Mozambique

Mozambique

key figures

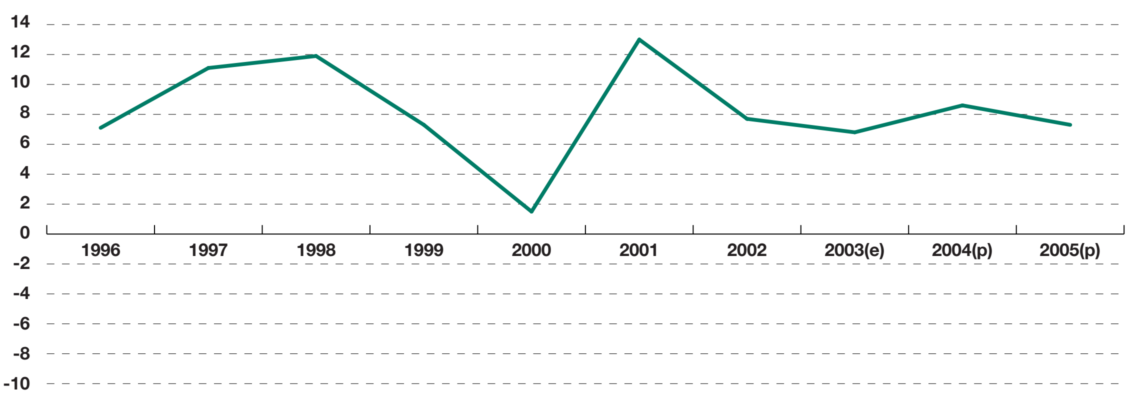
• Land area, thousands of km²	802
• Population, thousands (2002)	18 537
• GDP per capita, $ (2002)	194
• Life expectancy (2000-2005)	38.1
• Illiteracy rate (2002)	53.4

MOZAMBIQUE IS TODAY CITED as an example for the success of the economic reforms it has undertaken since the end of the civil war in 1992. These have resulted in remarkable growth rates which averaged around 8 per cent between 1995 and 1999. In 2000, the floods reduced growth to 1.5 per cent. Then, thanks to reconstruction of the infrastructures destroyed by the floods, carried out with the help of donors, and to good performances from the Mozal I aluminium smelter, the economy made up the lost ground with a 13 per cent increase in gross domestic product in 2001. In 2002, activity was again sustained by the reconstruction effort, as well as by the doubling of the capacity of the Mozal smelter and realisation of the Sasol gas pipeline between Mozambique and South Africa. Under these conditions and despite the drought which affected the south and centre of the country, GDP showed 7.7 per cent growth in 2002. In 2003, good performances by the manufacturing, transport and communications and trading sectors resulted in an estimated 6.8 per cent increase in activity. In 2004 and 2005, growth should reach 8.4 and 8.7 per cent respectively thanks to the coming on stream of Mozal II and Sasol.

Foreign direct investment in mega projects continues to remain the primary source of growth.

Private sector investment should be the principle motor of growth over the next few years. The government is making efforts to create an environment favourable to foreign and domestic investment, notably through the restructuring of a banking sector which is still highly concentrated and characterised by wide interest margins, through

Figure 1 - **Real GDP Growth**



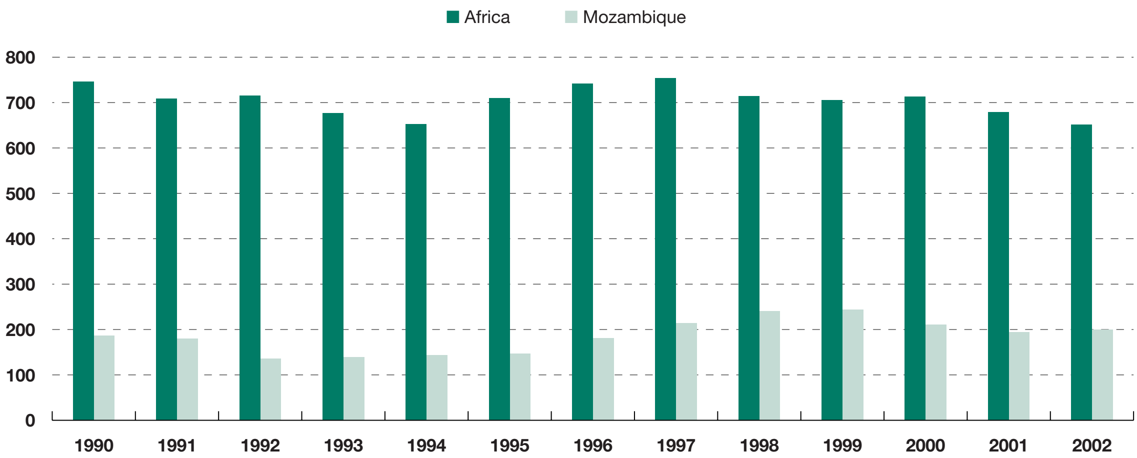
Source: Domestic authorities' data; projections based on authors' calculations.

improvement of basic infrastructures and through improvement of the business environment via the simplification of regulations. Beyond these positive prospects, however, the country must meet major challenges, notably those of reducing the level of absolute poverty and the rate of prevalence of HIV/AIDS. In February 2003, the authorities published a report evaluating the first year of implementation of the poverty reduction action plan launched in 2000. The evaluation turned out to be fairly positive with regard to the results obtained in health and education, in particular in such fields as the fight against HIV/AIDS (detection and prevention), vaccination cover and access to primary education.

Recent Economic Developments

Since 1996, the government has been striving to improve the economic environment which has stabilised under

Figure 2 - **GDP Per Capita in Mozambique and in Africa** (current $)



Source: IMF.

the influence of such different factors as the return of peace, the support of international donors for reconstruction and generally favourable climatic conditions, excepting the flooding in 2000. On this basis, Mozambique showed a record GDP growth rate of close to 13 per cent in 2001 before dropping to 7.7 per cent in 2002. Thanks to major investment projects, the key economic sectors showed strong growth in 2003.

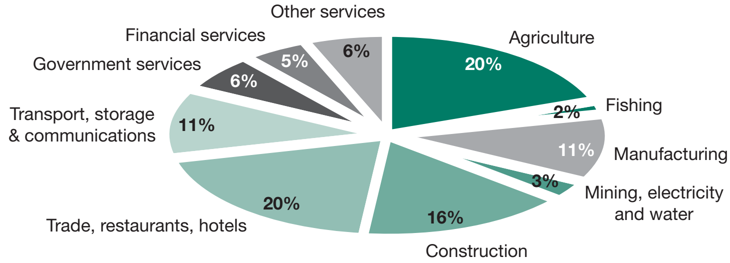
The agricultural sector represents 20 per cent of GDP. It consists essentially of subsistence agriculture and agriculture for export, predominantly cotton, cashew nuts and, above all, sugar cane. Despite the drought in the south, agricultural activity is thought to have grown by 4.2 per cent in 2003. This performance is due to growth in production of food and an increase in the production of cash crops, particularly for products such as sugar cane. This improvement in production is the result not only of good climatic conditions but also of major investment. The influx of commercial farmers from Zimbabwe, concentrated in zones on the Mozambican border (the province of Manica), also had a positive impact.

In the sugar cane sub-sector, foreign capital has flowed in on a massive scale under the effect of government incentives. Sugar was exempted from VAT in 2002 with the aim of stopping smuggling from Zimbabwe. In addition, the expectation of low prices for other products such as cashew nuts encouraged a number of small farmers to switch to more profitable crops, for example, sugar cane. In 2002, about 60 per cent of land planted with sugar cane was held by the large planters and only 40 per cent by the small planters. Even if sugar cane has above all benefited the large producers in recent years, rehabilitation of the sugar industry has generated work in the rural areas and created additional work for the small farmer population. Overall, the sector experienced exceptional growth of more than 130 per cent in 2002, and continued to grow in 2003 by an estimated 30 per cent.

In addition to sugar cane, other cash crops showed good performances. More particularly, cotton production has practically doubled these last two years, rising from 11 251 tonnes in 2000 to 25 000 tonnes in 2002. Growth slowed down in this sector in 2003, however, as a result of low prices on international markets.

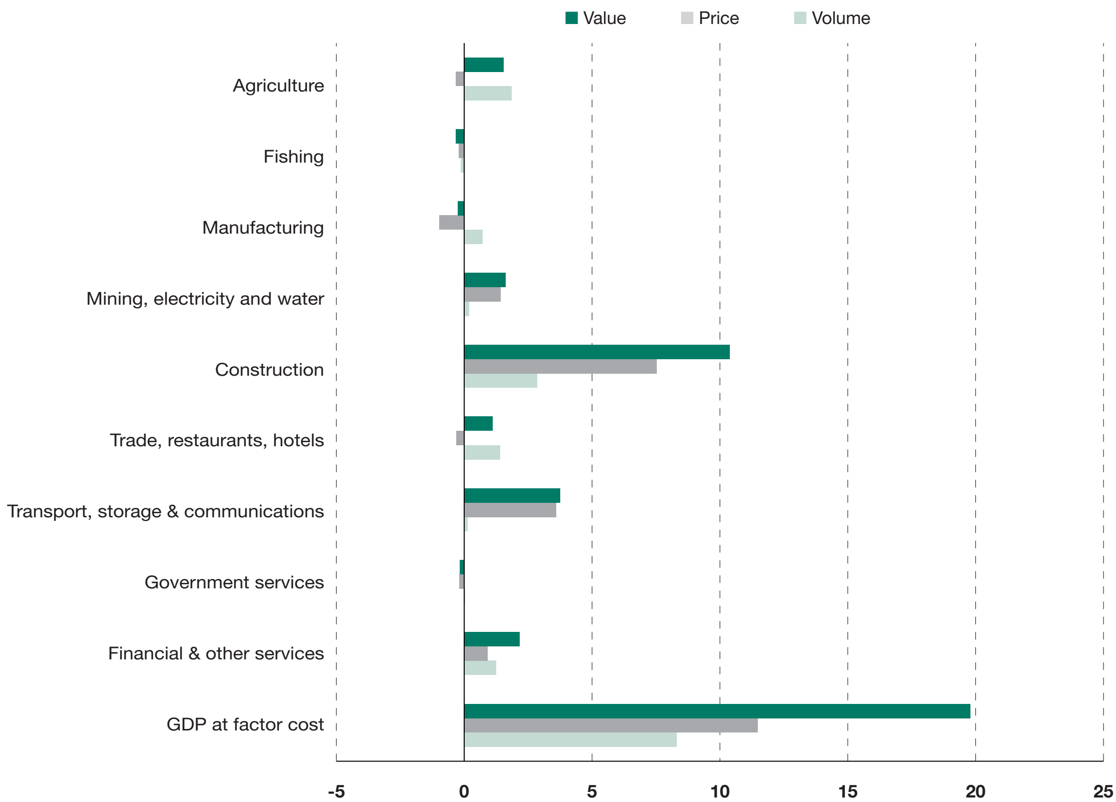
The performance of the cashew nut sub-sector has been poor. Already in the 1990s, liberalisation of the sector had a negative effect on farmers' revenues. Since 2000, the collapse of international prices has meant that it is no longer profitable to use fertilisers and other treatments. The sector's poor performances have not encouraged producers to invest in labour training or equipment and production has dropped regularly since 2000, falling by 6.4 per cent in 2002 and by 0.1 per cent in 2003.

Figure 3 - **GDP by Sector in 2002**



Source: Authors' estimates based on domestic authorities data.

Figure 4 - **Sectoral Contribution to GDP Growth in 2002**



Source: Authors' estimates based on domestic authorities data.

The dominant food crops are manioc and corn. In 2002, production of manioc was 5 400 000 tonnes, compared with 5 361 974 tonnes in 2000, and corn production was 1 236 000 tonnes in 2002, compared with 1 019 033 tonnes in 2000. Mozambique exports part of its production towards neighbouring countries but the large amount of food aid received by Malawi in recent years has raised questions about outlets.

Despite the progress recorded over the last five years, the country's agricultural potential remains partly unexploited. This can be explained by the lack of infrastructures, insufficient productivity and market fragmentation. To remedy these problems and improve co-ordination between the different operators in the sector, an agricultural investment programme (Proagri) was introduced by the Ministry of Agriculture and

Rural Development in 1997. Although the results of the first phase were mitigated, a second phase of the Proagri programme was approved in 2003. It fixes as a priority for the government, non-governmental organisations and foreign companies the creation and promotion of outgrower schemes, farmers' associations and other innovations likely to have a positive impact on the productivity and organisation of activities in the agricultural domain.

The manufacturing sector has experienced strong growth since 2001. The dynamism of production at Mozal I, which, at $1.3 billion, represents the biggest direct foreign investment ever realised in Mozambique, led to the construction of Mozal II, on which work was completed in 2003. The growth of the manufacturing sector was 4.1 per cent in 2002 and is estimated at 5.1 per cent in 2003. This growth should continue in 2004 as Mozal II is brought into production. Apart from aluminium, the most dynamic manufacturing sub-sectors in recent years have been agricultural processing and construction materials. The industry has benefited from lower import tariffs on intermediate and capital goods, as well as from more efficient customs procedures. The sector continues, however, to face a variety of difficulties which act as obstacles to the development of local privately-owned companies , including a shortage of domestic capital, high borrowing costs, excessive bureaucracy and inadequate infrastructures.

The construction sector has proved particularly dynamic since the end of the 1990s as a result of the major works associated with the inflow of direct foreign investment. After having progressed 51 per cent in 2001, this sector registered growth of 103 per cent in 2002 thanks to the extension of the Mozal smelter and construction of the Sasol gas pipeline. The sector benefited too from an increase in public investment in road infrastructure, the priority of the Ministry of Public Works. The road construction programme launched by the government in 2001 provides for the maintenance of 28 000km of road up to 2003 and the rehabilitation of 2 300km of road per year. In 2003, completion of the large-scale projects led to a 7.8 per cent contraction of the sector which is likely to continue in 2004.

The transport sector also performed well in 2001 as vast port and rail equipment modernisation programmes were launched in the development centres of Maputo, Nacala and Beira.

Since 2000, consumption has fallen as a percentage of GDP to reach 72.9 per cent of GDP in 2001 and then 68 per cent of GDP in 2002. This trend should continue until 2005. This trend reflects the fact that households are devoting an increasing share of their revenues to saving. The gap between savings and investments rates is closing year by year, thus reducing the country's dependence on foreign funds.

If gross fixed capital formation is increasing less rapidly than savings, it nevertheless rose from 41.5 per cent of GDP in 2001 to 44.7 per cent in 2002, thanks notably to an increase in foreign investment. Globally, private

Table 1 - **Demand Composition** (percentage of GDP)

	1995	2000	2001	2002	2003(e)	2004(p)	2005(p)
Gross capital formation	**28.0**	**36.6**	**41.5**	**44.7**	**45.5**	**43.2**	**45.8**
Public	16.1	10.6	16.6	14.3	11.6	11.4	10.9
Private	11.9	25.9	24.9	30.4	33.9	31.8	34.9
Consumption	**98.9**	**82.5**	**72.9**	**68.0**	**66.2**	**62.7**	**60.4**
Public	7.8	13.3	13.9	14.3	14.9	14.9	14.6
Private	91.1	69.2	59.0	53.7	51.3	47.8	45.8
External Sector	**-26.9**	**-19.1**	**-14.4**	**-12.7**	**-11.7**	**-5.9**	**-6.2**
Exports	12.1	20.2	29.2	33.0	35.6	35.2	33.7
Imports	-39.0	-39.3	-43.6	-45.6	-47.3	-41.1	-39.9

Source: Domestic authorities' data; projections based on authors' calculations.

investment is increasing and it is expected that it will represent well over 30 per cent of GDP over the next three years. The launch of a massive road and transport investment programme resulted in strong growth in public investment in 2001 and 2002. However, government expenditures diminished in 2003, owing to a shortfall in external grants disbursements. External demand is expected to improve over the period forecast owing to a fall in imports of capital equipment following completion of Mozal II and the Sasol gas pipeline.

Macroeconomic Policy

Fiscal and Monetary Policy

In October 2002, the Ministry for Planning and Finance set as a priority the introduction of policies and measures aimed at improving efficiency, transparency and responsible use of public funds. These policies, currently being put into effect, involve the creation of a central revenue authority (Autoridade Tributaria de Moçambique) which brings together notably the domestic tax administration (DNIA) and the client department. In the 2003 budget, the state adopted a system of classification by function which was even more detailed than in 2002.

The overall balance remains largely negative, showing a deficit of 7.9 per cent of GDP in 2002 compared with a deficit of 6.6 per cent in 2001 and 6.1 per cent in 2000. This deterioration in the overall budgetary balance is a result of the greater than proportional increase in current expenditure in relation to fiscal revenue. The budget deficit, just 2.7 per cent of GDP in 2003, was mainly due to a contraction of capital expenditure, including expenditures allocated to poverty-reduction projects. The reduction of this latter is principally attributable to delays in the implementation of local-level projects, themselves resulting partly from a marked fall in donor grants. Part of the reduction in capital spending has been compensated by an increase in current spending and, in particular, by overruns in public sector wages. The high cost of organisation of the 2003 local elections also contributed to the increase in current spending.

Table 2 - **Public Finances** (percentage of GDP)

	1995	2000	2001	2002	2003(e)	2004(p)	2005(p)
Total revenue and grants [a]	**20.9**	**21.3**	**28.1**	**26.2**	**25.2**	**23.6**	**22.6**
Tax revenue	10.2	12.1	11.8	12.5	12.9	12.6	12.6
Grants	9.7	8.0	14.8	11.8	10.4	9.2	8.1
Total expenditure and net lending [a]	**23.9**	**27.4**	**34.7**	**34.1**	**27.9**	**27.6**	**26.7**
Current expenditure	10.1	13.6	14.7	15.8	16.2	16.1	15.7
Excluding Interest	*8.5*	*13.4*	*14.0*	*14.3*	*15.0*	*15.1*	*14.8*
Wages and salaries	2.3	6.7	7.0	7.3	7.5	7.6	7.4
Interest	1.6	0.2	0.7	1.5	1.2	1.0	0.9
Capital expenditure	13.3	10.6	16.6	14.3	11.6	11.4	10.9
Primary balance	**-1.4**	**-5.9**	**-5.9**	**-6.4**	**-1.5**	**-2.9**	**-3.3**
Overall balance	**-3.0**	**-6.1**	**-6.6**	**-7.9**	**-2.7**	**-4.0**	**-4.2**

a. Only major items are reported.
Source: Domestic authorities' data; projections based on authors' calculations.

Fiscal revenues increased in 2003 achieving 12.9 per cent of GDP compared to 11.8 per cent in 2001. This increase is the result of new measures introduced by the government in 2002 to limit exemptions for investors. Budget revenues also benefited from the introduction of a new personal and corporate income tax code.

Under the terms of the 2004 budget, the government is committed to reducing total expenditure, particularly the level of the wage bill, and to directing budgetary resources to priority sectors. If expenditure is expected to fall in 2004, however, the reduction will be principally the result of a lower level of capital spending than that anticipated in the budget, while public sector wages will probably progress at a higher rate than that fixed by the authorities. Public revenues should continue to grow, moreover, as a result of greater efficiency in the collection of income and indirect taxes. The authorities also plan to introduce a mechanism for the automatic adjustment of fuel taxes on a quarterly basis in order to prevent the erosion of receipts by inflation. Because of a decline in the concessionality of financing provided by donors (more loans and less grants), however, these measures are not expected to prevent the deficit increasing from 4 per cent in 2004 to 4.2 per cent in 2005.

Inflation is strongly influenced by variations in the exchange rate of the rand since Mozambique imports a great number of food products from South Africa. Control of money supply, along with a series of reforms in the financial sector, allowed inflation to be reduced in remarkable fashion from 56.5 per cent in 1995 to 2.9 per cent in 1999. In 2000, the inflation rate rose to 12.7 per cent as a result of the economic disruption caused by the serious flooding and then settled at 9 per cent in 2001.

Despite a tight monetary policy in 2002 that reduced money supply to 20 per cent after 30 per cent in 2001, inflation rose again to 16.9 per cent under the impact of the drought in southern Africa which pushed up the prices of certain agricultural products. The rise in the price of imported oil at the end of 2002 and the beginning of 2003, coupled with the recent appreciation of the South African rand, contributed to maintaining inflation at 12.7 per cent in 2003. Improved food supply as well as an expected depreciation of the rand should, however, reduce inflation to below 9 per cent in 2004 and 2005.

Growing export revenues and major financing packages provided by donors have contributed to the relative stability of the metical in relation to the dollar. The Mozambican currency stayed virtually stable in relation to the dollar in 2003 and only depreciated by 2.3 per cent in 2002 compared with 36 per cent in 2001 and 50 per cent in 2000. The stability of the metical in relation to the dollar over the past year attracted bank deposits in Mozambican currency, which grew by 23 per cent in 2003 compared with growth of not more than 10 per cent for deposits in foreign currencies. The Mozambican banking sector remains nevertheless heavily dollarised since more than 50 per cent of deposits are denominated in foreign currencies.

The banking sector is very concentrated and is characterised by a very high interest margin. Whereas borrowing rates were at 32 per cent in June 2003, credit rates stood at around 12 per cent. The banks are nevertheless wary about lending. They have incurred a high level of bad debt and major reforms are due to be decided to improve the situation, including, notably, a reform of the land law aimed at simplifying inheritance procedures and property rights.

Entrepreneurs' difficulties in obtaining loans are due to the banks' demands for excessive guarantees.

External Position

The considerable efforts made by the government over these last ten years have given Mozambique an open and liberal commercial regime compared to those of its southern African neighbours. More particularly, import licences have been abolished and the structure of customs tariffs simplified. In 1999, the government approved the trade agreements concluded by the southern African countries and Mozambique belongs to the Southern Africa Development Community (SADC). The aim of the protocol is to develop duty-free trading within the southern African community, thus creating an economic space of more than 200 million inhabitants. Under the terms of these agreements, the authorities have reduced the top tariff rate from 30 to 25 per cent. They have indicated that they want to reduce the top tariff rate to 20 per cent in 2006. They do not intend, however, in the near future to abolish the export tax on non-processed cashew nuts and the sugar surcharge. This decision reflects the authorities' concern that protection for both the cashew nut processing industry and the sugar industry should be maintained.

The principal destinations for Mozambican exports in 2002 were Belgium (23 per cent), South Africa (9.1 per cent) and Germany (6.2 per cent). Imported goods in 2002 came principally from South Africa (27.5 per cent), France (8.9 per cent), the United States (7 per cent), Australia (6.9 per cent), Japan (6 per cent) and Malaysia (4 per cent). Imports consist essentially of machines and capital equipment, vehicles, metal products and textiles.

Following construction of the Mozal aluminium plant, the composition of the country's exports, which had been dominated during the last two decades by fisheries and traditional agricultural products (cotton and cashew nuts), has changed. Aluminium has become the principle export product since 2001 and represents more than half of export receipts, followed by electricity. Exports of this latter resource should increase over the coming years following the signing of a new power export agreement between South Africa and Mozambique, which should help to increase the sale price of the electrical energy produced by the latter. The sale of prawns now lies only in third place among exports.

In 2002, the external position of Mozambique deteriorated considerably under the impact of a strong increase in imports of capital equipment for the realisation of major foreign investment projects such as Mozal II and construction of the Sasol gas pipeline. On the other hand, net service imports returned to normal in 2002 after being taken to a peak in 2001 by major construction projects. Globally, the current account balance showed a deficit equivalent to 11.6 per cent of GDP in 2002, compared to 14.5 per cent in 2001.

The trade deficit was reduced to 14.9 per cent in 2003 by the dynamism of timber, aluminium and electricity exports. The deficit is projected to narrow further to reach 8.6 per cent of GDP in 2004 and 7.7 per cent in 2005. Exports should remain at a high level following the coming on stream of the second tranche of the Mozal aluminium smelter as well as the start of gas exports to South Africa. Completion of these two projects should also lead to a reduction in capital equipment imports.

Direct foreign investment is an important element in Mozambique's growth. Net inflows increased in 2003. In 2002, they represented 406 million dollars against $255 million in 2001. The abundance of natural resources, highly attractive tax incentives and political stability explain the massive flow of direct foreign investment into Mozambique. According to the Centre for the Promotion of Investment, the bulk of investment is currently being directed into the industrial and tourist sectors. There are nevertheless restrictions on the flow of foreign capital. Investors cannot repatriate loan repayments, dividends or capital representing more than $5 000 unless they have an authorisation from the competent authorities.

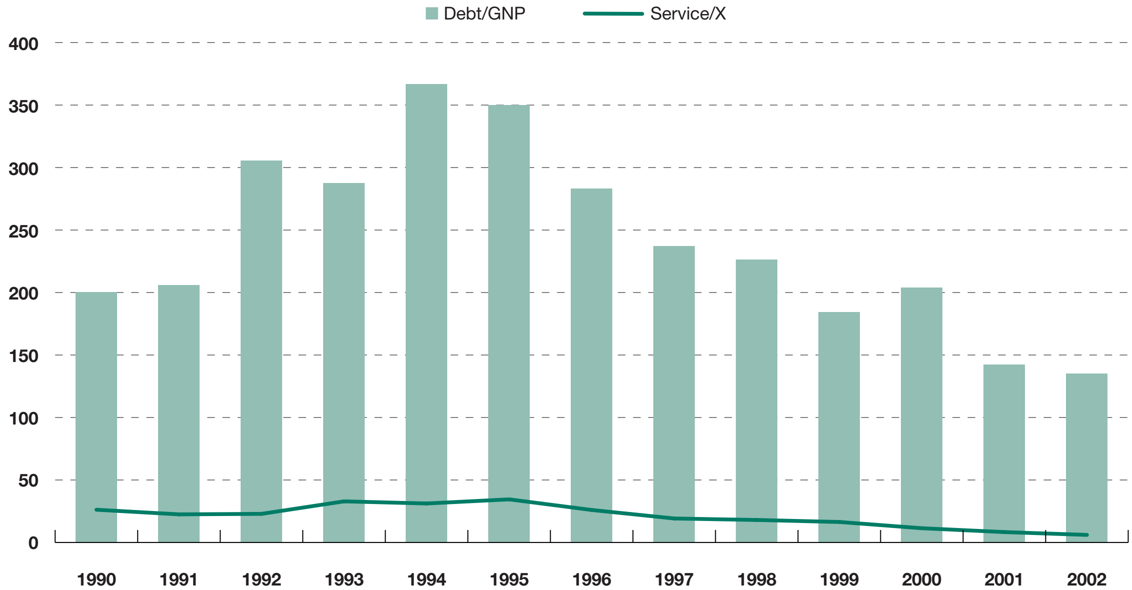
Table 3 - **Current Account** (percentage of GDP)

	1995	2000	2001	2002	2003(e)	2004(p)	2005(p)
Trade balance	-23.6	-21.7	-10.5	-16.1	-14.9	-8.6	-7.7
Exports of goods (f.o.b.)	7.4	9.9	20.5	18.9	21.4	22.9	22.9
Imports of goods (f.o.b.)	-31	-31.6	-31	-35.1	-36.4	-31.5	-30.6
Services	-5.3	-6.6	-17.6	-7.3			
Factor income[a]	…	…	…	…			
Current transfers	14.5	15.3	13.7	11.8			
Current account balance	**-14.4**	**-13**	**-14.5**	**-11.6**			

a. Factor income is included in services.
Source: Domestic authorities' data; projections based on authors' calculations.

The support of the international community remains very important for the pursuit of the country's development. To date, external financing and donor confidence has been based on continuing implementation

Figure 5 - **Stock of Total External Debt** (percentage of GNP) **and Debt Service** (percentage of exports of goods and services)



Source: World Bank.

of major economic reform programmes. Mozambique had a very high external debt, which reached 367 per cent of GDP in 1994 before being reduced to 135 per cent of GDP in 2002 following relief granted under the Highly Indebted Poor Country (HIPC) initiative. Initially, in June 1999, Mozambique's debt was reduced by $3.7 billion. Since, Mozambique has benefited from an additional reduction under the HIPC initiative, for which it reached the completion point in September 2001. The results achieved by the authorities opened the way to a new reduction by the Club of Paris on 17 November 2001, taking the total for the year to around $482 million.

Structural Issues

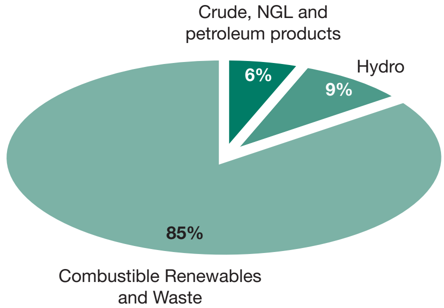
Mozambique has implemented ambitious structural reforms. The government has embarked, notably, on a vast privatisation programme since the start of the 1990s. In addition, liberalisation of the economy has been pursued in the telecommunications, port services and rail sectors. The government has also concentrated its efforts on reform of the financial sector and the removal of obstacles to private sector development.

The low level of urban population – about a quarter of the total population – limits access to commercial energy sources. The population uses wood or coal as an energy source. In 2001, the production of biomass represented 6 785 million tonnes of oil equivalent, which is to say 85 per cent of available energy supply.

Efforts are being made to make different energy sources accessible to the population. Discussions opened between the government and private sector are based on the need to increase commercial energy consumption in the years to come. Only 6 per cent of the population has access to electricity at the moment, while the rest remain dependent on biomass.

The electricity generating sector plays an important role in Mozambique. The country's installed production capacity is 2 384 MW and virtually all output is hydroelectric, most of it generated by the Hidroelectrica Cahora Bassa dam (HCB), owned 82 per cent and 18 per cent by Portugal and Mozambique respectively. More than 90 per cent of the electricity produced by the dam is exported and the remainder, which is used for local consumption, is distributed by the public sector company, Electricidade de Moçambique (EDM).

Figure 6 - **Structure of Domestic Energy Supply in 2001**



Source: International Energy Agency.

Electricity is principally consumed by industry (87 per cent), followed by households (9 per cent) and shops and public services (4 per cent).

Despite the efforts made to reach the objective of giving the whole population access to electricity, Mozambique's basic energy infrastructures remain fragile. To remedy the situation, the province of Inhambane was connected to the national electricity grid in 2002, bringing it 110KWh of high tension electricity supply. The government plans to build a new connection to enable the provinces of Lichnga and Pemba to be served by the national transmission network by the end of 2004.

The South African Power Pool (SAPP) was set up in 1995 with the objective of connecting the national networks of SADC to form a single electricity distribution network. Mozambique is already connected to South Africa and Zimbabwe, to which it supplies electricity from the Cahora Bassa dam. About 60 per cent of the electricity produced by HCB is sold to the South African Electricity Supply Commission (ESKOM) and 29 per cent to the Zimbabwean Electricity Supply Agency (ZESA). In October 2002, HCB stopped supplying ESKOM following a disagreement over prices. The dispute between HCB and ESKOM was resolved in 2003. The connection with Malawi should have been completed in 2002 but the date was put back to 2005. The project involves installing high tension cable over a distance of 220km and Mozambique wants to evaluate its environmental impact. The project is costly, moreover, at about $154 million. Mozambique has asked for the project to be considered for inclusion in the New Partnership for Africa's Development (NEPAD) programme.

The Mozambican government is also looking for investors for the construction in 2005 of a second hydroelectric power station on the River Zambesi with a capacity of 2 400 MW and at a cost of $1.3 billion.

The Moatize coal mine in the north west of the country was operated until 1977 by a South African company. Since the civil war, however, production has been at a standstill because of the absence of good transport links. A project to reopen the mine is underway, however, with the aim of achieving a production capacity of 3.3 million tonnes of coal for domestic use and steam powered machines.

The natural gas sector should become important in Mozambique since production is developing. Proven natural gas reserves represent 57 billion m^3. Ninety-seven per cent of production, which totalled 68 million m^3 in 2002, was used inside the country, mainly by power electricity generators. The 865km gas pipeline which links the province of Inhambane to Secunda in South Africa should lead to major development of the natural gas industry in southern Africa.

The privatisation programme started in 1989 with the approval of the first legislation, regulating the administrative procedures for the sale of state-owned enterprises, and the successive creation of a Technical Unit for Enterprise Restructuring (UTRE). Privatisation mainly concerned medium-and smallsized enterprises acquired by Mozambican nationals. However, the process produced mixed results; while large companies purchased by foreign multinationals have performed well, smaller companies have encountered a series of difficulties owing to their weak capitalisation, inexperienced management and poor access to credit.

In 2002, 20 large enterprises – predominantly in the transport and communication sectors – and 200 small SMEs remained to be privatised. However, private sector participation for these companies has been sought through various means, including direct equity participation, private management contracts and government leases. One of the most recent and significant privatisations has been the 15-year Maputo Port management contract, awarded in April 2003 to the Maputo Port Development Company (MPDC). The consortium, composed of British, Swedish and Portuguese companies, owns 51 per cent, and the government and the public company, Caminhos de Ferro Moçambique (CFM), own the remaining 49 per cent. Owing to the strategic location of the port, and its proximity to Johannesburg, South Africa's industrial centre, the privatised Maputo Port has the potential to compete strongly with the key South African port of Durban, which has become congested and is affected by long delays in handling cargo.

Progress is also envisaged for the privatisation of the state telecommunication company, *Telecomunicações de Moçambique (TDM),* evidenced by the bill approved by parliament in April 2004, which calls for full liberalisation of the telecommunications market. A 1999 law opened the market to private initiative and, subsequently, a second mobile phone operator, the South African company Vodacom, set up a subsidiary in Mozambique, offering competition to M-Cel, which is owned entirely by TDM. The approval of the new bill introduces competition also in the fixed phone network, and the government has pledged to privatise the company in 2004, finding a "strategic partner" to take a majority stake in TDM.

With the assistance of the World Bank, the authorities are planning a series of other reforms, including: the privatisation of *PETROMOC,* the state-owned petroleum distributor, the concessioning of part of the railroad system and management contracts for water systems in the five largest cities, as well as encouraging private sector participation in electricity provision.

In 2003, the government carried out a reform to improve the state of the banking system. Under this reform, international accounting standards will be progressively adopted by the financial institutions. The government is also committed to applying the Basle agreements on bank supervision and surveillance. In this context, the central bank is planning to negotiate and sign a protocol of co-operation with the supervisory authorities in Portugal and South Africa.

These banking sector reforms also involve the restructuring of the *Banco Internatiçonal de Mozambique* (BIM), which suffers from a large share of non-performing loans, and the gradual development of a more competitive banking system. The dominant position of BIM and the high operating costs of banking institutions represent, indeed, major obstacles to the private sector in accessing credit. Other major difficulties associated with the poor credit market include the absence of efficient judicial procedures to facilitate loan recovery, and difficulties in obtaining and using collateral to access bank credit. The constitution prohibits the private ownership of land and the procedures to obtain land titles are complex and lengthy. As a first step towards reform of the land tenure system, the government commissioned a study in 2003 on land tenure regulations and procedures to analyse ways to encourage agricultural investment.

In addition to financial sector reform, the government has started a series of initiatives to simplify the complex regulations and procedures that affect the business environment. The commercial code is being revised in line with the codes of neighbouring countries. Moreover, the authorities intend to create a one–stop shop in order to ease the procedures of registering new companies in the country. Some initiatives have also been undertaken to simplify labour market regulations that entail high retrenchment costs and expensive and cumbersome procedures for hiring expatriates. In order to overcome these rigidities, which exacerbate problems caused by the lack of skilled personnel in the economy, the authorities are amending labour legislation to simplify authorisation procedures. Furthermore, the Ministry of Labour is preparing a revised labour law that aims to reduce retrenchment costs to employers by broadening the coverage of the social security system.

Political and Social Context

Since the peace agreements of 1992 put an end to 16 years of civil war, Mozambique has returned to political stability. The municipal elections held in November 2003 confirmed the country's political and social stability. These elections allowed opposition parties such as RENAMO to participate for the first time. Organised throughout the country, they were judged by foreign observers to have been "free and open". Unfortunately, abstention was very high. The results showed the ruling party, FRELIMO, victorious except in the municipal councils of Beira, the country's second biggest city, Nacala, the economic powerhouse of the North region, Mozambique Island, the country's first capital, and Angoche. Presidential elections will take place in 2004.

Despite the scale of the projects started by the Mozambican government, which has made the reduction of poverty one of its priorities, the country is characterised by a high level of absolute poverty. The government's adoption of the Plan for the Reduction of Absolute Poverty (PARPA) for the period 2000-2004 then 2001-2005 shows the country's determination to fight poverty, with particular emphasis on education, health and rural development. The PARPA aimed to reduce the rate of poverty from 70 per cent in 1997 to 60 per cent in 2005 and 50 per cent in 2010, setting a series of social objectives including: enhancing primary school enrolment, expanding primary health care, improving mother/child health, and combating major economic problems. Thanks to rapid growth and increased spending in the social sector and on infrastructure, poverty levels seem to have been reduced over the past five years. In particular, preliminary results of a 2002/03 household survey indicate that the national rate of poverty has decreased to 54 per cent in 2002/03, compared to 69 per cent in 1997. However, this positive achievement masks significant regional variations. Incidence seems to have fallen dramatically in the centre, especially in the Tete and Sofala provinces, where poverty has fallen from above 80 per cent to 60 per cent and 36 per cent respectively. However, the province of Inhambane in the south continues to exhibit a poverty rate above 80 per cent.

In the field of health, the statistics remain alarming. Life expectancy was estimated to be 41.5 in 2002 for the population as a whole. Fifty-five per cent of the population was affected by malnutrition in 2001. Social indicators show that the most deprived people are concentrated in the rural areas where health services are practically non-existent. Nevertheless, the first progress report on the implementation of the PARPA, issued by the authorities in 2003, indicates some improvements have been made in attended births, maternal and infant mortality rates, and vaccination coverage. It should be noted, however, that progress was mainly concentrated in urban areas. The infant mortality rate was 125.5 per 1 000 live births in 2002 but 198.9 children in every 1 000 did not reach the age of five even though almost all (92 per cent) had been given the principal vaccines. The number of births in maternity facilities was 41 per cent in 2001 but, in the rural areas in particular, many woman give birth without medical assistance, resulting in high infant and mother mortality rates. To combat this problem, the government set itself the target of mobilising the rural communities via its prevention campaigns, as prescribed by the PARPA.

The rate of prevalence of HIV/AIDS among adults averaged 11.7 per cent in 2001 and 14.7 per cent for women alone. Eighty thousand children between the ages of 0 and 14 were estimated to be carriers of the disease and the number of children left orphans by AIDS was 420 000 in 2001. The same year, 433 people per 100 000 suffered from tuberculosis and many others faced death from malaria and hepatitis B. The government set the objective of preventing and reducing the impact of AIDS through education and information campaigns. In this context, several policies have been put into practice. In particular, six counselling and test centres were opened in 2001 and 18 in 2002. This policy enabled 21 766 people to be received for voluntary tests between January and September 2002 and the objective in the PARPA of achieving 24 000 tests in the year was exceeded. In 2003, the campaign has been intensified but, in addition to prevention, the government has tried to improve treatment infrastructures to cope with the increasing number of declared cases.

In the field of education, the government is concentrating its efforts on the principle of the universal primary school and access to school for all. In 2002, overall literacy stood at only 46.5 per cent, and only reached 31.4 among females.

According to the progress report on the PARPA, implementation access to primary education has improved, with the gross enrolment rate in EP1 (primary grades 1-5) rising from 70 per cent in 1998 to 104 in 2002, 2 percentage points above the target established by the poverty strategy. In tandem with improved enrolment, the proportion of girl students in EP1 improved during 1995-2001, rising from 41.8 per cent in 1995 to 43.9 per cent in 2001, broadly in line with the PARPA target of 44 per cent.

In 2002, about 275 new schools were opened in Zambezia, Gaza and Inhambane. Apart from the construction of new buildings, 956 new teachers completed their training in 2001. As for the quality of education, the government has instituted several policies to improve access to educational infrastructures and respond to the increase in demand for education at all levels.

