0.00	511.96	0.00	0.00
Portugal	0.00	120.25	0.00	133.03
Sweden	0.00	996.93	0.00	0.00
Switzerland	1,000.00	0.00	0.00	0.00
United Nations	1,650.81	0.00	2,610.40	0.00
<b>Total</b>	<b>19,863.31</b>	<b>71,735.75</b>	<b>5,234.92</b>	<b>133.03</b>

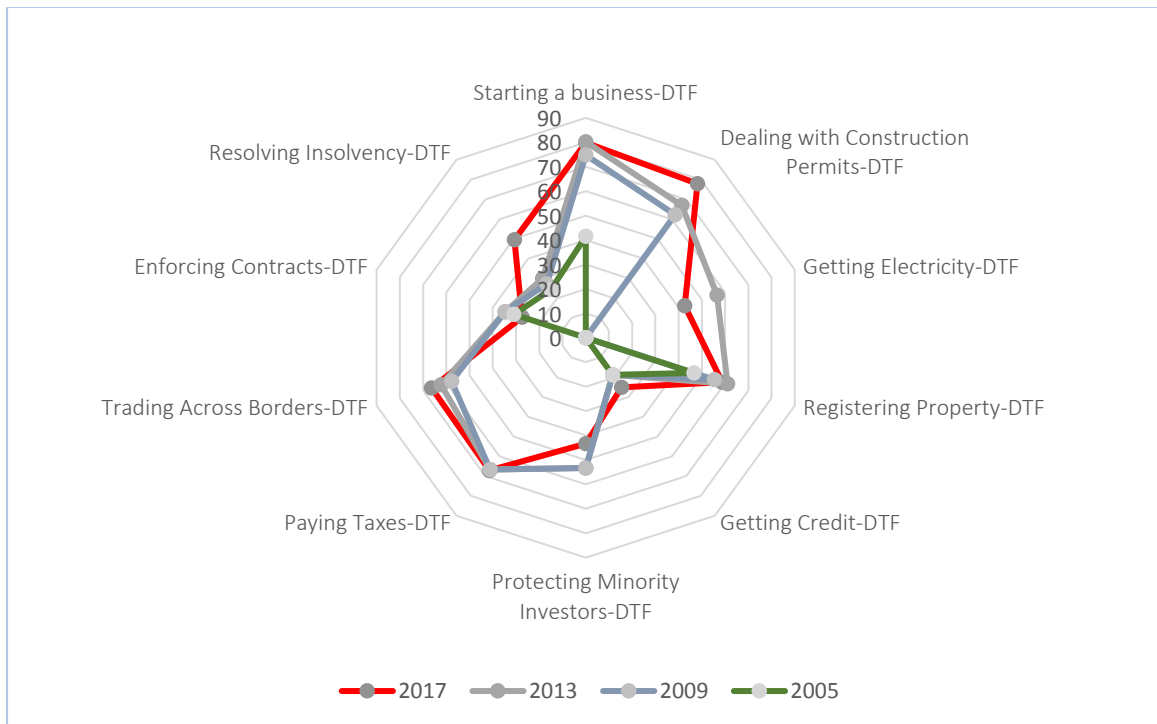
Source: DC-ODAMoz

Table 32: NSDS forecast of the evolution of Mozambique's main macroeconomic indicators

Description	dic-05	dic-06	dic-07	dic-08	dic-09	dic-10	dic-11	dic-12	dic-13	dic-14
Liquidity Swaps	9,8	16,0	13,9	12,4	8,0	13,07	11,67	2,75	3,40	3,11
Permanent Absorption / FPD	7,9	13,0	10,5	10,3	3,0	4,00	5,00	2,25	1,50	1,50
Permanent Assignment	13,6	17,5	15,5	14,5	11,5	15,50	15,00	9,50	8,25	7,50
Active Interest Rates (nominal averages / year)	19,2	23,2	22,2	21,8	19,2	21,67	23,68	21,38	20,31	20,75
Prime Rate	19,2	20,3	18,8	18,0	15,2	19,00	19,07	15,53	14,88	14,68
Passive Interest Rates (nominal averages per year)	8,52	12,37	12,66	11,64	10,15	12,18	13,35	11,46	9,14	9,14

Source: Banco de Moçambique. Authors' calculations.

Evolution of Doing Business indicators for the years 2005, 2009, 2013, 2017

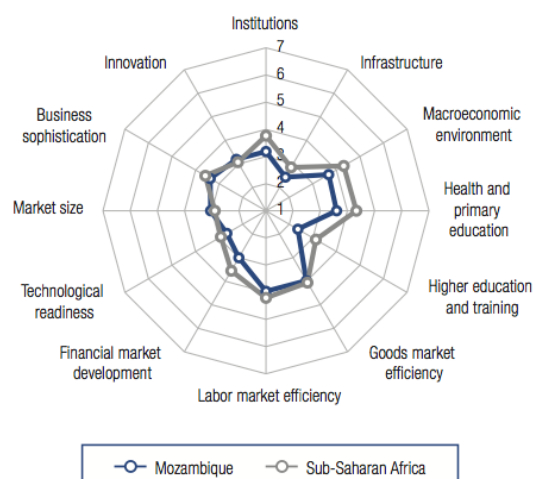


Source: Banco Mundial, Ease of Doing Business Reports 2005, 2009, 2013, 2017

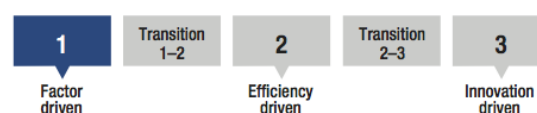
Figure 2 - Analysis of Mozambican Competitiveness Factors, according to the World Economic Forum

## Global Competitiveness Index

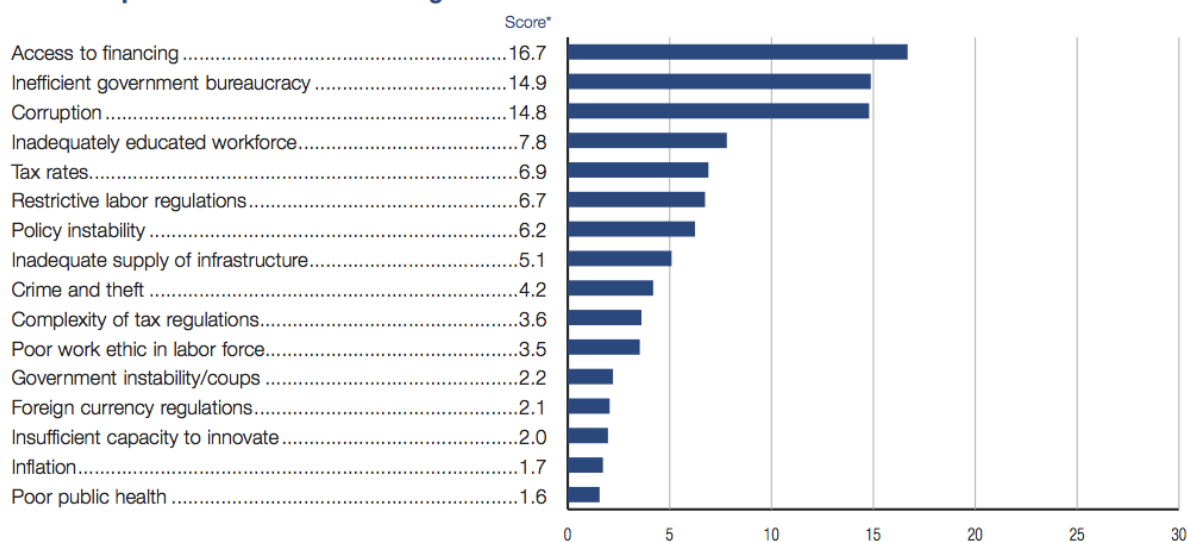
	Rank (out of 140)	Score (1–7)
<b>GCI 2015–2016</b> .....	<b>133</b>	<b>3.2</b>
GCI 2014–2015 (out of 144) .....	133	3.2
GCI 2013–2014 (out of 148) .....	137	3.3
GCI 2012–2013 (out of 144) .....	138	3.2
<b>Basic requirements (60.0%)</b> .....	<b>135</b>	<b>3.2</b>
1st pillar: Institutions .....	126	3.2
2nd pillar: Infrastructure .....	126	2.4
3rd pillar: Macroeconomic environment .....	122	3.7
4th pillar: Health and primary education .....	133	3.6
<b>Efficiency enhancers (35.0%)</b> .....	<b>132</b>	<b>3.2</b>
5th pillar: Higher education and training .....	136	2.4
6th pillar: Goods market efficiency .....	112	4.0
7th pillar: Labor market efficiency .....	98	4.0
8th pillar: Financial market development .....	126	3.0
9th pillar: Technological readiness .....	124	2.7
10th pillar: Market size .....	101	3.0
<b>Innovation and sophistication factors (5.0%)</b> .....	<b>108</b>	<b>3.3</b>
11th pillar: Business sophistication .....	120	3.4
12th pillar: Innovation .....	83	3.2



### Stage of development



## The most problematic factors for doing business



Source: WEF, *The Global Competitiveness Index in detail*



## The Global Competitiveness Index in detail

INDICATOR	VALUE	RANK/140
<b>1st pillar: Institutions</b>		
1.01 Property rights .....	3.5	116
1.02 Intellectual property protection .....	3.0	126
1.03 Diversion of public funds .....	2.4	123
1.04 Public trust in politicians .....	2.6	91
1.05 Irregular payments and bribes .....	3.0	114
1.06 Judicial independence .....	2.6	122
1.07 Favoritism in decisions of government officials .....	2.6	106
1.08 Wastefulness of government spending .....	2.7	94
1.09 Burden of government regulation .....	3.4	75
1.10 Efficiency of legal framework in settling disputes .....	3.3	94
1.11 Efficiency of legal framework in challenging regs. ....	2.9	111
1.12 Transparency of government policymaking .....	3.5	111
1.13 Business costs of terrorism .....	4.3	117
1.14 Business costs of crime and violence .....	3.4	118
1.15 Organized crime .....	3.4	125
1.16 Reliability of police services .....	2.9	124
1.17 Ethical behavior of firms .....	3.2	126
1.18 Strength of auditing and reporting standards .....	3.9	111
1.19 Efficacy of corporate boards .....	4.3	107
1.20 Protection of minority shareholders' interests .....	3.4	119
1.21 Strength of investor protection, 0–10 (best)* .....	5.2	85
<b>2nd pillar: Infrastructure</b>		
2.01 Quality of overall infrastructure .....	2.7	128
2.02 Quality of roads .....	2.3	137
2.03 Quality of railroad infrastructure .....	2.3	82
2.04 Quality of port infrastructure .....	3.6	89
2.05 Quality of air transport infrastructure .....	3.2	116
2.06 Available airline seat km/week, millions* .....	39.8	104
2.07 Quality of electricity supply .....	2.9	117
2.08 Mobile telephone subscriptions/100 pop.* .....	69.7	128
2.09 Fixed-telephone lines/100 pop.* .....	0.3	135
<b>3rd pillar: Macroeconomic environment</b>		
3.01 Government budget balance, % GDP* .....	-8.4	134
3.02 Gross national savings, % GDP* .....	12.4	116
3.03 Inflation, annual % change* .....	2.3	1
3.04 General government debt, % GDP* .....	55.4	90
3.05 Country credit rating, 0–100 (best)* .....	29.1	107
<b>4th pillar: Health and primary education</b>		
4.01 Malaria cases/100,000 pop.* .....	27,774.0	69
4.02 Business impact of malaria .....	3.6	62
4.03 Tuberculosis cases/100,000 pop.* .....	552.0	135
4.04 Business impact of tuberculosis .....	4.1	122
4.05 HIV prevalence, % adult pop.* .....	10.8	133
4.06 Business impact of HIV/AIDS .....	3.6	132
4.07 Infant mortality, deaths/1,000 live births* .....	61.5	131
4.08 Life expectancy, years* .....	50.2	136
4.09 Quality of primary education .....	2.1	138
4.10 Primary education enrollment, net %* .....	87.4	111
<b>5th pillar: Higher education and training</b>		
5.01 Secondary education enrollment, gross %* .....	26.0	139
5.02 Tertiary education enrollment, gross %* .....	5.2	127
5.03 Quality of the education system .....	2.8	119
5.04 Quality of math and science education .....	2.5	133
5.05 Quality of management schools .....	2.8	136
5.06 Internet access in schools .....	3.1	122
5.07 Availability of specialized training services .....	3.2	129
5.08 Extent of staff training .....	3.3	125
<b>6th pillar: Goods market efficiency</b>		
6.01 Intensity of local competition .....	4.6	108
6.02 Extent of market dominance .....	3.3	100
6.03 Effectiveness of anti-monopoly policy .....	3.1	123
6.04 Effect of taxation on incentives to invest .....	3.5	82
6.05 Total tax rate, % profits* .....	36.6	68

INDICATOR	VALUE	RANK/140
<b>6th pillar: Goods market efficiency (cont'd.)</b>		
6.06 No. procedures to start a business* .....	9	104
6.07 No. days to start a business* .....	13.0	74
6.08 Agricultural policy costs .....	3.3	109
6.09 Prevalence of non-tariff barriers .....	4.2	89
6.10 Trade tariffs, % duty* .....	7.4	87
6.11 Prevalence of foreign ownership .....	4.6	63
6.12 Business impact of rules on FDI .....	4.6	60
6.13 Burden of customs procedures .....	3.5	106
6.14 Imports as a percentage of GDP* .....	74.2	29
6.15 Degree of customer orientation .....	3.7	126
6.16 Buyer sophistication .....	2.8	120
<b>7th pillar: Labor market efficiency</b>		
7.01 Cooperation in labor-employer relations .....	3.7	123
7.02 Flexibility of wage determination .....	3.9	125
7.03 Hiring and firing practices .....	3.5	93
7.04 Redundancy costs, weeks of salary* .....	37.5	131
7.05 Effect of taxation on incentives to work .....	3.9	60
7.06 Pay and productivity .....	3.0	129
7.07 Reliance on professional management .....	3.4	124
7.08 Country capacity to retain talent .....	3.5	71
7.09 Country capacity to attract talent .....	3.7	51
7.10 Women in labor force, ratio to men* .....	1.04	2
<b>8th pillar: Financial market development</b>		
8.01 Availability of financial services .....	3.7	119
8.02 Affordability of financial services .....	3.6	117
8.03 Financing through local equity market .....	2.7	116
8.04 Ease of access to loans .....	1.9	126
8.05 Venture capital availability .....	2.2	116
8.06 Soundness of banks .....	4.4	95
8.07 Regulation of securities exchanges .....	3.6	111
8.08 Legal rights index, 0–12 (best)* .....	1	129
<b>9th pillar: Technological readiness</b>		
9.01 Availability of latest technologies .....	3.9	118
9.02 Firm-level technology absorption .....	4.2	99
9.03 FDI and technology transfer .....	4.2	82
9.04 Individuals using Internet, %* .....	5.9	129
9.05 Fixed-broadband Internet subscriptions/100 pop.* ..	0.0	134
9.06 Int'l Internet bandwidth, kb/s per user* .....	7.8	108
9.07 Mobile-broadband subscriptions/100 pop.* .....	3.0	130
<b>10th pillar: Market size</b>		
10.01 Domestic market size index, 1–7 (best)* .....	2.8	97
10.02 Foreign market size index, 1–7 (best)* .....	3.6	109
10.03 GDP (PPP\$ billions)* .....	31.1	108
10.04 Exports as a percentage of GDP* .....	35.2	79
<b>11th pillar: Business sophistication</b>		
11.01 Local supplier quantity .....	3.9	120
11.02 Local supplier quality .....	3.3	132
11.03 State of cluster development .....	3.5	92
11.04 Nature of competitive advantage .....	2.8	117
11.05 Value chain breadth .....	3.3	117
11.06 Control of international distribution .....	3.3	105
11.07 Production process sophistication .....	3.0	120
11.08 Extent of marketing .....	4.0	95
11.09 Willingness to delegate authority .....	3.2	119
<b>12th pillar: Innovation</b>		
12.01 Capacity for innovation .....	3.5	110
12.02 Quality of scientific research institutions .....	3.0	109
12.03 Company spending on R&D .....	3.0	89
12.04 University-industry collaboration in R&D .....	3.3	89
12.05 Gov't procurement of advanced tech products .....	3.3	73
12.06 Availability of scientists and engineers .....	3.1	124
12.07 PCT patents, applications/million pop.* .....	n/a	n/a

Other Official Funds (OFOs)

Table 33: Other Official Funds - credits per year per donor, at constant prices 2010.

MZN current prices 2010 VALUE in Million MZN current prices	INTER EST RATE	PERIOD OF GRACE (years)	MATURIT Y (years)	TYPE	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
<b>BADEA</b>					150	225	309	232	360	293	274	-	-	266	382
Construction and Equipping of Matola General Hospital Project	1%	13	33	Concessional	150	-	-	-	-	-	-	-	-	-	-
Const & Equip Geology & Min Polyt. Instit in Tete	1%	12	22	Concessional	0	225	-	-	-	-	-	-	-	-	-
Rural Electrification in Cabo Delgado Province-Phase III	1%	13	33	Concessional	-	-	309	-	-	-	-	-	-	-	-
1. Proj. of Sanitation of the City of Beira	2%	0	30	0	-	-	-	232	-	-	-	-	-	-	-
2. Proj. of Des. of the Save Valley Irrigation System	1%	0	30	0	-	-	-	-	360	-	-	-	-	-	-
3. Maputo Coastal Projection Project	1%	0	20	0	-	-	-	-	-	293	-	-	-	-	-
Construction and Equipment of two Secondary Schools and two Technical Institutes in the Provinces of Cabo Delgado and Niassa	1%	10	40	62,11% grant	-	-	-	-	-	-	274	-	-	-	-
Const. of Fisheries & M. Techn. Polytechnic	1%	10	30	51,87% grant	-	-	-	-	-	-	-	-	-	266	-
Construction of the Agrarian Polytechnic Institute of Nampula	1%	10	20	0	-	-	-	-	-	-	-	-	-	-	382
<b>BID</b>					481	403	754	-	842	-	329	-	-	539	6.060
Rehabilitation of Second & Tercialry	0%	7	25	Concessional	442	-	-	-	-	-	-	-	-	-	-
Rehabilitation of Second & Tercialry	0%	10	30	Concessional	39	-	-	-	-	-	-	-	-	-	-
The North of Cabo Delgado Prov. Rural Electrification Proj	0%	8	26	Concessional	-	403	-	-	-	-	-	-	-	-	-
Secondary Education Expansion Project	0%	7	25	Concessional	-	-	368	-	-	-	-	-	-	-	-
Gurue-Magige Road Project	0%	7	24	Concessional	-	-	386	-	-	-	-	-	-	-	-

MZN current prices 2010 VALUE in Million MZN current prices	INTER EST RATE	PERIOD OF GRACE (years)	MATURIT Y (years)	TYPE	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
. Proj. De Electrification - Niassa	0%	0	29	0	-	-	-	-	372	-	-	-	-	-	-
2. Proj. From Secondary School to 1st Cycle	0%	0	29	0	-	-	-	-	470	-	-	-	-	-	-
Water Sup. And Sanit. in the Prov.of C.Delgado and Gaza	0%	7	25	56,05% grant	-	-	-	-	-	-	329	-	-	-	-
Niassa Rural Electrif. Phase II Proj.	0%	7	25	53,12% grant	-	-	-	-	-	-	-	-	-	219	-
Inland Aquaculture & Artisanal Fisheries Project	0%	10	28	59,99% grant	-	-	-	-	-	-	-	-	-	186	-
Inland Aquaculture and Handcrafted Fisheries Project	0%	10	30	63,76% grant	-	-	-	-	-	-	-	-	-	134	-
Chimuara-Nacala Power Transmission Line	1.55+L ibor	5	15	0	-	-	-	-	-	-	-	-	-	-	6.060
<b>GOVERNMENT OF CHINA (several)</b>					<b>164</b>	<b>303</b>	<b>2.160</b>	<b>1.914</b>	<b>3.471</b>	<b>2.149</b>	<b>47</b>	<b>7.868</b>	<b>-</b>	<b>8.390</b>	<b>-</b>
Economic and Technical Cooperation	0%	10	19	Concessional	164	-	-	-	-	-	-	-	-	-	-
Construction of the Mozambique Stadium Project - M.J. Sports	0%	10	19	Concessional	-	303	-	-	-	-	-	-	-	-	-
Economic and Technical Cooperation	0%	10	20	Concessional	-	-	541	-	-	-	-	-	-	-	-
Construction Agricultural Technology Demonstration Center	0%	9	14	Concessional	-	-	226	-	-	-	-	-	-	-	-
Mozambique Attorney General Buildings & Rel Residences Project	2%	7	22	Concessional	-	-	1.393	-	-	-	-	-	-	-	-
1. Proj. of Construction of the Attorney General's Office	2%	0	20	0	-	-	-	1.287	-	-	-	-	-	-	-
2. Proj. of National Stadium Construction	0%	0	20	0	-	-	-	627	-	-	-	-	-	-	-
Economic and Technical Cooperation	2%	0	20	0	-	-	-	-	1.736	-	-	-	-	-	-
Construction of the Mozambique Stadium Project - M.J. Sports	2%	0	20	0	-	-	-	-	592	-	-	-	-	-	-
Economic and Technical Cooperation	2%	0	20	0	-	-	-	-	1.143	-	-	-	-	-	-
Construction Agricultural Technology Demonstration Center	2%	0	15	0	-	-	-	-	-	2.149	-	-	-	-	-

MZN current prices 2010 VALUE in Million MZN current prices	INTER EST RATE	PERIOD OF GRACE (years)	MATURIT Y (years)	TYPE	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Mozambique Attorney General Buildings & Rel Residences Project	0%	10	20	55,92% grant	-	-	-	-	-	-	47	-	-	-	-
1. Proj. of Construction of the Attorney General's Office	0%		0	0% grant	-	-	-	-	-	-	-	7.868	-	-	-
Prof. Buyer Cred. Reh Upgrat N6 Road Proj.	2%	7	20	35,67% grant	-	-	-	-	-	-	-	-	-	8.390	-
<b>OPEC</b>					-	577	-	-	500	261	371	-	-	-	-
Electricity IV Project	1%	7	21	Concessional	-	390	-	-	-	-	-	-	-	-	-
Matola Geral Hospital Project	1%	5	20	Concessional	-	187	-	-	-	-	-	-	-	-	-
1. Proj. of Development in Maputo - Cred. Add.	1%	0	15	0	-	-	-	-	54	-	-	-	-	-	-
2. Proj. of the Eduardo Mondlane University - Cr�d. Add.	1%	0	15	0	-	-	-	-	159	-	-	-	-	-	-
3. Proj. of Development of the system. of Irrigation. from the Save Valley	1%	0	15	0	-	-	-	-	287	-	-	-	-	-	-
4. Energy Development and Access Program	1%	0	15	0	-	-	-	-	-	261	-	-	-	-	-
Promotion of Artisanal Fisheries (PROPECA)	1%	5	15	35,25% grant	-	-	-	-	-	-	371	-	-	-	-
<b>EXIMBANK OF INDIA</b>					-	750	-	1.306	-	2.980	905	-	-	-	-
Line of Credit 2 - Electrification in Gaza Province	2%	6	27	Concessional	-	750	-	-	-	-	-	-	-	-	-
1. Electrif. And Perfur. Water Pools in Prov. Zamb.	2%	0	20	0	-	-	-	581	-	-	-	-	-	-	-
2. Draft Stat. Technological Park in Manh�a	2%	0	20	0	-	-	-	726	-	-	-	-	-	-	-
3. Rural Electrif. C. Del, Manica and Niassa Provs.	2%	0	15	0	-	-	-	-	-	815	-	-	-	-	-
4. Proj. District Headquarters Coverage Tel. F.TDM Network	2%	0	15	0	-	-	-	-	-	698	-	-	-	-	-
2. Construction of Quelimane Central Hospital Project	1%	0	20	0	-	-	-	-	-	1.467	-	-	-	-	-
Increase in Productivity of Rice, Wheat and Maize	2%	5	20	35,69% grant	-	-	-	-	-	-	548	-	-	-	-
Installation of a Factory of Solar Photovoltaic Modules	2%	5	20	35,69% grant	-	-	-	-	-	-	356	-	-	-	-
<b>KUWAIT</b>					-	535	-	-	-	-	-	-	-	-	-

MZN current prices 2010 VALUE in Million MZN current prices	INTER EST RATE	PERIOD OF GRACE (years)	MATURIT Y (years)	TYPE	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Const of Polytech Agrarian Sciences Instit Proj. in Manica Gaza	1%	7	31	Concessional	-	535	-	-	-	-	-	-	-	-	-
<b>EXIM B. KOREA</b>					-	-	-	1.306	-	3.717	1.645	-	-	3.332	258
1. Construction Project of Quelimane Central Hospital	1%	0	40	0	-	-	-	1.306	-	-	-	-	-	-	-
2. Construction of Quelimane Central Hospital Project	1%	0	20	0	-	-	-	-	-	1.467	-	-	-	-	-
3. Nacala Corridor Upgrading Project-Phase I	1%	0	20	0	-	-	-	-	-	652	-	-	-	-	-
4. Rural Electrification in Gaza Province Project	1%	0	25	0	-	-	-	-	-	1.598	-	-	-	-	-
Construction of Photovoltaic Power Plants	0%	15	40	80,31% grant	-	-	-	-	-	-	960	-	-	-	-
Emergency Information Management System	0%	15	40	80,31% grant	-	-	-	-	-	-	685	-	-	-	-
The Const. N104 Nampula & Namelil	0%	15	40	74,77% grant	-	-	-	-	-	-	-	-	-	2.026	-
The Const. of Landfil Maputo and Matola Pj.	0%	15	40	74,77% grant	-	-	-	-	-	-	-	-	-	1.306	-
Acquisition of Emergency Ambulances	0%	15	40	0	-	-	-	-	-	-	-	-	-	-	106
Acquisition of Equipment for the National Public Salvation Service	0%	15	40	0	-	-	-	-	-	-	-	-	-	-	152
<b>SAUDI FUND</b>					-	-	-	-	-	-	271	-	-	407	-
Coastal Protection of Maputo City	1%	10	40	62,11% grant	-	-	-	-	-	-	271	-	-	-	-
Niassa Province Rural Electrification Project	1%	10	30	50,18% grant	-	-	-	-	-	-	-	-	-	407	-
<b>BRAZIL</b>					-	-	-	-	-	-	2.193	-	-	8.594	-
Construction and Modernization of Nacala Airport	4,30%	4	15	11,05% grant	-	-	-	-	-	-	2.193	-	-	-	-
Moamba Major-Buyer Credit Loan Agreement	5%	5,5	15,5	-1,49% grant	-	-	-	-	-	-	-	-	-	8.594	-
<b>GOVERNMENT OF ROMANIA</b>					-	-	484	-	-	-	-	-	-	-	-
Rescheduling Agreement dated 21-05-2007- Romania	0,23 over LIBOR	8	25	Concessional	-	-	484	-	-	-	-	-	-	-	-
<b>SERBIA</b>					-	-	-	-	-	-	411	-	-	-	-

MZN current prices 2010 VALUE in Million MZN current prices	INTER EST RATE	PERIOD OF GRACE (years)	MATURIT Y (years)	TYPE	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Debt Rescheduling - Serbia	2%	1	10	0% grant	-	-	-	-	-	-	411	-	-	-	-
Total	1%	5,7	24,2		796	2.794	3.706	4.759	5.173	9.400	6.446	7.868	-	21.529	6.700
SSC / GDP					0,3%	0,9%	1,1%	1,4%	1,5%	2,7%	1,8%	2,0%		4,6%	1,4%

Source: MEF-DNT. Exchange rates of the Banco de Moçambique, with the exception of the metical-Yen rate. Rate MZN / JPY source OANDA.com. Authors' calculations.

Table 34: Key Income Indicators for the Exploitation of Natural Resources in Africa in 2015 (as% of GDP)

	Total Income from Natural Resources	Income from Petroleum (Oil)	Income from Natural Gas	Coal Income	Mineral Income	Forest Income
Angola	11.3	10.7	0	0	0	0.5
Benin	6.7	0	0	0	0	6.7
Botswana	2.7	0	0	0.2	2	0.5
Burkina Faso	21			0	9.8	11.2
Burundi	17.2			0	0.3	16.8
Cameroon	6.2	1.4	0.1	0	0.1	4.6
Central African Republic	15.4			0	0.1	15.3
Chad	13.1	6.8	0	0	0	6.3
Comoros	4.6			0	0	4.6
Congo, Dem. Rep.	34	0.3	0	0	14.4	19.3
Congo, Rep.	23.3	18.1	0.1	0	0	5.1
Cote d' Ivoire	5.5	0.4	0.2	0	1.6	3.3
Djibouti	0.9			0	0	0.9
Eritrea	19.2	0	0	0	17.4	1.8
Ethiopia	14.3		0	0	0.5	13.7
Gabon	13.1	9.9	0.1	0	0.3	2.9
Gambia, The	7.7			0	0	7.7
Ghana	17.1	1.7	0	0	5.5	9.8
Guinea	24.5			0	9.5	15
Guinea-Bissau	21.4			0	0	21.4
Kenya	3.3	0	0	0	0.1	3.2
Lesotho	6.9			0	0	6.9
Liberia	46.4			0	12.7	33.7
Libya	50.9	49.2	1.5	0	0	0.1

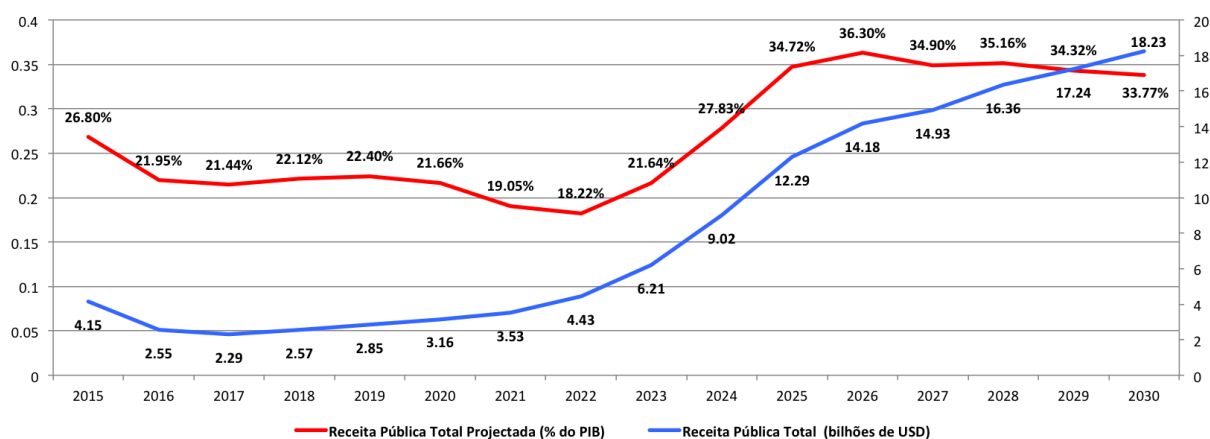
	Total Income from Natural Resources	Income from Petroleum (Oil)	Income from Natural Gas	Coal Income	Mineral Income	Forest Income
Madagascar	12.8			0	2.1	10.7
Malawi	9.6			0	0	9.6
Mali	12.5			0	8.3	4.2
Mauritania	31.8	2.1		0	27.6	2.1
Mozambique	13.1	0	1.1	1.5	0	10.4
Namibia	2.3	0	0	0	1.5	0.9
Niger	14.8	1.7	0.1	0.1	0.1	12.9
Nigeria	4.7	3	0.3	0	0	1.3
Rwanda	6.7			0	0	6.7
Sao Tome and Principe	3.1			0	0	3.1
Senegal	5.8	0	0	0	1.8	3.9
Sierra Leone	23.5			0	12.8	10.6
Somalia	17.8			..	0	17.8
South Africa	4.2	0	0	1.3	2.2	0.7
South Sudan	15.8	12	0.1	..	0	3.8
Sudan	4.2	0.7	0	0	2.2	1.3
Swaziland	2.9			0.1	0	2.8
Tanzania	6.9		0.1	0	2.2	4.6
Togo	24.7	0	0	0	16.1	8.6
Uganda	13.5			0	0	13.5
Zambia	14.4	0	0	0	10.1	4.3
Zimbabwe	8.7	0	0	0.6	3.3	4.8
<b>África Sub-Saharan</b>	<b>8</b>	<b>2.4</b>	<b>0.1</b>	<b>0.3</b>	<b>1.6</b>	<b>3.5</b>

Source: Banco Mundial: World Development Indicators 2015

#### Annex IV: Example of projections of major financial flows

433. Government early projections estimate the impact of the effect on public revenue once the companies holding the exploration concessions in the Rovuma basin begin production. The projections suggest a rapid growth in revenue from 2022 as a direct effect of these mega-investments in the economy.

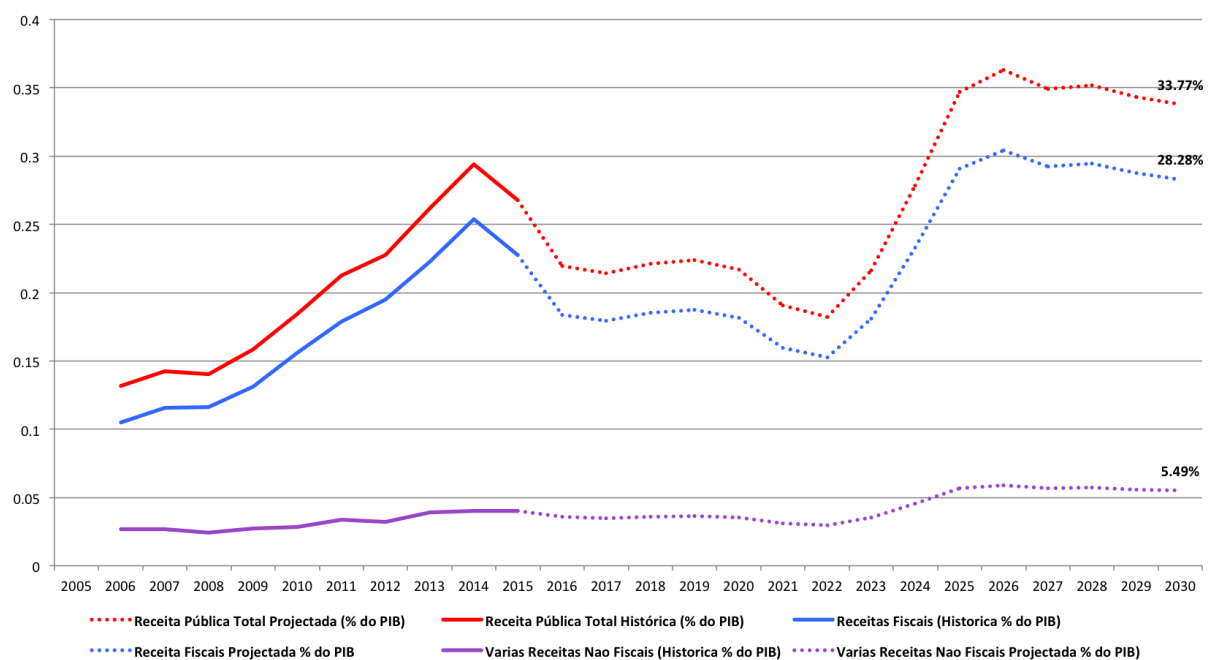
Initial government projections of revenue expansion with the expected effect of gas production



Source: Official government data, Authors' calculations

434. Government revenue, Scenario I: The total revenue data presented in Scenario I (Figure 64) corresponds to the initial government forecasts. The scenario assumed that the distribution of Tax and Non-Fiscal Revenues reproduce the same historical behaviour. According to this scenario, the Total Revenue in 2030 is 33.8%, corresponding to a total of 28.28% of Tax Revenue and Non-Fiscal Revenue (Non-Fiscal, Consigned and Capital Revenues) of 5.49% of GDP.

Scenario I: Distribution of Tax and Non-Fiscal Revenues while maintaining the current distribution



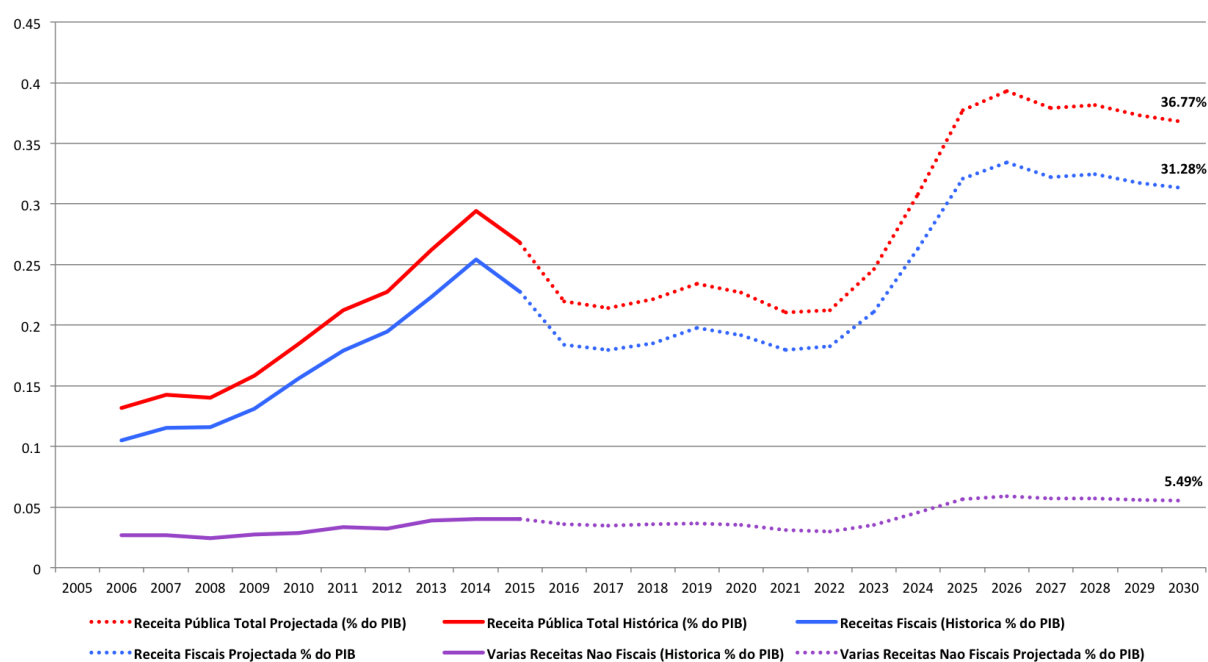
Source: AFD team based on official government data



**435. Government revenue, Scenario II.** This scenario is built assuming moderate increases in revenue from mining production. The total of mining output in 2015 was only 0.1% of GDP, which is significantly lower compared to the average for Sub-Saharan African countries (1.6%) and neighbouring countries such as Tanzania (2.2%), South Africa (2.2%) and Zimbabwe (3.3%). Revenue at these levels will depend on complex reforms to the megaproject incentive system to improve the cost-benefit ratio of the tax collection obtained. These reforms will certainly be politically laborious to negotiate and may take a long time, and at best will only affect future production.

**436. For this reason, the projection of this flow did not consider great effects until 2025.** The government also has elements to increase the short and medium-term collection on the current production, controlling more fiscally the tax evasion in the production and mineral export and of other materials (such as wood). The average value of illicit flows in the period analysed was 8.20% of GDP per year, and this type of production is certainly responsible for a significant part of this evasion. Therefore, it seems reasonable to expect that control efforts could generate growth of an average of 2-3% of GDP in the collection by 2024, which would lead the country to the level of the neighbouring countries already mentioned. If all these reforms are confirmed, the collection of new projects would produce additional effects which could lead to the collection of this type of revenue at levels well above 6% of GDP<sup>118</sup>.

Scenario II: Effect of moderate increase in mineral revenue (only controlling tax evasion)

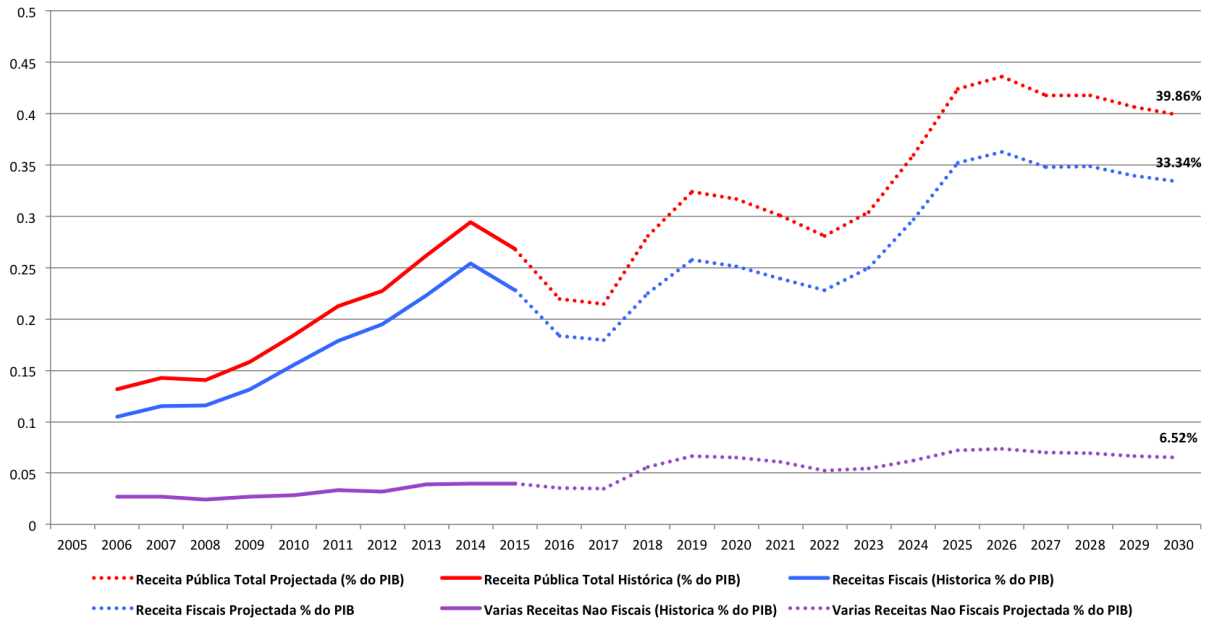


**437. In addition, it is also possible to increase the volume of non-tax revenue.** One factor that may be important is tax collection in the richer counties. Existing estimates state that only the municipalities of Nampula and Maputo could liberate a fiscal space of 2.2% to 5% of GDP. In addition, it is possible to further increase the volume of revenues in this category by improving efficiency in decentralized management.

<sup>118</sup> Although they are much larger than the ones that are current, these figures are still low compared to other African countries (see Figure 40, Section 4.4.5)

**438. The expected increase in these flows will produce a large volume of meticais in the short term, which in the current scenario is also significant as a percentage of GDP. But the expected growth of these revenues in nominal terms will not be able to keep up with the expected accelerated GDP (more than 7% from 2020).**

Scenario III: Combined Effect of Scenario II with Increase in Non-Fiscal Revenue



**439. Therefore, in relative terms, these values reduce their weight in the medium term.** In addition, all Non-Fiscal Revenue (Non-Fiscal, Consigned and Capital Revenues), analysed in Section 4.4.3, can also grow in this period. The final result is the one published in the evaluation.

Combined Effect of the main measures to increase Total Revenue

