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Foreword

The Investment Policy Review of Mozambique *is one of five reviews carried out in member states of the Southern African Development Community (SADC) on the basis of the OECD Policy Framework for Investment (PFI). Undertaken by the NEPAD-OECD Africa Investment Initiative in the context of the* "Unlocking Investment Potential in Southern Africa" *programme with the support of Finland, it reflects the growing co-operation between the OECD and its African partners.*

The Review *is the result of a self-assessment undertaken by a national task force composed of government agencies, the private sector and civil society established by the government of Mozambique and headed by the Ministry of Planning and Development (MPD) in collaboration with the Ministry of Finance and the Ministry of Industry and Commerce. The review process was launched during an inter-agency workshop in December 2010 in Maputo, which gathered 50 participants from various ministries, technical institutions, development agencies, private sector and civil society. Fifteen different government agencies were involved in responding to the PFI questionnaire and participated in all-stakeholder meetings as well as bilateral fact-finding sessions in July 2011 and May 2012. The findings of the* Review *were presented to all stakeholders and discussed in depth in March 2013, under the chairmanship of Adriano Ubisse (National Director for Investment and Cooperation, MPD).*

This Review *has been prepared by Carole Biau, Mike Pfister and Dambudzo Muzenda under the supervision of Karim Dahou, Executive Manager of the NEPAD-OECD Africa Investment Initiative. The report has benefited from inputs by Stephen Thomsen, Hélène François, Alexandre de Crombrugghe, and Mi-Hyun Bang from the Investment Division of the OECD Directorate for Financial and Enterprise Affairs; and by Michael Baxter acting as external consultant. The secretariats of several OECD bodies, including the Investment Committee, the Committee on Fiscal Affairs, and the Committee on Corporate Affairs contributed to various chapters of the* Review. *The views contained within do not necessarily represent those of NEPAD member governments.*

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Preface by the Hon. Aiuba Cuerencia, Minister of Planning and Development, Government of Mozambique

Mozambique's economy has long benefited from investment in aluminium and other extractive industries; in addition, recent discovery of significant gas reserves could turn our country into one of the world's largest Liquid Natural Gas producers. But we are fully aware that resources alone will not guarantee growth, employment and sustainability. We need substantial investments to add value to the resources we have not only in the extractive industries but also in tourism, agriculture, and infrastructure – to name just a few critical sectors.

We therefore consider that the private sector has a vital role to play in our country's growth and diversification agenda. Significant efforts are being made to improve the business climate and competitiveness of our economy. In 2009, the Code of Fiscal Benefits harmonised most investment incentives, and currently the Centre for the Promotion of Investment is working with sector-specific agencies to elaborate a national investment promotion strategy. An export promotion strategy is also in its final stages and will be another important step towards growing our non-traditional export sectors.

In the coming years, Mozambique's projected economic growth looks likely to match and even exceed that of its regional neighbours. Forward-looking international businesses are increasingly interested in the potential of our country. Yet, this interest can only materialise into concrete and lasting investment projects if investors, both foreign and local, benefit from conditions conducive to long term competitiveness. Our investment regime could be further simplified, more predictable and better communicated to investors.

In addition, more attention could be payed to the impact and desirability of existing investment incentives and on better leveraging the potential of the mining sector so that it can become a greater source of business linkages, local entrepreneurship and expansion of infrastructure networks. This would be fully in line with the growth model envisaged by the 2011-14 Action Plan for the Reduction of Absolute Poverty (PARPA II) which views that upstream

and downstream activities related to extractive industries can be promoted hand-in-hand with broader diversification efforts in order to generate more employment for the Mozambican people.

It is in this context that my Ministry requested the OECD to support the government of Mozambique in self-assessing its investment policy framework against global best practices. This interactive evaluation has taken place over the past couple of years and has stimulated rich dialogue across government and private sector stakeholders, covering issues of investment policy, investment promotion and investment in infrastructure.

The recommendations that follow from this process have allowed us to better identify necessary investment policy reforms. The Investment Policy Review has also positioned us within regional efforts for investment policy-making, in particular the forthcoming Regional Investment Policy Framework that the Southern African Development Community (SADC) will develop with the support of the OECD. I firmly believe that this review can help better poise Mozambique at this critical time so that it can make the most of the growing investor interest in the country while addressing the fundamental social and economic needs of its population.

Preface by Mr Rintaro Tamaki, Deputy Secretary-General, OECD

Twenty years have passed since Mozambique emerged from civil war, in 1992. Over this period the country has successfully made the transition towards a multiparty political system and market-based economy, putting in place an increasing number of measures to stimulate the private sector and improve the business climate.

Thanks in part to the reforms of the past two decades, GDP growth has averaged 7.5% since the turn of the millennium. Although foreign direct investment inflows to Mozambique increased only gradually in the early 1990s, two mega-projects – in the aluminium and gas sectors – created a landmark change in the early 2000's. To ensure that positive momentum in GDP growth and FDI inflows was accompanied by socio-economic benefits, government elaborated a series of Action Plans for the Reduction of Absolute Poverty (PARPA); yet the development impacts of these growth and investment trends have been limited to date, and poverty and unemployment rates remain high. The poverty rate declined from 69.4% of the population in 1997 to 55% in 2010, but poverty alleviation has since stagnated. Diversification out of the extractive sector (which still attracts 83% of total FDI inflows and generates 72% of exports) is a related challenge to tackle.

This *Investment Policy Review* illustrates the important progress made by the government of Mozambique in improving its investment climate over recent years. It highlights major initiatives and specific policy measures undertaken, as well as areas that need further reforms to attract more and better investment, both domestic and foreign. While numerous policy advances have been achieved, such as the elimination of many foreign investment restrictions and the elaboration of a regulatory framework for public-private partnerships, the *Review* identifies remaining challenges. These include an insufficiently transparent and predictable investment regime, large infrastructure gaps which especially hinder smaller entrepreneurs, and weak communication channels between public and private sectors. The *Review* recommends policy options which can respond to these challenges.

The government of Mozambique has demonstrated strong commitment and ownership throughout the review process. While the OECD is responsible

for the content of the *Review*, it reflects contributions from many levels of the government of Mozambique, from conception to completion. It also further illustrates Mozambique's efforts to reform its economy, which the OECD and its partners will continue to support at both national and regional levels.

Collaboration between the government of Mozambique and the NEPAD-OECD Africa Investment Initiative is indeed set to expand in coming years, as the 14 member states of the Southern African Development Community (SADC) have identified the OECD Policy Framework for Investment (PFI) as a reference for developing the SADC Regional Investment Policy Framework over 2012-15. As a conduit for trade and port access for its landlocked neighbours, Mozambique particularly stands to gain from this exercise and from co-ordinated improvement of investment policy across the region. As one of the five SADC countries to have undertaken a PFI-based OECD *Investment Policy Review* to date, Mozambique will be one of the leading partners in this project. This should further enhance the momentum for investment reform over the next few years and help put Mozambique on a path of robust and sustainable growth.

Acronyms and abbreviations

ACIS	Commercial and Industrial Association (*Associação de Comércio e Indústria*)
ANE	National Roads Administration (*Administração Nacional de Estradas*)
AT	Mozambican Tax Authority (*Autoridade Tributária de Moçambique*)
BAU	One Stop Shop (*Balcão de Atendimento Único*)
CACM	Center for Commercial Arbitration, Conciliation and Mediation (*Centro de Arbitragem Comercial, Conciliação e Mediação*)
CaDUP	Each District One Product (*Cada Distrito Um Produto*)
CDN	Northern Development Corridor (*Corredor de Desenvolvimento do Norte*)
CNELEC	National Electricity Council (*Conselho Nacional de Electricidade*)
CEPAGRI	Agriculture Promotion Centre (*Centro de Promoção da Agriculture*)
CFM	Mozambique Ports and Railways (*Portos e Caminhos de Ferro de Mozambique*)
CIN	Business Information Centre (*Centro de Informação de Negócios*)
COE	Centre for Entrepreneurial Advice (*Centro de Orientação ao Empresário*)
CPI	Investment Promotion Centre (*Centro de Promoção de Investimentos*)
CRA	Water Regulatory Council (Conselho de Regulação do Abastecimento de Água)
CTA	Confederation of Business Associations of Mozambique (*Confereração das Associações Económicas de Moçambique*)
DINATEFE	National Directorate of Land and Forestry
DUAT	Land Use and Exploration Right (*Direito de Uso e Aproveitamento de Terra*)
EITI	Extractive Industries Transparency Initiative
FDI	Foreign Direct Investment
FEWSNET	Mozambique Food Security Outlook
FIPAG	Investment and Asset Fund for Water Supply (*Fundo de Investimento e Património do Abastecimento de Água*)
FUNAE	Energy Fund (*Fundo Nacional de Energia*)

GAZED	Office for Accelerated Economic Development Zones (*Gabinete das Zonas Económicas de Desenvolvimento Acelerado*)
GDP	Gross Domestic Product
GIZ	German Cooperation Agency
GPIE	Office for the Promotion of Foreign Investment (*Gabinete de Promoção de Investimento Estrangeiro*)
IAB	Investing Across Borders
IACM	Mozambican Civil Aviation Institute (Instituto da Aviacao Civil de Mocambique)
ICSID	International Center for the Settlement of International Investment Disputes
IFZ	Industrial Free Zone
INATTER	National Institute of Surface Transport (*Instituto Nacional dos Transportes Terrestres*)
INATUR	National Tourism Institute (*Instituto Nacional de Turismo*)
INCM	Mozambique National Telecommunications Institute (*Instituto Nacional de Telecomunicações de Moçambique*)
INE	National Institute of Statistics (*Instituto Nacional de Estatística de Moçambique*)
INNO	National Institute of Standardization and Quality (*Instituto Nacional de Normalização e Qualidade*)
IPEME	Institute for Small and Medium Enterprises (*Insituto para a Promoção das Pequenas e Médias Empresas*)
IPEX	Export Promotion Institute (*Instituto para a Promoção de Exportações*)
IPI	Industrial Property Institute (*Instituto da Propriedade Industrial*)
IPR	Intellectual Property Rights
ISO	International Organization for Standardization
LMIS	Land Management Information System
MIC	Ministry of Industry and Trade (*Ministério da Indústria e Comércio*)
MIGA	Multilateral Investment Guarantee Agency
MINAG	Ministry of Agriculture (*Ministério da Agricultura*)
MZN	Mozambique metical (also MT)
MPD	Ministry of Planning and Development (*Ministério da Planificação e Desenvolvimento*)
MTC	Ministry of Transport and Communication (*Ministério dos Transportes e Comunicação*)
NEPAD	New Partnership for Africa's Development
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
OPIC	Overseas Private Investment Corporation

PARPA	Action Plan for the Reduction of Absolute Poverty (*Plano de Acção para a Redução da Pobreza Absoluta*)
PES	Economic and Social Plan (*Plano Económico e Social*)
PFI	Policy Framework for Investment
POE	Centre for Entrepreneurial Advice (*Ponto de Orientação ao Empresário*)
PPP	Public Private Partnership
SADC	Southern Africa Development Community
SEZ	Special Economic Zone
SIMA	Agricultural Market Information System
SISCAL	System for Licensing and Registration of Enterprises
SISTAFE	State Financial Management System (*Sistema de Administração Financeira do Estado*)
SME	Small and Medium Scale Enterprise
SPGC	Provincial Cadastral Service (*Serviço Provincial de Geografia e Cadastro*)
SQAM	Standardization, Quality Assurance, Accreditation and Metrology
UNCTAD	United Nations Conference on Trade and Development
USAID	United States Agency for International Development
WIPO	World Intellectual Property Organization

Executive summary

Market-based economic policies have been an important factor in stimulating economic development in Mozambique over the past 15 years, securing one of the highest growth rates of African non-oil economies during this period. Since the early 1990s the country has moved away from central planning, created the Mozambique Investment Promotion Centre (CPI) and reformed its investment code to strengthen investors' rights. This momentum is upheld today and since 2013 CPI is elaborating a national investment promotion strategy together with sector-specific investment promotion agencies.

However the Mozambican economy faces somewhat of a mis-match between growth and investment trends. Real GDP growth has been consistent and strong since 2002 (at over 7.5% annually), driven mainly by agriculture and by construction and tourism services. Yet agriculture absorbs only 10% of private investment, and expansion and value-addition beyond the cash-crop sectors remain hindered by inadequate infrastructure, commercial networks, and financing. By contrast the mining sector, which provided only 1% of GDP over 2010-12, concentrates the vast majority of export revenues and of FDI.

Mozambique has therefore historically depended on "mega-projects" in the extractive sector for its revenue and foreign exchange – and particularly on aluminium, which has been subject to large international price swings over the past few years. The country is also entering a "coal boom", and the opening of multiple new mining concessions caused FDI inflows to double over 2011. Nevertheless the share of FDI into non-mega projects (mainly in the agriculture, industry and tourism sectors) has gradually risen to 45% over the past five years – an encouraging trend which Mozambique could seek to further encourage in order to increase the spill-overs of investment across the broader domestic economy.

The legal framework for investment remains difficult to decipher and investor protection standards could be strengthened. This is particularly the case for intellectual property rights, access to land, protection from expropriation and the resolution of disputes. Moreover several sectors of the economy are restricted to foreign participation, and pre-conditioning all guarantees of the Investment Law on the possession of investment licenses

tends to disadvantage SMEs. Many of these persisting gaps and contradictions in Mozambique's investment policy framework are exacerbated by poorly-managed communication and weak feedback mechanisms between public and private sectors.

Processes for land registration and access pose an especially complex barrier for all investors. Land-use rights (DUATs) must be secured through multiple procedures involving disparate institutions, and procedures for community consultation and compensation are frequently protracted and costly. In addition land tenure rights are insufficiently secure as the DUAT can be revoked at any point if investors are deemed to contravene agreed land exploitation plans. Land registry and cadastre issues pose an obstacle not only for potential investors but also for investment promotion bodies in their efforts to identify and market available investment opportunities.

Inadequate infrastructure hinders business operations, and demand from large-scale consumers and export markets takes precedence over domestic needs. Electricity and transport infrastructure have traditionally served the needs of mega-projects and of consumers abroad. By contrast only 14% of the population has access to electricity. To meet the anticipated mining and exports boom, large investors are now looking to develop their supporting infrastructure. These investments by mining and other companies present significant network expansion opportunities, but may bring few benefits for the local population if operated as enclaves; they will therefore require careful co-ordination by government.

Key policy recommendations

Policies to strengthen and clarify the legal framework for investment

- Group all sector restrictions on FDI within a regularly updated negative list. This would detail all activities for which special treatment is provided to Mozambican nationals, or where foreign participation is limited to specific thresholds.
- Clarify the measures that are considered as national interest in cases of expropriation and nationalisation, and facilitate investor access to international arbitration.
- Consider eliminating investment licenses, or extending the scope of the Investment Law beyond those investors that have obtained investment licenses.

Policies to facilitate access to land for investors

- Revive and adequately maintain the electronic land registry and cadastre (LIMS) so as to accelerate land registration processes.
- Simplify procedures for community consultation and investor access to land use rights (DUATs) – notably by reducing the number of agency approvals necessary, and reviewing the distinction between a provisional and a definitive DUAT.
- Enhance security of land tenure by providing greater protection from expropriation within the DUAT, and by ameliorating the efficacy of the court system in adjudicating land disputes.

Policies to better promote and facilitate investment

- Establish a mechanism for systematic cost-benefit analysis of tax incentives for investment (including evaluation of the impact of Special Economic Zones); this analysis should consider alternative uses of the forgone fiscal revenue – notably structural policies to enhance infrastructure and human resources for investment attraction.
- Formalise mechanisms for collaboration among investment promotion agencies (CPI, INATUR, CEPAGRI, IPEX) and strengthen their role as channels of communication between government and the business community. The design, implementation and monitoring of forthcoming investment and export promotion strategies should closely involve all of these bodies.
- Provide more structured government support for private sector efforts to foster business linkages between small-scale domestic enterprises and larger investors – both in the extractive sector (through mining development

agreements), and by extending targeted linkage programmes to more labour-intensive sectors (such as agriculture or tourism).

Policies to meet domestic infrastructure needs

- Co-ordinate infrastructure investments by mining companies so as to enhance coherence with spatial development plans, build on joint economies of scale, and cater to domestic needs by extending infrastructure services beyond the areas immediately covered by the mining projects.
- Strengthen the regulatory framework for procurement and PPPs in infrastructure and empower procurement entities and PPP Units to better prepare and package projects for national as well as cross-border infrastructure.
- Empower sectoral infrastructure regulators not only for the pricing of public utility services, but for monitoring project implementation and revising privileges enjoyed by state-owned enterprises across infrastructure sub-sectors.

Chapter 1

Overview of investment policy challenges and recommendations for Mozambique

Mozambique has made marked progress in recent decades in terms of liberalization of its economy and improvement of its investment framework. This overview first provides a short description of the macroeconomic environment and investment policy context in Mozambique, taking stock of Mozambique's fundamental investment, privatization and business reforms. Second, it gives an overview of investment and growth trends over the last two decades. This helps shed light on dominant policy challenges faced by Mozambique in attracting investment across all economic sectors. Among other obstacles, many aspects of the investment policy framework remain insufficiently transparent and do not provide effective safeguards of policy predictability for both foreign and domestic investors. After years of successfully attracting investment into capital-intensive mega-projects, Mozambique now needs to diversify in more labour-intensive sectors such as agriculture and tourism, and to also increase business linkages in the mega-project sectors themselves. In order to facilitate this, many large infrastructure gaps will need to be addressed. Finally, this overview chapter provides recommendations for policy options to prioritise. These recommendations should assist the government of Mozambique in improving the general investment climate, notably so as to enhance its diversification strategy and stimulate greater investment in infrastructure.

1.1. Document summary

This chapter first provides a short description of the **macroeconomic environment and investment policy context** in Mozambique. Mozambique today has one of the highest growth rates of Africa's non-oil economies, averaging 7.5% since the turn of the millennium. The country has engaged in considerable economic reform since its emergence from civil war in 1992, with substantial support from development partners. The pace of reform and modernization has especially picked up since the mid-2000's, numerous investment policy reforms having been recently introduced and others being in the process of definition and implementation. Mozambique has undertaken many efforts to make it easier for enterprises to do business, and to increase the country's attractiveness for foreign and domestic investment – especially in the mining sector. Yet poverty and unemployment rates remain high, and in many other economic sectors Mozambique remains outperformed by neighbouring countries in the Southern African region. Moreover Mozambique's doing business performance (as calculated by the World Bank Doing Business indicators) has stagnated, and most recently declined.

Second, this chapter gives an overview of **investment and growth trends** over the last two decades. This illustrates that the Mozambican investment policy framework has generally encouraged both domestic and international private investment, particularly in larger, formal industries and most effectively in the extractive industries. It also highlights Mozambique's recognised need to diversify its economy towards more labour-intensive sectors such as agriculture and tourism; this could enhance employment opportunities, better distribute economic growth, and reduce the current variability in export revenues and FDI inflows.

Third, the document identifies **dominant policy challenges** faced by Mozambique in attracting investment across all economic sectors. Among other obstacles, many dimensions of the investment policy framework remain insufficiently transparent and do not provide effective safeguards of policy predictability for both foreign and domestic investors. Access to land is subject to complicated procedures, and provisions for investor protection are not clearly outlined within a common legal instrument. In the field of investment promotion, there is a need for more systematic analysis of the impact of existing investment incentives, including in special economic

zones; there is also unexploited potential for business linkages in the mining sector, and mechanisms for investor-State communication are weak and under-utilised. Finally the infrastructure gaps across all economic sectors remain vast, particularly as concerns the energy sub-sector.

Finally, this chapter suggests several **associated policy options** to address these obstacles. These policy options aim to enable Mozambique to better attract and leverage the role of foreign and domestic investment in the economy, so as to: better share the dividends of growth from the mining industry; stimulate competitiveness and investment attraction in other sectors of the economy; and enable the government to meet the employment and growth objectives of the current poverty reduction strategy (PARPA, 2011-14).

1.2. Macroeconomic environment

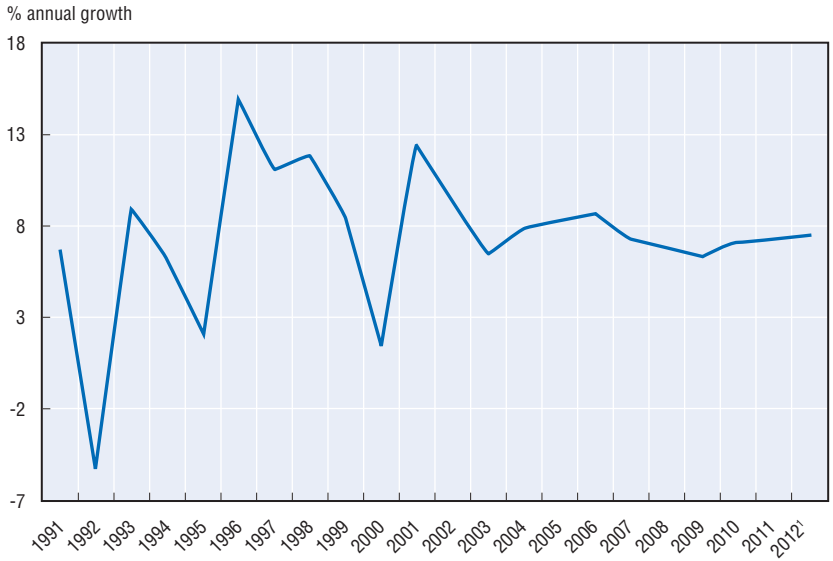
Trends and composition of growth since independence

Following Mozambique's independence from Portugal in 1975, from 1977 to 1992 the country was embroiled in a protracted civil war. By the time of the General Peace Accords of 1992 the country ranked among the poorest in the world, with very low social and economic indicators. The planned economy approach adopted under the presidency of Samora Machel was ended in 1987 with the **Economic Recovery Plan** (ERP), which included measures to stimulate the private sector and was reinforced in 1990 by legislation and the enactment of a new constitution providing for a multiparty political system, market-based economy, and free elections. The transition to a more liberalised economy was therefore underway before the end of the war.

Throughout the 1990s and with considerable support from the World Bank, the International Monetary Fund and other development partners, **a burst of economic reform took place** with a focus on moving away from central planning, engaging in privatisation and setting up a modern judicial and banking system. The investment code was reformed in June 1993 to clarify investors' rights and obligations, as well as fiscal and customs regulations. Mozambique's market-based economic policies have proven to be an important factor in national economic growth over the past 15 years, producing one of the highest growth rates of African non-oil economies during this period. Since 2002 annual real GDP growth has averaged over 7.5% (Figure 1.1). While GDP per capita has not experienced a continuous increase, overall the trend is also visibly positive (Figure 1.2).

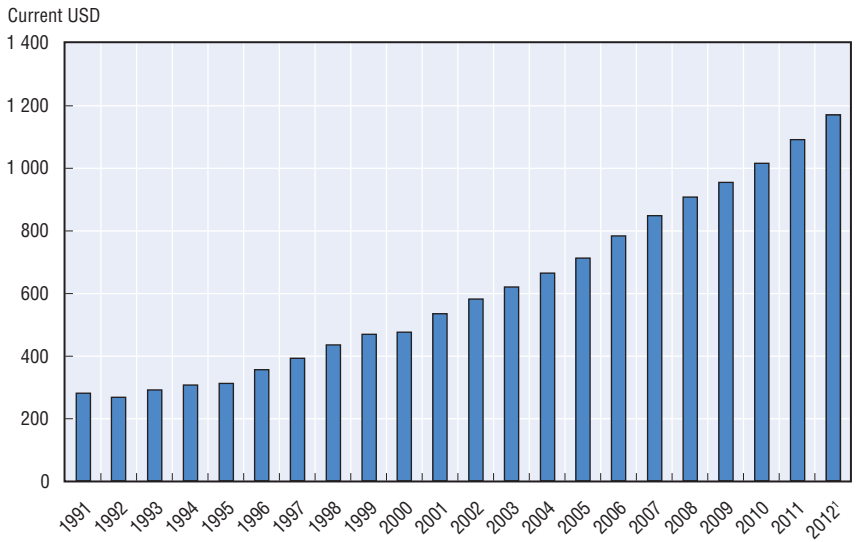
GDP remains driven by agriculture (mainly tobacco, sugar, cotton and cashews, accounting for 25% of GDP in the first quarter of 2012, Figure 1.3), and by services, which include construction and tourism (30%), commercial services (11%), transport and communications (11%), and finance and real

Figure 1.1. **Annual percentage GDP growth in Mozambique, 1991-2012**



1. 2012 figures are estimated.
Source: IMF World Economic Outlook, 2013.

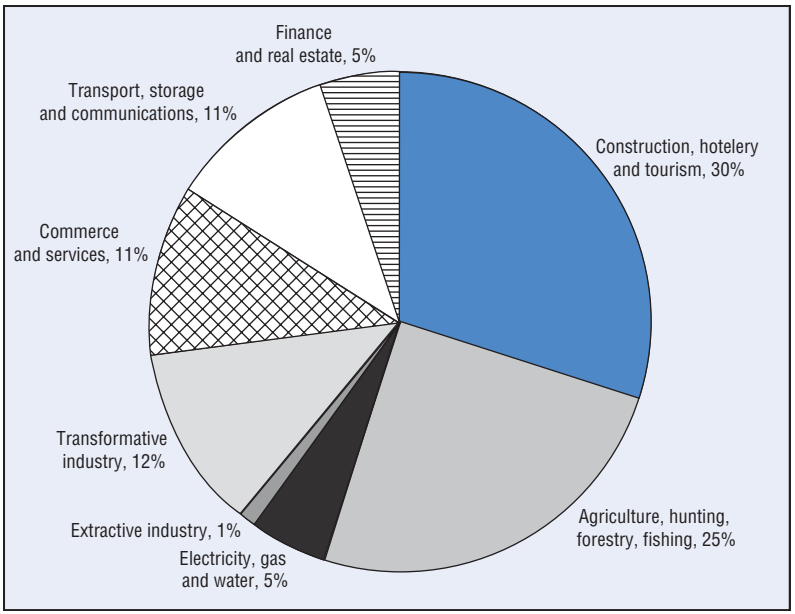
Figure 1.2. **GDP per capita in Mozambique (current USD at PPP), 1991-2012**



1. 2012 figures are estimated.
Source: IMF World Economic Outlook, 2013.

estate (5%). Agriculture therefore accounts for 80% of total employment in the country, and services for at least 13% (and probably much more if informal employment were also accounted for). The share of agriculture in total output has nonetheless declined since 1996, whereas services and industry have reached double-digit growth since 2003 (particularly the gas, electricity and construction sectors).[1] Meanwhile, although the mining sector (particularly aluminium) contributes to the vast majority of export revenues and also concentrates most of FDI flows (see following sections), it provides a very small share of GDP (only 1% over 2010-12). This contrast suggests that, unlike for agriculture and services, revenues from the mining industry are insufficiently spread throughout the economy and therefore do not substantially contribute to GDP growth.

Figure 1.3. **Mozambique GDP composition, 2012 (Quarter 1)**



Source: Bank of Mozambique, July 2012.

Poverty reduction and the role of "mega-projects"

In spite of encouraging growth rates in recent years, poverty remains a central challenge in Mozambique. While the poverty rate declined from 69.4% of the population in 1997 to 55% in 2010, recent survey data shows that poverty alleviation is stagnating and that regional disparities remain serious. Most Millennium Development Goals are unlikely to be achieved by 2015, and

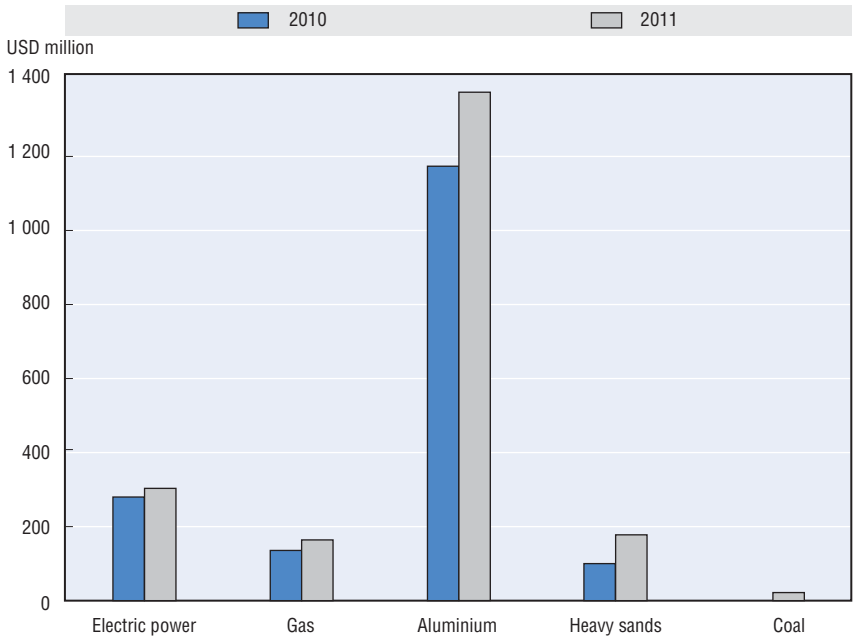
demonstrations and riots have emerged in 2008 and 2010 as a reaction to rising food prices. This has pushed the government to reconsider its diversification strategy from the angle of poverty reduction: the 2011-14 **Action Plan for the Reduction of Absolute Poverty** (PARPA II) evokes a growth model based on further developing extractive industries in the interest of creating more domestic employment opportunities. Mining projects are for example generating investment in the transport sector and in ICT, which continues to be the second-largest source of economic growth after agriculture.[2] PARPA II also emphasises the importance of diversifying investment partners (notably towards Brazil, China and India).

Government's "new growth model" thus explicitly places focus on further diversification *within* the extractive industries as a means of reducing poverty and generating employment – that is, creating more linkages between extractive mega-projects and the rest of the economy, thereby using mega-projects as a stimulus for growth in multiple other economic sectors. In this context the government is pushing for further momentum in creating **Special Economic Zones (SEZs)** and **Industrial Free Zones (IFZs)** in the extractive industries – especially for aluminium, but also increasingly for the extraction of gas, coal, and some oil. Close to half of the provisions in the 2009 Regulations of the Investment Law are indeed dedicated to licensing procedures and provisions for the establishment of these various economic zones. These zones (first created around the Mozal Aluminium Smelter, and more recently extended to the Nacala are) were intended to develop linkages between multinational and domestic enterprises.

Export composition and trade balance

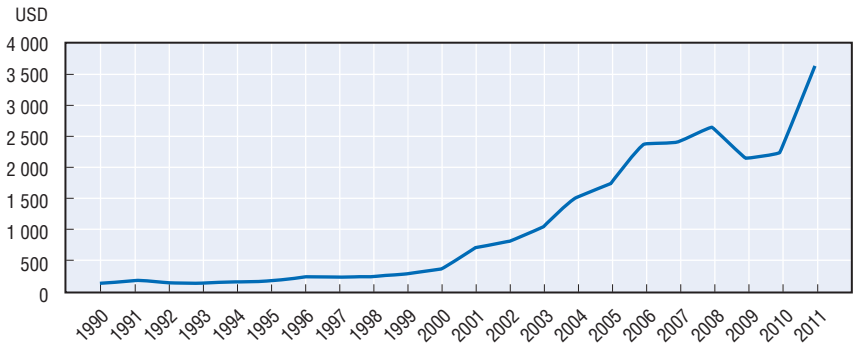
In 2011, 72.6% of Mozambique's **exports originated from mega-projects, especially in the aluminium industry** (but with a strong growth in exports of electric power, coal and heavy sands as well – Figure 1.4).[3] The remaining 27.4% of exports are centred in the agricultural sector, with tobacco and sugar as the leading industries (7% and 4% respectively). Close to 50% of export revenues are thus concentrated in aluminium, a commodity subject to wide price fluctuations. This strongly increases the vulnerability of the Mozambican economy to external shocks. Mozambican exports suffered from a reduction in aluminium demand and price in 2009 (when aluminium prices contracted by 14.9% – this dip is visible in Figure 1.5 below), following which recovery on the minerals markets has generated a 48.9% increase in aluminium exports over 2009-11.[4] Over 2007-11 the country's main export markets have been the EU (especially the Netherlands, with 52% of total exports), South Africa (18%), other SADC countries (6%), and China (2%).

Figure 1.4. **Composition of exports by mega-projects, 2011**



Source: Bank of Mozambique, June 2012.

Figure 1.5. **Export of goods and services, 1990-2011**

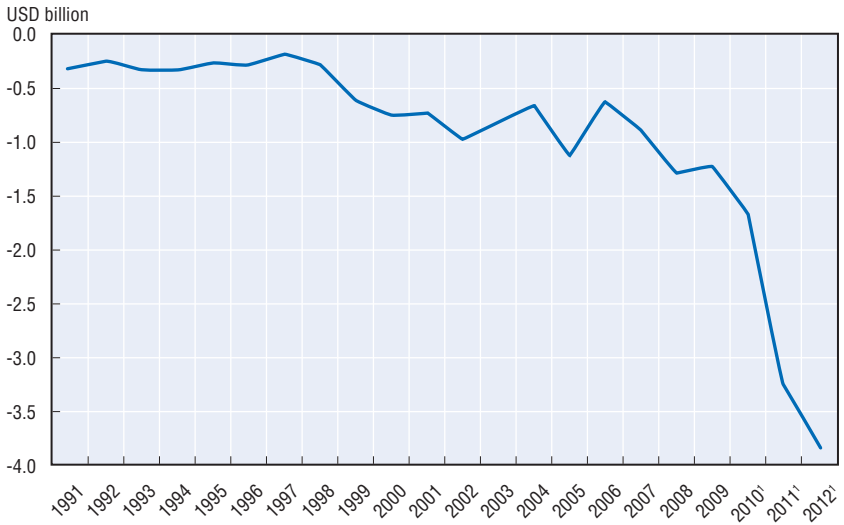


Source: UNCTAD Stat, 2012.

Such variability in export revenues may threaten the stability of Mozambique's **current account balance** (which has been in steep decline, especially since 2007 – Figure 1.6), especially since the Mozambican currency is structurally fragile and therefore relies on safeguard mechanisms put in

place by the government. The Bank of Mozambique attributes the particularly strong decline of the current account in 2011 to an increase in imports of machinery and construction services for expanding or recently-launched mega-projects, especially in Tete and Cabo Delgado provinces.[5] In addition gross fixed capital formation (GfCF, considered below) could likely benefit from more predictable export and growth trends.

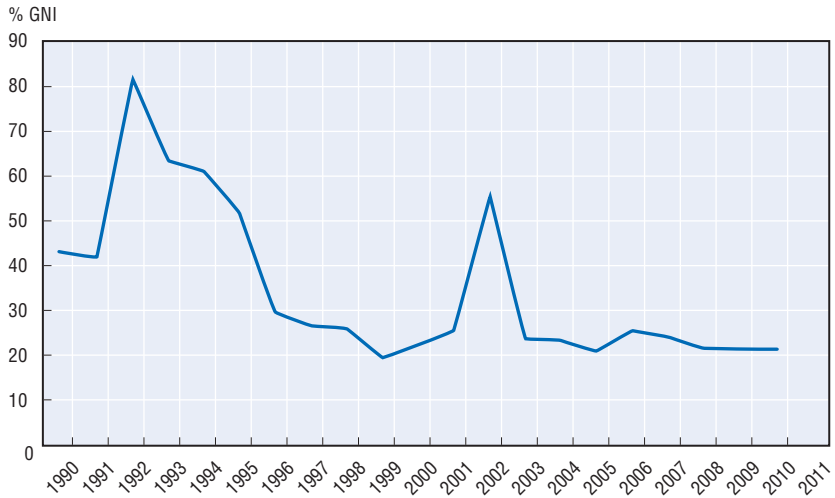
Figure 1.6. **Current account balance (BoP), 1990-2012**



1. 2010-12 figures are estimated.
Source: IMF World Economic Outlook, 2013.

Further compounding this fragility, Mozambique's national budget remains excessively **dependent on external aid**. Substantial progress has been made recently, ODA's contribution to the State Budget having been reduced from 56% in 2008 to 40% in 2012, with 31% projected in 2014.[6] Likewise, while ODA flows made up as much as 81% of gross national income (GNI) in 1992, it has averaged 22% over 2005-10 (Figure 1.7). Mozambique is currently working on a medium-term debt strategy (MTDS) that should be conducive for further improvements. Nonetheless this high reliance on aid for national expenditures and thus public investment places important caveats on the country's strong average growth rate since 2002.

Figure 1.7. **Net ODA received, % of gross national income, 1990-2010**



Source: World DataBank, 2012.

1.3. Investment policy context

Over the past two decades (and particularly since 2005 and the advent of the Guebuza administration), Mozambique's **economic framework** has undergone significant changes in the basic commercial code, labour law, fiscal regime of the mining sector, public procurement, tax code, public financial management, foreign exchange, public-private partnerships, commerce, intellectual property rights, as well as in the establishment of institutions to implement policy objectives.

Progress has been made in terms of **foreign ownership rights**, for instance by removing restrictions of the 1990 Constitution and simplifying the conditions for foreign investment. Overall, the investment framework in Mozambique is today governed by two pieces of legislation: the Investment Law 3/1993, and its updated Regulations, the Decree 43/2009. This framework does not however cover investments in petroleum, natural gas and mining, which are governed by separate legislation. The objective of the **Investment Law**, when it was promulgated in 1993, was to be in line with the Economic Recovery Plan and the then new Constitution. It reflected the will of the government to conduct open economic policy without distinctions based on investors' origin, and to provide all investors with equal rights and obligations. Among others, the Investment Law offers protection guarantees and includes provisions on the resolution of disputes. Although neither national nor foreign investors are obliged to comply with the Investment Law, only investors that follow the Law's provisions will have access to "investment licenses" from the

CPI. In turn, while this license is not mandatory for business operations, the benefits and provisions of the Investment Law apply only to those investors who hold it.

Decree 43/2009, meanwhile, is an update of earlier Regulations (Decree 14/93) that were related to the Investment Law. It abrogates all the provisions of Decree 14/93, except for Article 4 pertaining to the creation of the Mozambique Investment Promotion Centre (CPI). Among others, the new Decree defines the regulatory framework for investment and establishment in SEZs and IFZs, as well as several other types of special economic zones. Such zones nevertheless existed before enactment of the 2009 Regulations: in 1999 Mozambique set up its first **Industrial Free Zone Council**, which approved the Mozal aluminium smelter free enterprise zone (followed by Mozal II in 2001). On the policymaking front, the **Investment Council** (*Conselho de Investimento*) was created by Decree 44/2009 as the government body at the ministerial level responsible for designing policies to promote and attract investments, and for submitting these to the Council of Ministers.

As for **investment promotion**, the CPI took over operations as the national investment promotion agency in 1992 (replacing the earlier Office for Promotion of Foreign Investment). CPI, together with the Office for Accelerated Economic Development Zones (GAZEDA), has been put in charge of implementing the 2008-12 "Strategy for improving the business environment". This Strategy follows in the steps of the 2008 Decree on Simplified Licensing, and shares the latter's objective of simplifying and improving doing business. In 2009 the Code of Fiscal Benefits additionally harmonised investment incentives (accessible to international investments with a value of at least USD 100 000), although some specific sectors continue to operate under separate benefit laws. Most recently, in the course of 2013 CPI is elaborating a **national investment promotion strategy** together with other sector-specific investment promotion agencies (including CEPAGRI for agriculture and INATUR for tourism).

Mozambique's parastatals have also been progressively privatized, though the process remains slow and carefully controlled.[7] By May 2011 more than 1 200 state-owned enterprises (mostly small) had been privatized, and preparations for partial privatization and/or sector liberalization were underway for the remaining parastatals, including in telecommunications, electricity, ports, and the railroads. More efforts remain necessary to accelerate this process, and also to improve the efficiency of industries that remain state-owned. As part of the country's new growth strategy the government is additionally promoting Public Private Partnerships, especially in transport via development corridors.[8] Mozambique promulgated a new PPP law in May 2011 (the Law on PPPs, Large-Scale Projects and Business Concessions), and the associated Regulations were published in July 2012.

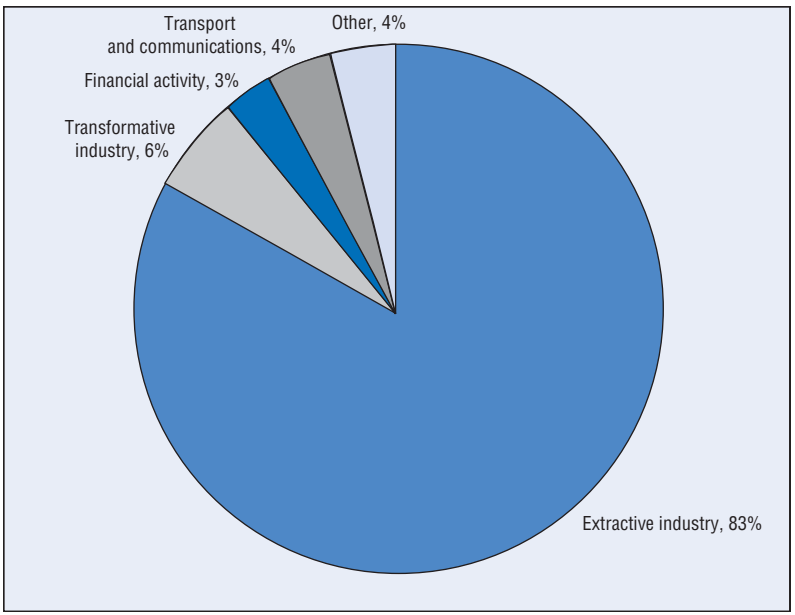
government is also considering developing a separate law for small-scale and municipal PPPs, and a new procurement law has also come into force. One of the stated objectives of the latter is to ensure that large investment projects multiply linkages with the local economy, thus better contributing to wealth and employment creation.[9]

The past decades of reforms have therefore positively re-oriented the trajectory of economic growth and development in Mozambique; nonetheless **policy implementation** is often weak, as several arms of the government remain committed to a regulated economy or lack the requisite technical capacity. There can therefore be a gap between promulgation of policy and its comprehension and enforcement – by individuals and corporate citizens, as well as by government staff overseeing policy implementation. Similar shortfalls are also noted by UNCTAD in its review of Mozambique's investment framework, which remarks that, "regulatory approaches akin to a planned economy continue to transpire in the investment framework, which leans towards giving a relatively heavy-handed and intrusive role to the regulator".[10] This gap between investment policy intent and practice is reflected in the annual results of the World Bank's *Doing Business Reports*. The overall standing of Mozambique dropped by seven places in 2012 compared to the previous year (to 139 out of 183 countries surveyed); meanwhile although Mozambique had improved by four places overall in 2011, improvements were concentrated in only one of nine surveyed areas: "starting a business" (Table 2.1, Chapter 2). Given this uneven progress, the government's aim of having the best Doing Business ranking in SADC by 2015 (as was announced with donors and other development partners in 2007, and which would imply a ranking in the twenties) remains far out of reach.

1.4. Investment trends

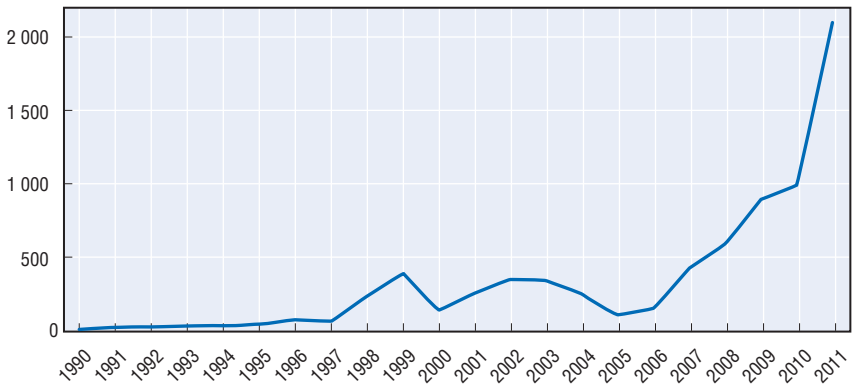
Foreign direct investment (FDI) inflows to Mozambique increased only very gradually in the five years following the 1992 peace agreement. However in the early 2000's two mega-projects – the Mozal project for aluminium, and the Sasol project in the gas sector – created a landmark change in these trends and catalyzed subsequent FDI inflows. These inflows have been mostly **export-oriented and concentrated in mining** (aluminium and increasingly coal, driven by the mines in Tete Province), and in oil and gas. In 2011 extractive industries thus accounted for 83.3% of total FDI inflows (Figure 1.8). Construction and manufacturing also attract a substantial share of FDI, but remain heavily dependent on the extractive sectors: over 90% of activity in manufacturing results from inflows linked to the Mozal aluminium smelter. Rising aluminium prices therefore largely explain the considerable expansion in FDI since 2009, and the opening of multiple new coal and aluminium mining concessions triggered a doubling of FDI inflows over 2011 (Figure 1.9). In

Figure 1.8. **Sectoral composition of FDI, 2011**



Source: Bank of Mozambique, June 2012.

Figure 1.9. **Net FDI inflows in Mozambique, 1990-2011**



Source: World DataBank and UNCTAD Stat, 2012.

2011 most of this FDI originated from Brazil (43%), Mauritius (22%), South Africa (6%, including investments in agriculture and agro-industry), and the EU.[11]

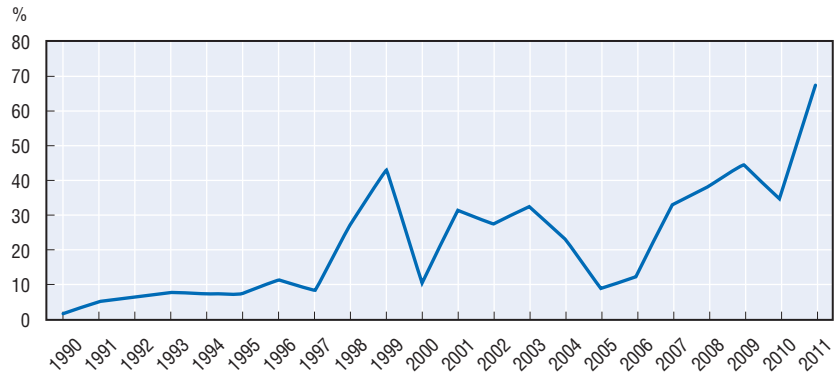
Meanwhile **agriculture**, despite being the primary contributor to GDP composition and employment creation, absorbs only 10% of private

investment (of which 90% is geared to export-oriented crops, including tobacco, cotton, cashews, prawns, sugar, and timber). Although Mozambique has large amounts of unexploited arable land, expansion and value-addition in small-scale agriculture remain hindered by inadequate infrastructure, commercial networks, and financing. Coherent export development initiatives have been scarce in the agricultural sector, and fuel and mineral exports have therefore experienced much faster growth compared to agricultural exports over the past two decades. As a result, and because most food production remains at the subsistence level, Mozambique has long depended on imports for food, oil and basic manufactured goods. Its main imports are thus: manufactured goods (55% of imports in 2009, including vehicles, textiles, and especially machinery and equipment for use as mega-project inputs); foodstuffs and other agricultural products (16.62%); and fuel and mining products (close to 16%, these being mostly production inputs such as chemicals and metal). In 2011 mega-projects accounted for 36.9% of total imported goods.[12] These imports are mainly supplied by South Africa and the EU, particularly the Netherlands and Portugal. Mozambique has nonetheless been attempting to reduce this reliance especially in recent years, via steady increases in local production and export diversification in agriculture and manufacturing.[13]

More recently **FDI has therefore been rising in agriculture**, where some mega-projects are also underway – especially in vegetable oils and bio-fuel processing. Over the past five years FDI in non-mega projects (mainly in agriculture, industry and tourism) has in fact doubled, reaching almost 45% of FDI inflows. A central objective of the PARPA for 2011-14 is to increase productivity in the agricultural sector, and government has developed an Agricultural Development Plan (PEDSA, which is rooted in the country's 2008-12 Green Revolution Strategy)[14] as well as a Strategic Biofuel Policy (currently in its 2009-15 pilot phase). In its review of Mozambique's investment framework, UNCTAD thus describes FDI outside of mega-projects as an "underestimated factor" in the country.[15] This encouraging trend would deserve more active recognition in Mozambique's overall investment promotion and poverty reduction strategies.

Nonetheless for a country of 22 million inhabitants, these total FDI inflows remain modest, and the challenge of stimulating more foreign and domestic investment in the country – across all economic sectors – still looms large. In addition, the **contribution of FDI to growth** in general, and to **gross fixed capital formation** in particular, has been very variable. Over the past decade FDI has ranged from as low as 2% of GDP (USD 113 million) in 2004 to up to 70.2% (USD 5 699 million) three years later. Meanwhile the contribution of FDI to GfCF has increased from a very low base (less than 5% in 1990 and barely 10% by 1997) to much higher levels in recent years (peaking at 67% in 2011). While these ratios compare favourably against international standards, they remain very volatile, with a steep drop in 2005 (Figure 1.10).

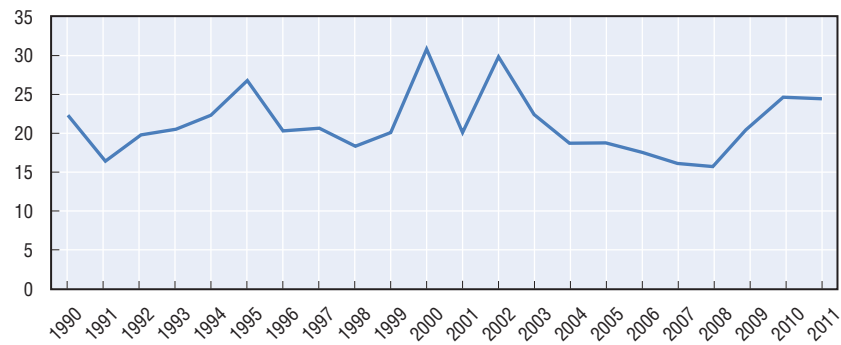
Figure 1.10. **FDI inflows as a percentage of gross fixed capital formation, 1990-2011**



Source: World DataBank and UNCTAD Stat, 2012.

Likewise the ratio of **GfCF as a percentage of GDP** has strongly fluctuated over 1990-2011, without a consistent increase (varying between 15 and 25%, with the exception of peaks at 30% in 2000 and 2002 – Figure 1.11). These variations are in part a reflection of heavy FDI concentration in mining, and highlight the risks of relying too heavily on resource-based investment and production for foreign exchange revenues, fiscal sustainability and growth. The GfCF/GDP ratio remains close to the standard for African countries (about 21-22%) and for industrialised countries (where marginal returns to additional capital are in any case low, due to large volumes of pre-existing capital stock – about 23-25%). This ratio however falls far short of fast-growing countries in East Asia, which have reached rates as high as 40%. Such variability in GfCF limits the role of FDI as a potential source of capital accumulation, and can seriously constrain room for progress in terms of economic competitiveness and investment-driven innovation.

Figure 1.11. **GFCF as a per cent of GDP, 1990-2011**



Source: World DataBank, 2012.

1.5. Central policy challenges

The strategy of poverty-reduction via mega-projects has met with little success

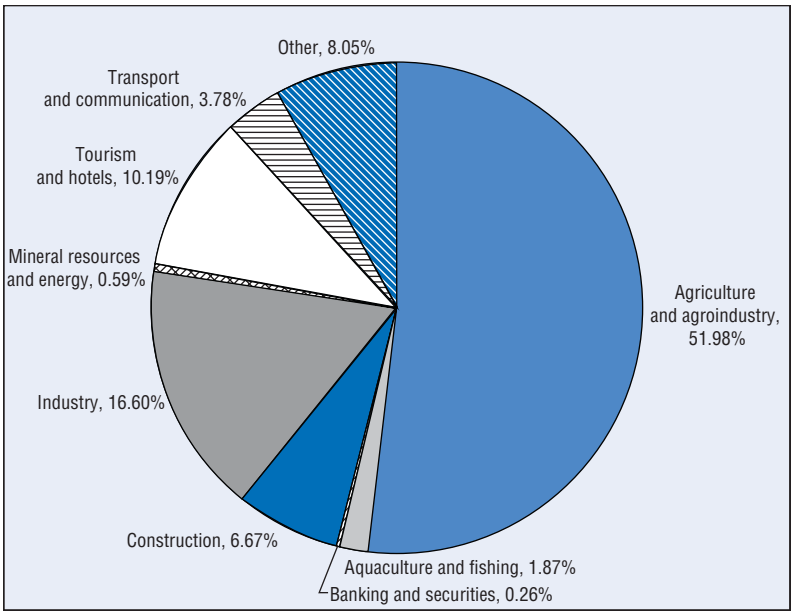
The **long-term effects of the "mega-project" approach** to poverty reduction have not been clearly demonstrated so far: although large-scale projects in mining, oil and gas have certainly triggered investments in terms of energy generation and transport, the ultimate impact on employment and social development has been limited. The CPI reports that while mega-projects accounted for 72% of total capital investment over 1992-2010, they only generated 5% of total expected employment.[16] As noted by UNCTAD, it is instead "FDI *outside* of mega-projects" that has so far "provided the type of developmental impact that Mozambique needs the most":[17] the CPI forecasts that recently registered mega-projects will generate only 1.7 jobs per USD 1 million invested, compared to 77 jobs for other registered projects.

Several **economic sectors outside of mining** (such as agriculture, tourism, construction and manufacturing) might therefore provide higher payoffs in terms of employment and local linkages. As Figure 1.12 indicates, agriculture, industry and tourism are among the sectors with a better track record in terms of value-addition and local employment generation (although these benefits are not necessarily automatic, as cautioned in Section 3.7 below). This strongly suggests that diversifying simply *within* the extractive sector (and therefore relying on this sector as the main stimulus for growth in other areas of the economy) might not allow Mozambique to fully reach its development and poverty alleviation objectives.

Insufficient investment policy safeguards

Laws and regulations dealing with investments and investors play an important role in providing for a predictable and transparent regime. In Mozambique however, the **legal framework for investment** is difficult for investors to decipher: the Investment Law of 1993 is still active but its Regulations have been replaced by the Regulations of 2009, and meanwhile several different economic sectors (including mining and petroleum) are subject to separate legislation. Moreover although several sectors of the Mozambican economy are barred to foreign participation or have limits on the size of foreign investment share-holding, there is no clear negative list of these sectors and such restrictions are dispersed in different legal documents. Likewise investor protection safeguards (including on intellectual property rights, access to land, protection from expropriation and the resolution of disputes) exist but could be strengthened and clarified so as to enhance investors' overall protection. These safeguards are not grouped within the same legal text; nor are such laws automatically provided in their English

Figure 1.12. **CPI-approved FDI in terms of number of staff employed (outside of mega-projects), 1992-2010**



Source: CPI and UNCTAD, 2011.

translations on ministerial websites. The result is an investment policy framework that is insufficiently legible for investors, particularly foreign, thereby reducing investor confidence in the country. Finally, in practice the use of investment licenses as the pre-condition for accessing all benefits and guarantees provided in the Investment Law engenders discrimination between small and large investors. In investor protection as in several other domains, SMEs continue to operate on a "tilted playing field" *vis-à-vis* larger enterprises.

An **efficient judiciary** is another essential component of credible investment policy safeguards. Mozambique's judiciary has been reorganised in 2007. Alternative dispute resolution is legally recognised and most cases of commercial disputes can be submitted to the Law on Arbitration, Conciliation and Mediation. However, the judicial system is still relatively weak and specialised commercial courts have not yet fully entered into force, while judges lack adequate skills. Besides, the bankruptcy process is outdated and urgently needs to be reformed. Revision of a new Bankruptcy Law has been underway for several years to date.

Prohibitive procedures for access to land

Processes for registration of land continue to pose an especially complex barrier for investors in Mozambique; recently they have also generated discussions at the local community level. Although the Land Law provides a good balance between the protection of investors and local rights, its implementation remains particularly difficult: **procedures to access land** are often poorly understood; securing the necessary investment approvals and land-use rights (DUATs) requires undertaking multiple procedures which are not streamlined within a common institution or agency (see Figures 2.1 and 2.2 in the following chapter); and procedures for community consultation and compensation (required before a DUAT can be issued) are frequently protracted and costly. Moreover payment for compensation is required before the investment and its associated revenue flows can begin, making it financially unfeasible for many investors. In addition land tenure is insufficiently secure even once the final ("definitive") DUAT is obtained, as it can be revoked – and the associated land plot reclaimed by the State – at any point if the investor is deemed not to abide by the agreed land exploitation plan.

Aside from the complex DUAT process, the **land registry and cadastre** in Mozambique remain to be considerably clarified – although the integrated e-Land Registry and Land Management Information System (LMIS) were launched in 2004 in view of digitalising national cadastre services and thereby supporting the management of Mozambican land, these necessary projects have since been hampered by insufficiently skilled human resources, unavailability of adequate infrastructure, and illiteracy on the user end.

Weak communication between public sector and investors

Persistent weaknesses in the legal and regulatory framework for investment remain in Mozambique, creating barriers for both domestic and foreign investment. In fact some recent legal reforms (such as the new Foreign Exchange Law, discussed in Section 2.6 of Chapter 2) have increased restrictiveness for certain investments, despite promoting liberalisation overall. Many of these gaps and contradictions are the symptoms of **poorly-managed communication** between public and private sectors, whereby inputs and active buy-in from the investor community on policy content and design are insufficiently sought after. As a result, important elements of the investment climate in Mozambique may not be realistically taken into consideration by the regulators, due in part to **weak feedback mechanisms** and mutual misunderstanding between public officials and private sector representatives. While the Mozambican government must be commended for developing new policies, this insufficiently inclusive approach to policy development can lead to shortfalls in the relevance and performance of investment climate reforms.

Fiscal sustainability and desirability of investment incentives

There are ongoing discussions in Mozambique as to whether **fiscal incentives** used to attract foreign and domestic investment into large extractive-industry projects are well-designed, and avoid imposing unnecessary fiscal costs on the country (see Chapter 3). Mozambique's extractive industries have long remained largely exempt from taxation (especially at the exploration phase); nevertheless some modifications to mining and oil tax incentives have been introduced in 2009, and a new Mining Law (to be approved in the course of 2013) may introduce some taxes for investors entering the mineral production phase. In addition although Mozambique's **IFZs and SEZs** focus on attracting investment through favourable tax structures, the latter have generated few benefits for the local economy in return – often because small-scale domestic entrepreneurs lack the skills and capacity required to mobilise the potential of domestic linkages and business opportunities associated with the zones. Robust frameworks for encouraging value-addition may therefore be needed alongside, together with supply-side structural policies. So far, formal assessment of the results achieved by both fiscal investment incentives and economic zones has been minimal, and remains highly necessary.

Coherence and monitoring of investment policy

While the government has a business environment improvement strategy, there seems to be a lack of commonly agreed vision for the role of investment, both domestic and foreign, in the overall growth and development objectives of the country. Mozambique needs a clear national development strategy into which investment objectives can be embedded – one that has more vision and scope than just meeting the objectives of the country's poverty reduction strategies (the PARPA series), or the PES. Developing this wider vision would help the country ensure that improvements in the overall investment framework are most efficiently leveraged towards Mozambique's long-term development, including poverty reduction.

In this context the national investment promotion strategy (which CPI is elaborating together with other investment promotion agencies in the course of 2013) presents a good opportunity to accurately **reflect sectoral policies** and strategic investment objectives. Addressing and effectively communicating **a commonly agreed vision for the role of investment** within this document would moreover help reduce tensions as well as negative public perceptions of investment, especially foreign. The Investment Council (*Conselho de Investimento*, created at ministerial level in 2009 for the consultation and co-ordination of policies to promote and attract investments) could play an important guiding role in this regard.

On the implementation side, investment promotion efforts are hindered by a **multiplicity of agencies** with overlapping roles and unclear chains of authority (such as the CPI, CEPAGRI, INATUR, IPEX and GAZEDA). A multitude of investment promotion activities is not unusual, but governments with a track record of successful promotion have managed to establish clear co-ordination with one agency overseeing national and regional measures and efforts. Sector-specific agencies should therefore more clearly define their roles *vis-à-vis* CPI, and develop stronger private sector representation and sufficient political support. In order for these agencies to bring relevant inputs to the current momentum for enhanced trade and investment policy implementation, they will moreover need to be staffed and capacitated accordingly – including with the data management skills necessary for undertaking **regular monitoring** of investment policy effectiveness, which can help shore up investor confidence and identify areas most in need of reform.

Insufficient export diversification

While between 1994 and 2006 Mozambique effectively introduced 18 new manufacturing and agricultural products to its export basket,[18] more steps need to be taken towards **export diversification**. Indeed, investment promotion efforts need better co-ordination with harmonised strategies for growth and export promotion in non-mining industries. Beyond expansion into extractive industries, the government's diversification strategy must consider the need for strengthening the agricultural sector – especially given its importance for food security and employment. More attention to the tourism, manufacturing, services and construction sectors, which are also labour-intensive and have scope for value-addition, would likewise be beneficial. Given the volatility of aluminium export revenues mentioned earlier, increasing investment across these sectors would also help stabilize Mozambique's current account.

The government has clearly begun to take these priorities on board. While Mozambique has to date lacked a clear **export promotion strategy**, the national export promotion agency (IPEX) has been elaborating such a strategy over the course of 2012 and early 2013. This forthcoming document, developed with support from the International Trade Centre and currently awaiting government approbation, will aim to encourage entrepreneurs in export industries to add more value to their investments, and to facilitate the shift from traditional commodity exports to a number of identified non-traditional sectors.

Development of such export industries will crucially depend on a dense network of enabling infrastructure and structural policies, which however remain sub-optimal (see below). In addition it will be important to ensure the alignment between this export promotion strategy and the forthcoming

investment promotion strategy (mentioned above); mechanisms should be put in place to co-ordinate the work of each strategy's respective implementing agencies.

Weakly articulated infrastructure strategy

Infrastructure provides **investment opportunities** in Mozambique, especially as the country's favourable geographic location can enable it to serve as an important channel for cross-border trade and investments in neighbouring countries. Electricity sales to South Africa are a significant revenue source for the government, while transport systems like the North-South Corridor have knock-on effects on the domestic economy. However the focus on these regional infrastructure arrangements risks coming at the expense of local infrastructure provision – by themselves they will not be enough to address the dearth of local infrastructure and low access rates among the Mozambican population. Weak performance across infrastructure sectors continues to discourage large-scale domestic and foreign investment, and hampers local SME growth. Together with unskilled human capital and inadequate financing, the high cost of energy and transport infrastructure in Mozambique partly explains why SME competitiveness remains low compared to that of Mozambique's regional peers.

In addition Mozambique's infrastructure deficit is a central **bottleneck to broadening diversification** outside of the extractive industries: up to now, electricity and transport infrastructure have traditionally served the needs of mega-projects, with less regard for other industries. The stimulus role that the mega-projects have played in terms of infrastructure development is important, and should be further encouraged; nonetheless other economic sectors may suffer by contrast. Small-scale agriculture lacks the storage facilities and transport infrastructure necessary to distribute food efficiently country-wide; and the tourism industry in turn depends on high-quality air, road, and water and sanitation infrastructure for its regional and international attractiveness. As noted by the World Bank's 2009 Investment Climate Assessment (ICA) for Mozambique, only after more than 15 years of reconstruction is Mozambique's infrastructure beginning to approach the level of its regional competitors.

Insufficiently coherent strategy for development of the energy sub-sector

Although Mozambique exports electricity to South Africa, its electricity sector faces a large **transmission challenge** domestically – there is a growing gap between domestic energy demand and existing supply, which is exacerbated by the rapid expansion of the energy-intensive extractive industry sector. Mozambique's electricity consumption has dramatically shot

up since the late 1990s, coinciding with the establishment of Mozal and Mozal II (see Figure 4.2 in Chapter 4 below). The Mozal aluminium smelter alone consumes 900 megawatts, equivalent to over 70% of the total power output of the Cahora Bassa hydroelectric plant. More importantly the national approach to energy infrastructure development is insufficiently coherent, as catering to export and extractive industry needs conflicts with the supply of electricity to the domestic population: Mozal relies on energy imports from South Africa to satisfy its needs, as 80-90% of the Cahora Bassa power reaches Southern Mozambique via South African transmission lines.

1.6. Investment policy options to prioritise

The Review that follows and the recommendations that result from it outline steps through which Mozambique can not only improve its general investment climate across all economic sectors, but also render its development strategy more sustainable in terms of employment generation, value-addition and long-term industrial development. The suggested recommendations below seek to make Mozambique's business environment more inclusive, transparent, efficient, and better-aligned with the country's underlying development potential and human and natural resources.

Strengthen and clarify the legal framework for investment

Several fields of the investment framework need to be improved. They are summarised as follows:

- **National treatment:** clarifying paragraph 4.2 of the Investment Law (on Equality of Treatment), which stipulates that some activities by nationals may obtain special treatment, would considerably help establishing a non-discriminatory investment climate in Mozambique. While it is fully legitimate for the government to reserve some economic activities for domestic entrepreneurs only, transparency and predictability *vis-à-vis* foreign investors could be improved by grouping all of these sector restrictions within a regularly updated **negative list.** This would detail all activities for which special treatment is provided to Mozambican nationals, or where foreign participation is limited to specific thresholds. As an example Mozambique could for instance look to the Bilateral Investment Treaty currently under negotiation with Japan (this Treaty, which should be concluded by mid-2013, will contain a list of sectors – especially within manufacturing – for which there will be percentage restrictions for Mozambican and Japanese ownership).
- In addition, **conditions with which investors need to comply** in order to repatriate funds are numerous and complex, which also indirectly discriminates against foreign investors. These could usefully be reviewed in

the light of international best practices. Careful review of provisions of the Foreign Exchange Law may also be considered.

- **Investor protection:** the government should also envisage clarifying the measures that are considered as national interest in cases of expropriation and nationalisation, as this would increase investor protection and hence confidence. Similarly, in case of investor-State disputes, investors should have easier access to international arbitration, and not solely upon express agreement of both parties. Most BITs that Mozambique has ratified are more flexible on this aspect, and can be a source of inspiration for possible reform of the 1993 Investment Law.
- **Investment licenses:** the scope of the Investment Law should go beyond those investors that have obtained investment licenses and apply to all investors equally. Investment licenses, while they are currently not mandatory, could either be eliminated or the processes required to obtain them reviewed and simplified (particularly in view of greater inclusiveness for SMEs).
- **Clarity, transparency and disclosure:** for clarification and coherence purposes, **all relevant regulations and laws could be gathered in a single instrument** that would bring under a single umbrella document core investment protection and promotion provisions, and provide the institutional framework for investment regulation and promotion. Such a document should also include the negative list of sectors mentioned above. Such a process of clarification would be a valuable opportunity to further engage all relevant stakeholders in an effort of coordination, consultation and consensus. Alternatively, the authorities could consider the **option of drafting an Investment Code.** Such a Code could aim to strike a better balance between elements of promotion and facilitation (which are substantially incorporated in the 2009 Regulations of the Investment Law, especially as concerns special economic zones) and equally essential core principles of investor protection.

Improve access to land and judicial enforcement

Facilitating and clarifying the **legal and administrative framework for access to land** should be envisaged by the government. This includes: increasing the effectiveness of the court system; reviving and adequately maintaining the electronic land registry and cadastre (LMIS) so as to accelerate land registration processes; and reviewing and simplifying procedures for community consultation and investor access to DUATs. The latter measure would include reducing the number of agency approvals necessary for obtaining the DUAT (see Figures 2.1 and 2.2 in the following chapter), and possibly reviewing the distinction between a provisional and a definitive DUAT

(which essentially requires the lengthy approval process, with all of the agencies and costs that it involves, to be repeated on two separate occasions). Moreover **security of land tenure** would need to be considerably reinforced – in particular the definitive DUAT provides little protection from expropriation: the land right can be revoked at any time during the 50 years of DUAT validity, should the investor no longer abide to the initial land exploitation plan. A more flexible and secure approach to land tenure would enhance incentives for domestic and foreign entrepreneurs to engage in long-term land improvements, and would also increase land registration rates. The recently-established Land Consultative Forum could be a suitable venue for actively pushing such reform forward.

More broadly, an important push on **law enforcement** is needed. While this can take the form of accelerating ongoing reforms, such as the Bankruptcy Law, the government has a number of other options available to increase confidence among investors. For example, while wider efforts to increase the effectiveness of the court system (such as online arbitration to reduce time taken) need to be launched, the proper implementation and use of commercial courts – with well-trained judges – could be a useful ingredient to boost investor confidence. In addition, government could take concrete measures to improve the transparency and availability of investment-related laws (many of which are difficult to obtain and are only available in Portuguese). Article 2.6 of the Bilateral Investment Treaty (BIT) signed by Mozambique with Uganda provides an interesting provision on the obligation to **publicly disclose all investment-related laws, regulations and administrative procedures**. This provision should be a general one in Mozambique's broader investment framework to support its effective implementation.

Streamline the institutional structure for investment policymaking, as well as for investment promotion and facilitation

On the policymaking front, stronger national-level guidance in terms of a long-term investment vision and strategy is clearly needed in Mozambique, which the **Investment Council** would be well-placed to provide. However since its creation in 2009, this Council has yet to meet its full potential. A clearer structure of authority and responsibilities would need to be specified in order to facilitate and guide investment policy reform; specific reference to the Council and to its powers relative to other policymaking and implementing bodies (various ministries, but also investment promotion agencies such as GAZEDA and CPI) could be incorporated in national legislation. Although Article 4 of the 2009 Investment Regulations introduces a necessary clarification of "Competency for the coordination of investments", this therefore remains an insufficient step forward. Empowering **inter-ministerial**

committees could also accelerate policymaking and implementation, especially for elements of investment policy that cut across the domains of different ministries.

On the investment facilitation front, specialised **investment promotion agencies** like INATUR (tourism), CEPAGRI (agriculture) and IPEX (for all exports) should play a more active role in promoting private investment in their respective sectors, and their collaboration with CPI should be better co-ordinated or rationalised. This includes better informed consultative mechanisms; the **investment promotion and export promotion strategies** under elaboration over 2012-13 (respectively under CPI and IPEX leadership) present particularly good opportunities for formalising such structures. These could subsequently be put to use for the joint implementation and monitoring of associated investment and export promotion activities. Lessons learned from successful and innovative investment promotion efforts in specific sectors (such as the Mozambique Tourism Anchor Investment Programme, concluded in 2011) could notably be consolidated at the level of each specialised investment promotion agency, and then relayed to a common dialogue platform involving CPI, IPEX and the Investment Council, so as to feed in to a coherent sector-wide approach for export competitiveness and investment attractiveness.

"Target" industries and stakeholders should be actively involved in the elaboration and implementation of both of these national strategies. **Capacity shortcomings** in institutions undertaking investment promotion should also be addressed if promotion at sectoral level is to be effective and genuinely upgraded. In order for these agencies to bring relevant inputs to the current momentum for developing and implementing trade and investment strategies, they will notably need to develop stronger private sector representation and sufficient political support, and also to acquire the data management skills necessary for **regular monitoring** of investment policy effectiveness. Progress on both of these fronts would facilitate public-private dialogue on investment policy, help identify policy areas most in need of reform, and ultimately shore up investor confidence.

Establish a mechanism for regular and systematic cost-benefit analysis of investment incentives, both for tax structures and accelerated economic zones

While fiscal reforms in 2009 have been a good first step to simplifying the tax system, continued efforts need to be made in order to better share resources from mineral exploitation and to put SMEs on a more equal footing with other investors. A mechanism for **systematic cost-benefit analysis** of investment incentives would support the government in moving its tax reform agenda forward by highlighting the resources that are lost to

ineffective fiscal exemptions, and would reduce the transaction costs faced by the tax administration and associated with managing multiple derogatory systems. The relevance and appropriateness of incentive strategies should be examined at regular intervals, possibly by the authorities responsible for delivering these incentives, which could then report to the Ministry of Finance. Such evaluations should measure the economic benefits of investment incentives against their budgetary and other long-term costs. These assessments (both *ex ante* and *ex post*) should involve open public consultation so as to accurately include social – and not only financial – costs and benefits in the analysis.

This assessment of incentives would notably allow an in-depth evaluation of the operations and achievements of **SEZs and IFZs**, in view of improving or restructuring them to enhance their potential in terms of value-addition and generating local economies of agglomeration. Government should also consider the **alternatives to investment incentives** – that is, whether forgone fiscal revenues sacrificed for incentives may better be used for enhancing structural policies (geared at education, infrastructure and so forth – for instance through the Technical and Vocational Education and Training system) that could increase investment attractiveness.

Support effective implementation of a comprehensive export promotion strategy

The export promotion strategy currently under finalisation by IPEX will be an important step towards facilitating the growth of non-traditional export sectors. The strategy should notably give due attention to undervalued economic sectors that have high employment potential – such as niche markets within agriculture, tourism, construction and manufacturing. It should also propose targeted measures for allowing SMEs to tap into these export markets, including by suggesting measures for building investment and trade linkages, and by providing clear export guidance for domestic firms. Such a strategy and its alignment with investment policy, the private sector development strategy, and overall national development goals would allow Mozambique to **capitalise on its sectoral advantages** and better achieve its diversification and job creation objectives.

It is essential that the authorities responsible for elaborating this strategy operate in **close collaboration with bodies responsible for investment policy design**, given the very strong links between investment and trade. Given that Mozambique is concurrently elaborating a national investment promotion strategy (through CPI), it may be desirable to establish a common task-force for the joint finalisation of both strategies. This taskforce could co-ordinate inputs from the private sector as well as from other relevant government bodies (such as those responsible for human resource development and for

the country's infrastructure master-plans). Equally importantly, it could set the groundwork for co-ordinating and monitoring the implementation of both strategies once they are being operationalised.

Balance domestic and strategic needs in infrastructure (and especially energy) development

While maximizing the potential of infrastructure as an enabler of growth, Mozambique will need to balance its regional and large-scale consumer needs with those of other domestic infrastructure users. With this objective in mind, Mozambique could formulate a long-term strategy for energy development to succeed the Energy Sector Strategic Plan 2010-14 that focuses on extending access to infrastructure services. The government should especially exploit the opportunities presented by mega-projects by providing incentives for mining companies to extend the infrastructure systems they will build to cover areas not immediately related to their mining activities. More broadly, **infrastructure investments by mining companies** (which are set to expand yet further with Mozambique's growing coal boom) should be **carefully co-ordinated by government so that they contribute to a coherent national framework**. Rather than being undertaken by individual companies in isolation and each according to its own needs, infrastructure projects would thus build on joint economies of scale, while simultaneously addressing the population's requirements and tackling gaps in the national network. Road and rail transport, as well as energy provision, are infrastructure sub-sectors where this co-ordinated approach would be particularly beneficial.

Also in view of greater end-user accessibility, a **decentralised strategy** for power provision would be well-suited to Mozambique's dispersed population. Mozambique has already made use of decentralised solutions and community-based operations to expand service provision in water and telephone services (especially for rural areas), and this approach can be scaled up as well as applied in the power sector. **Community-managed projects** are promising, as the examples of self-generation from natural gas in a number of towns in Inhambane illustrate. With government support and private sector involvement, community initiatives can be scaled up and help fill the capacity gap at national level. The government can make use of management contracts with private companies for water service provision or for small-scale power projects, especially in clean energy, so that they can perform the functions normally carried out by utilities in urban areas. In the energy and water sectors, private sector-led off-grid solutions to developing energy infrastructure could be promoted.

Encourage the growth of the renewable energy sector

The government should expand the scope of its energy projects to include wind, solar and biomass generation in addition to hydropower. **Policies to promote renewable energy** in Mozambique, such as the Biofuels Strategy, should be harmonized with rural development and environmental policies to maximise their impact. Feed-in tariffs for wind, solar, biomass and hydropower generation can also help draw in private investment, if these are sustainable for the government and if adequate phasing out strategies are provided for. The government can also consider lifting duties on the import of "green goods" such as solar panels to encourage renewable energy generation. Attention must nonetheless be taken that new hydropower projects do not cause undue damage to the environment, especially with dam construction. Public consultation, resettlement and compensation schemes will need to be considered. Finally the government may want to consider giving preference or a **greater allocation to domestic users** instead of neighbouring countries for conventional and renewable energy projects currently in the pipeline.

Strengthen the framework for private participation in infrastructure

Mozambique needs to strengthen the **regulatory framework for procurement and PPPs** in infrastructure. The 2012 Regulations for the Law on PPPs, Large-Scale Projects (LSP) and Business Concessions (BC) and the establishment of a PPP Unit are good steps in this regard. Moreover should government move forward in its consideration of a law for small-scale and municipal PPPs (which could unlock important investment opportunities for decentralised infrastructure provision, as mentioned above), this should be done in careful consideration of the project management and financial capacities of local governments. A simpler arrangement for PPP oversight, instead of the current four-agency approach, should also be considered to reduce bureaucracy. Relevant **sectoral regulators** should moreover be better empowered not only for the accurate pricing of infrastructure services, but also in terms of monitoring project implementation – so as to avoid missed performance targets and contractual conflicts. For example, although in 2006 the government put in place a strategy to transform the National Electricity Council (CNELEC) from an advisory body into a fully independent regulator with final decision-making authority, this unfortunately still remains a work in progress.

Increase competition in the power sector

As the government plans to implement its priority energy projects, it should create a level playing field for all actors to compete, notably through revising special privileges enjoyed by **state-owned enterprises** across

infrastructure sub-sectors. Mozambique's Competition Authority (which was set up in 2012) will also have a role to play in this regard. In the power sector, a first step might be to create more space for independent power provision (IPP) by establishing standard Power Purchasing Agreements (PPAs) between the monopoly "single buyer" (EDM) and private electricity providers. A framework could for instance be put in place to encourage IPPs to secure electricity generation licences, while standard off-taker agreements would provide greater assurance that tariffs will be stable or that IPPs will receive a minimum return on their sales. This would enhance the predictability and attractiveness of the electricity market for private actors, as opposed to the current approach whereby generation contracts are negotiated on a case-by-case basis.

At a later stage, government could also consider further **unbundling the sector** and allowing for private investment outside of the generation segment alone (that is, moving beyond the "single-buyer" model and introducing competition in electricity transmission and distribution as well). In this view, corporatisation of electricity utilities, including creating business lines and performance-based incentives for staff, could help identify where profits and losses are made, and therefore which services would be left to the private sector. A similar approach could also be considered in the water sector.

Better design concessions as well as regional infrastructure contracts

Better **packaging of infrastructure projects** is necessary in order to attract private contractors and address Mozambique's significant national infrastructure investment needs. The government can consider a package model for transport concessions or electricity generation agreements, for example by inviting private contractors to develop both a main road and a secondary feeder road at the same time. During the tendering process, government should consistently provide all policy and project documents in both English and Portuguese to capture a wider spectrum of investors. The multiple procurement systems in use, especially with donors, must be rationalised to enhance transparency and efficiency in infrastructure construction and service provision. On the regional front, while it may be difficult to revise long-standing regional power purchase agreements such as with Eskom in South Africa, Mozambique can take measures to ensure that future agreements with its neighbours have **clauses for their periodic revision**.

Undertake targeted supply-side efforts for business linkage development

Efforts to enhance local industry linkages with large-scale investment have had limited success so far. In the extractive industries, these linkage efforts rely mostly on voluntary private-sector-led initiatives – while these can

have significant impacts, a system of **structured government support** would be useful for further encouraging them and extending them to more companies. Development agreements established with extractive companies could usefully consider national infrastructure development schemes. In coal mining for instance, the government could encourage mining companies to extend their infrastructure systems to include areas not immediately related to their mining activities. Targeted linkage programmes could also be extended to more labour-intensive sectors (such as agriculture or tourism) where employment creation and value-addition can be much higher.

Systematically gather investor feedback in view of monitoring the impact of investment policy measures

The content, organisation, leadership and delivery of the business environment improvement strategy should be assessed objectively against the needs of investors and consumers in Mozambique. Establishing systematic feedback mechanisms with investors and the public would result in better-targeted and stronger policies. Through widespread consultation in both public and private sectors, the Investment Council could help better embed investment objectives within Mozambique's national development strategy, and prepare corresponding **output and outcome indicators** together with time-bound steps for implementation of reform. Structuring more constructive and regular communication with the umbrella private sector group, the Confederation of Business Associations (CTA) would also allow greater ownership of the reforms by the first concerned (investors).

Establish an SME task force to review the practical needs of the sector

Building on policy and institutional initiatives, a **task force involving SMEs** could be set up to assess their needs across all economic sectors, with regards to national investment-related policies. This could build on or increase the capacity of the Institute for Small and Medium Enterprises (IPEME). Ministries, supported by CPI and IPEME, should shape a strategy that ensures that small investors are better-represented in inter-ministerial processes for investment policy design and implementation. Indeed greater communication and exposure of the needs of SMEs is required across fields of economic policymaking. Removal of the CPI investment license, or revision of the license threshold with a view to reducing the bias against smaller enterprises, also remains necessary to ensure that SMEs retain access to the same level of protection and benefits as do larger investors.

Sector-specific efforts may also be necessary, given that SME needs vary by industry and are more accentuated in certain sectors. The forthcoming investment and export promotion strategies could be an appropriate venue for

better integrating SME concerns – especially as regards the promotion of more labour-intensive economic sectors. This would need to go hand-in-hand with enhancing access to finance and further simplifying tax requirements for SMEs.

1.7. Addressing these challenges in the context of an OECD *Investment Policy Review*

Box 1.1. **The OECD Policy Framework for Investment**

The Policy Framework for Investment (PFI) was developed to help governments "mobilise private investment that supports steady economic growth and sustainable development, and thus contribute to the prosperity of countries and their citizens and the fight against poverty" (PFI Preamble).

Inspired by the 2002 United Nations Monterrey Consensus on Financing for Development, which ascribes to governments the responsibility for creating the right conditions for private investment to flourish, the PFI aims to support development and the fight against poverty and to promote responsible participation of all governments in the global economy.

The PFI represents the most comprehensive multilaterally-backed approach to date for improving investment conditions. It addresses some 82 questions to governments in 10 policy areas to help them design and implement good policy practices for attracting and maximizing the benefits of investment. The PFI is based on the common values of rule of law, transparency, non-discrimination, protection of property rights in tandem with other human rights, public and corporate sector integrity, and international co-operation for development.

Several countries participated in developing the PFI, including some 30 OECD and 30 non-OECD governments. Business, labour, civil society, and other international organizations, such as the World Bank, also played an active role, and regional dialogue and public consultations were organized around the world. The PFI was endorsed by OECD ministers in 2006, when they called on the OECD to continue to work with non- member governments and other inter-governmental organizations to promote its active use. Already, Morocco, Indonesia, China, India and Zambia are some of the countries that have undertaken a self-assessment of their investment framework based on the PFI. Moreover the Southern African Development Community (SADC) has decided to develop its Regional Investment Policy Framework using the OECD PFI as its reference.

Box 1.1. **The OECD Policy Framework for Investment** *(cont.)*

The subsequent chapters of this review therefore represent the government of Mozambique's self-assessment based on the OECD PFI. Based on analysis of what sectors would most benefit from reform and best stimulate the rest of the investment environment (as explored in the preceding overview), the Ministry of Planning and Development (MPD) of Mozambique decided to focus on three distinct policy areas of the PFI: investment policy; investment promotion and facilitation; and infrastructure development. They are covered by Chapters 2, 3 and 4, respectively.

Source: www.oecd.org/investment/pfitoolkit.

Notes

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16. Mozambique Investment Promotion Center.
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Chapter 2

Investment policy in Mozambique

This chapter highlights the progress made by Mozambique in improving its investment framework, notably through: the 1993 Investment Law and its related 2009 Regulations. The Land Law 1997 and subsequent processes of land allocation and registration, as well as intellectual property and the judiciary, are likewise investigated from an investment perspective. Mozambique has also initiated several recent reforms, where effectiveness and implementation will need to be carefully evaluated – while it aims for increased liberalisation, the 2009 Foreign Exchange Law for instance introduces some additional constraints on foreign investors. More broadly, although there are few sectoral restrictions on foreign investment, the Investment Law is somewhat ambiguous in its provisions on national treatment; moreover, some indirect forms of discrimination against foreign investors are contained within public procurement and labour laws. In addition, the potential role of overarching bodies for investment policy design and dialogue, such as the Investment Council and the newly-established Land Consultative Forum, is also explored. This overview of the legal framework for investment highlights certain considerable weaknesses that continue to create barriers for investment in Mozambique.

2.1. Investment policy regulation and design

What steps has the government taken to ensure that the laws and regulations dealing with investments and investors, including small and medium sized enterprises, and their implementation and enforcement are clear, transparent, readily accessible and do not impose unnecessary burdens?

Clear, transparent, accessible, predictable and non-burdensome regulations are a foundation of an attractive investment environment, and benefit both investors and society. This section explores the regulatory framework for investment in Mozambique as well as its design process. The coordination of responsibilities for investment policy implementation is also looked into, in order to clarify the institutional framework within which such policy is embedded. The extent to which the laws and regulations dealing with investment truly improve the business environment and facilitate investment – including for small and medium-sized enterprises (SMEs) – is assessed with reference to laws on investment, intellectual property, and foreign exchange transactions among others.

Mozambique bases its national investment and development strategies on two key policy documents: the Five Year Plan (PQG – *Plano Quinquenal do Governo*, which outlines general areas of intervention for the government) and the annual Economic and Social Plan (*Plano Económico e Social* or ESP, which specifies social and economic policy measures – including on investment matters). These plans exist alongside the Action Plan for the Reduction of Absolute Poverty (PARPA in Portuguese), which is elaborated in collaboration with the G19 international donor group and constitutes the basis for the release of international funds to Mozambique. Both the current Five Year Plan (adopted by Parliament in April 2010) and the 2011-14 PARPA are to be implemented within the ESP, under the ambit of the Finance and Planning and Development ministries. However, operational coordination and interaction among these three strategy documents could be enhanced, as responsibilities for implementation are still unclear.[1]

Several agencies have been established to implement and oversee investment policy reform

On the policy level, the Investment Council (*Conselho de Investimento*) created by Decree 44/2009 is the government body at the ministerial level responsible for designing policies to promote and attract investments, and for submitting these to the Council of Ministers. The Investment Council is chaired by the Minister of Planning and Development, with the Minister of

Industry and Trade and the Minister of Finance as co-Deputy Chairs. Other members of the Council include the Ministers of Public Works and Housing, Agriculture, Energy, Transport and Communications, Labour, Tourism and Environment, as well as the Governor of the Central Bank (*Banco de Moçambique*) and heads of the Investment Promotion Centre (*Centro de Promoção de Investimentos*, CPI) and of the Special Economic Zones Office (*Gabinete das Zonas Economicas de Desenvolvimento Acelerado*, GAZEDA). The main ministries involved in business environment reform therefore include those of Industry and Trade (for which business environment reform is a central ministerial objective under which its performance is monitored), Planning and Development, Finance, Labour, Justice and State Administration, as well as the Central Bank.

On the implementation level, CPI, under the Ministry of Planning and Development, has the mandate to promote and facilitate foreign and domestic investment in Mozambique. As such, its services include the reception and registration of investors, institutional assistance in the implementation of their projects, the facilitation of the concession of fiscal and customs incentives and matchmaking with potential partners. Meanwhile, GAZEDA, also under the tutelage of the Ministry of Planning and Development, has the mandate to promote and coordinate investment activities in the Special Economic Zones (SEZs) and Industrial Free Zones (IFZs). In addition, in order to strengthen support to the private sector, especially for SMEs, the Ministry of Industry and Trade also established a Business Information Centre (*Centro de Informação de Negócios*, CIN) in 2006 in Maputo, and Decree 14/2007 created one-stop-shops (*Balcão de Atendimento Único*, BAU) for business licensing and information dissemination. These BAUs now operate in all 11 provinces, as detailed in Section 3.1 of the following chapter.

Mozambique's investment framework remains governed by the 1993 Investment Law

The investment framework in Mozambique is governed by two pieces of legislation: the Investment Law 3/1993 and its updated related Regulations, the Decree 43/2009 (which replaces the earlier Regulations, Decree 14/1993). The objective of the Investment Law, when it was promulgated in 1993, was to be in line with the Economic Recovery Plan and the then new Constitution (approved and enacted at the end of 1990, but revised since then in 2004). The Constitution itself already reflects Mozambique's openness to FDI, as it states that "foreign ventures shall be permitted in all of the national territory and in all economic sectors, except those that are reserved exclusively for ownership or development by the State".

The Investment Law of 1993 reflects the will of the government to build an open economy with no distinctions based on investors' origin. It hence does not discriminate between foreign and national investors and provides them with equal rights and obligations. The Law guarantees the security and legal protection of property rights. It provides "just and equitable compensation" in cases of nationalisation or expropriation, the latter occurring only for reasons of national interest or public health and order, according to the Law. It provides guarantees on the transfer of funds abroad in connection with: exports; royalties; amortization of loans and payment of interest on loans; proceeds of any compensation in case of nationalisation or expropriation; and invested and re-exportable foreign capital. Transfers of funds abroad are however subject to a number of conditions (see Section 2.6). The Investment Law also provides provisions on the resolution of disputes and allows for international arbitration in cases of State-investor disputes.

Important is to note that neither national nor foreign investors are obliged to comply with the Investment Law – non-compliance simply forfeits access to the rights, protection and investment incentives provided within the law. Investors who wish to invest following the provisions of the Investment Law are provided with investment licenses by CPI or GAZEDA, and these licenses secure access to all benefits and provisions included in the Law. In practice, whereas most foreign companies invest through the Investment Law, national investors, in particular SMEs, tend to sidestep it. Also, the Law excludes from its scope of application investments in petroleum, natural gas and mining, the latter being the main sector in which FDI is concentrated.[2]

Decree 43/2009 is an update of the former Regulations related to the Investment Law (Decree 14/1993). While the Investment Law remains the main governing piece of investment legislation, Decree 43/2009 abrogated all the provisions of the Decree 14/1993, except for Article 4 pertaining to the creation of the CPI. Among others, the new Decree provides additional detailed information on minimum value of FDI and forms of investment, the processing of investment proposals as well as the competencies, time periods, amendment and revocation of project authorisation. The Decree 43/2009 also defines the regulatory framework for investment in SEZs and IFZs. The framework of tax and customs incentives in relation with the Investment Law is also further elaborated in the Code of Fiscal Benefits (Law 4/2009), under which these benefits are accessible to international investments with a value of at least 100 000 USD. The mining and petroleum sectors again have separate benefit laws (see Chapter 3 for more detailed analysis of investment incentives).

The newest Investment Regulations (Decree 43/2009) increase flexibility of the 1993 Investment Law

Article 7 of the Investment Law lists specific objectives for the contribution of investment projects to social and economic development:

- development or rehabilitation of infrastructure necessary to supporting essential economic activity;
- promotion of technological development and increase of efficiency and productivity in firms;
- job creation for nationals and skills transfer;
- expansion and improvement of national productive capacity, or provision of support services for production;
- export creation;
- import substitution;
- improving the country's balance of payments; and
- improving supply conditions for the local market.

Prior to 2009, investors had to meet at least seven of these objectives in order to be eligible for an investment license, and therefore for the incentives and guarantees provided by the Law. Under Decree 43/2009, which approved the Investment Law Regulations, these conditions have been eliminated. This better aligns the Law with WTO requirements under the agreement on trade-related investment measures (TRIMs), and has facilitated business access to investment licenses. In addition, the previous Regulations (Decree 14/1993) reserved several areas for the public sector – including production of electrical energy, postal services, public water supply, operation of national parks, and production, distribution and trade of arms and munitions. These sectors were thus restricted for private investment, both foreign and national. By contrast the new Regulations no longer define restricted economic sectors for private investment.

The 2009 Regulations moreover introduce a chapter on the "Coordination of investment procedures" (Chapter 2), of which Articles 4 and 5 stipulate that the Minister for Planning and Development affairs has the competency to coordinate the investment process. Meanwhile CPI and GAZEDA each have the competency to promote economic opportunities within their respective areas of operation, to assist investors during the implementation phase, as well as to monitor and verify that their investment projects comply with the applicable legislation. When requested by CPI or GAZEDA, the Ministers, Provincial Governors and other heads of State institutions are to appoint representatives to ensure the necessary inter-institutional coordination. These representatives are in turn responsible for the issuance of the advisory

opinions and authorisations that are necessary for the approval, implementation and realisation of investment projects.

Although Chapter 2 of the 2009 Regulations does not refer to all bodies relevant to the investment policy process in Mozambique, it therefore brings an important clarification of responsibilities and accountabilities with regard to the Investment Law. This is a necessary step towards making the institutional and operational structure for investment policy reform more coherent and transparent understood for investors and policymakers alike.

Recent regulatory initiatives have potential for enhancing private sector participation in the economy

Complementing the 1993 Investment Law and its 2009 Regulations, some important regulatory initiatives related to the business environment have been taken since 2005 and are progressively having a significant impact on the investment climate, as illustrated by the World Bank 2012 Doing Business indicator on starting a business, that ranks Mozambique 70th out of 183 economies, which positively contrasts with its overall rank at the 139th position. These regulatory initiatives include:

- **Commercial Code, Law 10/2005**, which entered into force in 2006 and aims to regulate the establishment of companies. The promulgation of a new commercial code was a very necessary reform, as the previous one dated from 1888, and is seen as a very positive improvement by the private sector. It has enhanced the legal environment for investment and eased the creation of new businesses. Among other effects linked to modernising corporate governance rules, it has led to the introduction of electronic business registration, eliminated the provisional registration and made notaries optional, all of which has reduced company registration time.[3]
- **Foreign Exchange Law, 11/2009** (revising Foreign Exchange Law 3/96) and its Regulation, Decree 83/2010, which regularises foreign exchange operations, makes them more bank-based, and requires conversion of foreign exchange held in Mozambique into the national currency (although the benefits of this law are debatable – see Section 2.6 below);
- **Procurement Law, 15/2010** (Regulation for Contracting Public Works, Goods and Services to the State, *Regulamento da Contratação de Empreitadada e Obras Públicas, Bens e Prestação de Serviços ao Estado*), which updated public procurement procedures (see Section 4.3 in the Infrastructure chapter below); **Complementary Law on Public Private Partnerships, Large Scale Projects and Business Concessions, Law 15/2011**, known as the PPP Law, which focuses on national participation in the benefits of large projects (see Chapter 4 on infrastructure below).

- Meanwhile on the implementation front, the **2008 Decree on Simplified Licensing and the 2008-12 Strategy for Business Enabling Environment** spearhead improvements in the business environment, and are investigated in more detail in Chapter 3 (on investment promotion and facilitation).

But investment policy improvements remain constrained by inconsistent implementation and support

While government has taken important steps to improve the business environment, the combined impact of these initiatives has nonetheless been limited. The reality is that full implementation of Mozambique's legislation would be necessary to make its business environment significantly less difficult, arbitrary and cumbersome, especially for medium and small scale investors (as further investigated in Section 3.7 below). Despite the introduction of the 2008 Decree on Simplified Licensing, the Investment Law remains overly complex for many small enterprises, which therefore opt out of the requirements that, under the Investment Law, condition access to investment licenses. This places SMEs on an uneven playing field *vis-à-vis* larger investors, as they thereby forgo the investment rights and incentives to which these licenses secure access. The licensing system also remains intricate for sectors that fall outside of the ambit of the Decree on Simplified Licensing (as detailed in Chapter 3 below – the list of sectors covered by the Decree has been expanded further in February 2012).

Across all economic sectors and scale of investments, efforts to improve the business and investment environment have been significant but progress has been slow due to several factors, including: insufficient communication between the government and the public on investment policy and how it relates to the country's development objectives, leading to a negative public perception of foreign investors; poor and irregular evaluation of the fiscal benefits and other investment incentives granted to large investors (see Section 3.6 below); and variable commitment or capacity for implementing investment policy reform across government bodies – in part due to weak inter-ministerial coordination,[4] and also because donor support and priorities for business environment reform are not always well-aligned with the government agenda. The Investment Council, created in 2009 as an overarching body for investment policy design at ministerial level, might have been under-utilised in this regard so far – despite Mozambique's clear need for strong and coherent investment policy guidance. The Investment Council could notably be more active in organising consultations with the private sector to better understand the shortcomings of the business climate, and also in proposing adequate policies to the government to improve the investment framework.

Albeit the creation of the Investment Council, further clarification of the responsibilities and accountabilities of all institutions and individuals involved in investment policy design is therefore required in order to make additional progress in improving the national business and investment environment. Likewise, although Article 4 of the 2009 Investment Regulations introduces a necessary clarification of "Competency for the coordination of investments", this remains an insufficient step forward. While several ministries and the Central Bank have important roles to play in practical terms for improving the business environment, only the Ministry of Industry and Trade monitors its business environment performance through sectoral and five year plans. Moreover, inter-ministerial committees have limited agency in their work with the Ministry of Industry and Trade. The fact that the Investment Council, CPI and GAZEDA are under the tutelage of another ministry (Planning and Development) does not support effective coordination regarding the improvement of the business environment.

Finally, in order to facilitate full and proper implementation of the investment regulatory framework, the government could also take concrete measures to improve transparency, and increase information disclosure and availability of the investment-related laws. Many of them are difficult to obtain (especially in English), which makes it difficult for investors to be aware of their rights and obligations. In this respect, Article 2.6 of the Bilateral Investment Treaty (BIT) signed by Mozambique with Uganda provides an interesting provision on the obligation to publicly disclose all investment-related laws, regulations and administrative procedures. This provision should be a general one in Mozambique's broader investment framework to support its effective implementation.

2.2. Ownership regulation and access to land

> What steps has the government taken towards the progressive establishment of timely, secure and effective methods of ownership registration for land and other forms of property?

General Objective 1 of the PARPA for 2011-14 (to boost production and productivity in agriculture and fisheries) recognises the importance of "improving and expanding access to factors of production", and notably commits to "speeding the process of awarding land title for local communities and economic agents". Similarly, one of the components of General Objective 3 (Social Infrastructure) is to "promote access to and secure tenure of serviced land and support self-construction".[5] However the 2012 *Doing Business* survey

indicates that Mozambique ranks 156th out of 183 countries in terms of registering property. This is Mozambique's second-to-worst score across all 2012 indicators (after access to electricity), and reflects a drop by six places since 2011. As illustrated in this section, processes for registration of land continue to pose an especially complex barrier for investors in Mozambique; recently they have also generated heated debate at the local community level.

Land ownership and transfer under the 1997 Land Law

The legal framework for land registration and ownership in Mozambique is the 1997 Land Law (Law 19/1997). Following its passage, the 1997 Land Law generated substantial debate over two topics which remain of relevance today: first, on whether it should be possible to sell or mortgage land "titles" or leases; and second, on the underlying tension between protecting land users versus improving conditions for potential investors.[6] As concerns the first issue, the national Constitution states that all land is owned by the State and cannot be bought or sold. Article 16(5) of the Land Law stipulates that only immovable assets and real estate, and authorised improvements which have been made on the land, can be mortgaged or sold. The Law recognises the right of people and communities to use the land and sell assets on the land, in rural and urban areas, but not to sell the land *per se*. Moreover, as land is generally licensed for a specific purpose in the land right acquisition process, changing its designated usage can be difficult.

Nonetheless the exchange of land titles – at minimum of leases, since ownership is not allowed – is extremely important to economic development, particularly in agriculture where the inability to cumulate land leases may impede a natural trend towards concentration of agricultural production and scale economies. Therefore the 1997 Land Law does provide for transfers of the document giving access to land use (the DUAT, *Direito de Uso e Aproveitamento de Terra*, or Land Use and Exploration Right), including by inheritance (Article 16[1]). Individual and corporate international investors may hold a DUAT provided an individual investor has been a national resident for at least five years, or in the case of a corporate entity, that it is registered in Mozambique. However, DUAT transfers are subject to strict limitations, particularly for rural land – as Figures 2.1 and 2.2 outline below, they require an application to the authorities, along with proof that the land exploitation plan (included in the initial DUAT application) has been completed. Meanwhile, as concerns mortgaging of DUATs, Article 16(5) provides only for mortgaging of improvements made on the land – and not the land itself.[7] Likewise although Article 13(2) of the Land Law permits DUAT titles to be presented in the context of credit applications, outside of this circumstance, DUATs cannot be easily transferred or mortgaged. The absence of clear regulation for the mortgaging of rural land itself clearly increases the costs and insecurity of any borrowing secured against the DUAT.[8]

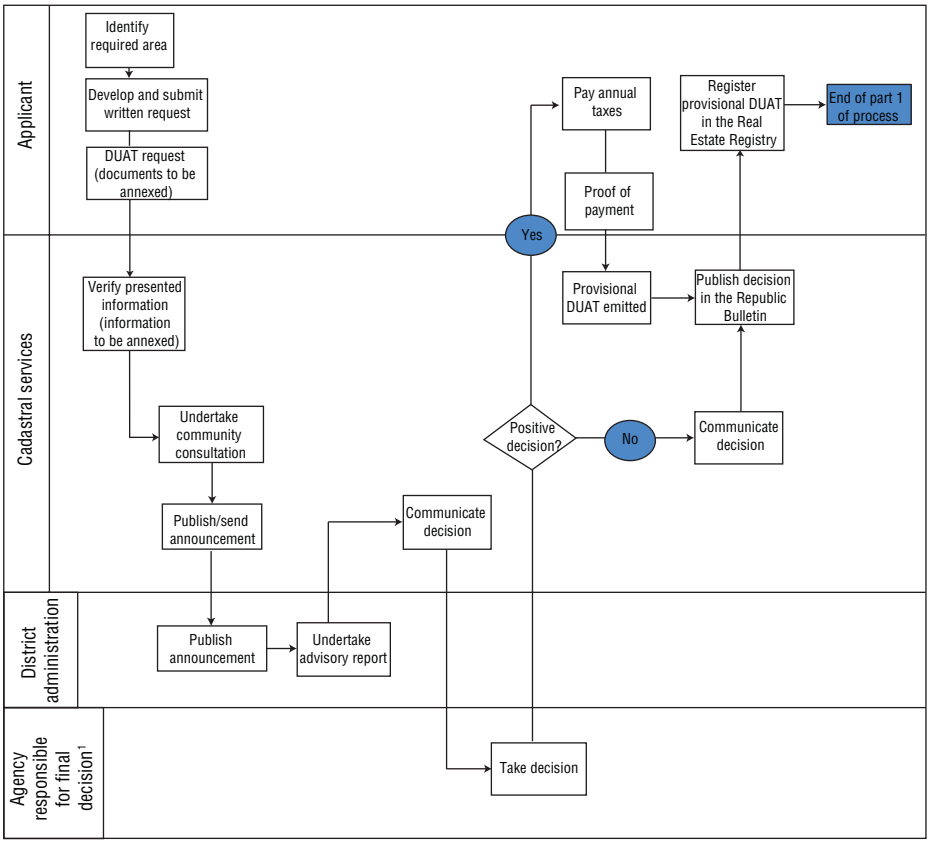
Tensions over the process for securing Land Use and Exploration Rights (the DUAT)

The second issue – the tension between investment and the protection of local rights – is meanwhile clearly embodied in the process for accessing land rights through the DUAT. The development of the Land Law followed a widespread consultative process, and as a result the text of the Law strikes a balance between protecting customary rights and enhancing land access for investors. Securing local community approval is officially a central step in the DUAT award process, and the administrative level at which the land allocation decision is made varies with the size of the investment (reaching the Council of Ministers for the largest projects). The documents to provide for a DUAT application therefore include, among others, a community consultation act and an exploitation or investment plan.

However in practice, the process of land access via DUATs involves a series of overly complex steps, from community consultation to approval and registration procedures, and often lengthy analysis of the investment plan and financing sources. As summarised graphically further below, there are two sets of steps in the DUAT process: first (Figure 2.1), the application is verified based on the investor's land use plans, and through consultation and any required compensation with the local community. Successful applicant investors are then granted provisional authorisation to use the land – this authorisation is valid for two years for foreign investors and five years for nationals, after which an inspection is conducted to verify that the proposed investment or exploitation plan is on-schedule. This first set of steps, according to the agricultural investment promotion agency CEPAGRI, takes on average 90 days; only after this can the second set of steps be undertaken (Figure 2.2) – the full procedure is approved and the long-term ("definitive") DUAT is provided to the investor.[9] The authorities involved in both procedures are, in turn: the Provincial Cadastral Service (SPGC, *Serviço Provincial de Geografia e Cadastro*); followed by the District Administration; and finally the decision-making authority. The specific authority with final decision over the provisional DUAT depends on the size of the project: the Province Governor for land plots of up to 1 000 Hectares; the Ministry of Agriculture for land plots of 1 000 to 10 000 Hectares; and the Council of Ministers for land plots larger than 10 000 Hectares.

Figures 2.1 and 2.2 on the following pages illustrate the number and sequence of these steps together with the actors partaking in the process; this level of complexity is significant, and can act as a strong deterrent for investors. Moreover these processes for securing a DUAT are not made available to investors in a legible and widely accessible manner – the figures below are for instance derived not from the central investment promotion

Figure 2.1. **First step of the DUAT process: Obtaining a provisional land right**



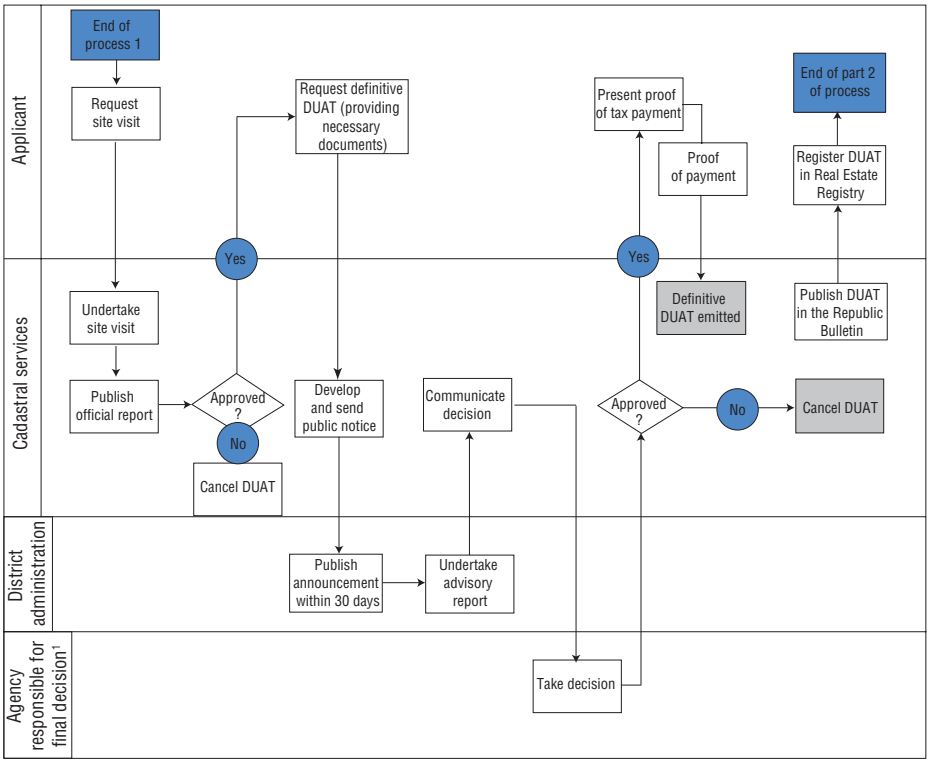
1. The agency responsible for decision varies with the size of the requested land plot: the Province Governor for land plots of up to 1 000 hectares; the Ministry of Agriculture for land plots of 1 000 to 10 000 hectares; and the Council of Ministers for land plots larger than 10 000 hectares.

Source: Replicated and translated from: CEPAGRI, *Manual de Procedimentos de Investimentos em Agro-Negócios*, December 2011.

agency CPI, but from CEPAGRI (in a manual which seeks to facilitate agricultural investment, and which is available in Portuguese only). In addition while the "definitive" DUAT is allowed for a period of 50 years, this is renewable only once and is conditional on the investor abiding to the agreed land exploitation plan. The DUAT can thus be terminated at any time – with no legal provision for compensation – should the investor be deemed to fall short of the exploitation plan; this further threatens investment confidence, as detailed in Section 2.5 below.

Therefore, the DUAT process poses a considerable hindrance to economic activities – not only for mega-projects or large-scale agricultural development, but also for smallholders who may lack information and resources, and for

Figure 2.2. **Second step of the DUAT process: Obtaining a definitive land right**



1. The agency responsible for decision varies with the size of the requested land plot: the Province Governor for land plots of up to 1 000 Hectares; the Ministry of Agriculture for land plots of 1 000 to 10 000 Hectares; and the Council of Ministers for land plots larger than 10 000 Hectares.

Source: Replicated and translated from: CEPAGRI, *Manual de Procedimentos de Investimentos em Agro-Negócios*, December 2011.

service industries such as tourism. Indeed, as pointed out by a 2006 FIAS investigation of Mozambique's tourism value chains, obtaining a good business location can be difficult for both small and large hospitality establishments. In particular, competition for land-use rights in attractive coastal areas is increasing, fuelling conflict between investors and rural communities. Such conflictual cases make it highly likely that local communities block the DUAT approval process. The price of land compensations can also be very high, but must be made before the economic activity (and its associated revenue flows) are underway. Box 2.1 below summarises the land access challenges faced by the Mozambique Tourism Anchor Investment Programme (MTAIP, undertaken by government in partnership with the World Bank's International Finance Corporation), and the countervailing steps taken to overcome these obstacles. These challenges are

Box 2.1. **The Mozambique Tourism Anchor Investment Programme**

Over 2007-11 the World Bank's International Finance Corporation (IFC) co-operated with INATUR (the national investment promotion agency for the tourism sector) in the roll-out of the **Mozambique Tourism Anchor Investment Programme** (MTAIP). This programme marketed two large resort sites and supported the development of an improved regulatory framework for resort tourism. **Difficult access to land was a severe obstacle faced by the Anchor Programme**; these challenges and the solutions developed (including special mechanisms for allocating land for tourism development) are outlined below.

Main challenges in land access faced by the Anchor Programme:

- Although the Programme ensured that local communities were met with in advance of the formal land-registration process, the process remained hindered by the absence of a mechanism for government to register land for economic development: INATUR, the tourism investment promotion agency and the main government party in the Programme, had to apply for land like any other investor.
- While the legal framework allows transfer of land titles, this is only permitted after the construction of value-added infrastructure (in part to safeguard against speculation). This hampers the roll-out of investment projects that cover large land areas, whereby project land may need to be sub-divided (and DUATs transferred) among secondary developers early in the project cycle.
- Although the Tourism Ministry issued a **Strategic Plan for Tourism Development** in 2003 that identifies 18 **Priority Areas for Tourism Investment** (PATIs), and although the **2004 Tourism Law** allows it to designate tourism zones of interest, neither instrument was yet operational. Moreover there is no legal instrument to reserve land for tourism development within these zones: land is legally required to be developed within five years of registration, without a formal mechanism to pre-emptively register the land until it can be most effectively developed.
- Compensation costs for land were very high and INATUR could not raise funds until project investments had been finalised. Therefore although INATUR could not pay for compensation up-front, it was difficult to obtain provisional DUATs to begin the development activities. Such challenges would be faced for investors across economic sectors: if land rights are not yet secure, financing will be difficult to unlock based on project approvals and feasibility studies.

Box 2.1. **The Mozambique Tourism Anchor Investment Programme** *(cont.)*

Solutions implemented by the Anchor Programme: the Anchor Team developed a legal instrument to allow the ministry to reserve land for tourism development: the Tourism Interest Zones Regulations (Decree 77/2009). Various amendments to existing laws were also suggested – as incorporated within the latest Regulations of the Investment Law (Decree 43/2009, which attributes Special Economic Zone status to integrated resort projects), the Code of Fiscal Benefits (56/2009), and the Tourism Interest Zones Regulations (77/2009).

Source: Investment Climate Advisory Services, World Bank Group. "Facilitating Large-Scale Tourism Resorts in Mozambique: The Tourism Investment Generation Approach", March 2012, Available at: *www.wbginvestmentclimate.org/uploads/CoastalResortsStudy.pdf*.

central and can hamper investment across all economic sectors, beyond tourism alone.

The steps taken above within the context of the Tourism Anchor Investment Programme were effective, but are only palliative efforts which do not address the underlying tensions of land access in Mozambique. The same caveat applies to the three recommendations made by the FIAS report as concerns acceleration of the DUAT process: reinforcing mechanisms to maintain the balance of relationships between local communities and tourism investors, such as through community-driven preparation of land for tourism activities; providing investors in each industry with a one-stop source of accurate information and processing of land user rights, which clearly delineates the roles and responsibilities incumbent to local and central levels of government; and increasing the capacity of local governments to process DUAT applications.[10] Likewise, the 2009 Investment Law Regulations introduces some flexibility into land use rights, but only for companies operating in Special Economic Zones and Industrial Free Zones: Article 22 states that the renewal of DUATs and benefit rights for these companies only requires proof of fulfilment of the approved project, and is to be decided upon within a maximum of 30 days.

These are all meagre improvements in the face of Mozambique's considerable land allocation difficulties: these initiatives do not foresee any change to the fundamental State ownership of land, and no specific timelines or mechanisms are proposed for speeding up land award processes outside of special zones. Moreover, issues of local development planning and zoning in urban areas, as well as house construction, also depend on the question of serviced land tenure. Increasing the effectiveness of the court system, significantly simplifying procedures for access to DUATs across all economic sectors (including reducing the number of agencies involved in granting the

DUAT, and potentially reviewing the distinction between provisional and definitive DUATs), and accelerating initiatives aimed at simplifying land registration remain indispensable in Mozambique. The recently-established Land Consultative Forum (see below) could be a promising venue for addressing these concerns.

A new platform for addressing land issues: The Land Consultative Forum

The community and customary ownership dimension of land rights is gaining importance on the government agenda, largely due to heated public debate on large-scale land transfers (between January 2004 and June 2009, use rights for 2.7 million ha of land were transferred to private investors).[11] Although the DUAT is expected to protect constitutional interests and to safeguard the rights of local communities by allowing customary rules to coexist with modern legislation, community consultations have often fallen short of their stated objectives in practice: a 2011 study examining foreign large-scale land acquisition in Ghana, Mozambique, Tanzania and Zambia indicates that while all of these countries have constitutional, policy and/or legislative provisions to safeguard customary land rights and to consult communities during land transfer, the consultative process itself is often deficient and reduced to mere formalities. Identifying land for biofuel and large-scale forestry plantations has been particularly controversial in Mozambique, sparked by the granting of rights to substantial portions of land to large foreign investors. Several communities voicing serious grievances have subsequently obtained the re-definition of the boundaries of land acquired by investors, or have reached a compensation agreement. Nonetheless, public reactions to these large-scale land transfers remain frequent, with many denunciations of "land grabbing".[12]

Whether or not these claims are justified, they have pushed the government's Council of Ministers to establish a Land Consultative Forum (*Fórum de Consulta sobre Terras*, FCT), which held its first meeting in March 2011.[13] Headed by the Minister of Agriculture, the Forum has a large Consultation Group that meets bi-annually and includes 15 ministries, municipalities, professional associations, and civil society. The Forum has been given a list of "urgent issues to debate" by the Council of Ministers:

- land taxes (which were raised by 150% in January 2011);
- separating individual plots from community land;
- women's rights to land;
- transfer of land rights;
- clarifying interpretations of the 1997 Land Law;

- inspection of investment projects and investment plans before awarding final titles; and
- community structures to manage land.

The third session of the Forum, held on 21-22 March 2012, gathered 150 participants and discussed: mechanisms for transfer of DUATs; the creation of a Single Land Cadastre; the revision of DUAT rates; and the case of DUATs for joint-ownership companies.[14] Given the many problems encountered in the implementation of Mozambique's land acquisition regulations – both for investors and local communities – the creation of the Land Consultative Forum is an extremely necessary step. The Forum faces a very arduous agenda, and this promising momentum should be strongly upheld by the government and all participating stakeholders.

Land registration and the LMIS initiative for digitalizing national cadastre services

In addition to complex land acquisition and registration procedures, significant amounts of land are held in concessions by private firms and individuals but not effectively utilized for production or local employment. While there is little vacant land remaining in Mozambique, under-used land is plentiful. For example in agriculture, the FAO estimates that only about 13% of Mozambique's 36 million ha of cultivable land were cultivated for arable and permanent crops in 2003, and the World Bank forecasts that the total land used for cropping and mixed farming will remain under 40% up to 2020. Obtaining information on available land is particularly difficult, and ambiguous regulations have in the past opened avenues for delays, corruption and arbitrary bureaucratic proceedings.[15] While a range of initiatives are underway within government and with donor support to regularize information on landholdings (none of which being contrary to the basic position that all land is owned by the State), progress remains frustratingly slow on this front.

A National Land Cadastre is maintained in Mozambique to define the legal, economic and occupancy status of land. The government has also established the "*Centro de Promoção da Agricultura*" (CEPAGRI), which is well positioned to play a more significant role in tackling access to land issues, as is seen in Chapter 3. Among the initiatives underway to regularise information on landholdings, CEPAGRI, in collaboration with the National Directorate of Land and Forestry (*Direcção Nacional de Terras e Florestas*, DINATEF) and the CPI, is compiling an updated national land registry for rural land. In addition, the government of Mozambique has been engaged in multiple e-government initiatives to support development, in the context of the ICT Policy Implementation Strategy approved in 2002. The integrated e-

Land Registry and Land Management Information System (LMIS) was launched in view of digitalising national cadastre services and thereby supporting the management of Mozambique's land, forestry and other natural resources. The LMIS has been implemented since 2004 by the National Directorate of Land and Forestry (DINATEF) with Italian bilateral funding. LMIS has the following aims:

- to provide information to decision-makers about land use;
- to solve land conflicts based on reliable information; and
- to provide and negotiate land investment based on this information.

Broader aims of the e-Land Registry programme include increasing security of tenure for rural communities by supporting the implementation of the 1997 Land Law, and completing a survey of land use and occupation. To date, LMIS has registered land tenures and achieved functionality for searching records, but it remains hampered by insufficiently skilled human resources, unavailability of adequate infrastructure, and illiteracy on the user end.[16] Implementation at the provincial and district level has also been haphazard. By contrast to some other e-government projects (such as e-SISTAFE, the State Financial Administration System which tracks poverty reduction through controlling public finances and which covers an increasing number of institutions across the country), many users have therefore abandoned LMIS due to lack of proper maintenance.[17] Yet, a system like LMIS would be highly beneficial for speeding up land-related processes for investors, for instance by enabling online land registration or electronic payment of land usage taxes. A recent Land Tenure Services Project, launched in 2011 by the Millennium Challenge Corporation (MCC) for operations over 2012-17, seeks to upgrade LMIS in order to establish more efficient and secure access to land for investment, and to help beneficiaries meet immediate needs for registered land rights.[18] Such attention to reviving the LMIS system is highly necessary and should be fully encouraged.

2.3. Protection of intellectual property

Has the government implemented laws and regulations for the protection of intellectual property rights and effective enforcement mechanisms? Does the level of protection encourage innovation and investment by domestic and foreign firms? What steps has the government taken to develop strategies, policies and programmes to meet the intellectual property needs of SMEs?

Three agencies for securing intellectual property rights

The definition and enforcement of laws promoting intellectual property rights, including for SMEs, contribute to fostering investment confidence. In Mozambique, intellectual property rights are set by three different agencies:

- the Institute of Industrial Property (IPI), which was created through the 2006 revision of the Code of Industrial Property. The IPI is placed under the Ministry of Industry and Trade and assumes and expands on activities that had been previously undertaken within the Ministry (including patents, geographical indication, and branding);
- the Ministry of Culture, through the National Institute of Books and Discs, deals with copyright issues; and
- the Ministry of Science and Technology, which handles strategic and policy issues, such as the preparation and implementation of the national Strategy for Intellectual Property, 2008-18.

The intellectual property rights legal framework derives from several items, among which the main laws are the Industrial Property Code (*Código de Propriedade Industrial*, Decree 4/2006, a revision of the 1999 code) and the Copyright Law (*Lei de Direitos do Autor*, Law 4/2001). Other related legislation includes the Law on the Protection of Cultural Heritage (10/1988), the Law on Telecommunications (8/2004), the Investment Law (Article 13 deals with protection of industrial property rights), as well as the national Constitution and the Civil Code (*Código Civil*). This comprehensive intellectual property legislation brought Mozambique in compliance with the WTO agreements on trade-related aspects of intellectual property rights (TRIPs). Mozambique is also a signatory to a number of international agreements on patents and intellectual property, such as: the World Intellectual Property Organisation (WIPO) Convention, Paris Convention, Patent Cooperation Treaty, Madrid Agreements, Madrid Protocol and Nice Agreement. Mozambique has also started undertaking measures to adhere to the Berne Convention and, at regional level, is a member of the African Regional Intellectual Property Organisation (ARIPO).

Besides, the national Strategy for Intellectual Property 2008-18 has the following objectives: dissemination and training on industrial property rights for the general public and specifically to promote innovation and industrial competitiveness, scientific and technological research, and traditional and biodiversity knowledge; developing a culture of creativity; and improved management of the intellectual property rights system. Implementation of the strategy is yet to be evaluated. However, as indicated below, there are signs of greater awareness of the significance of intellectual property and of its role in investment promotion and protection.

A novel field in which further awareness-raising needs to be fostered

Intellectual property rights are a new subject matter in Mozambique: there is limited knowledge among the public about these rights and their significance, though this is not the case with investors.[19] Numerous government agencies are thus disseminating information on IPR programmes to the judiciary, universities and media. The National Innovator Programme (*Programa Nacional do Inovador*) and the National Association of Innovators have produced brochures on IPR specifically for SMEs. There are indications that these dissemination efforts are paying off: in ten years the level of registration by Mozambican companies increased dramatically – from 3% in 1999 to over 50% by 2009 – and over 27 000 brands have been registered with IPI and WIPO (which Mozambique joined in 1996). Mozambique was also one of the nine states to sign the Swakopmund Protocol on the protection of traditional knowledge and expressions of folklore in August 2010. In the lead up to this, Mozambique had organized a Workshop on the Protection of Genetic Resources, Traditional Knowledge and Expressions of Folklore in Maputo in August 2009.[20] It is therefore somewhat of a regional frontrunner in this regard.

As foreseen in the Strategy for Intellectual Property (one of its objectives is "specifically to promote innovation and industrial competitiveness"), such increased familiarity with intellectual property rights can have numerous benefits for Mozambique. As investors gain confidence in the durability of their rights, they become willing to invest in innovation, and to create applications and products with added value. The government should be encouraged to evaluate this intellectual property strategy, including its impact on international and domestic investment in Mozambique. Alongside this, it will be necessary to strengthen the capacity of the Institute of Industrial Property (IPI), which is not backed by sufficient staff nor by an effective enforcement mechanism.

2.4. Contract enforcement and dispute settlement

> Is the system of contract enforcement effective and widely accessible to all investors? What alternative systems of dispute settlement has the government established to ensure the widest possible scope of protection at a reasonable cost?

Effective and accessible contract enforcement, including through alternative dispute resolution and arbitration mechanisms, is a base of sound investment policy. In Mozambique, the 1990 Constitution declares the

establishment of an independent judiciary. It has been reorganised in 2007 under Law 24/2007. The court hierarchy is made up by four levels: the Supreme Court, high courts of appeal, provincial courts and district courts.

A Law and Centre on Arbitration, Conciliation and Mediation have been established

Specialised courts do exist on several matters (administrative, customs, fiscal, maritime and labour courts) but commercial courts are not yet fully operational. Nevertheless, since 1999, alternative dispute resolution is legally recognised and most cases of commercial disputes can be regulated by the Law on Arbitration, Conciliation and Mediation (LACM, Law 11/1999), which is the main legislative source relating to arbitration in Mozambique. The LACM is mostly based on the 1985 United Nations Commission on International Trade Law (UNCITRAL) Model Law and is formulated to cover both domestic and international commercial arbitration. In particular, the following issues can be submitted to arbitration: intellectual property rights, antitrust, competition, securities transactions and intra-company disputes.[21] Parties have the possibility to be represented by foreign lawyers. The Judicial Court of Maputo enforces arbitration awards and enforcement decisions can be appealed to the Supreme Court. According to the World Bank, on average, it takes around 46 weeks to enforce an arbitration award rendered in Mozambique and 121 weeks for a foreign award.

The Centre for Commercial Arbitration, Conciliation and Mediation (CACM), which is supported by USAID, offers effective commercial arbitration, conciliation and mediation. It was created in 2001 and has offices in Maputo, Napula and Beira. Since 2009, it also conducts mediation and arbitration for labour disputes. Besides, there is also an informal arbitration mechanism (*Gabinete de Arbritagem*) associated with a private sector representative group, the Confederation of Economic Associations (*Confederação das Associações Económicas*, CTA), which is rather used in labour disputes. As far as land is concerned, the Land Consultative Forum, established in 2011, is expected to facilitate dispute resolution over land rights.

The Bankruptcy Law is highly necessary but its revision process has been protracted

Other tools that are used for contract enforcement in Mozambique include provisions of the Investment Law (e.g. Article 13) and the Bankruptcy Law, which is in the process of being revised. Indeed, the absence of a unified bankruptcy framework is one of the primary challenges to contract enforcement in Mozambique. The bankruptcy process is governed by the Code of Civil Procedure, approved by Decree-Law 44,129 of December 28, 1961, and amended by Decree-Law 47,690 of May 11, 1967. The ineffective and out-dated

nature of that framework is suggested by the fact that in 2008 there were only about ten bankruptcy cases in the courts even though many more companies were in a state of technical bankruptcy.[22] In the 2012 World Bank *Doing Business* report, Mozambique thus ranks 131st in terms of enforcing contracts (out of 183 economies). According to the report, 30 procedures on average are required to enforce contracts, while 730 days are necessary to resolve a dispute and the cost of court fees account on average for 143% of the amount claimed. These figures have not changed over the past four years and do not compare well with the average of Sub-Saharan Africa (respectively for 39 procedures, 655 days and 50% of the amount claimed). Meanwhile, the *Doing Business* ranking on resolving insolvency (also an important part of contract enforcement, for which a robust legal system for bankruptcy is needed) has dropped by 9 positions between 2011 and 2012.

A revision of the bankruptcy process is much needed, and has in fact been underway for some years. The proposed 2009 Draft Law of Insolvency and Recovery by Business Entrepreneurs is based on international best practice. The Draft law is modelled on the 2005 Brazilian law; it is complete and would replace Mozambique's existing insolvency legal framework with a much more modern model. It would apply to insolvency proceedings or recovery of commercial entrepreneurs, as well as associations and foundations, civil societies and cooperatives. It would not be applicable to public companies, credit institutions or financial companies, public or private pension entities, health insurance companies, insurance companies, or capitalization companies, as these all have their own specific regimes. Enactment of this new law would require strengthening the judicial system's capacity to manage and decide insolvency cases, and the reform of related legal and institutional frameworks supporting creditor rights (such as the enforcement of judgments and secured transactions).[23] Unfortunately, the slow pace of revision of the legal framework for bankruptcy however suggests that it has not been a government priority so far; until it is updated, it will continue to be a barrier to attracting investment.

2.5. Compensation for expropriation

Does the government maintain a policy of timely, adequate, and effective compensation for expropriation also consistent with its obligations under international law? What explicit and well-defined limits on the ability to expropriate has the government established? What independent channels exist for reviewing the exercise of this power or for contesting it?

Whenever a government exercises its legitimate right of expropriation, there is an uncontested need for compensation. The compensation must be fair and adequate and paid promptly. In addition, the government decision to expropriate land or other property must meet three other conditions for a lawful expropriation: motivation by a public purpose; observance of due process of law; and non-discrimination. As expropriation is perceived as a major political risk for an investor, clear and complete provisions regulating expropriation are needed and constitute an investment guarantee.

Compensation provisions under the 1997 Land Law

Property rights in Mozambique are guaranteed by the Constitution, which establishes under Article 82 (Right of Ownership) the recognition and protection by the State of ownership of property. It specifies that expropriation may only take place for motives of national necessity, utility or interest. In addition, Article 13 of the 1993 Investment Law addresses the protection of property rights in further details. Section 13.1 guarantees the juridical protection of assets and rights, including rights to industrial property. Investors are guaranteed "just and equitable" compensation for any nationalisation or expropriation of goods or rights (undertaken "when deemed absolutely necessary for weighty reasons of national interest or public health and order"). Compensation is also an entitlement in the case of deterioration of goods and any financial prejudices incurred under explicit responsibility of the State. The filing process for compensation is led by a commission created for that purpose or by a recognised audit agency, following which the relevant State organ disposes of 45 days in which to make a decision. Compensation payment is expected to be made within less than 90 days from the expropriation decision.

To foster more clarity and investor confidence, the likely "reasons of national interest" that could justify expropriation, as well as the forms and timeframe of compensation that this would entail, could be set out in more detail by law. Moreover, as for all other matters dealt with in the Investment Law and related Regulations, these provisions and the thereby guaranteed protection only apply to those investors that have obtained investment licenses; this places enterprises that choose to forgo the license application process – such as many SMEs – at particular risk.

Furthermore, these compensation rights do not apply to land, all of which was nationalised following independence in 1975. Under the 1990 Constitution, all land still belongs to the State, and cannot be owned on a private basis. In 1992, citizens were given a period of time to reclaim residential property but the government retained commercial property, some of which was sold off as part of the privatisation process. Given the nationally-owned status of Mozambican land, the absence of clear compensation

mechanisms and of frameworks for managing expropriation in the case of land severely deters investment. Moreover, land use rights can be terminated (or essentially, a DUAT revoked) if the investor fails to meet the investment plan set out in the DUAT application. Article 18(2) of the 1997 Land Law states that, "upon termination of the right of land use and benefit, the non-moveable improvements [made on the land] shall revert to the State". This clause applies both to termination provoked by the investor (due to inappropriate land use) and to natural termination due to expiry of the 50-year renewable DUAT. Article 18(2) thus does not provide compensation for land improvements under the law, further increasing the risks of investment.[24] As mentioned in Section 2.2 above, the ownership and lease structure of land rights is therefore a key concern for Mozambique to address. This issue would deserve careful consideration by the recently established Land Consultative Forum.

International investment agreements and MIGA support

In addition, Mozambique joined the Multilateral Investment Guarantee Agency (MIGA) in 1994. MIGA guarantees protect, *inter alia*, against expropriation, and have supported many of the early-movers into Mozambique's post-conflict economy. Since 1998, MIGA has supported 12 projects in Mozambique, mostly in the form of extractive mega-projects (such as the MOZAL aluminium smelter, the Moma Titanium Minerals Mine established in Nampula Province by Ireland's Kenmare Resources, and the Sasol gas project), but also in the agricultural sector (such as the Marromeu sugar project). MIGA support was essential for providing political risk cover for these early investments, given Mozambique's recent history of conflict.[25] Finally, it is worth mentioning that most international investment agreements signed by Mozambique contain an expropriation provision; although content and wording differ among the treaties, most BITs cover both direct and indirect expropriation, and usually cite the four criteria for a lawful expropriation.

2.6. Principle of non-discrimination

Has the government taken steps to establish non-discrimination as a general principle underpinning laws and regulations governing investment? In the exercise of its right to regulate and to deliver public services, does the government have mechanisms in place to ensure transparency of remaining discriminatory restrictions on international investment and to periodically review their costs against their intended public purpose?

Provisions for non-discrimination in the 1993 Investment Law are ambiguous

As highlighted in Section 2.1, the principle of non-discrimination on the grounds of nationality is stipulated both in the Constitution and in the Investment Law (and its 2009 related Regulations). It reflects the will of the government to build an open economy and attract foreign investment. No sectoral restrictions are specifically mentioned in the Law or its Regulations.

However, the Law's scope of application is somewhat ambiguous. In fact, Article 4.1 of the 1993 Law guarantees equality of rights and duties to all national and international investors and workers, but Article 4.2 notes that, in a small number of instances, activities by nationals may receive special treatment due to the nature or scale of investment. This paragraph of the Law is vague and provides grounds for discrimination against foreign investors. A more specific delineation of criteria for special treatment, and the nature of this treatment, is highly recommended as it would reduce the risks of arbitrary application of this clause and could strengthen the overall investment framework. Similarly, Article 12 of the Investment Regulations 2009 imputes the decision regarding the approval of an investment project received by CPI (and hence the issuance of investment licenses) to different bodies depending on the origin and scale of investment: the Governor of the Province approves national investment projects of under MZN 15 million (about USD 520 000); the General Director of CPI approves foreign and/or national investment projects with an investment value of under MZN 25 million (about USD 870,000); the Minister with oversight of Planning and Development matters for foreign and/or national investment projects of under MZN 135 million (about USD 4 700 000); and the Council of Ministers approves projects with more "specific circumstances" – namely investments that: are very large (over MZN 135 million); require either a land area greater than 10 000 hectares or a forestry concession larger than 100 000 hectares; or have foreseeable political, social, economic, financial or environmental impacts. Such practices are also an open door to arbitrary judgment and discrimination of certain investors. In practice, large foreign investors tend to obtain investment licenses more easily than small foreign investors and national investors. This does not reflect a non-discriminatory investment framework.

As for sector-specific restrictions, most of Mozambique's industries are open to foreign equity ownership, and restrictions apply only to media and telecommunications: the Media Law 18/1991 stipulates that only Mozambican citizens may own media companies, where foreign capital participation is capped at 20%. Similarly, fixed-line telecommunications are reserved for public investment, with the right to establish and operate fixed-line telecommunication services exclusively reserved to Mozambique S.A.R.L.[26]

Elements of the labour and public procurement laws grant preference to domestic investors

Nonetheless, the national legal system does promote positive discrimination. For example, the Labour Law (*Lei de Trabalho*, 23/2007) promotes the hiring of nationals, and the public procurement law (*Regulamento de Contratação de Empreitada de Obras Públicas, Fornecimento de Bens e Prestação de Serviços do Estado,* 15/2010) allows preference to national firms in certain circumstances. Article 26.2 of the public procurement law, on national bidders, thus states that the contracting authority can restrict participation to national bidders if the contract is for reinforcement of public works or supply of goods or services, and if the contract value does not exceed specific monetary ceilings[27]. Contracting authorities that do not restrict participation to national bidders in the conditions set out in Article 26.2 must compensate for this by granting national bidders preferential bidding margins. Article 26.3 sets these margins at 20% of the gross value of the contract for public works projects, and 15% for goods and service projects. Article 26.4 notes that in order to secure these margins, producers must prove that corresponding national factors will be incorporated into the production process, amounting to at least 20% of the finished product value[28]. These provisions are quite restrictive and in some cases may conflict somewhat with WTO requirements on local content. It is not clear that the government has specific mechanisms in place to ensure transparency of remaining discriminatory restrictions on international investment, and to periodically review their costs against their intended public purpose.

> Has the government reviewed restrictions affecting the free transfer of capital and profits and their effect on attracting international investment?

Restrictive conditions for transfer of capital under the Investment and Foreign Exchange Laws

The Investment Law guarantees the transfer of funds (including profits, royalties, principal and interest payments on loans, capital from the sale of assets, and proceeds from expropriation or nationalisation), a process which is overseen by the *Banco de Moçambique*. However, even under the Investment Law Regulations of 2009, this transfer guarantee has quite restrictive eligibility criteria. As outlined under Article 6 of the 2009 Regulations, for eligibility for external remittance of profits and re-export of invested capital, the minimum value of equity capital foreign direct investment is set at MZN 2.5 million (approximately USD 85 000). Investors that do not meet this criteria remain

eligible if they meet one of the following requirements: from the third year of operations, generate an annual sales volume of at least three times the minimum value above (MZN 2.5 million); register annual exports of goods or services with a value equivalent to MZN 1.5 million (approximately USD 50 000); and create and maintain from the second year of operations at least 25 direct employment positions for Mozambican nationals who are registered with the social security system.[29] These conditions are unusually constraining compared to international best practice and hence create some discrimination against foreign investors. Nonetheless, most BITs signed by Mozambique contain a transfer of funds provision that is usually well drafted and non-discriminatory.

The new Foreign Exchange Law (11/2009, the regulations for which came into force in June 2011) has changed key elements of exchange management in Mozambique. To a certain extent, the new law is a step forward in terms of liberalisation of existing foreign exchange operations, as it eliminates the constraints applicable to payment transfers between residents and non-residents. Article 8 details provisions for entry and exit of foreign currency, which is freely permissible for foreign residents within certain monetary limits. Exit of foreign currency for residents meanwhile requires proof of legitimate retention and possession. Under Article 6 of the Law, any current payments made in foreign currency are subject only to registration with the Bank of Mozambique, but not to prior authorisation (with some exceptions, noted in paragraphs 6.2 and 6.3).

Yet alongside these changes, other facets of the 2009 Foreign Exchange Law go towards stronger restrictions and remain quite far from international standards. Capital payments thus require both registration and authorisation with the Bank of Mozambique, without which the right of investors to remit and repatriate profits arising from an approved investment project may be compromised. A particularly controversial provision for domestic investors, aimed at bolstering the country's exchange rate stability, also requires that resident entities declare all acquired monetary amounts and rights generated or held abroad, and remit to Mozambique the income from the export of goods, services and foreign investment. This amounts to mandatory repatriation to Mozambique of export income, and its conversion into local currency (parties can maintain only up to 50% of their overseas earnings in foreign currency, and on the condition that these funds are held in a national bank account or used to repay foreign currency loans contracted with national banks). Contravening any of the registration, authorisation or export revenue repatriation requirements within the Foreign Exchange Law is punishable by way of a fine of MZN 10 000 to 100 000 (USD 350 to 3 500) if the offender is an individual person, or of MZN 40 000 to 400 000 (USD 1 400 to 14 000) if the offender is a collective person. These fines are augmented in case of simultaneous commission of more than one foreign exchange offence.[30]

As noted by the Support Programme for Economic and Enterprise Development (SPEED) of USAID/Mozambique, while the new foreign exchange regulation could increase the effectiveness of monetary policy by controlling inflation and stabilizing the exchange rate, and may also limit capital flight, it is therefore seen by investors as a backward step in the liberalization process and is criticised for insufficient prior consultation with private sector representatives.[31]

Specific provisions for foreign exchange operations of SEZs and IFZs

The Foreign Exchange Law states that remittances from Mozambican emigrants, the stock exchange, and free enterprise zones benefit from special treatment. Foreign exchange operations for IFZs and SEZs are thus to be regulated separately from the Foreign Exchange Law, as set out by the Investment Law Regulations (Decree 43/2009), which contain a large number of provisions specifically targeted at these enterprise zones. With respect to the Foreign Exchange Regime and to external and internal transfers of funds, Articles 33 and 34 of the Regulations state that:

- IFZs and SEZs are permitted to open, maintain and transact accounts in foreign exchange inside and outside of Mozambique, provided that the opening of external accounts be with corresponding banks of national banks;
- the maintenance and operation of external accounts is subject to the prior authorisation of the Bank of Mozambique;
- the import of capital funds or other type of financial contribution for the constitution or increase of the IFZs or SEZ share capital is to be registered by submitting documentary proof to the Bank of Mozambique;
- within a SEZ, the permitted foreign exchange regime is unrestricted and to be considered as "off-shore" operations; and
- external remittance of profits and dividends, as well as repatriation of capital, is permitted subject to the prior authorisation of the Bank of Mozambique and provided that the investments have been previously registered with it and all taxes due have been paid.

2.7. International investment agreements

Are investment policy authorities working with their counterparts in other economies to expand international treaties on the promotion and protection of investment?

Mozambique has signed investment promotion and reciprocal protection agreements with 23 countries: Algeria, Belgium, China, Cuba, Denmark, Egypt, Finland, France, Germany, India, Indonesia, Italy, Mauritius, Netherlands, Portugal, South Africa, Spain, Sweden, Switzerland, United Kingdom, Viet Nam, USA and Zimbabwe. Mozambique first signed BITs with regional partners (Zimbabwe, Mauritius, South Africa) and with its historical partner, Portugal, in the beginning of the 1990s. It then expanded BITs with both countries from the OECD and the developing world, building a network of investment agreements with strategic partners. This trend toward the signature of numerous BITs, which started in the beginning of the 1990s, thus went hand in hand with the implementation of policies aiming at liberalising the economy and opening it to foreign investment. As Table 2.1 illustrates, the vast majority of these BITs have been ratified and are thus in force – only the latest treaty, signed with Spain in October 2010, has not yet been ratified. This signals a very positive ratification record, especially as compared to many countries of Sub-Saharan Africa.

Table 2.1. **Mozambique BIT signature and ratification record (as of June 2012)**

Partner	Date of signature	Date of entry into force
Algeria	12 Dec. 98	25 July 00
Belgium	18 July 06	1 Sep. 09
Luxembourg	18 July 06	1 Sep. 09
China	10 July 01	26 Feb. 02
Cuba	20 Oct. 01	26 Feb. 02
Denmark	12 Oct. 02	30 Dec. 02
Egypt	8 Dec. 98	–
Finland	3 Sep. 04	21 Sep. 05
France	15 Nov. 02	6 July 06
Germany	6 Mar. 02	15 Sep. 07
India	19 Feb. 09	–
Indonesia	26 Mar. 99	25 July 00
Italy	14 Dec. 98	17 Nov. 03
Mauritius	14 Feb. 97	26 May 03
Netherlands	18 Dec. 01	1 Sep. 04
Portugal	28 May 96	31 Oct. 98
South Africa	6 May 97	28 July 98
Spain	18 Oct. 10	–
Sweden	23 Oct. 01	1 Nov. 07
Switzerland	29 Nov. 02	17 Feb. 04
UAE	24 Sep. 03	–
UK	18 Mar. 04	12 May 04
USA	1 Dec. 98	3 Mar. 05
Viet Nam	16 Jan 07	29 May 07
Zimbabwe	12 Sep. 90	–

Source: UNCTAD 2013.

Most countries of origin of FDI in Mozambique have thus signed BITs, which are in majority well drafted and reflect best practices. They include provisions on expropriation, transfer of funds and international dispute settlements. Similar agreements are being prepared with 21 other countries, including with Japan over the first half of 2013. Interestingly, this treaty will include a list of sectors (especially certain manufacturing activities) in which Mozambican participation is restricted to a certain percentage and where priority is granted to Japanese companies; this could set an innovative precedent for future BIT negotiations.

In addition double-taxation and fiscal evasion treaties are in place between Mozambique and Macau, Mauritius, Portugal, South Africa and the United Arab Emirates. Mozambique has also engaged in initiatives for non-discrimination and trade and investment promotion at the sub-regional level. The country's favourable location *vis-à-vis* its neighbours involves it in 70% of traffic transit in the SADC; it therefore plays a major role in regional trade, as highlighted in Chapter 4 (on infrastructure) below. In accordance with the SADC regional Free Trade Agreement, Mozambique has liberalised 85% of its import tariffs and signed most of the 29 associated economic and regional integration protocols. It has also signed bilateral agreements with Malawi and Zimbabwe.[32]

2.8. Settlement of investment disputes

Has the government ratified and implemented binding international arbitration instruments for the settlement of investment disputes?

Mozambique is a member of the International Centre for the Settlement of Investment Disputes (ICSID). It signed and ratified the ICSID Convention in 1995, following again the country's then new trend of economic reform and liberalisation. Article 25 of the Investment Law (on Resolution of Disputes) stipulates that any disputes arising between the government of Mozambique and foreign investors that cannot be resolved amicably should be submitted to the competent judicial authorities in accordance with Mozambican law. If still no resolution can be found, disputes can be submitted to international arbitration, following the rules of ICSID, those of ICSID Additional Facility or those of the International Chamber of Commerce. Important is to note that the Law mentions that this is possible only if both parties agree to do so. Furthermore, once again, only foreign investors holding investment licenses are entitled to these provisions. As of October 2012, no Mozambican cases had been brought to ICSID.

Going further than the Investment Law's provisions, the BITs analysed provide for an amicable settlement of disputes and/or conciliation (e.g. the BIT signed with India). They provide that, after a cooling-off period of usually six months, the dispute can automatically be brought to national court[33] or international arbitration. BITs provide for a choice of fora and usually refer to ICSID or ad-hoc arbitration under UNCITRAL rules. Mozambique also signed in 1998 the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. In this regard, most of the BITs signed by Mozambique also mention that arbitral awards are final and binding, meaning that the State has an obligation of enforcement.

Notes

1. Bertelsmann Stiftung, *BTI 2012 Mozambique Country Report*, 2012. Available at: *www.bti-project.org/countryreports/esa/moz/2012/#chap9*.
2. For example, Law 13/2007, Fiscal Benefits for Mining and Petroleum, establishes rates for customs duties and VAT, which are in fact not significantly different from other priority investment sectors under the 2009 Code.
3. World Bank (2008) and *WTO Trade Policy Review of Mozambique* (2009).
4. Such complexity is suggested by the fact that in addition to the *Banco de Moçambique*, the main ministries involved in business environment reform include Industry and Trade, Labor, Justice, State Administration, Finance, and Planning and Development. Of these ministries, only Industry and Trade has business environment reform as a central ministerial objective under which its performance is monitored through sector and five year plans.
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Chapter 3

Investment promotion and facilitation in Mozambique

Investment promotion and facilitation measures can be effective instruments to attract investment, provided they aim to correct for market failures and are developed in a way that can emphasise the strong points of a country's investment environment. Mozambique has taken important steps in building a more enabling framework for setting up businesses, including under the "Strategy for improving the business environment in Mozambique" (EMAN, for 2008-12). This chapter examines various measures adopted by the government to reduce administrative burdens on investors, and notably the role of the Centre for the Promotion of Investment (CPI). The CPI would benefit from greater responsibilities in terms of interaction with established investors and spearheading the EMAN Strategy. This chapter also highlights the need for a more systematic evaluation of the impact of investment incentives, especially within Accelerated Economic Zones and in sectors such as mining which host most of the country's mega-projects. The governance and administration of these incentives could also benefit from further transparency and coherence. Finally, efforts remain necessary to tackle the fiscal, financial and human resource constraints facing SMEs, so as to enable them to feasibly latch onto investment linkage opportunities.

3.1. Investment promotion and facilitation strategy

Does the government have a strategy for developing a sound, broad-based business environment and within this strategy, what role is given to investment promotion and facilitation measures?

Strategy for improving the business environment in Mozambique (EMAN), 2008-12

In March 2008, the national government released its "Strategy for improving the business environment in Mozambique, 2008-12" (*Estratégia para a Melhoria do Ambiente de Negócios em Moçambique*, or EMAN 2008-12). This strategy reflected the focus of the *Doing Business* methodology developed by the World Bank, and addressed five priorities:

- simplification of procedures to start a business (including passage of the Simplified Licensing Decree, Decree 2/2008 – see following section);
- simplification of the system of requirements and procedures for the licensing of economic activities;
- creation of a single general inspection system for economic activities;
- adoption and adaptation of international (ISO) and regional standards, in accordance with the needs of the private sector; and
- simplification of procedures concerning imports and exports.

In addition, the 2008-12 EMAN Strategy focused on the following main areas: legal reform; tax and finance; governance; infrastructure; implementation mechanisms; and monitoring and evaluation. It sets out three main objectives: improving the legal, fiscal and financial environments; ameliorating corporate governance; and tackling excessive energy prices and inadequate infrastructure. As 2012 draws to a close, EMAN II (for 2013-17) is currently being elaborated by government in consultation with the private sector, and should be approved by the Council of Ministers at the end of 2012. It is expected that EMAN II will include legal, institutional and doing business reforms, with a focus on industrial development, SME promotion, and improvement of public services.

EMAN is implemented by the following organs: the inter-ministerial commission for public sector performance (headed by the Prime Minister); the inter-ministerial group for the reduction of barriers to investment (responsible for public-private dialogue and charged with co-ordinating provincial and national levels of government); and the inter-sectorial provincial group (composed of all Province Directors and led by Province Governors who are charged with strategy implementation at the provincial level).[1] Functions of investment promotion and facilitation under EMAN are delegated by the Ministry of Planning and Development to the Centre for the Promotion of Investment (CPI, Mozambique's lead agency for investment promotion – see Section 3.2) and the Office for Accelerated Economic Development Zones (GAZEDA).

Yet the EMAN framework lacks clear benchmarks for monitoring progress as well as provisions for garnering feedback from the investor community. The ongoing elaboration of EMAN II provides an opportunity for more clearly stating the Strategy's intended impacts, as well as how its objectives will be achieved. Progress towards short-term, quantifiable goals (such as business facilitation and attracting more domestic and foreign investment) should also be tracked in a systematic manner, including through greater feedback from targeted investor groups – across all industries and notably at the SME level. EMAN II could moreover be usefully embedded within an over-arching national investment strategy, so as to reach a wider scope than business facilitation alone. The Strategy could for instance meaningfully look beyond the World Bank Doing Business indicators, and also consider the effects of attracted investments on economic diversification, food security or employment creation. There is also potential for better co-ordinating EMAN with the objectives of the 2002 ICT Policy Implementation Strategy and the 2006 e-government Strategy. The latter notably plans for a System for Licensing and Registration of Enterprises (SISCAL), which may significantly accelerate doing business procedures providing it is implemented in a timely and diligent manner.[2]

2008 Decree on Simplified Licensing

The 2008 Decree on Simplified Licensing aims to provide regulatory simplification by reducing the time and documentation required for registering new activities. It applies to registered businesses with an annual turn-over of less than MZM 2 500 000 (approximately USD 86 655), and covers a large variety of retail, service, micro and small industrial, and agricultural activities. Meanwhile activities that remain outside of the Decree's scope undergo either the commercial licensing or the industrial licensing procedures (detailed further below).

Under the 2008 Decree, simplified licensing is open to activities which are deemed not to carry health, environmental or security risks, and licenses can be issued in the applicants' presence at provincial One-Stop Shops (*Balcões de Atendimento Único* or BAUs, see below), at district administrations and at municipal councils. In February 2012, government approved a decree extending the coverage of simplified licensing procedures to fisheries and culture, thus adding two sectors to the seven already covered (agriculture; commerce and service provision; construction; sports; industry; transport and communications; and tourism). Over 100 eligible activities within these sectors are listed in Annex 2 of the Decree. Such projects are notably exempted from the paperwork related to arranging site inspections (*vistorias*), as well as from certain forms of impact assessment. The 2012 decree also allows documents to be submitted by e-mail, and establishes the same licensing fee (set at 50% of minimum monthly wage paid in the public administration) for all activities concerned.

One-Stop-Shops in Mozambique (Balcões de Atendimento Único, BAUs)

At the national level, CPI and GAZEDA are the sole agencies responsible for the licensing and registration of businesses and investment operations. These are however complemented at the province level by multiple *Balcões de Atendimento Único* (BAUs, or One-Stop-Shops), which undertake the bulk of their activity in four key sectors: industry, commerce, transport, and tourism. After several years of operation without a dedicated legal framework, Mozambique's BAUs were strengthened by the 2007 "Organic Statute" for One-Stop Shops (*Estatuto Orgânico dos Balcões de Atendimento Único*). Yet this Statute does not fully decentralise BAU operations: although it transfers licensing authority to BAUs, BAUs are made subordinate to their respective provincial governments, and their operations are placed under the tutelage of the Ministry of Industry and Commerce (MIC). Under Article 6 BAU functions include: licensing of economic activities (for which BAUs are expected to refer to central government organs for the licensing decisions); charging taxes on the provided services; emitting identification and other documents dispatched by the public administration; and technical training.[3]

The 2007 Organic Statute reduced delays in authorisation processes, and improved the perception of BAUs (previously viewed as instruments of the central government at provincial level, rather than as multi-sectoral instruments of the provincial government).[4] However BAU efficiency remains hampered by: unclear delineation of responsibilities among BAUs and line ministries at central and provincial levels; unclear funding mechanisms; and poor training of staff. This is especially the case outside of Maputo. There is also insufficient business awareness of the services provided by BAUs, and poor articulation between BAUs and the CPI.[5] Moreover, despite the

enactment of the 2008 Decree on Simplified Licensing, licenses are still required for nearly every economic activity in Mozambique – with the result that little decision-making authority is actually delegated to BAUs. Procedures remain particularly complex in sectors such as tourism, construction and health, which are not regulated by MIC.

Recognising these limits, the consolidation of BAUs is one of the stated goals of the Public Sector Reform Programme (Phase II), undertaken by the Public Service Ministry. In the context of this programme, capacity-building of BAU staff has been underway since 2009 in all provinces. Several services have also been identified for transfer to BAUs in the short and medium terms, including the decentralization of certain energy services in coordination with the Office for Support to the Private Sector and the MIC. Proposals are also under preparation for a clearer distribution of taxes levied by BAUs during the licensing process.[6]

Poor Doing Business scores reflect an inconsistent investment promotion strategy

The standing of Mozambique in the World Bank's Doing Business Survey has fluctuated over the last six years, varying between 110th of 155 economies in 2007 and 146th of 185 countries in 2013. This latest ranking marks a seven-notch deterioration from the previous year, where Mozambique placed 139th out of 183 countries. Past improvements in ranking have moreover been associated with isolated 'one-shot' reforms, rather than inscribing themselves in a continuous process of business climate improvement. For example the decision that a foreign company establishing itself in Maputo would no longer be required to seek an investment approval (unless it wanted to access the investment incentives offered by CPI) reduced the number of days for starting a business from 29 in 2008 to 13 in 2011, undercutting both Sub-Saharan African and global averages. The resulting four-notch improvement in Mozambique's overall Doing Business ranking over 2010-11 was thus almost exclusively concentrated on the "starting a business" indicator. This is incidentally the category on which performance dropped most sharply over 2012-13 (by 14 positions, see Table 3.1).

Mozambique's un-sustained performance on these rankings in part reflects the insufficiently facilitative role of the CPI and of BAUs in streamlining investment procedures. government's aim to have the "best Doing Business ranking in SADC by 2015" is unfortunately growing further out of reach – requiring urgent responses from investment policymakers. The forthcoming national export promotion and investment promotion strategies, under elaboration over 2012-13, may have the potential for tackling the variability and "one-shot" nature of earlier Doing Business improvements – by helping to embed such reforms within a broader and more strategic approach to long-term amelioration of the investment climate.

Table 3.1. **Mozambique Doing Business Survey results, 2012-2013 (out of 185 economies)**

Indicator	2012 rank	2013 rank	Change 2012/13
Starting a business	82	96	–14 decline
Construction permits	135	135	No change
Getting electricity	174	174	No change
Registering property	160	155	+5 improvement
Getting credit	127	129	–2 decline
Protecting investors	46	49	–3 decline
Paying taxes	103	105	–2 decline
Trading across borders	135	134	+1 improvement
Enforcing contracts	132	132	No change
Resolving insolvency	146	147	–1 decline
Overall rank	***146***	***139***	***–7 decline***

Source: World Bank, Doing Business Survey, Mozambique, 2013.

3.2. Establishment of an investment promotion agency

Has the government established an investment promotion agency (IPA)? To what extent has the structure, mission, and legal status of the IPA been informed by and benchmarked against international good practices?

Establishment and functions of Mozambique's Centre for Investment Promotion (CPI)

The CPI is Mozambique's official investment promotion agency. It was created by Decree 14/1993, and thus replaced the *Gabinete de Promoção de Investimento Estrangeiro* (GPIE) which had assisted the government in attracting FDI in early post-Independence years. The transition to CPI was aimed at enabling the agency to better meet the needs of a more liberalized economy. Decree 14/1993 coincided with CPI's work on the then up-coming Mozal project. With the creation of GAZEDA in 2010, CPI's role was narrowed to business promotion, information and marketing, while GAZEDA was entrusted with the management of Accelerated Economic Development Zones. Today CPI's main activities include targeted events, fairs, forums, official government visits and private sector missions; nevertheless CPI retains important regulatory functions as per the 1993 Investment Law, which sometimes generates investor confusion or conflicts of interest with its promotion and marketing functions.[7]

In addition to identifying and disseminating investment opportunities, CPI offers the following services to facilitate national and foreign investors' access to government investment incentives:

- institutional assistance to investors in approval and implementation of investment projects;
- promotion, reception and registration of investment projects;
- guarantee of fiscal and customs incentives to investors;
- identification of potential financial and/or technological partners for joint ventures; and
- promotion of business linkages between national and foreign companies (including through programmes of business development assistance, for SMEs and large companies – see 3.6 below).

In spite of these functions however, CPI has not yet been empowered as an effective One-Stop-Shop (OSS) for facilitating investment. There is also weak articulation and unclear lines of responsibility *vis-à-vis* other government agencies involved in the approval and monitoring of investment projects – including BAUs, but also a variety of sectoral investment promotion agencies (Table 3.2 below). The insufficient co-ordination of activities with these agencies is exacerbated by the absence of a national investment strategy document, which could provide all relevant bodies with shared guidance and long-term objectives.

Sector-specific investment and export promotion agencies

Table 3.2 outlines the functions of Mozambique's sector-specific investment and export promotion agencies, which operate alongside the CPI. These include GAZEDA for special economic zones, CEPAGRI for agriculture, and INATUR for tourism. In addition IPEME services the needs of small enterprises, and IPEX is mandated to coordinate policies and measures supporting the development of national exports. These agencies provide sector-specific support and guidance to investors – for instance in December 2011 CEPAGRI released a "Procedures Manual for Investment in Agribusiness", which clarifies basic operational procedures for investors in the industry. The Manual thus includes both general information for business operations in Mozambique (such as how to: establish a company; deal with labour relations; obtain approval for investment projects; and obtain water and DUAT land rights), as well as guidance more targeted towards agricultural investment (such as procedures for: obtaining an environmental license; importing and exporting pesticides; exporting fishery and horticulture products; and trading and producing seed).

Table 3.2. **Mozambique's sector-specific investment and export promotion agencies**

Investment promotion agency	Relevant Act	Related activities and implementation strategy
GAZEDA (Office for Accelerated Economic Development Zones; *Gabinete de Zonas Económicas de Desenvolvimento Acelerado*)	Established in 2007 based on the 1993 Investment Law, which allows for the creation of centres of economic development through the establishment of special economic zones.	GAZEDA has the responsibility to promote and coordinate activities related to the creation, development and management of Special Economic Zones, including Industrial Free Zones. The first and only area currently under GAZEDA jurisdiction is the Nacala Special Economic Zone (ZEEN).
CEPAGRI (Centre for Promotion of Agriculture, *Centro de Promoção da Agricultura*)	Decree 20/2006 under the Ministry of Agriculture (MINAG), with the mandate to promote investment in the agriculture sector.	CEPAGRI is notably responsible for facilitation of investment projects and articulation with different relevant ministries (especially MINAG) with respect to issues such as industrial licensing.
INATUR (National Tourism Institute, *Instituto Nacional do Turismo*)	Decree 36/2008, under which INATUR replaces FUTUR (Fundo Nacional do Turismo). INATUR operates under the Ministry of Tourism (MITUR).	INATUR engages in promotion and development of the tourism sector, the classification of tourism establishments, the development of tourism zones; and the promotion of touristic activities. Since its creation it has been engaged with the World Bank Group (IFC) on the Mozambique Tourism Anchor Programme, focusing on the roll-out of two Integrated Resort Schemes. This programme is facilitated together with the Ministry of Tourism and GAZEDA at country-level (see Box 3.1above).
IPEME (Institute for Small and Medium Enterprises, *Instituto para Pequenas e Medias Empresas*)	Decree 47/2008, placing IPEME operations under the Ministry of Industry and Trade (MIC)	IPEME operates to provide technical support to SMEs and to generally boost awareness of the challenges faced by small and medium businesses. IPEME has developed strategies for four sectors: agricultural commercialisation; textiles and clothing; chemicals; and rural industrialisation. It is also developing two programmes at the District level that target value-addition and competitiveness of SMEs in the agricultural sector (see Section 3.5 below).
IPEX (Export Promotion Institute, *Instituto para a Promoção de Exportações*)	Decree 25/1990, placing IPEX under the Ministry of Industry and Trade (MIC)	IPEX objectives include: increasing the export production base; promoting exports of local products; providing trade and commercial information to public and private sector interests; and assisting exporters with specific emphasis on SMEs. IPEX is based in Maputo with regional centres in Beira and Nampula. Since 2007 and based on analyses of constraints in the export value chain, IPEX has been active in locating international markets for Mozambique products.

Yet while at first glance this array of specialised agencies provides a clear investment and export promotion landscape, the operational reality is different. Much of the guidance made available by these agencies is firstly insufficiently disseminated, and more heavily geared towards domestic rather than foreign investors – the CEPAGRI manual for instance, while very helpful for investors, does not appear to have been widely circulated and is so far only available in Portuguese. More concerning, many of these agencies have insufficient capacity and little autonomy from their parent ministries. For example CEPAGRI's activities have so far focused more on serving the investment and planning needs of the Ministry of Agriculture (mostly through data collection and project registration) than on supporting investors in agriculture and agri-business. Nor is CEPAGRI actively involved in formulating or guiding the investment dimensions of government initiatives to stimulate the agricultural sector – such as the Agricultural Development Plan (PEDSA), the 2009-15 Strategic Biofuel Policy, or objective 1 of the 2011-14 PARPA (which aims to boost production and productivity in agriculture and fisheries).[8] More active involvement in investment policy formulation by a specialised body such as CEPAGRI could help strengthen the investment component of new agricultural strategies, and ensure that these are mutually beneficial to both small-growers and larger investors.

In terms of export promotion strategies, IPEX is similarly under-utilised. Although IPEX hosts two departments of significant strategic importance to the competitiveness of Mozambican production (namely, the Product Development Department which engages in sector development plans and collaborates in the design of export incentives; and the Market Development Department which identifies and promotes markets with high absorptive capacity), in effect the activities of these departments have so far been relatively constrained. Their functions are often overtaken by a dominant focus on the three other activities of IPEX: planning and statistical analysis; financial and administrative functions; and dissemination of trade-related information, including through the organisation of trade fairs. By contrast, there has in general been little emphasis on actively investigating investment prospects in innovative export sectors, and tackling supply-side barriers to export competitiveness. IPEX has nonetheless been more active on this front of late: with the support of the International Trade Centre over 2012-13, it has elaborated a national export promotion strategy which is currently awaiting government approval.

Need for co-ordinated investment and export promotion strategies

Partly as a result of IPEX's and other sector-specific investment promotion agencies' lack of capacity and strategic vision to date, there has been relatively limited domestic or international investment in areas such as

processing, manufacturing or agro-industry. For example the export promotion potential of the agriculture sector is vastly under-exploited: the government stance to increasing agricultural productivity in the PARPA 2011-14 focuses heavily on food security and subsistence farming, with little view to encouraging value-addition or to tapping external markets. The poor articulation between sectoral development plans and investment policy further penalises economic sectors with a strong growth and employment potential such as agriculture, tourism, manufacturing and construction.

The ongoing elaboration of both an export promotion strategy (by IPEX since 2012) and a national investment promotion strategy (by CPI together with other investment promotion agencies over the course of 2013) are therefore extremely promising and necessary moves. It will be particularly important to ensure that these strategies are aligned with each-other and that mechanisms are in place to co-ordinate the work of each their respective implementing agencies. These strategies will also need to be coherent with the existing business improvement strategy and overall national development goals (under EMAN and PARPA), so as to significantly enhance export performance and contribute to stabilising Mozambique's current account balance.

The forthcoming export and investment promotion strategies will need to go hand-in-hand with a pro-active and well-targeted strategy for short and long-term human resource development. This would help expand formal employment opportunities by encouraging the development of labour-intensive industries outside of mega-projects, and increasing the integration of these industries into global value chains. Indeed although linkage programmes around extractive industry investments have certainly created local employment and value-addition (as detailed in Section 3.6 below), these contributions are limited by the capital-intensive and import-reliant nature of most mega-projects. Addressing human resource constraints on the supply-side would moreover expand opportunities for SME linkages by providing multi-national enterprises and international investors with competent and reliable local suppliers. In addition, SMEs could also benefit from clear export guidance, ranging from simplified procedures and information on quality standards to export market identification.

It will be important to directly involve all sector-specific investment promotion agencies (from CEPAGRI to INATUR and IPEME) in the elaboration and roll-out of these national investment and export promotion strategies, in close collaboration with CPI and IPEX. At the Ministerial level, Mozambique's Investment Council could have an important guiding and co-ordinating role to play (see 3.4 below). There is thus a strong need, on both investment and export fronts, for the responsibilities of sectoral agencies to stretch beyond registration and data collection functions. In order to bring relevant inputs to the current momentum for enhanced trade and investment policy formulation and

implementation, these agencies will need to be staffed and capacitated accordingly. Sector-specific agencies will also need to more clearly define their roles *vis-à-vis* CPI, and to develop stronger private sector representation and sufficient political support.

3.3. Benchmarking and monitoring of the Investment Promotion Agency

Is the IPA adequately funded and is its performance in terms of attracting investment regularly reviewed? What indicators have been established for monitoring the performance of the agency?

CPI funding and performance evaluation

CPI functions under the Ministry of Planning and Development, but is administratively autonomous. 60% of CPI budget is funded by government, with remaining funds obtained from investment application fees and donor support. Project management (including processing applications and monitoring authorised projects) accounts for the large majority of budget spending. Yet CPI has no public monitoring performance indicators; its internal indicators focus on its own events and activities, not on their impacts on investment, and their efficacy is thus not known.

The only completed evaluations of CPI performance have therefore been undertaken externally. A 2004 review by the South African Institute of International Affairs (SAIIA) for instance investigated the experience of South African firms in doing business in Mozambique, and noted that most South African investors entered the Mozambican market through the CPI's assistance but later encountered a series of delays when approaching other government departments to complete their business registration. These resistances, in spite of investors detaining the CPI's official approval, suggest that CPI does not effectively function as a One-Stop-Shop for investment; it is not sufficiently empowered so as to accelerate investment approval processes in other government departments, including as concerns access to land titles.[9] More recently, the 2012 UNCTAD review of Mozambique's investment policies adopted a specific focus on the CPI in response to government request. Among other conclusions, this report recommends sharpening the focus of the CPI on promotion rather than regulation of investment, and possibly eliminating CPI's role in delivering investment licences.[10]

While such external studies are clearly beneficial and do provide some idea of the quality of the CPI's track record, they cannot compare with a strong, systematic and publicly available performance management system

implemented by CPI itself. Developing such a system, based on regular feedback from investors as well as specific indicators of progress, would be an important step toward increasing the effectiveness and transparency of investment promotion activities in Mozambique. Moreover CPI performance should be discussed regularly on various platforms for investment policy dialogue (with the Investment Council, but also with the private sector – see Section 3.4 below) in order to enhance the legibility of Mozambique's investment framework and to build investor confidence. Both of these elements should be fully reflected in the investment promotion strategy currently under elaboration by CPI and sector-specific investment promotion agencies.

3.4. Consultative framework among government, the IPA and investors

In its capacity as a facilitator for investors, does the IPA take full advantage of information on the problems encountered from established investors? To what extent does the IPA promote and maintain dialogue mechanisms with investors? Does the government consult with the IPA on matters having an impact on investment?

Existing platforms for public-private communication fall short of their potential

Although investor consultation is an essential component of investment policy formulation and adjustment, government under-utilizes the available platforms for dialogue with the investor community (listed below):

- The **Confederation of Business Associations of Mozambique** (CTA, for which membership is open to business associations). CTA is the main umbrella private sector group in Mozambique, and has five sectorial working-groups (on tourism; civil construction; agribusiness; industry, commerce and services; and transports) as well as four cross-cutting working-groups (labour policy; financial policy; public services policy; and fiscal policy, customs and trade). These groups aim to: reduce or remove administrative barriers to business; create an appropriate framework for economic and sectorial policies; improve the conditions of basic infrastructure; and establish a venue where the business community can voice suggestions for policy and/or legislative improvements. The stated purpose of these working-groups is to create and promote debates between the government and the private sector on prioritised issues, with focal points on the government side. government has held annual meetings for

over a decade with the CTA, to discuss issues of mutual concern. CTA also comments proposed regulations that may have an impact on foreign and domestic investors.

- The **Association of Commerce and Industry** (ACIS), a non-profit business association representing over 300 companies throughout Mozambique, and for which membership is open to individual businesses. ACIS services include translations of relevant Mozambican legislation into English, publications including Legal Framework Guides which are designed to assist existing and potential investors, and participation in business promotion events.
- The **Investment Council**, the government body at the ministerial level responsible for consultation and coordination of investment promotion policies (see 2.1 above). The Investment Council meets every trimester. Its role involves: proposing policies to promote, encourage and accelerate national and foreign investment in Mozambique; coordinating the actions of the various government bodies to improve the investment environment; advising on proposed legislation and other legal instruments that have an impact on the promotion and attraction of investment; reviewing investment project proposals with large financial and socio-economic impact; and proposing measures to the Council of Ministers for the development of Industrial Free Zones and Special Economic Zones.

Despite the existence of these platforms, focused efforts on behalf of investment agencies and ministries to fully utilise them and to seek direct feedback from all stakeholders is lacking. Moreover, in most communication with these investor platforms as well as with individual investors, the Ministry of Industry and Commerce functions as the lead interlocutor instead of CPI. Rather than an agency that is broadly competent for interacting with established investors, CPI's role is therefore largely relegated to branding the country and to attracting investors. As a result, policy changes affecting the private sector and investors in Mozambique have been greeted with increasing frustration in recent years: each major adjustment to investment conditions and incentives (such as the 2007 Labour Law, the 2009 Foreign Exchange Law and the 2011 PPP Law) has been accompanied by regular and conflictual interactions with industry and investors who do not believe that their concerns are well understood by policymakers. For instance the "export surrender" requirement contained in the 2010 Regulations of the Foreign Exchange Law (requiring exporters to hold 50% of their export revenues as local currency in Mozambican banks) has evoked strong private sector objections.

These negative perceptions have frequently made concrete dialogue between CTA and the government conflictual rather than constructive. A more

carefully-structured and openly consultative framework for gathering investor inputs to investment policy evaluation and formulation, particularly by reinforcing the institutional role of CTA, would be worth considering. Possible mechanisms for more fruitful platforms of public-private dialogue could notably be established within the forthcoming national investment and export promotion strategies; in fact private actors should be regularly consulted during the elaboration process of these strategies themselves, and private sector inputs should also be sought after for any necessary revisions once the strategies are released in 2013.

3.5. Evaluation of investment incentives

How is the legal framework for investment incentives defined? Has a public statement of all tax incentives for investment and their objectives been made within a common governing framework? Have efforts been made to consolidate all tax incentives within the tax law, so as to increase their transparency?

Transparency and clarity of legal framework for incentives

Tax incentives should only be granted in accordance with a comprehensive policy, which lays down principles and policy objectives for the introduction or continuation of each incentive. Governments should provide a justification for tax incentives (such as regional or territorial development, employment creation, etc.) together with the expected costs and intended benefits. These objectives and their rationale should be communicated publicly through regularly updated statements, so as to provide the basis for the assessment of tax incentives, to avoid overlap and duplication, and to allow governments to be held accountable for all tax incentives granted.

Moreover, for transparency reasons it is important that tax incentives for investment be provided through tax laws only – such as the income tax law, rather than dispersed across multiple laws governing investment (including Special Economic Zones laws and procurement laws, as well as stand-alone decrees, agreements and regulations). Such dispersion in the legal provision of tax incentives creates grounds for duplication and can hide the true extent of the incentives. Rather all tax incentives provided, along with their eligibility criteria, should be consolidated and publicised in the main body of tax law, in order to increase transparency and to empower the tax authority in its administration of investment incentives. This consolidation can also ensure that all tax incentives are scrutinized by the law, and thus facilitate their ratification of through law-making bodies or parliament.

Mozambique's 2009 Code of Fiscal Benefits (CFB)

As mentioned in Chapter 1, tax incentives in Mozambique are determined by two tax benefit "packages": the 2009 Code of Fiscal Benefits (CFB) and the Regulation of this Code (RCFB). These pieces of legislation replace the 2002 CFB Code and were introduced in 2009 to rationalize the incentives regime and enhance its cost-effectiveness. The CFB notably eliminated the "exceptional incentives" for investment in mining and petroleum concessions that were defined under the 1993 Investment Act, and cut the eight-year 25% tax reduction for investment in mining. As such the 2009 reform is an important step towards the international best-practice described above, as it groups almost all investment incentives in Mozambique (including for Special Economic Zones) within a single legal document. Moreover the CFB is made integral to Mozambique's body of tax laws – Article 53 of the CFB states that, "the provisions of the Corporate Income Tax Code, the Personal Income Tax Code, the VAT Code, the Customs Dispute Procedures, the Tax Dispute Procedures, the Tax Executions Code and any other applicable legislation shall apply to any omission in the Code, unless contradicted by the provisions of the Code".

However the reach and clarity of this legal framework for investment incentives remains undermined by the fact that additional incentives in the mining and petroleum sectors still fall under the Mining and Petroleum Law. Additionally, the fact that access to incentives in Mozambique is made conditional on obtaining the CPI investment license is at odds with international best-practice. It is recommended that any taxpayer meeting the conditions for prescribed tax incentives under the relevant tax laws (such as the CFB 2009) be able to claim these incentives, without negotiating with any granting authority (such as the CPI or a given ministry). In Mozambique by contrast, it remains necessary for investors to obtain the CPI license before the incentives of the CFB 2009 are concretely accessible.

The CFB 2009 scales back tax holidays, while providing the following benefits: tax deductions; deductions from taxable income; accelerated depreciation and reintegration; investment tax credit; and exemption and reduction of tax rates, together with deferral of the tax payments. Chapter 1 of the CFB covers generic benefits (on import of goods, under Section 1 of the chapter, and fiscal benefits in respect of income, under Section 2). Generic benefits in respect of income for example include a deduction of Corporate Income Tax (IRPC) over the first five years of a project – this deduction reaches 5% of the total investment value in Maputo, and 10% in other regions. Investments in certain tangible fixed assets (including construction and repair of buildings, passenger vehicles, and social equipment among others) are excluded from these provisions. Meanwhile Chapter 2 of the CFB (Sections 1 to 10)

addresses specific benefits, which are available to the following ten sectors of material importance to national economic policy:[11]

- basic infrastructure creation (such as rehabilitation of roads, rail, airports, water supply, electricity and telecommunications);
- commerce and services in rural areas;
- manufacturing, transforming and assembly (where annual invoicing must exceed 3 million meticals or USD 104 500, and where value-added on the final product must reach at least 20%);
- agriculture and fishery;
- hotelry and tourism;
- science and technology parks;
- large-scale projects (investments that exceed 12 billion 500 million meticals, or USD 434.2 million, as well as investment in public domain infrastructure);
- rapid Development Zones (areas of considerable natural resource potential, but lacking in infrastructure and economic activity);
- industrial Free Zones; and
- special Economic Zones.

The above categories benefit from one or more of the following tax incentives:

- approximately 80% reduction in corporate income tax over 2009-15, and 50% reduction over 2016-25 (the specific rates and durations vary by category – for instance IFZ projects obtain full IRPC exemption for the first ten years of operation, and SEZ projects for the first five years; meanwhile Large-scale projects do not benefit from any reduction in IRPC);
- VAT benefits (exemption from payment of customs duties and VAT for equipment classified as class "K" of the Customs Tariff Schedule, including spare and accompanying parts).
- incentives for professional training (under Article 18 of the CFB, costs of investments in training of Mozambican employees are deductible from taxable income for the first five years of operations); and
- incentives for modernization and new technology use (under Article 17, the amount invested in specialised equipment using new technology can be deducted from taxable income upto a ceiling of 10%, and for the first ten years of operations – although what qualifies as "new technology" is not clearly specified in the Code).[12]

How are tax incentives administered and governed? Are incentives placed under the authority of a single government body to ensure transparency and avoid unintended overlap and inconsistencies in incentive policies? Is the amount of revenue loss attributable to tax incentives reported upon regularly, for instance as part of an annual Tax Expenditures Report?

Administration and governance of tax incentives

Where various Ministries are involved in the administration and granting of tax incentives, they may not coordinate their incentive measures (tax and non-tax) with each other or with the national revenue authority. As a result incentives may overlap, be inconsistent, or even work at cross-purposes. Administrative discretion in the management of incentives also seriously increases the risk of corruption and rent seeking. Moreover, once particular tax incentives are introduced this creates constituencies in their favour, which in turn can make it politically difficult to remove the incentive once it is no longer needed or has proven to be ineffective.

It is therefore considered good practice to place all tax incentives under the authority of one government body, ideally the Ministry of Finance, rather than under the responsibility of several different ministries (such as trade or investment or other ministries). Consolidating administration of all incentives under a single body can: limit risks of corruption and rent seeking; increase transparency by limiting the discretionary power of policymakers; help to avoid unintended overlap and inconsistencies in incentive policies; and enable policymakers to coherently address problems that may arise with the governance of tax incentives. In Mozambique, since 2007 the authority of the Council of Ministers to negotiate special tax arrangements and fiscal benefits for mining and petroleum projects has been removed; this is a positive step toward consolidating the administration of these incentives. In addition the 2009-10 Strategic Plan for Reform of the Tax Authority (Autoridade Tributária) aims to create an integrated central management for large taxpayers and mega-projects.

Reporting of tax incentives and calculation of revenue forgone

Tax authorities should also periodically carry out audits of cases where tax incentives have been claimed to ensure that they are not misused. Although Article 8 of the CFB makes provisions for regular inspections and audits by the tax administration, this is a front on which the Mozambique Tax Authority (AT) remains insufficiently active. The CFB also specifies minimum transparency conditions to be met by taxpayers (such as: tax registration and accounting standards, under Article 9; submitting a declaration with the

amount of investment realised and the respective calculation of the value of the tax benefit provided, under Article 12; and payment of taxes to the State Treasury, under Article 49). Under Articles 49 and 50, infractions to these requirements may result in suspension of the incentives. These requirements could be made more specific, for instance by detailing the items for inclusion within the tax return (both regarding VAT and Income Tax incentives). In addition to enhancing transparency, such taxpayer information could contribute to data for determining the efficiency and equity of tax incentives (see below).

Other recommendations for transparent and effective governance of tax incentives include calculating and regularly reporting on the amount of revenue forgone attributable to tax incentives for investment – ideally through an annual, publicly released statement of tax expenditures which covers all main tax incentives. This requires that data be collected systematically to underpin the statement of tax expenditures. Such calculations can shed light on the revenue cost of tax incentives, rather than scrutinising cash expenditure budgets alone. Embedding estimates of revenues forgone by tax incentives in the yearly budget process can provide policymakers with timely required inputs for informing policy decisions, and support medium-term fiscal planning. The calculation of revenue forgone is particularly important in the case of long-term investments such as mineral extraction, where realisation of revenues may take many years and where losses need to be assessed over the life of the projects. Annual tax expenditure reports can also highlight the largest beneficiaries of tax incentives for investment, as making such information accessible can enhance the public legitimacy of governments and their revenue authorities, and enhance tax compliance more broadly.

What mechanisms has the government established for the evaluation of the costs and benefits of investment incentives, their appropriate duration, and their impact on the economic interests of other countries?

Impact evaluation of tax incentives

Internationally, strong evidence increasingly calls into question the effectiveness of some tax incentives for investment – in particular tax free zones and tax holidays. Ineffective tax incentives are no compensation for, or alternatives to, a poor investment climate. They may be unsuccessful in attracting sustainable investment, and may damage a country's revenue base. There is a significant regional competition dimension in the granting of investment incentives as well, where a "race to the bottom" on tax incentives

among neighbouring countries may make competing countries in a region collectively worse off. Indeed, as tax incentives are often provided in response to what neighbouring countries and competitors are offering, the issue of tax incentives cannot be tackled in isolation. Governments can work together on a regional basis to increase co-operation in the area of tax.

These many national and regional risks make it essential to adequately analyse the costs and benefits of investment incentives in a national context, to support government decision-making and allow frequent review of incentives provided. In Mozambique as in many other countries, there is limited data collected on granted tax incentives – including on the qualifying investments made, direct and indirect benefits to the host economy, and the fiscal cost of these incentives. Moreover even information that should be more readily available – such as lists of tax incentives and beneficiaries – is not widely available in Mozambique, outside of the information provided within the regulatory framework of the CFB 2009.

In order to ensure that incentives are fulfilling their objectives, i.e. attracting more investment, they also need to be subjected to both *ex ante* and *ex post* evaluations to determine their effectiveness and their impact on the national budget. Performance reviews of tax incentives for investment may be conducted once every few years and should include the costs as well as the benefits of the tax incentive and if it has met its intended goals. This requires that data be collected systematically by tax authorities and the Ministry of Finance. The results of such periodic reviews, publicly reported together with the review criteria, can inform decision-making around the continuation or removal of individual tax incentives. These assessments should involve open public consultation so as to accurately include social – and not only financial – costs and benefits in the analysis. Authorities also need to consider their commitments under international agreements, to ensure that incentive schemes remain consistent under these.

No systematic evaluation of incentives is conducted internally in Mozambique

Taxes on company income in Mozambique are not particularly high relative to other countries in the region. Mozambique might consider making taxation for mega-projects (especially in mining and petroleum) stricter: in light of its attractive natural resources, tax incentives might not be indispensable for attracting mega-project investment. This could create fiscal space for reducing tax rates for SMEs, and for greater spending in infrastructure, education and security – which are the real drivers of investment decisions. However regular evaluation of the impact of tax incentives on investment, which could help guide and justify these re-allocations, is lacking. Domestic studies evaluating the impact of fiscal incentives for investment have been

very rare, with the exception of a study led by the Tax Authority in 2009 in the lead-up to passing the revised CFB. Instead, most evaluations of tax incentives remain externally-led. These include a 2006 FIAS study, which provides a summary of tax policy and administration (including incentives and the effective tax burden both economy-wide and by sector), and IMF staff reports in the context of Reviews under the IMF's Policy Support Instrument for Mozambique.[13]

Domestic cost-benefit evaluations are also necessary for Mozambique's accelerated economic zones. The only area currently under GAZEDA jurisdiction is the Nacala Special Economic Zone (ZEEN), located at the end of the Nacala Development Corridor (CDN) that links the provincial capital Nampula to Malawi and Zambia.[14] The government aims to complete creation of seven IFZs and one SEZ in Nacala before 2014.[15] Given this current push for SEZ and IFZ creation, investment policymakers and GAZEDA would do well to carefully investigate the social and economic benefits provided by such zones, as well as the extent to which they are streamlined with Mozambique's overall investment strategy and its policies aimed at developing human resources, removing trade barriers and the like.

Transparency in the management and fiscal sustainability of mining investment incentives should improve with Mozambique's entry to the Extractive Industries Transparency Initiative (EITI), expected before mid-2013. In the context of its EITI candidacy, the government is considering options to enhance revenues from the natural resources sector. This includes: analyzing the perspectives for potential renegotiation of fiscal benefits and incentives with willing investors, while safeguarding the stability of the business climate; and assessing the feasibility of creating a stabilization fund that could channel revenues from Mozambique's minerals endowment to targeted long-term spending.[16] Mozambique's Ministry for Mineral Resources is currently developing a new Mining Law, which is in the process of being approved by the government for 2013 and which has the objective of "streamlining and simplifying procedures" for investors. Aside from minor modifications to royalties, this law is however not expected to change the tax rates faced by mining companies in the exploration phase. The legislation will seek to increase taxes only for companies moving to the mineral production phase (a novel stage for many of Mozambique's mining companies). The law may also oblige mining companies to invest in infrastructure and schools – though it is not yet clear how these obligations will be specified or enforced.[17] In the lead-up to preparing this law, it becomes particularly urgent for the government to take effective action on both evaluation and gathering incentive data, which could help update investment incentives rather than leaving them untouched.

3.6. Promotion of business linkages and addressing SME challenges

This section first outlines several key challenges for SME development in Mozambique: regulatory and supply-side constraints; fiscal challenges; and difficult access to finance. Government efforts to address these constraints are then detailed. These different obstacles all limit the extent to which SMEs can tap into the overall benefits that the economy derives from mega-project investment and FDI. This investigation is followed by analysis of a closely related topic: existing initiatives to develop business linkages between large-scale (foreign as well as domestic) investors, and smaller enterprises in Mozambique.

What measures has the government put in place to address the specific investment obstacles faced by SMEs, and to facilitate investor access to finance?

Regulatory and supply-side constraints to SME development in Mozambique

SMEs are numerous in Mozambique; they account for 42.8% of private sector employment, approximately 12% of which are engaged in productive activities (agriculture, manufacturing and construction) and the rest in retail trade.[18] Yet important investment barriers still remain for SMEs across all economic sectors, and prevent them from effectively latching onto business linkage opportunities (see below). In the tourism industry for example, heavy bureaucratic requirements such as licensing pose a bigger barrier to entry for small companies, and as a result informal operators have a large share of the market. Meanwhile in the agricultural sector, although important agro-business opportunities exist in Mozambique (including in rice, sugar, ethanol, biodiesel and horticulture), the enabling investment environment is very poor for the small-scale farmers that make up 99% of farming activity in the country: about 5% of farmers have access to credit, 35% have adequate access to price information, and 14% have access to extension services. Productivity-enhancing inputs such as fertilizer, irrigation or animal traction are also rare (4% for the first two and 11% for the latter).[19] Poor contract enforcement, access to finance (detailed below), and implementation of regulations, are prohibitive for SMEs across economic sectors. This is exacerbated by the fact that most SMEs side-step registration with the CPI for cost and time reasons – thereby forfeiting access to the CPI's certificates of incentives, as well as to the investor protection clauses of the 1993 Investment Law.

Linkages in the tourism sector (among other sectors) have also been underexploited due to inadequate supply in the local economy: most of the inputs for hospitality and tourism businesses are partly or wholly sourced from outside Mozambique, as local markets (even for raw products such as fruit and vegetables) are considerably underdeveloped. Over 90% of skilled labour in tourism was likewise sourced from South Africa in 2006.[20] These human resource and capacity constraints create a gap on the domestic supply-side, which compounds the lack of an enabling SME business environment. Combined, these factors severely hamper the development of the tourism sector at large, by limiting the potential for selling in international markets and by compromising quality of service (safety regulations are for instance not systematically enforced, which precludes a significant number of firms from contracting for international tour operators).[21] In investigating the different linkage initiatives discussed below, it is important to keep such supply-side constraints in mind. Indeed, human resources and productivity are indisputably a challenge in Mozambique, and there is a clear need for improving long-term investment in education and sector-specific vocational training. In the short term, providing training to expand ancillary services, and identifying which key inputs can best be sourced locally so as to focus on development of those markets, can be helpful first steps.

Fiscal challenges facing SMEs

Some revisions of the tax structure have been made since 2009 to encourage more SME investment in sectors with high-employment and value-addition potential. This notably includes enactment of the Simplified Tax for Small Contributors (ISPC, Law 5/2009): this law is designed to make formalization more attractive by providing a simplified regime for enterprises with a turnover less than 250 million MT (USD 8.6 million) per year. Enterprises with a turnover of up to 36 times the minimum wage are moreover exempt from tax. The ISPC thus reduces effective tax rate from approximately 7% of turnover to 3%, develops simpler registration procedures, and plans to increase geographical outreach by opening new offices and launching mobile tax units for peri-urban and rural SMEs. Certain dimensions of the regulatory framework for investment likewise aim to lighten the administrative load on smaller firms. The costs of inspection for investment projects in the industrial licensing process are for instance adjusted by company size: inspection is not required for micro-firms, and inspection costs are multiplied by a factor of two, four and six for small, medium and large firms respectively. Similar calculations apply to taxes.[22] However despite thes reforms, the ISPC law does not address the basic reasons for which SMEs continue to operate on an uneven playing field *vis-à-vis* large companies – and in particular the fact that access to major tax incentives remains conditional on obtaining an investment license from the CPI, a heavily bureaucratic procedure which many smaller companies bypass.[23]

Nevertheless, several fiscal obstacles continue to compound the supply-side capacity constraints mentioned earlier. These include: a low tax yield and narrow tax base; excessive complexity of the tax system; lack of public information; and poor compliance and arbitrary enforcement. In addition SMEs have differential access to tax incentives, since these are made available only by registering with the CPI. As a result companies that access tax incentives enjoy a competitive advantage, while the tax rate faced by smaller non-incentivised companies is higher than in neighbouring countries.

Difficult access to finance for SMEs and other businesses

The quality of the regulatory framework in the financial sector, and the level of accessibility for all types of investor (domestic and foreign, large and small) are both crucial for ensuring that the financial sector effectively supports enterprise development. In Mozambique, regulation of the financial sector has improved significantly since the banking crisis of 1998-2000. Financial Sector Assessment Programmes undertaken by government in conjunction with the World Bank and the International Monetary Fund have helped reinforce the regulatory and competitive environment of the sector since 2005. The national financial system has accordingly begun showing some visible improvements: the banking system is steadily growing, and financing of the private sector through the national banking system doubled in 2010-11. Changes that have come about as a result of the on-going Financial Sector Assessment Programme include:

- strengthening the regulatory and supervisory roles of the central bank, *Banco de Moçambique* (together with a possible financial surveillance system, and a stronger framework for oversight of non-banking financial institutions);
- opening the banking sector to competition (including to micro-finance institutions, although more competition would remain necessary to further raise deposit mobilisation and lower borrowing costs);
- strengthening social security coverage and management;
- improving the legal and judicial environment for loan provision operations;
- extending financial services, especially to rural areas; and
- a raft of on-going financial regulation to address concerns such as money laundering, exchange management, national payment systems, bankruptcy, collateral requirements, and credit information and regulation.

Nonetheless, beyond financial regulation and creditor protection, the difficulty of accessing credit is a central factor inhibiting private investment in the country – particularly for smaller enterprises and in the agricultural sector where the absence of collateral is a very constraining issue. Moreover SOEs dominate the enterprise sector, accounting for 80% of total credit to "private"

sector enterprises and effectively crowding out smaller firms.[24] Mozambique's performance under the World Bank *Doing Business* 2012 report has therefore been particularly disappointing in the "Getting credit" indicator, where it has fallen by 20 notches since 2011 (now ranking 150th out of the 183 countries covered). Poor legal rights for borrowers and creditors are responsible for much of this shortfall. Overall, lack of finance remains frequently cited as one of the most important constraints for businesses in Mozambique. High interest rates continue to challenge SMEs in particular: Box 3.1 highlights some key features of difficult access to finance for Mozambique's SMEs.[25]

Box 3.1. **Causes of difficult access to finance in Mozambique**

Mozambique's financial infrastructure is improving, but more needs to be done to support the growth of the private sector. Poor access to finance is a result of the following features:

- *Highly concentrated banking sector:* Two-thirds of commercial banks hold close to 90% of total financial assets in the country. These provide services primarily to enterprises that are larger, audited, and able to provide collateral – in 2008 78% of firms responding to a 2008 World Bank Enterprise Survey had an effective demand for credit, but only 13% of these obtained credit from the banking sector. The situation does not appear to have changed significantly since. Meanwhile the microfinance segment, destined to assist smaller enterprises, is relatively small and highly concentrated as well.
- *Geographic distribution of banks:* Most credit institutions are still concentrated in Maputo city. Although commercial banks have embarked on expanding their services in rural areas, poor rural infrastructure is slowing the shift towards a banked economy. As a result the ratio of private credit to GDP remains below the sub-Saharan average, particularly for rural areas. Clearly this geographic component is also an inhibitor to the valorisation of the agricultural sector, which remains far behind the extractive sectors in terms of access to banks and credit.
- *A comparative disadvantage for SMEs:* Limited competition in the banking sector has created a non-dynamic financial system with low levels of financial intermediation, high profit margins, excessively high fees on banking services, and a large interest rate spread between deposits and loans. This stifles innovation, job creation and productivity in small-scale sectors such as agriculture, and hinders the regional competitiveness of local enterprises: Mozambican firms are for instance at a large disadvantage when compared to firms in Zambia and especially in South Africa. Excessive domestic borrowing by the government has moreover put upward pressure on interest rates in recent years, at the risk of crowding out the private sector.

Source: World Bank Enterprise Surveys, Mozambique.

Recognition of SME needs in government development strategies

In recognition of these challenges (both process-based and supply-side), the government of Mozambique has defined a strategy for SME development for the period 2007-12.[26] This intends to consolidate the base for SME development by addressing the challenges posed by: variations in sector policies; regulatory barriers; limited and costly financial resources; high fiscal burden;[27] poor market access; and a weak entrepreneurial culture and insufficiently qualified workforce. Some business licensing procedures, as well as tax levels, are also adjusted according to the size of enterprises. This is for example the case of the industrial licensing procedure, which is required of most projects that do not qualify for the provisions of the 2008 Decree on Simplified Licensing: micro-industry is not required to obtain an industrial license and is only required to register as a commercial venture; meanwhile small-scale industrial licenses are issued at the provincial level; and only licenses for medium- and large-scale industrial projects are issued at national level, by the Ministry of Industry and Commerce.[28]

The national procurement law also includes some benefits for SMEs,[29] and the 2011-14 PARPA places a central focus on SME development and the promotion of investment linkages (see Box 3.2). This focus on SME challenges within the PARPA is encouraging; nevertheless, the scope of the PARPA with respect to SMEs is ambitiously broad; a clearer sequential prioritization of initiatives may be necessary in order to secure all these improvements by 2014. Moreover, the PARPA lacks a clear definition of how responsibilities for these SME-related activities will be administratively shared – more explicit mention of the respective roles of IPEME, GAZEDA, CPI, CEPAGRI and other related bodies would be necessary so as to minimize duplication and ensure that concrete progress is made toward these necessary targets.

Box 3.2. **SME-relevant objectives of the Poverty Reduction Action Plan (PARP) 2011-14**

General Objective 2 of the PARP 2011-2014 (for employment promotion) lists the following steps for facilitating SME development, access to finance, and linkages with mega-project. While very broad-ranging, these targets are highly encouraging in that they are a clear indication that the government of Mozambique is fully cognizant of the need to diversify the economy into more labour-intensive sectors instead of relying too heavily on mega-project development. Making progress towards any of these three objectives will play a key role in better integrating MSMEs in the country's economic development, and increasing employment generation both inside and out of the mining sector.

Box 3.2. **SME-relevant objectives of the Poverty Reduction Action Plan (PARP) 2011-14** *(cont.)*

Sub-objective 1: Favourable investment environment for MSMEs and expansion into labour-intensive industries

- approve and implement the general statute of MSMEs, establishing a new classification of MSMEs that accords them specific treatment;
- generalize the simplified licensing regime for economic activities, and extend it to other areas (in particular, approve and implement the "negative licensing regime" for micro-enterprises);
- special tax regime for micro-enterprises, which will simplify procedures by moving to payment of tax liabilities on a quarterly installment basis, with filing of a simple form and the NUIT ("single taxpayer identification number");
- create "business incubators" to foster the development of MSMEs by training entrepreneurs to transform business ideas into successful projects, and ensure that entrepreneurs can make use of incubator equipment and facilities until they reach the "maturity" phase;
- create industrial parks to attract investment for the country's development, giving pride of place to MSMEs;
- establish Knowledge Transfer Centers and make them operational, so that local communities can learn to use agro-processing equipment, good practices for managing industrial units, and procedures for creating a firm. The centers will also be able to process local products; and
- proceed with land zoning for purposes of agricultural and industrial activity and facilitate the award and transfer of titles for land use and management.

Sub-objective 2: Access to credit and to services for the support and development of MSMEs

- Expand the Entrepreneurial Guidance Centers at the provincial level in order to train local entrepreneurs in the preparation of business plans, entrepreneurial management, and procedures for creating a firm, and to make useful information available to entrepreneurs.
- Create a comprehensive service to provide financing and support to MSMEs, with a focus on women.
- Promote and encourage the development of initiatives for adding value to natural resources, with special attention for those that allow greater participation by women.

Box 3.2. **SME-relevant objectives of the Poverty Reduction Action Plan (PARP) 2011-14** *(cont.)*

Sub-objective 3: Promote linkages between small and big firms, with emphasis on megaprojects

- Create programmes for linkages/complementarity between MSMEs and big companies with a view to encouraging the provision of goods and services.
- Identify geographic sites for the creation of specialized financial markets grouping firms engaged in the same branch of activity, with a view to enhancing their competitiveness, reducing transaction costs, encouraging specialization, and attracting other businesses.

Source: Republic of Mozambique. "Poverty Reduction Action Plan (PARP) 2011-14", 3 May, 2011.

More specifically concerning access to credit, *Banco de Moçambique* is working in collaboration with the private sector and the International Finance Corporation to create a registry of borrowers to strengthen banking supervision and manage risk. This should support the use of property as collateral and thereby expand small business access to external sources of credit. Attempts to improve SME access to finance have also been undertaken within the IFZ context: Mozal has for instance begun developing a triangular arrangement with local banks and its SME sub-contractors, whereby Mozal is the SME's guarantor *vis-à-vis* the bank and loan amortization is deducted from Mozal's payments for the SME's services.[30]

Government agencies promoting the development of SMEs: IPEME and INNOQ

Addressing SME needs in Mozambique falls under the responsibility of IPEME, the Institute for Small and Medium Enterprises. Placed under the Ministry of Industry and Commerce, IPEME is working with the National Statistics Institute (*Instituto Nacional de Estatísticas, INE*) and the Tax Authority to establish a single definition of SMEs (as currently each sector has its own definition, which leads to divergent data). In addition to this definitional work, as part of the national SME strategy the government is preparing legislation on SMEs to consolidate and expand policy measures to support SME development. IPEME has started to include SMEs in government trade-promotion missions, as well as in fairs for networking and marketing focused on SMEs. The German International Co-operation (GIZ) is supporting the development of a monitoring and evaluation procedure for IPEME.

IPEME has developed strategies for four sectors: agricultural commercialisation; textiles and clothing; chemicals; and rural industrialisation. It is also developing two programmes at the District level that target value-

addition and competitiveness of SMEs in the agricultural sector: *Cozinha Mocambique* (Mozambique Kitchen, which provides mobile capacity building for entrepreneurs on increasing value-added in food production); and CaDUP (*Cada Distrito Um Produto* or "Each District One Product", which will establish demonstration centres where entrepreneurs learn about processing techniques for agricultural goods). CEPAGRI and the national tourism development institute, INATUR (*Instituto Nacional de Turismo*), have also actively started to develop SME-oriented programmes.[31]

The Centre for Entrepreneurial Advice (*Centro de Orientação ao Empresario*, COE) was additionally set up by IPEME in August 2010 to disseminate information on investment opportunities, training and marketing. The ultimate goal is to engage SMEs in improving the quality and quantity of agricultural products, and to match the quality standards of both local and external markets.[32] The support most commonly requested of COE is for business plan design, starting a company, sources of financing, organized accounting, and general business advice. Although initially COE was only operational in Maputo, starting in 2011 other centres have progressively been opened in Manica, Tete and Sofala provinces – with the goal of reaching all provinces by end 2013. IPEME also plans to expand the COE SME advice service to the district level through District Centres for Entrepreneurial Advice (*Pontos de Orientação ao Empresario*, POE).

Another organisation that has a potentially significant impact on SME investment and development is the National Institute of Standardization and Quality (*Instituto Nacional de Normalização e Qualidade, INNOQ*). INNOQ was created through Decree 2/1993 under the direction of MIC. INNOQ has been supported by government and donors since 2006 in terms of training and technical resources. INNOQ certification is necessary for firms' marketing purposes, and is a requirement for companies supplying government under the national procurement code. INNOQ plans to work in collaboration with IPEME on certification issues applicable to SMEs, which could help open new markets for the latter.

What steps has the government taken to promote investment linkages between businesses, especially between foreign affiliates and local enterprises?

Business linkage development allows local business to participate in major investments, thereby potentially improving local competitiveness, service quality and overall community development. Business linkage programmes usually take the form of local supply chain development in

which a lead company (be it foreign or domestic) develops local suppliers; this can help smaller-scale companies to improve strategic production areas such as quality, just-in-time delivery, safety, health and environment standards. Especially if it forms backward linkages (from buyer to supplier), local supply chain development can also: generate reductions in costs and logistical risks; promote technology, knowledge and skills transfer from larger companies to smaller businesses; and strengthen community relations through increased employment and income generation. Domestic SMEs can moreover be provided with training and mentoring (as has been done in Mozambique through Mozlink – see Box 3.3), and sometimes financing, to build their capacity for competing more effectively for procurement contracts.

Efforts to promote businesses linkages in Mozambique have especially been pronounced in the extractive industry mega-projects – this is partly because of the size of these investments, and because of the recognition that such linkages do not develop automatically in these sectors. Both private-sector and government-led initiatives for building linkages in the extractive industries are explored below.

GAZEDA and CPI initiatives for increasing business linkages between SMEs and foreign investors

Both CPI and GAZEDA have developed business linkage programmes in the interest of SMEs.[33] GAZEDA aims to work with companies beyond those that possess investment licenses, to develop linkages between different sectors, and to liaise with a range of government departments to facilitate transactions. Such cluster approaches can both promote specialization among groups of small-scale suppliers and enhance technology and knowledge transfers from larger companies licensed by GAZEDA to a network of smaller support firms. CPI, meanwhile, operates a linkage programme which is coordinated by its Department of Business Linkages. This follows on CPI's early support of Mozlink (Box 3.3 below). CPI sees its supportive role as including: identifying potential partners or financing opportunities; complaint resolution; facilitating contacts with government institutions; and helping to complete project application forms.

CPI also has a role in managing Industrial Parks which aim to foster business linkages. The Beluluane Industrial Park (BIP) is for instance a partnership between a private company and the State of Mozambique (represented by CPI). The BIP covers 700 hectares of land along the Maputo Corridor, of which 24 hectares have so far been serviced with infrastructure to accommodate SMEs. It offers companies a cost-effective and reliable local labour supply, low operational overheads, and tax incentives, as well as geographic advantages. Being only 2 km from the N4 highway linking Maputo to South Africa´s economic heartland, and adjacent to the MOZAL aluminium

Box 3.3. **Two private sector-led business linkage efforts: MozLink and Moma Titanium**

The MozLink programme, a local supplier development programme jointly created by Mozal Aluminium Smelter, IFC and CPI in 2003, is a follow-on project from the initial SME development project in place at the construction phase of Mozal (the SME Empowerment and Linkages Programme, SMEELP). Being the first major commercial development after the end of the war there was a need to create technical and business capacity to allow local companies to become more competitive and participate in this development by supplying quality goods and services, increase local purchasing power and promote job creation. The impact of the programme has been significant: from 2002-05, Mozal increased its expenditure with local SMEs from USD 5 m to USD 17 m per month, the number of SMEs involved increased from 45 to 250, over 2 000 jobs were created, and generated over USD 50 million in revenues for participating SMEs. The Mozlink extension phase is to include new corporate partners, Sasol, Coca-Cola and SAB Miller/Cervejas de Moçambique.

Another less-cited example is the **Moma Titanium Minerals Mine**, set up by Ireland's Kenmare Resources in Nampula Province, one of Mozambique's poorest regions. Kenmare obtained MIGA coverage for its equity investment in 2003, and is operational since 2007. The Kenmare Moma Development Association (KMAD) was established as a separate non-profit organization in 2004, with the aim of contributing to the development of the communities close to the mine and to build on possible business linkages. Egg production to supply the mine was for instance stimulated, enabling farmers to now produce in surplus and sell on local markets. Business training has also been provided to farmers who now operate independently in terms of sourcing materials and marketing their produce.

Sources: Esteves, Ana Maria, David Brereton, Daniel Samson and Mary-Anne Barclay, 2010; Jenkins, Beth, Anna Akhalkatsi, Brad Roberts and Amanda Gardiner, 2007, *Business Linkages: Lessons, Opportunities and Challenges*, International Finance Corporation. Jaspers, Frans-Jozef, Ishira Mehta, 2007, *Developing SMEs through Business Linkages:The MozLink Experience – A Manual for Companies*, NGOs and government Entities, IFC.

MIGA, World Bank Group, "Mozambique Mining Project Delivers More than Minerals", 17 October, 2011.

smelter, the BIP should notably provide BIP-based companies (including SMEs) with opportunities to bid for supplying the smelter with goods and services.

Business linkage potential of special enterprise zones

Through providing tax benefits and an enabling infrastructure framework for investing companies, special economic zones aim to become valuable platforms for value-addition and local capacity-building, allowing large and

small enterprises to mutually benefit from each-other's presence. If well-structured and managed, special economic zones can indeed generate economies of agglomeration, by reducing transaction costs among firms and stimulating creativity and cooperative innovation. These benefits do not arise automatically and cannot be taken for granted – indeed special economic zones often run the risk of instead becoming micro-economies, with poor linkages and transfer of technology to other parts of the economy, and where practices such as transfer pricing and declaration of losses are facilitated. Mozambique's IFZs and SEZs focus mostly on attracting investment through favourable tax structures, but do not have robust frameworks for encouraging value-addition alongside. Structural policies are moreover lacking on the supply-side: the local economy often lacks the skills and capacity required to take advantage of the domestic linkages and business opportunities created by the zones. Working on assessing and encouraging such dynamics could be a highly valuable niche for GAZEDA to occupy.

Private initiatives for increasing business linkages

Linkages programmes can also be led by companies themselves through corporate supplier development programmes, as well as by civil society or through partnerships among these various actors. The most successful business linkages experiences from Latin America and Southeast Asia have indeed stemmed from effective public-private partnerships in linkages promotion. In Mozambique, beside the business linkage efforts of GAZEDA and CPI, large (and mostly foreign) enterprises have played a direct role in seeking to stimulate the local economy. This is especially the case in the extractive industries, where firms have the most financial and technical capacity to develop linkage programmes, and where natural linkage creation is most limited. The Mozal aluminium smelter's Mozlink programme is a leading example of such company-level initiatives, and Moma Titanium Mine has also provided examples of effective linkage development (Box 3.3).[34] Rather than solely relying on the goodwill and voluntary efforts of large firms in this regard, such private initiatives can be further encouraged through formal legislation. For example the 2009 Code of Fiscal Benefits gives reductions in income tax for investments in basic public infrastructure projects, which have a high potential for employment creation, and the forthcoming revision of the mining law may also encourage mining companies' investments in infrastructure and schools.[35]

Notes

1. *Estratégia para a Melhoria do Ambiente de Negócios em Moçambique 2008-12.*
2. In addition other e-strategies have potential for increasing the transparency and speed of bureaucratic procedures. Such schemes include the Integrated Financial

Management Information System (e-SISTAFE, which aims to track poverty reduction through controlling public finances) and the Government Electronic Network (GovNet, which connects public institutions among themselves). The 2006 e-government Strategy also includes an integrated e-Land Registry and a Land Management Information System (LMIS), as well as the SISCAL. Efforts have also been underway over 2011-12 to develop and roll-out customs and tax IT systems: the single window and e-Tax, respectively.

3. United Nations Industrial Development Organisation, "ONE-STOP SHOPS: Republic of Mozambique", 2005. Available at: *www.tourisminvest.org/mozambique/downloads/Investment%20climate%20background/Licensing/One-Stop%20Shops.pdf*.

4. Gonzalez-Hernandez, Oscar, "Report: One Stop Shops", United Nations Industrial Development Organisation, Republic of Mozambique, 4 November 2005. Available at: *www.tourisminvest.org/mozambique/downloads/Investment%20climate%20background/Licensing/One-Stop%20Shops.pdf*.

5. USAID, "Improving Business Licensing and One-Stop Shops in Mozambique", July 2007. Available at: *www.tourisminvest.org/mozambique/downloads/Investment%20climate%20background/Licensing/Improving%20Business%20Licensing%20and%20One-stop%20shops%20in%20moz.pdf*.

6. Ministério da Função Pública, Unidade Técnica da Reforma do Sector Público – UTRESP, "Relatório da Implementação da Reforma do Sector Público Fase II", Terceiro Semestre de 2009, Dec. 2009

7. UNCTAD, *Investment Policy Review of Mozambique*, October 2011

8. Republic of Mozambique. "Poverty Reduction Action Plan (PARP) 2011-14", 3 May, 2011. Available at: *www.imf.org/external/pubs/ft/scr/2011/cr11132.pdf*.

9. Grobbelaar, Neuma, The South African Institute of International Affairs (SAIIA), "Business in Africa Research Project: The Experience of South African Firms Doing Business in Mozambique", 2004. Available at: *www.sarpn.org/documents/d0000871/P987-BIA_SA-Firms_Mozambique.pdf*.

10. UNCTAD, *Investment Policy Review of Mozambique*, October 2011.

11. Veira de Almeida & Associados, Flash News, "Tax Incentives to Investment in Mozambique: Perspectives and Opportunities", February 2010. Available at: *www.tourisminvest.org/mozambique/downloads/Investment%20climate%20background/tax/Tax%20Incentives%20To%20Investment%20in%20Mozambique.pdf*.

12. Veira de Almeida & Associados, Flash News, "Tax Incentives to Investment in Mozambique: Perspectives and Opportunities", February 2010, Available at: *www.tourisminvest.org/mozambique/downloads/Investment%20climate%20background/tax/Tax%20Incentives%20To%20Investment%20in%20Mozambique.pdf*.

13. The three main resources sector mega-projects that were negotiated prior to the 2007 fiscal regime are the Mozal aluminium smelter, Sasol natural gas and Kenmare titanium. There are now some 38 mining companies of all scale active in Tete Province alone.

14. Nacala is the third-largest deep water port on the eastern coast of Africa, giving ZEEN strong potential for sub-regional trade. The main investments already in progress in ZEEN include Bakhresa Grain Milling, the new Nacala Airport, and expansion of the Cement Company CIMPOR; the zone is therefore not heavily focused on the extractive industry sector.

15. NEPAD Business Foundation, "MAPUTO & NACALA TRADE MISSION (22-26 AUGUST 2011)", 31 August 2011. Available at: *www.jadafa.co.za/LinkClick.aspx? fileticket=oG4 fLiLhGAU%3D&tabid=436*.

16. International Monetary Fund, "Republic of Mozambique: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding", May 2011. Available at: *www.imf.org/external/np/loi/2011/moz/ 052011.pdf*.

17. Mapote, W., "Mozambique suspends Tete coal licence issuances", 24 February 2012, Available at: *http://news.yahoo.com/mozambique-suspends-tete-coal-licence-issuances-151359384.html*.

18. African Development Bank, *Republic of Mozambique: Country Strategy Paper 2011-15*, May 2011. Available at: *www.afdb.org/fileadmin/uploads/afdb/Documents/Policy-Documents/Mozambique%20-%202011-15%20CSP.pdf*.

19. Ministry of Agriculture Agriculture Promotion Centre (CEPAGRI), "Mozambique Agrobusiness Opportunities", September 2009. Available at: *www.mcli.co.za/mcli-web/events/2009/30sep09/Cepagri.pdf*.

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28. ACIS in collaboration with SAL&Caldeira Advogados Lda and GIZ Pro-Econ, "The Legal Framework for Company Start-up in Mozambique", Edition IV, December 2010. Available at: *www.acismoz.com/lib/services/publications/docs/Company%20 Registration%20Ed%204%20ENG.pdf*.

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30. UNCTAD, *Investment Policy Review of Mozambique*, October 2011.

31. It should be noted, however, that there are a range of definitions of "SMEs", and that these various government initiatives to promote SMEs, although valuable of themselves, are likely to be centered on larger SMEs and SMEs in the formal sector. None of these SME-oriented investment promotion programs appears to have been formally evaluated.

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Chapter 4

Infrastructure investment framework in Mozambique

This chapter maps progress in developing and attracting investment in all key infrastructure sectors: telecommunications, electricity, transport, and water and sanitation. It also evaluates the policy framework for public procurement and PPPs in infrastructure projects. The government of Mozambique has integrated infrastructure investment into broader economic growth objectives under several medium and long-term planning documents, most notably the Action Plan for the Reduction of Absolute Poverty (PARPA). However, there is generally a need to strengthen inter-ministerial collaboration in the planning of public investment in infrastructure. In addition, Mozambique can, and should, embrace the new opportunities presented by an expected boom in coal mining and the development of related infrastructure. The country has exported electricity to its neighbours in the past and also played a role as a regional transportation node, but now needs to focus more on meeting domestic infrastructure needs. Some decentralised initiatives in water supply and renewable energy have made an impact but more can be done to scale and replicate them to achieve maximum effectiveness.

4.1. Overview of Mozambique's infrastructure system

In some ways, Mozambique is at once held back by its past and on the cusp of embracing new opportunities that can accelerate the pace of its infrastructure development. On the one hand, Mozambique's protracted civil war led to the destruction of much of its infrastructure: the Cabora Bassa power plant and the Sena railway lines are just two examples. After the war, many infrastructure assets had to be rehabilitated and a lost period for infrastructure development regained. Despite its domestic setbacks, Mozambique has played a historic role as an electricity exporter to its neighbours and a regional transportation node. It has made progress in telecommunications and is connected to two fibre optic undersea internet cables that connect to its coastline. It also depends on surface water inflows from neighbouring countries. However, Mozambique's regional arrangements are not enough to address the dearth of local infrastructure. Moreover, the focus on megaprojects overlooks the importance of increasing access to the Mozambican population at large. A key challenge is therefore to develop infrastructure in a way that serves both Mozambique's regional commitments – such as its electricity sales to neighbouring countries –and its domestic needs.

In terms of financing, most infrastructure projects are financed by public sources (government revenues and user charges) and development partners, with scant private investment or financing from emerging economies. Given scarce budgetary resources and weak prospects for increased development aid, new sources of funding are needed to address the country's significant infrastructure backlog. More generally, innovative approaches to tackling access issues may help to accelerate the pace of infrastructure development and unlock the opportunities that are opening up in all infrastructure sub-sectors. Experiences in other countries, especially in Asia and in neighbouring South Africa and Mauritius, suggest that governments that harness infrastructure's power as an enabler of economic activities can reap rewards in terms of a better investment climate, a more diversified economy and sustainable economic growth.

Mozambique can, and should, embrace the new opportunities presented in part by an expected boom in coal mining and the development of related infrastructure that will accompany it. Up to now, electricity and transport infrastructure have traditionally served the needs of mega-projects. For instance, the Mozal aluminium smelter, the country's biggest investment

project to date, is also the largest consumer of electricity in Mozambique, accounting for 70% of consumption from Cabora Bassa.[1] However, only 14% of the population has access to electricity[2] and small and medium enterprises and households are under-served in their electricity needs. A key challenge is therefore to balance the needs of different users instead of concentrating infrastructure services on large-scale consumers.

The government has attempted some policy interventions, such as decentralised, community-led water management, to tackle the problem but implementation has been haphazard. Moreover, while there have been some successes, such as with the submarine cables that promise to make internet and telecommunications more readily accessible and cheaper, more needs to be done to extend the benefit of these services to all parts of the country, not just a few cities. The government can examine ways to exploit its significant renewable energy resources and develop climate-resilient infrastructure as a way to both address energy poverty and adapt to climate change. Evaluations by the Intergovernmental Panel on Climate Change (IPCC) show that Mozambique has been experiencing increasing rainfall levels and extreme weather events marked by catastrophic floods.[3] Poor communication networks exacerbated the impact of the floods, thus calling for improved telecommunications infrastructure to better respond to natural disasters such as these in future.

Lastly, adequate infrastructure systems can enable the growth of other sectors. Measures such as investing in a far-reaching transport network; extending electricity coverage; forming linkages between undersea submarine cables and domestic ICT backbones; and managing water resources to ensure their sustainable use can all spur agricultural production; tourism; manufacturing; industry and services. Conversely, inadequate infrastructure poses unnecessary obstacles to economic growth and national development. Increased, sustainable investment in all infrastructure sub-sectors could increase the gains already won, address the infrastructure backlog, and meet growing demand.

4.2. Process used to evaluation infrastructure investment needs

What processes does the government use to evaluate its infrastructure investment needs? Does the national government work in co-operation with local and regional governments to establish infrastructure investment priorities? Does the government have clear guidelines and transparent procedures for the disbursement of public monies funding infrastructure projects? Are the regulatory agencies that oversee infrastructure investment and the operations of enterprises with infrastructure investments independent from undue political interference?

The government of Mozambique has developed a number of strategies to accelerate economic development and fight poverty. Infrastructure features as a key driver of growth in many of these strategies. The 2011 Social and Economic Plan (Plano Económico e Social para 2011), for instance, identifies infrastructure sectors (transport, communications, water and electricity) as key engines of economic growth, in addition to agriculture, fisheries, extractive industries and manufacturing. A number of sector-specific policies and strategies have also been put in place. There are also a number of financing modalities for meeting the costs of capital expenditure, operations and maintenance of the country's infrastructure assets.

Mozambique faces a significant challenge in financing its infrastructure development. An estimated 26% of its GDP per year is needed for investment in new assets and maintenance and rehabilitation, which is higher than the Sub-Saharan African average of 15%.[4] Investment at this level would allow Mozambique to catch up to the regional infrastructure leader, Mauritius. As of 2007, a total of USD 645 million was being spent annually to finance Mozambique's infrastructure. Most of the financing (42%) came from domestic sources, while Official Development Assistance (ODA) provided a significant amount as well (35%) but there is less private financing (20%) and even less from emerging economies.[5] The bulk of the financing (close to 50%) has traditionally been directed to the transport sector. Most of the public financing is managed by state-owned enterprises and the greatest share is allocated to operations and maintenance, with very little spent on developing new infrastructure assets. However, public investment in capital expenditure is projected to increase over the 2011-13 period, with a focus on projects that meet the needs of the extractive industry and in special economic zones. Also, according to one estimate, the private sector is expected to invest USD 22.32 billion in Mozambique's infrastructure development, which is equivalent to two-thirds of investment from all sources.[6] The increase in private investment will be fuelled by the boom in coal mining activities due to the influx of mining companies in recent years.

Rapid Rural Development Zones (ZRDs) give priority to infrastructure

Mozambique has identified a number of Rapid Rural Development Zones (ZRDs), which are currently under-developed but have the potential to become significant economic hubs given the right supportive framework. The zones so far include: Tete and Niassa provinces; Nacala district in Nampula province; and some districts in Zambezia, Sofala and Manica provinces. Priority funding is given to the ZRDs for pre-defined activities, including water supply, electricity generation, transport and telecommunications. Other sectors include agriculture, education, health and tourism-related activities. Projects in these sectors are eligible to receive fiscal benefits such as exemption from

VAT and customs duty on the import of goods and a 20% investment tax credit for five years on the total investment (see also Section 3.6 on tax incentives).[7]

Disbursement of public funds

Disbursements of public funds for infrastructure investment are managed and monitored through the Ministry of Finance's State Financial Administration System (*Sistema de Administração Financeira do Estado*, SISTAFE), which aims to create a transparent management system for real-time financial operations, reporting and analysis. SISTAFE has been implemented since 2005 and is operating in all 127 districts.[8] CPI, the national investment promotion agency, provides guidance on investment opportunities in public infrastructure and is involved in processing applications and monitoring projects [see Sections 3.2-3.5]. Local bodies and municipalities also play a role in planning, procurement and budget execution. Moreover, the Conselho de Investimento (Investment Council – see Section 3.5), which aims to enhance policy co-ordination for investment policy, comprises several ministers, including those from energy, transport and communications, public works and housing.

Historical reliance on external funding for infrastructure

Donors have in the past provided significant support to Mozambique's infrastructure. However, in recent years, overall donor funding has declined from a peak of 14.5% of GDP in 2009 to 12.5% of GDP in 2010 and is projected to fall below 10% from 2011 onwards.[9] Portugal, a long-standing supporter of Mozambique's infrastructure, illustrates this decline in donor support. In June 2009, the Portuguese government entered into an agreement with the government of Mozambique to provide a credit line worth euros 300 million for Portuguese companies to invest in infrastructure projects and social activities in Mozambique. However, the sovereign debt crisis may undermine Portugal's ability to honour this agreement and the release of the funds has already been delayed by two years. The Mozambican government must therefore anticipate less donor funding, explore other funding sources, notably private investment, and better manage public investment in infrastructure.

Opportunities from coal mining

Coal mining in Mozambique, especially in the Zambezi Basin in Tete province, is poised to take off in the coming decades, as shown by the massive foreign investments that occurred in 2011 (see Chapter 1). Because the existing infrastructure is not sufficient to meet the anticipated boom in mining and exports in the coming years, mining companies have been negotiating contracts with the government to develop the necessary infrastructure to support their operations. Notably, Vale from Brazil and Riversdale from

Australia – acquired by Rio Tinto in 2011 – have secured contracts from the government to mine for coal and also construct, upgrade or expand road, railway and port infrastructure, as well as power plants, to facilitate coal exports. Currently, the Cahora Bassa hydropower plant is used mainly for electricity exports to neighbouring countries and also serves the Mozal aluminium plant, so new sources of energy generation need to be developed. Some of the mines are planning to construct their own power plants to supplement the electricity generated from Cahora Bassa, but these projects are currently in the pipeline. For example, the Brazilian mining company, Vale, has developed a power plant at the Moatize coal mine in Tete province and plans to construct a railway line from Moatize to the Nacala port through Mozambique. This in turn can fuel economic activities, especially in commercial agriculture, along the Nacala-Maputo corridor [see Section 1.2 for details on the investment potential of the Nacala special economic zone]. Also, in late 2011, the government gave approval to Jindal Steel and Power, an Indian company, to contruct a 2 640 MW coal-fired power plant in Tete province at a cost of about USD 3 billion. The plant is expected to start production in 2015.[10]

Especially since these infrastructure investments by mining companies are set to rapidly expand yet further with Mozambique's coal boom, it is crucial that government establish a mechanism for carefully co-ordinating them among each-other. Indeed the risk to date is that such projects are undertaken by individual companies in isolation and each according to its own needs, rather than within a common and coherent national framework. These projects would instead need to build on joint economies of scale, while simultaneously addressing the population's requirements and tackling gaps in the national network. Road and rail transport, as well as energy provision, are infrastructure sub-sectors where this co-ordinated approach would be particularly beneficial.

Significant transport and storage infrastructure is needed to fully benefit from coal mining

There are currently two railway lines in place that can be used to transport coal. The 665 km Sena railway line links the Moatize coal basin to the port of Beira and the 317 km Machipanda line connects Beira and Machipanda on the Zimbabwean border. The Sena railway line – even when refurbished – has low capacity and will have to be supplemented by other road and railway infrastructure. The Nacala railway, operated by Corredor de Desenvolvimento do Norte, runs from Nacala in the northwest province of Nampula, to Malawi. Vale, the Brazilian mining company, also has a stake in the railway and plans to extend the railway to connect to its Moatize coal mine in Tete province, which borders Malawi. At the ports, new container terminals

will have to be put in place to absorb the increased loads coming from the coal mines. Moreover, barging on the Zambezi River, while at an exploratory stage at the moment, can be an option for transporting coal.

Insufficient infrastructure capacity could create bottlenecks in coal production if the demand for transport and energy services accelerate too rapidly. Recognising this potential problem, the government has adopted a more cautious stance when granting mining concessions. In late 2011, the national mining inspector announced a suspension on new coal prospecting licences in Tete, as the province has become "overloaded with coal projects".[11] Suspending the issuance of new licenses could also help ease the pressure on the existing infrastructure network. The government could also use the opportunity to reflect on ways to make infrastructure projects in the pipeline benefit local populations and create knock-on effects on non-mining sectors. Otherwise, transport and energy projects developed by the mining companies could operate as an enclave, with few opportunities for the local population to fully benefit.

4.3. Measures taken to uphold transparency and procedural fairness in tendering

What processes does the government use to evaluate its infrastructure investment needs? Does the national government work in cooperation with local and regional governments to establish infrastructure investment priorities? Does the government have clear guidelines and transparent procedures for the disbursement of public monies funding infrastructure projects? Are the regulatory agencies that oversee infrastructure investment and the operations of enterprises with infrastructure investments independent from undue political interference?

The legal framework for procurement has greatly improved

Public procurement in Mozambique has undergone a series of adjustments, culminating in the 2010 Procurement Law (an update of the 2005 Law), which regulates the contracting of public works, and the supply of goods and services to the state and was developed with some input from contractors in this field. Among its provisions, the Procurement Law allows for domestic preference (Article 26) and favourable terms that allow SMEs to compete (Article 90). These provisions could encourage dometic SMEs, which have been in the shadow of larger and foreign firms in the past, to flourish. The 2010 law also simplified tender documentation and defined a hierarchical claims system for dispute cases. In addition, the Decree on Public Works Contracts

and Supply of Goods and Services regulates the procurement of public works and contracts with private entities for the provision of goods and services to the state. The regulations of the Decree are applicable to national bodies as well as to local authorities that have the right to contract out certain services.

Procurement units, known as UGEAs, have been established in sector ministries and government agencies at national and sub-national level, including provincial governments and municipalities. Procurement bids are evaluated against set criteria, including best price offer; lowest rate or price to be applied in relation to users; best quality of services or goods made available to the public; and best service and satisfaction of demand.[12] The Administrative Court (*Tribunal Administrativo, TA*) has ultimate authority over the legality of administrative acts and oversees public expenditure. All concession, procurement and public works contracts that generate public expenditure and are executed by the state are subject to a pre-audit review by the TA.

Overall, transparent public procurement is becoming more common. FIPAG, for example, uses government of Mozambique procurement regulations and donor procedures that encourage transparency and fairness through, *inter alia*, public announcements of tenders and other forms of contracting, model contracts and objective eligibility requirements and evaluation criteria. The rights of contractors are addressed through contract clauses dealing with indemnities and independent oversight is applied in the case of public works. The 2010 Procurement Law has made positive steps to improve the procurement framework in Mozambique. However, more can be done to strengthen transparency and attract a wider range of bidders in the tendering process. Often, especially for small-scale projects, procurement documents are only available in Portuguese, which can be obstacle for international bidders. Another challenge is to rationalise the plethora of procurement systems in use. A DFID study, for instance, found that about 52% of ODA was provided through procurement systems separate from the Mozambican system and external financiers like China also continue to use their own procurement systems.[13] Aligning these various procurement provisions can help to reduce administrative hurdles and create a level and transparent playing field for all potential bidders.

PPPs and large-scale projects programme, and areas of the PPP programme that can be improved

To reduce the country's infrastructure deficiency, the government of Mozambique has decided to pursue public private partnerships (PPPs) for the provision of infrastructure, megaprojects worth USD 500 million or more and general business concessions, excluding the mineral and petroleum domain. To that end, the Law on PPPs, Large-Scale Projects and Business Concessions (no 15/2011)[14] was approved in 2011 (Box 4.1).

Box 4.1. **Mozambique's PPP Law (2011)**

The PPP Law (2011) defines the rules for contracting, implementing and monitoring the cycle of PPP projects and defines the scope of PPP undertakings, and outlines the sharing of responsibilities and benefits between the government and the private contractor. The Law recognises three PPP modalities: concessions, operating or leasing contracts and management contracts, and sets a maximum of 25 years for concessions, 20 years for leases, and 15 years for management contracts. The Law also makes provision for the establishment of Special Purpose Vehicles (SPV) to manage all aspects of a given project, and authorizes the provision of guarantees and incentives from the government to the private contractor. The Law also obliges the State General Account to report on the performance of PPPs at the end of each fiscal year. The Law also states that PPPs should be appropriately accounted for in the budgeting framework because they can create long-term commitments on the public budget. However, the Law provides no further guidance on how this accounting should be undertaken although it is reasonable to assume that the Ministry of Finance will be responsible. At least four public entities have oversight functions over the undertaking of PPPs: direct oversight from sectoral ministries; indirect oversight from the Ministry of Finance over the use of guarantees and fiscal and budgetary elements of the PPP; the newly formed PPP Unit; and the sectoral regulatory agencies. The number of entities involved can create redundancy and constrain rather than facilitate the relationship between the public and private partners.

The PPP and Megaprojects Law is well-defined in some respects but quite weak in other areas. The narrow definition of the types of legally acceptable PPPs may hamper potentially effective forms of private sector participation, such as a Build Operate Own (BOO) arrangement where contractors would normally have ownership rights in the project, thus allowing them to mortgage assets and secure better financing terms. Another issue is the number of concession fees imposed by the state. These include award fees; an additional fee for the concession or operating license and taxes on the company. The award fee varies from 2% to 5% of the value of the asset and can deter private investors by increasing the amount of initial costs they have to commit upfront, before the project has had a chance to generate revenues. The concession fee comprises a fixed fee of 5% to 10% of the asset value plus a variable fee of 5% to 10% of the revenue generated by the concession company, net of tax. As for the management fee, it has been set at 10% of the concessionaire's gross revenue, which bucks the trend of most management contracts, as the public entity usually pays the private company instead. The combination of the award fee, concession and operating royalties (or

management fees, depending on the case) may prove to be excessive for some investors, effectively creating a barrier to investment. Moreover, the Law does not establish the contractors' rights to retain their earnings, nor does it state the terms under which contractors can be compensated if their contracts are terminated.

Regulations on PPP implementation have been finalised

To implement the PPP legislation, the government finalised and released regulations specifying sectoral oversight for PPP undertakings; the institutional framework, including the creation of a new PPP Unit; the tendering process; and guidelines on contracts, guarantees and risks.

The Regulations on PPPs, which were finalised in July 2012, provide clear specifications on how PPPs are to be undertaken and how issues that bear on PPP implementation are to be managed. The regulations provide details on how a range of risks, such as fiscal, fiduciary and management risks, are to be shared between the public and private co-contractors. Moreover, a PPP unit has been created under the Ministry of Finance which is a positive step signalling the government's commitment to the PPP programme. It is important to clarify how the Unit's responsibilities would differ from other government bodies that perform duties such as approving bids or issuing operational licenses. Also, the Regulations indicate that the state should offer financing for non-commercially viable projects that have a high social impact, but committing the state in this way should be done with due consideration for budgetary constraints. The regulations allow direct awards for contracts in case of emergencies or if the winning bidder withdraws and stipulate that the public interest must be protected in these instances. However, extra provisions would help ensure that direct awards are negotiated and the case for resorting to this option must be made transparent.

4.4. Electricity sector

Has government developed a strategy to ensure reliable access to electricity services by users, and economic incentives to invest and supply electricity? What programmes exist to ensure on a least-cost basis access to electricity services by a wide range of users? Are these programmes time-bound and based upon clear performance targets?

Two sides to Mozambique's electricity profile

Mozambique is at once energy rich and energy poor. Its energy wealth comes from its hydropower potential, which, at an estimated 12 500 MW a year

is much greater than that of other water-rich neighbours such as Zambia, whose hydropower potential is 6 000 MW a year. As a result, Mozambique enjoys a fairly steady power supply, with only 3 days per year of power outages compared to an average 10 days per year in other low income countries. Electricity tariffs, comparatively speaking, are also quite low.

At the same time, Mozambique is energy poor, as only 14% of its population has access to electricity, a lower level than the Sub-Saharan average of 20%.[15] The low access rates can be explained by the limited reach of transmission lines, especially in rural areas, and the unequal distribution of electricity between industry and other consumers. The civil war destroyed some of the transmission lines, creating an infrastructure backlog that Mozambique is still struggling to address. Extractive industry megaprojects account for the bulk of electricity consumption in the country (already 84% in 2008). However, the domestic energy infrastructure barely serves communities outside the resource extraction hubs or the capital city and other industrial centres, resulting in one of the lowest per capita usage of electricity in the world – less than 500 kWh/capita/annum.[16]

Electricity needs to be available on a wider geographic scale if business is to truly take off. Moreover, Mozambique has regressed in this field: "Getting electricity" is Mozambique's worst-performing indicator in the latest World Bank Doing Business Reports, putting the country in the 174th position out of 185 countries in both 2012 and 2013. Part of the reason for this regression is that power consumption has been increasing steadily by 6-8% a year throughout the 2000s, a rate that mirrored the economic growth rate. The government needs to increase generation capacity and expand electricity services beyond the main cities and extractive areas to respond to this increasing power demand and avoid shortages.

Government policies to develop the energy sector

The government of Mozambique initiated reforms in the electricity sector in 1997 with the approval of the Electricity Law (Law 12/97). The law opened the generation and transmission market to private enterprises, and created the National Electricity Advisory Council (CNELEC) to perform advisory and regulatory functions on issues such as electricity policy, setting tariffs, and approving concessions. CNELEC also undertakes mediation and arbitration functions for disputes that arise between the government and its contractors. CNELEC is also authorised to monitor the performance contract between the government and EDM, a directive that bolsters the regulator's influence as EDM is a state-owned company. The other main actors in the electricity sector include:

- The Ministry of Energy, which is responsible for planning and policy in the sector.

- The National Energy Fund (Fundo Nacional de Energia, FUNAE), which provides funding and guarantees for energy projects, equipment, technical assistance and dissemination of energy technology and products to rural areas.
- Mozambique Electricity (Electricidade de Moçambique, EDM), a vertically integrated state-owned company, which is responsible for the distribution of electricity.

The government has set a target in its 5 year development programme (Programa Quinquenal do Governo 2010-14) to increase energy access rates from 14% in 2009 to 23% in 2014.[17] It also aims to increase the use of renewable energy technology. The Energy Sector Strategic Plan 2010-14 covers electrical energy, fuel, new and renewable energies, and different economic sectors. It aims to undertake 90 000 new connections annually through low-cost systems in rural areas financed by FUNAE.

Financing needs for the energy sector

Of all the infrastructure sub-sectors, power has the greatest financial needs – USD 771 million a year compared to USD 403 million a year for transport, USD 331 million a year for water and sanitation and USD 156 a year for ICT as of 2009 – and this need has only augmented since with the expansion of further mega-projects in the aluminium and coal industries. Current funding to the power sector is below the estimated USD 771 million that is needed to increase national access rates to 20%, increase hydropower generation capacity by 900 MW and install 1 400 MW capacity interconnectors.[18] Most of the financing needs (92%) are for capital development and 8% for operations, maintenance and rehabilitation. Current funding sources are almost entirely derived from the public sector (tax revenues and user charges) and ODA, with very little from emerging market financiers (China, India and the Arab Funds) and virtually no financing from the private sector.

The gap in Mozambique between funding needs and available funding resources, at 10% of GDP, is one of the biggest in Southern Africa. Part of this gap can be covered by addressing inefficiencies, for example, 25% of electricity is lost in distribution and only 71% of the cost of electricity provision is recovered.[19] Overstaffing in EDM is also a problem, accounting for about 20% of revenue.[20] Theft and illegal connections also undercut revenues. Addressing these inefficiencies could increase the resource envelope but will not be enough to cover the substantial funding gap in the power sector.The government therefore has to consider other sources of funding.

Main sources of electricity generation

Mozambique's electricity generation is derived mostly from hydro (94%) with a small proportion from oil (6%)[21] and coal deposits, at 87 million tons,

are some of the largest in the world. Moreover, Mozambique has significant natural gas potential, with reserves estimated at 4.5 trillion cubic feet (tcf), compared to the continental leader, Nigeria, which has 5.2 tcf in reserves. There are three natural gas fields at Pande, Temane and Buzi-Divinhe but gas production has up to now been limited to Pande and output is only sufficient to power the local village.

The government, in its five-year development plan for energy (2010-14), sets out the priority projects in the energy sector (Box 4.2). A key project is the expansion of the Cahora Bassa dam's generation capacity from 2 075 MW to 3 220 MW over five years at a cost of USD 1 billion. The expansion can help exploit the dam's full generation potential, which has been estimated to reach 14 000 MW, as up to now only the southern part of the Cahora Bassa plant has been used for power generation.

Box 4.2. **Priority energy projects for the government of Mozambique**
(excluding renewable energy projects)

- Mphanda Nkuwa Hydropower Dam, Phase 1, 1 500 MW
- Cahora Bassa Hydropower Dam, North expansion 1 245 MW
- Moatize Thermal Power Plant, Phase 1 600 MW
- Benga Thermal Power Plant, Phase 1 500 MW
- Chicamba (39 MW) and Mavuzi (52 MW) hydroelectric plants rehabilitation
  - Tete-Maputo electrical transmission line
  - Construction of Infulene – Manhiça – Macia transmission line (110 kv)
  - Construction of Mozambique – Malawi interconnection line (220 kv)
- Complete the North-South distribution line
- Electrify district capitals not yet connected to the national electricity line

Source: Energy Sector Five Year Plan (*Programa Quinquenal do Governo 2010-14: Sector de Energia*).

The government also plans to construct the Mphanda Nkuwa hydroelectric dam, 60 km downstream from the Cahora Bassa dam, to add about 2 500 MW to the grid (the Mphanda Nkuwa project was presented in a roadshow undertaken by CPI to investors – see Section 3.5). EDM holds a 20% stake in the project while a local company, Energia Capital holds 40% and a Brazilian company, Camargo Correia accounts for the remaining 40%. To complement the projects at Cahora Bassa and Mphanda Nkuwa, a double transmission line will be built to deliver electricity generated at the two dams to Maputo and to the Southern African Power Pool as well. EDM will finance the USD 1.7 billion project in partnership with Camargo Correia. A number of

small-scale (25 MW-120 MW) hydropower projects have also been identified at Massingir, Lurio, Majawa and Malema.

There has been some concern from environmental interest groups that the Cahora Bassa extension and the Mphanda Nkuwa construction projects could have potentially harmful effects on the environment, especially in the lower Zambezi where the hydroelectricity will be produced. Environmental interest groups have argued that the dam construction could elevate the levels of the Zambezi river, damage its ecosystem, and displace local communities. government planners can pre-empt these ecological problems by undertaking detailed environmental impact assessments and identifying compensatory measures in case of ecological or social harm. Another issue is to take into account the risk of extreme weather events, as floods in the past, especially in 2000, destroyed transmission lines and resulted in power cuts in some cities and towns. Better disaster preparation is needed to prevent similar devastating effects from floods in the future.

Predominance of Hidroelectrica de Cahora Bassa

Hidroelectrica de Cahora Bassa (HCB) is an independent power producer (IPP) and Mozambique's largest energy company. It operates and owns a majority stake in the Cahora Bassa hydroelectric project. EDM, the vertically-integrated utility responsible for electricity generation, transmission and distribution, has a relatively small installed generation capacity – 233 MW – compared to HCB's 2 075 MW. Because its own capacity is insufficient to meet domestic demand, EDM purchases power from HCB. A few private mining companies have been given contracts to develop greenfield power plants although most are still in the pipeline. Historically, the Portuguese government owned a majority stake in HCB but through negotiated sales in 2007 and 2010, the government of Mozambique has increased its shares up to 85% of the company, with Portuguese and Mozambican companies retaining the rest.

Mozambique's role as an electricity exporter

Because of the lack of adequate transmission networks in Mozambique, there is no direct connection between the Cahora Bassa plant and Maputo. Instead, about 85% of the electricity currently generated at Cahora Bassa is exported to South Africa, so as to transit through the transmission system of South Africa's utility, Eskom, before it is re-imported for use in Maputo in the southern part of the country.[22] HCB accordingly has a long-standing power purchase agreement with South Africa and Mozambique, which was signed in 1969 but has not been renegotiated since. As part of the agreement, HCB was obligated to export a minimum of 1 450 MW of electricity to Eskom. Mozambique Transmission Company (Motraco), a company whose

shareholders include Eskom, EDM and SEB, also has a concession agreement with the utilities of Mozambique, South Africa and Swaziland to transmit electricity and carry out operations there. However such arrangements provide only very unsatisfactory solutions to the lack of adequate power transmission networks in Mozambique: distribution losses are inevitable when electricity is transmitted over such a long distance, using South African transmission lines.

Mozambique also exports electricity to Botswana, Zambia and Zimbabwe.[23] These electricity exports provide Mozambique with a significant source of revenue but it also exposes the country to fluctuations in demand and disputes over electricity sales. For instance, disagreements have arisen between HCB and Eskom since the signing of the PPA over the price of electricity and in 2002, HCB cut off electricity supplies to Eskom because of the low tariff rate. Moreover, the power purchase agreement is denominated in rands, thereby exposing revenues to currency fluctuations. Moreover, Motraco purchases electricity from Eskom for onward transmission to Mozambique but in the past, Eskom has had to reduce the electricity it provided to Motraco when it faced shortages in South Africa in 2008.[24] The pipeline of hydro and natural gas projects provide an opportunity for HCB and Motraco to diversify their client base and wean themselves from depending on South Africa for transmission lines. The government must also prioritise domestic electricity needs when the new power plants come online in order to increase access within its borders.

Government efforts to increase electricity access rates

The number of households connected to the grid has grown at a rate of 15% per year between 2000 and 2007. Despite the progress, the rate of people with access to electricity, at 14%, remains quite low. Because of insufficient generation and transmission infrastructure, electricity is the least used energy source. Many households have resorted to using kerosene, charcoal and biomass to meet their energy needs, particularly for cooking and lighting. Firewood use is also prevalent throughout the country, although it is most concentrated in the centre-northern rural districts, which have many low-income households.[25] Charcoal and electricity, higher grades than kerosene, are used mainly in urban areas while kerosene is used extensively in rural areas, although evidence suggests that it has adverse effects on the environment and on human health.[26] There is therefore an imperative to increase clean energy production, such as bagasse, to not only serve the domestic needs of rural communities but improve their health and protect the environment.

With support from the World Bank, the government of Mozambique has put in place an Energy Reform and Access Project (Box 4.3). In addition to

addressing the supply-side problem by extending the grid, EDM is also tackling the demand side constraints of electrification. EDM's revenues come mainly from industrial consumers – for example in Nacala, 60% of its revenues come from industrial consumers while 40% is derived from domestic consumers.[27] However, EDM needs to improve its operational efficiency. As Mozambique's low score on the World Bank Doing Business indicator for "Getting electricity" suggests, the process for connecting businesses is for instance very slow even when they are within full reach of the grid: connection requires a lengthy process – including requesting an authorization for the project to the Ministry of Energy and obtaining an external inspection by EDM and the provincial energy directorate – before the supply contract can be signed and the metre installed. EDM moreover lost USD 13 million due to theft and illegal connections in the first half of 2010 alone.[28] The regulations and governance structure of the SOE also fare quite badly based on measures of institutional reform.

Box 4.3. **Energy Reform and Access Project (ERAP)**

ERAP is aimed at increasing access to electricity among Mozambique's unserved and under-served rural and urban areas. The project consists of four components. The first is institutional reform that includes separating EDM into several business operations, introducing private sector participation in distribution and the creation of a new public entity tasked with electricity transmission and supply. A second component of the project includes connecting rural areas to the grid by constructing new transmission lines that will link to distribution sub-stations across the country. The third component includes boosting investment in renewable energy through a co-financing facility. Underpinning all these aspects is the fourth over-arching component: technical assistance and capacity building. So far, the project has been somewhat successful. Between 2003 and 2010, for example, the number of new grid connections increased to 39 000 in peri-urban areas and 931 km of transmission lines had been constructed as of May 2010, just under the target set to construct 941 km by March 2011. A performance system for EDM has been put in place, based on public consultations and performance contracts, whereas none existed before the beginning of ERAP. The cost of EDM customer connections to the grid have also declined. Some targets, however, have been quite challenging to meet, namely connecting schools, clinics and communities although evaluation results are pending for these indicators.

Source: Based on information provided by a World Bank report: Implementation Status and Results; Mozambique; Energy Reform and Access Project.

The electricity tariff structure and demand-side options

The government laid out the retail electricity tariff methodology in Decree No. 29/2003 of 23 June 2003. The methodology makes provisions for automatic annual adjustments to the average tariff baseline, and sets a goal of achieving an average tariff of USD 9.1 cents by 2009. EDM has four categories of tariffs: social, household, farming and a general tariff. However, there are no regional variations in tariffs so the same tariffs apply regardless of location within the country. The Mozambique Electricity Law of 1977 put in place a "social tariff" at subsidised rates for low-income households consuming up to 100 MW a month of electricity. However, qualifying for the tariff involves a complicated process that includes receiving certification from the Welfare Service Centre of the household's low-income status; and demonstrating that the consumption of the electricity would be for domestic uses only, excluding self-employment or productive activities of any kind. As a result of these demands, less than 1% households have been able to access the social tariff.[29]

EDM offers a prepaid service, CREDELEC, which allows consumers to purchase electricity through various modalities: ATMs, petrol stations, vouchers and online. By eliminating electricity bills, the prepaid system can potentially increase the amount of revenue collected by EDM, which has lost millions in the past due to uncollected bills. Moreover, the CREDELEC system obviates the need for meter readings, thus freeing utility staff to tackle other issues. Even though the service costs more than regular billing, about 80% of EDM's customers have opted to use the CREDELEC system. At its most developed, the system could facilitate access to electricity services for those in rural or peri-urban areas who are within reach of the grid but do not have bank accounts to create an account with EDM.

Challenges for rural electrification

To respond to the country's energy needs, especially in rural areas, the government has developed a decentralised approach to rural electrification and established a dedicated rural electrification agency and fund to increase rural electrification. FUNAE, the national energy fund, administers off- grid electrification projects located more than 50 km from EDM's national grid. Financing for rural electrification initiatives is a challenge, as experience from other developing countries suggests that rural electrification agencies and/or funds rarely succeed in attracting private capital because rural poverty renders co-financing or equity investment unattractive to private entities and commercial banks.[30] In Mozambique's case, low population density has also made it difficult to expand electrification beyond urban areas because of the high costs of rural transmission and distribution projects. FUNAE collaborates with microfinance institutions on financing small-scale energy projects.

Decentralised solutions can fill the connection gap

The government can consider decentralised generation and distribution strategies such as mini or off-grid systems, solar PV, mini hydro and hybrid generation sources. These options are associated with more reliable power supply, a more benign effect on the environment, and lower costs in remote areas compared to on-grid electrification.[31] While financing is challenging, some options include government grants to cover the upfront costs, public subsidies to ensure affordability of the service and development finance to cover capital costs. The government may want to consider measures such as exemptions on the imports of renewable energy inputs such as solar panels and other green goods in order to reduce the cost of developing renewable energy.

As natural gas fields at Pande, Teme and elsewhere are exploited, the government could consider incentives for people to use natural gas for cooking, which is usually energy intensive, instead of biomass and kerosene, the most commonly used option for most of the population without access to electricity. The conversion to natural gas would reduce pressure on the grid while expanding national coverage and ensuring a more secure energy supply, as natural gas is a renewable resource.[32] There could also be a benefit to the environment, as biomass and kerosene can be highly polluting. A number of towns – Vilanculos, Inhassaro and Nova Mambone in Inhambane province have turned to self-generation by using natural gas from the nearby Pande field. While the central government owns the generation and distribution assets, the towns used management contracts with private companies for operating the generation and distribution system. The co-operation proved to be effective, but because the assets remained in government hands, the private company had no incentive to increase the number of household connections or invest in new generation capacity.

The lesson from this experience is that decentralised solutions can be effective but incentives have to be put in place for private companies to increase connection rates, improve bill collection and expand system capacity. A concession model may therefore be a better alternative than management contracts with private companies.[33] Indeed, the government tested this approach in Vilanculos, where a concession was given to a consortium of Mozambican and South African companies. While the concession was somewhat successful, no other cities matched Vilanculos' circumstances and the model was therefore not rolled out beyond that city.[34]

Prospects for renewable energy

Mozambique has significant potential in renewable energy but the focus thus far has been disproportionately placed on large-scale hydropower

projects, with little effort to harness the country's considerable solar, wind and biomass resources. Hydropower has been developed only at a large-scale in Mozambique, with relatively less focus on small-scale generation. FUNAE has undertaken feasibility studies on mini hydro in Tete, Manica, and Zambezia provinces, which have significant water resources, so the prospects for smaller projects are encouraging.[35] Mozambique has Africa's second largest coastline but thus far, the potential for wind energy production along the coast has not been explored. There are also indications of at least 25 MW of exploitable geothermal power especially in the Metangula area close to the East African Rift Valley in the far north of the country. Developing these potential renewable energy sources could help Mozambique to strengthen its energy security and help to increase access rates among its population.

The government has taken some steps to increase renewable energy production and to attract private actors into the sector. An Energy Strategy was developed in 2009 and among other measures, it makes provisions for private investors to obtain concessions on projects smaller than 15 MW.[36] In 2010, the government lifted subsidies on fossil fuel and this could help non-conventional energy sources to compete.[37] Other measures, such as feed-in tariffs and lifting import duties on renewable energy goods, could also have an impact in attracting investment into the sector.

In 2009, the government put in place a policy to encourage the development of biofuel (jatropha, ethanol and seed oil from sunflowers and cotton). Mozambique has about five sugar plantations in Maputo and Sofala that can be used for bagasse and cogeneration. There are about 41 million hectares of land available for energy production from sugar cane waste.[38] However, care should be taken that biofuel production does not needlessly supplant regular food crop production. Institutional co-ordination is also important to nurture the fledgling biofuels sector. The active involvement of CEPAGRI, which is mandated to undertake investment facilitation, could help ensure that new agricultural strategies such as for biofuel expansion provide small-growers with additional opportunities for income generation while stimulating rural development. Mozambique's Strategic Biofuel Policy for instance (also referenced in Section 1.2) recognises a role for CEPAGRI in terms of registering biofuel investment projects while other responsibilities have been handed over to the National Biofuel Commission. Other government institutions, such as FUNAE (Box 4.4), can also play a role in biofuels and stimulating renewable energy overall.

Box 4.4. **FUNAE's co-operation with local communities in small-scale energy projects**

FUNAE was established in 1997 to promote renewable energies and expand access to energy. It is under the aegis of the Ministry of Energy and receives the bulk of its funding from donors in addition to funding from the state budget and revenue from its projects. FUNAE works in Manica, Inhambane, Niassa and Cabo Delgado provinces, providing finance, guarantees and technical assistance to local governments for various projects. Current renewable energy projects (of about 3-5 years duration) include:

- World Bank: a biomass project Belgian Cooperation financed Mini-Hydro Power and Windmill Pumps.
- The European Union is funding mini hydros in villages.
- India is funding the construction of a solar panel factory, an investment of USD 13 m.
- South Korea is funding the building of three photovoltaic power stations, at a total of USD 35 m.

FUNAE works with local governments to select the villages and schools that will benefit from its programmes. FUNAE oversees the tendering process and local government authorities accompany the entire process. Elected local management committees, made up of community leaders, teachers, nurses and so on, oversee and manage the installed systems. Maintenance is undertaken by provincial directorates together with FUNAE. This partnership approach can help to cover as many areas as possible but FUNAE's reach is all the same limited to the areas under its jurisdiction. A scale-up of its activities should be considered to maximise its impact.

4.5. Transport infrastructure

What processes are followed to make informed decisions on the development of new transport facilities, as well as the maintenance of existing investment in transport infrastructure? Are the requirements for all modes of transport regularly reviewed, taking into consideration investor needs and the links between different modes of transport infrastructure?

Institutional framework for the transport sector

Transport administration in Mozambique is managed by a combination of national, provincial and private authorities.

- The Ministry of Planning and Development sets investment priorities for the sector to ensure it aligns with the objectives of the PARPA.
- The Ministry of Transport and Communications sets policy and regulations for road, rail, air and ports.
- The Ministry of Public Works and Housing is responsible for construction and operations and supervises the National Road Administration (ANE) and the Road Fund (FE).
- The National Road Administration is in charge of all road works, maintenance and repairs. The Road Fund is comprised of a combination of fuel charges, bridge tolls and transit charges.
- A Council of Ministers that includes the Ministry of Public Works and Housing; the Ministry of Finance; the National Road Administration; and provincial governments – aims to ensure co-ordination across the government on all matters of transport administration.
- Mozambique Ports and Railways Company (CFM) is a state-owned enterprise comprised of four branches: CFM North, CFM Central, CFM South and CFM Zambezia. It operates the railway lines in these geographic areas and is also responsible for port infrastructure and services.
- The sector regulator, the National Institute of Surface Transport (Instituto Nacional dos Transportes Terrestres, INATTER) was created on 5 July 2011. The objective of INATTER is to regulate, monitor and supervise activities involved in land transport, with respect to the transport needs of people and goods, and the promotion of the security, quality and rights of the users of road and rail transport. The practical implications of this mandate are not yet clear given the recent establishment of the institute.

Policy framework for the transport sector

The government has developed a five year strategy (2007-11)[39] for the road sector covering six inter-related areas:

- Sustainability (financial; institutional and maintenance).
- Connectivity.
- Accessibility through secondary roads, that serve the main economic areas; and tertiary roads and vicinal roads that serve rural areas.
- Transitability: ensuring that roads remain navigable throughout the year, including spot repairs on damaged roads.

- Asset preservation: preventative action to ensure that neglected roads and under-maintenance do not lead to high costs in the long-run.
- Maintainability: measures to maintain road systems, such as drainage.

Moreover, the government developed a Strategy for Integrated Development of the Transportation System (Programa Integrado do Sector de Estradas or PRISE).[40] It mades provisions for funding in three areas: operations (7% of total funding); maintenance (25% of total funding); and rehabilitation and upgrading (68% of total funding) to be met from the Road Fund, the central government budget, and donors over 2007-09 (Table 4.1).

Table 4.1. **Summary of sources and expenditures of funds, PRISE 2007-09 (USD millions)**

Line No.	Component	Estimated needs	Financing			Total financing
			Road fund	Government of Mozambique	Donors	
1	Overhead	69.6	29.9		39.7	69.6
2	Maintenance	263.9	165.1		98.7	263.9
3	Rehabilitation and improvement	709.8 709.8		139.1	570.7 570.7	709.8 709.8
	Total	1 043.2	195	139.1	709.1	1 043.2

Source: Programa Integrado do Sector de Estradas (Integrated Transport Sector Programme).

The transport sector receives the most funding by far from all sources: USD 296 million a year out of USD 659 million total for all infrastructure sub-sectors.[41] Donors are providing the bulk of capital expenditure for the sector, although when operations and maintenance included, the public sector provides the most (43%) funding, donors provide 34%, the private sector 19% and emerging financiers 3%.[42] The Resolution on Transport Policy No. 5/96 allows private sector participation in railway construction, rehabilitation, operations and management. Road, rail and port concessions are also permitted by law. Private sector participation is more prevalent in transport than in other sub-sectors with some notable successes, such as the Maputo Corridor, a cross-border PPP.

Challenges in the transport network

The road network in Mozambique is rather poor and totals 30 056 km (Table 4.2). Moreover, the road density is less than 0.02 km/m^2 and 0.86 km per capita compared to 0.2 km/m^2 and 36 km per capita (that is, respectively ten and forty times higher) on average for other low-income countries.[43] Mozambique's roads are also the most overloaded in the SADC region.[44] While Mozambique has a number of national and international corridors, rural roads

have been under-developed because of constrained resources to fund them. While maintenance funds have been allocated to and are managed by provincial road authorities, priority should also be placed on ensuring transitability and constructing additional tertiary and vicinal roads.

Table 4.2. **The state of Mozambique's road network**

Classification	Paved	Unpaved	Total
Primary	4 728	1 243	5 971
Secondary	838	4 078	4 916
Tertiary	667	11 936	12 603
Vicinal	54	6 513	6 567
Grand total	6 287	23 770	30 057
% of total	**20.9%**	**79.1%**	**100%**

Source: National Road Administration/ANE.

A 30 year concession to construct a 700 km road in Tete province was signed with Portuguese firms Mota-Engil and Soares da Costa, a local Mozambican firm, Infra Engineering Mozambique, contracted to design, build, finance, operate and maintain the road network. The project was able to successfully reach closure after the government guaranteed minimum net revenue on the toll road. Also, an agreement was reached to review the toll sum yearly and index it to inflation. The government also promised not to grant concessions for any other road or bridge in the same area as the Tete road concession.[45]

Construction prices have been increasing

Road construction prices rose significantly in the decade between 2000 and 2010. For example, a study of six projects in the road sector found that prices quoted by bidding companies at tender rose by 216% during this time. For some projects, such as the rehabilitation of the Pemba-Montepuez Road, prices increased by 365%.[46] One reason for the increase in costs is due to inefficiencies in the procurement process: delays in procurement and payment, inadequate pre tender investigations and resulting inaccurate tender documentation, and erroneous preconstruction quantitative and financial estimates.[47] These inefficiencies have led to miscalculations and increased costs as a result. Also, because the financial resources allocated by government for road projects are not enough to meet the costs put forth by bidding companies, the works cannot be carried out to their full extent.

Regional and domestic transport linkages

The current transport and logistics system in Mozambique is designed to link neighbouring countries to Mozambique's ports and domestically, to link mines and industry to the ports as well. Secondary roads and all-season rural roads are scarce and the transport system is so deficient that it is actually cheaper to purchase crops from outside the country than to buy it from surplus regions within Mozambique and distribute it to other regions in need.[48] There is therefore enormous scope to increase domestic transport systems, especially secondary roads, which can in turn facilitate trade, agricultural development and other economic and human activities. While the government has acknowledged the importance of developing rural roads, progress has been scant. Donor funds will not be sufficient to address the backlog in construction or to meet maintenance needs and develop international corridors. The private sector, which has been quite active in transport, can scale up its participation to address the challenges faced and complement the government's and donors' efforts.

Private sector participation in the transport sector

A number of mining companies have contracted to develop or rehabilitate railway and port infrastructure to facilitate the transportation of coal from their mines to the ports for export. For example, the Brazilian mining company Vale, plans to build a 570 mile railway line connecting its coal mines in Moatize to the Nacala deep water port. The project will involve investment in increasing the capacity of the Nacala port to handle the expected increase in coal to be shipped abroad. Together with Riversdale, Vale is financing the upgrading of Berth 8 at Beira port to increase the capacity of coal it can carry. Riversdale will also co-finance the construction of a new coal terminal at Beira with the government of Mozambique. Mining companies are also supporting the development of transport corridors within Mozambique. For instance, the railway network is managed by CDN, a consortium comprised of CFM (49% stake) and the North Development Corridor Corporation (SDCN) which has a 51% stake. Brazilian mining company, Vale, bought a 51% stake in SDCN in 2010, thereby assuring its interests in the Nacala Corridor railway system. This is part of Vale's strategy to ensure transport modes for exporting coal from its mines in Tete province to Nacala port and abroad and to complement the low-capacity of the Sena railway line.

The government is also planning to grant concessions for the construction of new toll roads to link Maputo to KwaZulu Natal province in South Africa.[49] The viability of tolls on some roads, notably Vanduzi-Changara, is questionable, given the low income levels of the users in these mainly rural areas. Regional projects could help address affordability

constraints, as the example of the Maputo corridor shows. The Corridor is funded mostly by fees from wealthier South African road users, who subsidize the toll fees paid by lower-income Mozambican users. These questions must be clearly addressed when involving the private sector in these projects, especially when tolls are relied on as the main means of cost recovery for the private actor.

Private sector participation in transport has not been easy

However, there have also been some difficult experiences in engaging the private sector in transport projects. For example, the government contracted the rehabilitation of the Sena and Machipinda railway lines to RICON, a consortium of two Indian private companies. A completion deadline for the rehabilitation of the Machipanda line, which runs from Beira to Zimbabwe, was set for January 2009 but construction was delayed due to flooding in the Zambezi Valley. RICON also reportedly failed to put in place drainage channels on the railway line.[50] After several warnings and deadline extensions, the government cancelled the concession with RICON in December 2011.

Another example of a failed partnership is the maintenance contract the government signed with CETA, a Mozambican construction company. Within months of the completion of the maintenance works, potholes appeared on the road again and the National Roads Administration (ANE) was criticised for poor inspection of road operations. Both the RICON and CETA cases suggest that the government needs to play a greater role in monitoring works, and perhaps stiffer enforcements of performance targets is desirable.

Ports need additional capacity

Mozambique has three major ports at Beira, Maputo and Nacala, which act as important conduits for trade in the neighbourhood, especially for landlocked countries. It has about 13 other small ports located along the coastline. Beira port will have to be dredged and modernised and new terminals built to accommodate the growing amount of coal that is expected to pass through Beira in the years to come. The Nacala port, Mozambique's third largest port, is another important point for moving coal to markets. CDN, a Mozambican private company, currently holds the concession for managing Nacala port together with the government. However, Nacala port faces a number of difficulties: high terminal handling charges (e.g. for weighing, container storage, and wharfage); low productivity of container operations; insufficient port equipment such as shore cranes to load and unload cargo; and lengthy periods in which containers remain at the terminal.[51] There is a possibility to transport coal through barges on the Zambezi River. Riversdale has conducted feasibility studies but there are significant concerns about the potential impact on the environment and the high operating costs as a result

of constantly dredging the riverbed. Nacala port in the north of Mozambique in Nampula province, offers an alternative for barging.

Monopolistic air transport sector

Mozambique has 25 airports, including an international airport in the capital city Maputo. There are also international airports at Vilanculos, Tete, Beira, Nampula and Pemba. However, there is a lack of competitivity as the flag carrier, LAM, and South African Airways (SAA), dominate the airline sector. In April 2011, LAM and all airlines certified by the Mozambican Civil Aviation Institute (IACM) were banned from flying in the EU due to safety inadequacies such as failing to provide qualified technicians. The decision forced LAM to cancel the Maputo-Lisbon route and to lease planes and crew from Euro Atlantic, a Portuguese company. It also undermined Mozambique's code shared agreements with other airlines because tour operators are obliged to inform travelers who use a Mozambican airline for part of their trip that the airline is blacklisted. The African Airlines Association (AFRAA) criticised the European Commission's decision, citing LAM's impeccable safety record and lack of "serious" accidents in the past. The Commission's decision is expected to reduce Mozambique's inter-continental flights and could adversely impact business and tourist travel.

Competitiveness in the aviation sector was undermined when 1Time, a South African low-cost airline, pulled out of Mozambique in 2011 because it was allocated only 560 seats a week in flights even though its airplanes can carry up to 1099 seats a week. ComAir, a franchise of British Airways, took over the Maputo-Johannesburg route but this service ended within a short period of time. Because most of the airline travel to Mozambique is from South Africa, which accounts for 46% of all visitors to Mozambique[52] – it is particularly important to keep the air routes between the two countries operating smoothly. However the government has been slow in licensing private operators and the sector remains essentially a duopoly of LAM and SAA. Until the situation changes, the sector will remain closed and ticket prices quite high.[53]

The government plans to revamp some existing airports, such as the Nacala military air base, which will be converted to a commercial airport. The Brazilian contruction and engineering firm, Odebrecht, won the contract for this project, which is estimated to cost USD 110 million. The work involves building new passenger and cargo terminals, putting in place a new control tower, and refurbishing the current runway. The Inhambane airport in the south of Mozambique and the Pemba airport in the north will also be refurbished as part of a strategy to facilitate traffic in these two tourist zones. The Maputo international airport is being upgraded with the help of Chinese financing. A Chinese company has also won a contract to upgrade and

modernise the airport in the coastal tourist town of Vilanculos in the South of Mozambique.

Regional transport network

Mozambique is an important regional transportation hub, as it sits along three transport corridors linked to neighbouring countries. The most prominent example of regional transportation is the Maputo Corridor, completed in 2000 (Box 4.5).

Box 4.5. **The Maputo Corridor**

The Maputo Corridor, a PPP, links South Africa (Gauteng, Mpumalanga and Limpopo provinces) with Maputo and its port. The Corridor has been managed by the Maputo Logistics Initiative (MCLI), a consortium of public and private companies, since 2004. The rehabilitation of the 380 km highway that comprises part of the Maputo Corridor also involved an upgrade of the railway line and privatising the operation of Maputo port. The positive experience with the Maputo Corridor suggests that other transport projects, especially those to be undertaken by mining companies, should make linkages to other transport infrastructure and other sub-sectors like power. The 600 km long N4 toll road is a major part of the Maputo Corridor that links Pretoria to Maputo. It was completed in 2000 through a 30 year concession awarded to Trans African Concessions (TRAC), a public company comprised of Mozambican and South African companies. Following the completion of the N4 toll road, traffic rose by 6% per year and private investment in other sectors also increased. Moreover, average daily traffic is rising by up to 10% a year. One of the reasons for the success of the Maputo Corridor is that the project risks were appropriately shared, with the private party bearing the construction and operational risks while the public party had responsibility for the demand risk. Initially, the contract did not specify truck load regulations, placing the road at risk of degradation but in 2004, the concessionaire worked with the South African and Mozambican governments to establish axle load regulations. A strategy of load enforcement was implemented in 2002 and fines are imposed for non-compliance. The rate of overloaded vehicles on the road consequently declined, from 23% in 2001 to 9% in 2004. However this enforcement mechanism could be stricter: currently only 29% of offenders pay fines, 14% of cases are withdrawn, and in 43% of cases the courts award a discounted fine.

Source: Compiled from information from the *African Economic Outlook 2005-06* and the World Bank/ SSATP 2010 (M.I. Pinard author).

4.6. Water resources and access to water and sanitation

Has the government evaluated the investment needs in water required to support its development goals? To what extent is the private sector involved in water management, supply and infrastructure financing?

Mozambique has a wealth of water resources, including 104 river basins and two large lakes, Lake Niassa and Lake Chirua, that are shared with Malawi.[54] It is also home to 12 major dams with a total capacity of about 77.47 km^3, including the significant storage capacity of the Cahora Bassa dam. However, due to the country's high dependence on shared water resources and climatic variability, Mozambique is highly water vulnerable. Also, more than half of the country's annual runoff is generated outside the country and, as a result, water availability in Mozambique can be significantly influenced by upstream neighbouring countries' water usage. Tropical cyclones and the El Niño and La Niña phenomena exacerbate Mozambique's water variability, causing extreme floods and droughts every three to four years. These weather events necessitate the construction of climate-resilient infrastructure, including telecommunications systems, to reduce the impact of natural disasters.

Managing water resources for socio-economic development

As all economic sectors are dependent on sound water supply, water management in Mozambique is important for the growth of the economy and thus for alleviating poverty. Agriculture is by far the largest water consumer, using about 73% of total withdrawn water while industry uses about 2%, indicating that at least 75% of water use has direct impact on the performance of the Mozambican economy. The rest of the water supply is for domestic use.

Mozambique has one of the lowest rates of access for drinking water and sanitation in the world. Nationally, 47% of the population has access to drinking water while 17% of the population has access to sanitation facilities.[55] In rural areas, where 29% of the population has access to clean drinking water and 4% to sanitation, the dearth of infrastructure and services is particularly dire. Part of the explanation for the low coverage in rural areas lies in the weak institutional capacity of the Regional Water Administrations (ARAs). The five ARAs (ARA South, ARA Centre, ARA Zambezi, ARA Centre-North, ARA North) were created during the decentralization process in the 1990s. They were tasked with collecting hydrological information and water bills and for controlling irrigation systems in their respective regions. However, the ARAs have still not become fully operational except for ARA-South.

Consequently, irrigation potential in rural areas remains largely untapped and water-related constraints hamper socio-economic development in rural areas, where more than 80% of the population depends on agriculture.

Water resources management in national development strategies

The national Action Plan for the Reduction of Absolute Poverty (PARPA) specifically acknowledges the importance of water infrastructure for economic development. The PARPA 2011-14 makes reference to the importance of water resources management in relation to priority development areas such as rural development, water supply and sanitation, natural disaster management, food security and nutrition, and the environment. Specifically, the PARPA considers the development of infrastructure to be an important means of boosting agricultural productivity and PROAGRI, the government's national programme for agricultural development, also emphasises the importance of rehabilitating water supply and storage infrastructure.[56] If irrigation is adequately developed, the amount of cultivated land is expected to increase by almost 70%. However, a concerted effort is needed to increase financing in the water sector, including for water-related infrastructure such as irrigation. Water's share in the budget is small relative to other PARPA priority areas such as road construction and education.[57] The government could consider making use of its coal mining windfall to increase funding to the sector. Private sector financing could also be an important source of funding for the water sector.

Government reforms in water supply sector: private sector engagement and decentralization

The Water Law was promulgated in 1991 and the National Water Policy was approved by the government in 1995. In the 1990s, the government's aim was to restore basic services, particularly water supply in urban, peri-urban and rural areas, as the prolonged civil war had destroyed water supply infrastructure throughout the country. Decentralisation played an important role in this context. As part of the decentralisation process, the Delegated Management Framework (DMF) was introduced in 1998. Under the framework, two autonomous institutions – the Fund for Water Supply Investment and Assets (FIPAG); and the Council for the Regulation of Water Supply (CRA) – were created to replace the functions and responsibilities of the National Directorate for Water (DNA) in urban areas. FIPAG is an asset-holding investment fund that was established to promote investment and manage operations, rehabilitation and maintenance of water supply infrastructure in the country. It is also mandated to contract private operators to manage water infrastructure.[58] CRA, the independent regulator for urban water supply, is in charge of regulating services, ensuring water quality, setting tariffs and mediating between the government and concessionaires.

Through the delegated private-sector management approach, USD 350 million of foreign investment flowed into the country between 2002 and 2008. Moreover, FIPAG's geographical coverage grew from five cities to 14. This resulted in increased access rates for potable water and improved sanitation in urban areas (around 52% and 64% respectively).[59] As with transport and electricity, the government is open to partnering with mining companies for the provision of water supply and sanitation services. In 2010, FIPAG contracted Vale, the Brazilian mining company, to provide water treatment and distribution services in the town of Moatize in Tete province, where the company has significant mining interests.[60]

In recent years, water management has become increasingly centralised and investments in the sector have been problematic. In 2010, Aguas de Portugal (AdP) sold its 73% share ownership in Aguas de Mocambique (AdM) to FIPAG, making the latter AdM's biggest shareholder. The rest of the shares are owned by Mazi Mocambique, a group of local investors. AdP's divestiture in AdM follows the departure of Saur International, a French water company, in 2002. As a result, FIPAG is now in charge of the 18 largest water systems and owns the 3 regional business units (south, center and north) running the systems. A new agency, the Water and Sanitation Infrastructure Administration (AIAS), owns national sanitation assets and infrastructure assets in the rest of the towns not under FIPAG's jurisdiction. A handful of smaller systems are under private management through leases. By increasing private sector participation in the water sector, the government could see efficiency gains through improved competition.

Increased industrial water demand in Maputo

Maputo water demand projections provided by FIPAG show that from 2007 to 2028, the domestic and industrial water demand is expected to more than double in the south of the country where large industrial projects are taking place. In response to the emerging shortage of bulk water supply, FIPAG is taking the lead in upgrading water treatment and transmission facilities. The government's intention is to better connect the Pequenos Libombos Reservoir on the Umbeluzi River to Maputo so that it can supply bulk water to the city. At the same time, FIPAG is taking measures to increase efficiency in the water delivery system by reducing water losses in distribution. The Corumana and Moamba Major dams are considered to be essential to ensure water supply to the city of Maputo as well as to accommodate the development expected over the next 20 to 30 years. However the government project for the Moamba Major dam, estimated to cost USD 600 million, has not been realized due to difficulties in attracting funding. Vale had expressed interest in developing Moamba Major Dam but the Brazilian Minister of Development, Industry and Foreign Trade suggested that Brazilian investment

in the project should be guaranteed by the Mozambican government using revenues generated from coal mining in the country.[61] However, as of spring 2012, no agreement had been reached and the funding for the Moamba Dam has not yet materialised.

4.7. ICT as an enabler for other sectors

> In the telecommunications sector, does the government assess market access for potential investors and the extent of competition among operators? Does the government evaluate whether telecommunication pricing policies are competitive, favouring investment in industries that depend on reliable and affordable telecommunications?

Mozambique was the first country in the Southern African region to reform its telecommunications sector. Following the peace accord in 1992, the government began partial liberalization in the ICT market, transforming the national telecommunications operator into a state-owned enterprise (SOE), Telecommunications of Mozambique (TDM). In the same year, the government established the National Telecommunications Institute of Mozambique (INCM), a regulatory body that was given a mandate to regulate both telecommunications and the postal service. INCM is guided by the Ministry of Transport and Telecommunications and its responsibilities include tariff proposals, setting technical standards, frequency allocation, monitoring service quality and establishing licensing fees.[62]

Rapid growth of mobile market and new opportunities

Mobile phone service was first introduced in Mozambique in 1997. Until the opening of the mobile telephone market in 1999, TDM's Mcel was the only license holder. The 1999 Telecommunications Act opened the mobile market for competition and Vodacom was awarded the second license for mobile telephony operation in 2002. Vodacom is a venture between the South African-based Vodacom Group, an affiliation of Vodafone, and local investors. Mcel and Vodacom share certain infrastructure, including TDM's fibre-optic cables and antenna towers. In 2008 and 2009, however, serious connection failures occurred with TDM's fibre-optic cable, leading to a failure rate measured at 180 hours on average per month. As a result, Vodacom invested USD 63 million in building its own network in 2010.[63]

Since the adoption of mobile phone services, Mozambique has seen a continuous increase in the mobile penetration rate. From 2005 to 2010, the growth rate averaged above 34% but the market is far from being saturated

given the 35 % penetration rate. INCM and the government issued a tender for the third mobile license to increase the penetration rate and enhance the territorial coverage rate as well as to improve the quality of service through competition.[64] Movitel (a venture between Viettel Group, based in Vietnam, and SPI Gestao e Investimentos, a holding company owned by Mozambique's ruling party, won the license at USD 29 million and began operations in January 2012. Movitel's infrastructure system is made up of 1 000 second and third generation 2G and 3G base stations as well as 5 500 kilometres of fibre optic cables covering all of Mozambique's provinces and cities.[65] In the first five years of operation, Movitel is expected to invest USD 436 million in establishing its network and this could contribute to the qualitative growth of the mobile telephony market.[66]

Remaining challenges in fixed telephony

While the mobile penetration rate has surged, the fixed telephony coverage rate has been more or less even. In order to tackle the stagnation of the fixed telephony market, the government adopted a pro-competition Telecommunications Act in 2004 that aimed at liberalizing the fixed market by 2007. In line with the liberalization policy, TDM was privatized in 2008 and the market has been open since. Despite the efforts of the government, there has been no visible change in the fixed telephony market and TDM remains the sole operator. One explanation is that the heavy investments required in building networks for fixed telephony service acts as a barrier that impedes new operators from entering the market. Another explanation is that, on the whole, while prices for mobile telephone services have decreased over time, the cost of fixed line telephone services have actually gone up, making it cheaper to call from a cellphone than from a landline.

Achieving universal access and rural development

Universal access (UA) has been part of the government's objective in the ICT sector since 2004. The Telecommunications Act of 2004 established the Universal Access Fund (UAF) with the aim of accelerating the use of ICT by the wider population in Mozambique. The fund was established in 2006 and is managed by INCM. Funding comes from operators who are obliged to make contributions equal to 1% of their income after taxatio. Due to INCM's lack of expertise in this area, it took the fund two years to implement its first project. In its first year of operation, UAF only utilised USD 1.8 million, or 21%, of its accumulated funds suggesting that disbursement is a challenge to be tackled.

Regional submarine fibre-optic cable networks present new opportunities

Internet in Mozambique was first introduced by Eduardo Mondlane University in 1993 through the university's information centre. Affordable internet access with nation-wide services only became available in 1997 when TDM became the national internet service provider. Internet connectivity is still considerably low in Mozambique: as of 2010, 4.2% of individuals had access to the internet, compared to 6% in Botswana and 11% in Tanzania. The high cost of bandwidth is a significant factor behind the low connectivity rates. Also, personal computers are not affordable to most households in Mozambique and as a result, household connection rates remain negligible.[67]

Despite the challenges, Mozambique's internet landscape is about to experience significant changes with the operation of two regional submarine fibre-optic cable networks, SEACOM and EASSy, that both have inland connecting points in Maputo. SEACOM and EASSy connect the whole region of Southern and Eastern Africa to other parts of the world including Europe, the Americas, the Middle East and Asia. SEACOM became operational in 2009 and EASSy in 2010.

In order to fully benefit from improved international connectivity, investments are needed to develop domestic backbone networks that connect Mozambique to the submarine cable networks. A sound policy to develop the domestic backbone network must encourage private investment in commercially viable areas such as urban centres and provide public resources for investment in less profitable areas such as rural villages. With domestic backbone networks in place, Maputo can become the regional hub for neighbouring landlocked countries to access EASSy and Seacom. Such regional co-operation could facilitate the development of inter-regional backbone networks and enlarge the e-commerce trade among African countries as well. E-commerce could in turn catalyze the growth of SMEs and micro-sized enterprises in Mozambique and once the internet connection is stabilized, Mozambique would have better prospects to house Business Process Outsourcing (BPO) facilities such as call centres for Lusophone countries.

Prospects for ICT in agricultural development

ICT innovations have made it possible for small-holder farmers in Africa to get access to real-time information on commodity prices, consumer trends, weather forecasts, and pests and disease control. However, the role of ICT in agriculture has not been visible in Mozambique due to constraints such as low internet accessibility and insufficient information available online. As the mobile penetration rate is rapidly growing and internet is becoming cheaper

with the introduction of WiMAX, the wireless internet service, and the undersea cables, Mozambique's ICT environment has nonetheless seen steady improvements in recent years. ICT tools can help Mozambique to prevent and minimise damage caused by natural disasters such as floods and droughts.

In order to better integrate ICT into agricultural sector policies, long-term perspective is needed and policies must be carefully tailored for Mozambique's particular circumstances. In fact, one study found that when government failed to include farmers in deciding which information to collect and disseminate, the information turned out to be less useful for end-users than if they had been consulted in the first place.[68] To avoid such inefficiency, stakeholders from different sectors including government, farmers' community unions, research experts from universities and research institutions need to pool their ideas and exchange information on a regular basis, possibly under the form of multi-stakeholder learning mechanisms.[69]

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