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Working Paper

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WIDER Working Paper, No. 2020/136

Provided in Cooperation with:

United Nations University (UNU), World Institute for Development Economics Research (WIDER)

Suggested Citation: Macuane, José Jaime; Muianga, Carlos (2020) : Natural resources, institutions, and economic transformation in Mozambique, WIDER Working Paper, No. 2020/136, ISBN 978-92-9256-893-1, The United Nations University World Institute for Development Economics Research (UNU-WIDER), Helsinki,
<https://doi.org/10.35188/UNU-WIDER/2020/893-1>

This Version is available at:

<https://hdl.handle.net/10419/229360>

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WIDER Working Paper 2020/136

Natural resources, institutions, and economic transformation in Mozambique

José Jaime Macuane¹ and Carlos Muianga²

October 2020

In partnership with



This study was prepared under the Mozambique component of the Economic Development and Institutions (EDI) Programme funded with UK aid from the UK government in collaboration with the Inclusive Development in Mozambique (IGM) Programme funded by the Governments of Finland, Norway, and Denmark. The EDI Programme Directorate includes the following institutions that work in partnership: Oxford Policy Management, University of Namur, Paris School of Economics, and Aide à la décision économique.

Abstract: In the light of Mozambique's natural resources boom—especially its large-scale investments in mining, oil, and gas—this paper analyses the prospects for the extractive industries to contribute to economic transformation from an institutional perspective. To this purpose, we address the institutional dynamics of the resources sector and consider the underlying causes of the identified outcomes. The National Development Strategy, as the instrument presenting the vision for economic transformation and diversification, is discussed. The paper is based on a desk review—documental and bibliographic—and on primary data gathered by the authors as part of their research into the field of natural resources and the political economy of development. We conclude that, given Mozambique's political patronage and clientelism, intra-ruling elite competition, limited productive base, weak state capacity, high level of poverty, and recurrent fiscal deficits, the prospects of the current resource boom leading to economic transformation, despite its considerable potential, are at best uncertain.

Key words: economic transformation, extractive industries, institutions, Mozambique, natural resources

JEL classification: O13, O23, O25, O43

Acknowledgements: The authors would like to acknowledge the inputs to the research and to the paper and the support throughout the process of the Copenhagen University team: Professor Finn Tarp, Dr António Cruz, Dr Inês Ferreira, and Mr Johnny Flentø. We would also like to acknowledge the valuable comments and contributions made by Dr Vasco Nhabinde, from the Ministry of Economy and Finance of Mozambique, and Tony Addison. These contributions notwithstanding, the authors are responsible for the content of the paper.

Note: The translated version of the paper in Portuguese is available [here](#) ([disponível em Português](#)).

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This study is published within the project on [Inclusive growth in Mozambique—scaling-up research and capacity](#).

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Information and requests: publications@wider.unu.edu

ISSN 1798-7237 ISBN 978-92-9256-893-1

<https://doi.org/10.35188/UNU-WIDER/2020/893-1>

Typescript prepared by Joseph Laredo.

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The Institute is funded through income from an endowment fund with additional contributions to its work programme from Finland, Sweden, and the United Kingdom as well as earmarked contributions for specific projects from a variety of donors.

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The views expressed in this paper are those of the author(s), and do not necessarily reflect the views of the Institute or the United Nations University, nor the programme/project donors.

1 Introduction

Until recently, the contribution of the extractive sector (mining and gas) to Mozambique's Gross Domestic Product (GDP) was below 4 per cent, on average. Agriculture is still regarded as the basis of the country's development, employs more than 70 per cent of the labour force, and contributes over 20 per cent of GDP. This situation is set to change with the growing importance of the extractive industries, particularly the gas industry. The production of this commodity started in 2004 with the Pande and Temane projects of the South African company SASOL. The discovery of vast gas reserves in the early 2010s in the northern province of Cabo Delgado heralded the beginning of a new economic era, with prospects of foreign direct investment (FDI) that would dwarf the current US\$14 billion GDP and make an estimated US\$50 billion contribution to state revenues by 2050 (República de Moçambique 2018). The past decade and a half has also seen an upsurge of investment in the mining sector. Kenmare's heavy sands project in Moma began in 2007 (US\$460 million), and the coal projects of Rio Tinto and Vale (US\$1.3 billion) in the Tete Province and the Montepuez Rubi Mining gems project all started operations in 2011 (Deloitte and EITI 2018).

Recent developments in the gas sector, including the investment projected for the coming decades, have prompted significant changes in expectations over its contribution to the economy. The main gas projects in the Rovuma basin (Areas 1 and 4) are expected to attract investment of over US\$50 billion in the next few years (IMF 2019).

The Area 1 consortium, led by Total (formerly by Anadarko)¹, announced its final investment decision (FID) in June 2019. The consortium plans to invest about US\$23 billion and the project is expected to generate US\$2.1 billion in state revenues over a 25-year period. It is also expected that about 5,000 workers will be employed during the construction phase and US\$2.5 billion will be devoted to the purchase of goods and services from Mozambican companies. In July 2020, Total signed all financing contracts, securing all the US\$15.8 billion funding for its Rovuma project.² This followed a decision by the United States (US) EXIM Bank to secure a loan of about US\$4.7 billion to finance American suppliers to liquefied natural gas (LNG) development in Mozambique. Additionally, it is said that the loan could support about 16,700 American jobs over the five-year construction period.³ An additional US\$1 billion from United Kingdom (UK) Export Finance is on track to be approved, and this would support about 2,000 jobs for British people.⁴ These recent developments mark a turning point in the negotiations to start LNG production in the Rovuma basin.

The ENI and Exxon Mobil-led Area 4 project announced its initial investment decision of about US\$500 million in October 2019. The FID of about US\$30 billion was to be announced last year

¹ Area 1 LNG shareholders are Total E&P Mozambique Area 1 Ltd (26.5 per cent), ENH Rovuma Area 1, a subsidiary of the state company ENH (15 per cent), Mitsui E&P Mozambique Area1 Ltd (20 per cent), ONGC Videsh Ltd (10 per cent), Beas Rovuma Energy Mozambique Ltd (10 per cent), BPRL Ventures Mozambique B.V. (10 per cent), and PTTEP Mozambique Area 1 Ltd (8.5 per cent).

² <https://clubofmozambique.com/news/mozambique-lng-consortium-led-by-total-has-already-signed-all-financing-contracts-o-pais-164769/>

³ <https://www.bloomberg.com/news/articles/2020-05-15/u-s-throws-down-gauntlet-to-china-with-mozambique-gas-mega-loan>

⁴ <https://cartamz.com/index.php/politica/item/5533-emprestimos-de-5-7-bilhoes-de-usd-para-a-total-vao-garantir-18-700-empregos-nos-eua-e-no-reino-unido>

but was postponed to an unknown date.⁵ Reports from June 2020, citing the INP chairman, claim that the ENI-led Coral-Sul Floating Liquefied Natural Gas (FLNG) project is on schedule, as the construction of the FLNG unit is 73 per cent complete with no significant delays expected. The global supply chain is due to be completed in 2021 and production is expected to start in 2022.⁶

The combined gas projects are set to produce about 30 million tonnes of LNG per year—about ‘17 per cent of total 2017 trade or 7.5 per cent of projected LNG trade by 2026’ (IMF 2019: 4).

Mozambique’s resource abundance also prompted an upsurge of investment, especially FDI, in extractive resource-related projects and other auxiliary services, and the country became one of the most important destinations of FDI in Sub-Saharan Africa. This investment upsurge lasted until 2016, when the economy was hit by a crisis of commodity markets, which affected some of the main Mozambican export commodities, in particular coal. The investment decline was further aggravated by the discovery of undisclosed loans—known as ‘hidden debts’—of about US\$2.2 billion in 2016 to supposedly fund three government-related security companies on the assumption that they would profit from the new gas industry (Roe 2018).

The growth of the extractive sector has triggered discussions in various academic and political contexts over the prospects of natural resource exploitation in Mozambique and developing countries more generally. One of the issues in discussion is the country’s prospects to reduce or even end its dependence on external resources—development aid and FDI—which dominated and drove the country’s economy in most of the post-independence period (Vollmer 2013). Another point is the prospect of economic transformation, through the use of natural resources to boost industrialization, transfer technology and knowledge to local companies, create economic linkages, and stimulate the diversification of the economy (Dietsche and Esteves 2018). Managing the macroeconomic dimensions is also crucial: these include the avoidance of ‘Dutch disease’ and other adverse consequences of a sudden increase in foreign exchange inflows linked to the natural resources boom (Saad-Filho and Weeks 2013). Henstridge and Roe (2018) suggest that governments can use macroeconomic policies—fiscal and monetary—to mitigate the risk of the disease. However, they warn that in low-income countries such as Mozambique, ‘fiscal policy has to bear the brunt of responsibility, with monetary policy normally taking the stage as a supporting player’ (Henstridge and Roe 2018: 165).

As the literature suggests, diversification of the economy and economic transformation require an industrial policy and a certain level of state capacity, which depend on the relations between and support of relevant political actors (Whitfield et al. 2015). Also important is understanding the political economy of the development strategy, and the issues arising from this, e.g., the conflicting interests emerging from the implementation of the policy or strategy, the winners and losers in this process, and the ability of the state to manage such conflicting interests in a productive way (Chang and Andreoni 2020).

Since the turn of the 21st century, especially over the past decade, it has been widely argued that ‘industrial policy is back’, with new approaches, theories, and practices on the topic emerging (Aiginger and Rodrik 2020; Chang and Andreoni 2020; Dietsche 2018b; Stiglitz 2017). Most economists agree, however, that the reliance on ‘perfect markets’ has not brought about satisfactory economic and social outcomes in most of the developing world (Chang and Andreoni 2020; Rodrik 2004; Stiglitz 2017). With regard to Sub-Saharan African economies (including

⁵ <https://furtherafrica.com/2020/06/05/mozambique-expects-exxon-gas-fid-in-2021/>

⁶ <https://allafrica.com/stories/202006040840.html>

Mozambique), for instance, it has been documented that, despite the high growth rates of the past two decades, these economies ‘have experienced unsatisfactory productive transformation’ and low job creation in manufacturing and services (Aiginger and Rodrik 2020: 1). Most of these countries’ growth patterns are highly dependent on commodity production and exports, including minerals, gas, oil, and other agricultural commodities. These countries have failed to translate their resource endowments’ ‘comparative advantages’ into structural transformation and significant poverty reduction. The case for industrial policy and its practice in the extractives sector is built upon these and other issues related to the development outcomes of resource dependence.

In the context of the growing extractives-led development agenda, Dietsche (2018b) argues that, despite its increasing importance, the contribution of industrial policies and strategies to structural transformation is not clear, especially regarding what positive institutional change they can bring about that can sustain the gains in economic transformation over time. The same is applicable to the promotion of local content strategies and policies as a way to link foreign investment to the local economy, as these are seen as having an equally narrow focus and lacking the facility to track the contribution they make in terms of productive knowledge and technologies. Amidst the lack of consensus on the contribution of industrial policy to economic transformation, the best that public authorities can do in this context, according to Dietsche (2018b), is to provide institutions that reduce transaction costs.

Buur et al. (2019) argue that for large-scale natural investments to attain their transformational goals, they need to create the proper conditions to prevent key actors from blocking their implementation. They analyse the relations between three main actors—ruling elites, investors (international and domestic), and local populations—and suggest that the way these actors negotiate their interests can affect the creation of conditions favourable for the implementation of large-scale investments in natural resources. In particular, they call attention to the importance of the relations between ruling elites and local populations, which have generally been neglected in studies in this area.

A World Bank study argues that countries that are successful in using natural resources—natural capital—to promote development are those that invest in other forms of capital, such as human and productive capital, and even in assets in other countries. The study further asserts that the appropriate use of natural capital depends on the quality of the governance and institutions of the country (World Bank 2014). This discussion is linked to the question of how much to save or spend when a country has a resource windfall, as in the case of Mozambique. A key issue is the creation of a sovereign wealth fund (SWF) from natural resources revenues and how this should be used, which has implications for the implementation of policies for structural transformation.

The insight of the above-mentioned scholarship is that a development strategy should link the exploitation of natural resources and the use of its revenues to the country’s development goals. It should define a framework of relevant national and sectoral policies, and identify institutions for the articulation and coordination of different interests. In the case of Mozambique, the National Development Strategy (NDS) 2015–2035 highlights the role of natural resources in the structural transformation of the economy. Therefore, to some extent, the NDS has an extractives-led development component. The question is how this plays out in practice and what the prospects are for that contribution to be effective. In Mozambique, with its political patronage and clientelism, intra-ruling elite competition, limited productive base, weak state capacity, high level of poverty, and recurrent fiscal deficits, the prospects of the current resource boom leading to economic transformation, despite its considerable potential, are at best equivocal. The critical issue of how and when to use the resources was clouded by the debt crisis, when loans were contracted and then restructured on the assumption of future revenues from gas projects. This casts doubt

on the willingness and ability of the political elites to use extractive resources for economic transformation.

This paper analyses the prospects for the natural resources/extractive industries to contribute to economic transformation in Mozambique from an institutional perspective. To this purpose, we address the institutional dynamics of the resources sector and consider the underlying causes of the identified outcomes.

The paper is structured as follows: Section 2 presents the conceptual and analytical framework. Section 3 describes policies and institutions that are relevant to the process of structural transformation based on the development of the extractives sector. Section 4 assesses how policies and institutions relate to the process of economic transformation in the context of the growing importance of natural resources. Section 5 explains the dynamics of economic transformation and institutional performance, looking at their underlying causes. The paper closes with conclusions and an assessment of the opportunities for natural resources to play an effective role in economic transformation, taking into account the context of Mozambique.

2 Conceptual and analytical framework

Structural transformation, as it is broadly understood, ‘requires raising productivity across different sectors and achieving competitiveness in progressively higher value-adding sectors’ (Khan 2018: 42). It is also understood as the reallocation of economic activity across the broad sectors of the economy, namely agriculture, manufacturing, and services (Herrendorf et al. 2013). It entails the reallocation of resources—including labour—from less to more productive sectors of the economy and involves changes in the level of productivity across sectors. With regard to extractive industries or natural resources (we use the two terms interchangeably), we refer to mining and oil and gas (O&G). Whilst in some cases (e.g. revenues) the paper will consider aggregate data on the two sectors, the analysis of the sectoral dynamics will focus on large-scale investments or megaprojects (investments of more than US\$500 million), which are the dominant feature in the sector.

Here, institutions are considered as the political, social, and economic rules of the game—formal and informal norms—that are largely accepted and mediate the relations between individuals and collective actors in society (North 1990; North et al. 2009). In the economic realm, these institutions can be at different levels, such as belief systems and formal rules on the one hand, and the institutions responsible for putting the rules in place (governance) and ensuring the efficient allocation of resources as the market on the other (Diestche 2018a). The analytical framework of the paper is built on the concepts of new institutional theory and the role and effects of institutions on development (Acemoglu and Robinson 2012; North 1990).

We also assume that institutional performance is contingent on the context, and that similar institutions might perform differently in different contexts (Khan 2010; North 1990). One explanation for this variable performance can be found in the interface between formal and informal institutions. As Khan (2018) argues, inclusive institutions—considered as having a positive effect on development everywhere (Acemoglu and Robinson 2012)—might have different outcomes in developing countries, where powerful groups constrain broad-based growth. Therefore, we do not adopt a normative vision of the ‘best institutions’ but rather use the theoretical categories to describe the institutional dynamics and their impact on development.

We also consider policies as a type of rule, although much easier to change than institutions (Khan 2018). As a complement to this analytical framework and to provide a more critical and nuanced view of institutions, we refer to more recent literature on the political economy of development in the context of Africa and Mozambique, based on the political settlement framework, applied to governance and large-scale natural resources investment (Buur et al. 2019; Macuane et al. 2018; Macuane et al. forthcoming; Salimo et al. forthcoming; Weimer et al. 2012; Whitfield et al. 2015). Whilst we acknowledge that institutional analysis and political settlement analysis are different approaches (Behuria et al. 2017), we depart from the institutionalist analytical and conceptual framework to identify the analytical categories of our study. Additionally, we consider that outcomes depend on a combination of institutions and the context, among them the role of actors (groups and individuals) and their ‘holding power’—the capacity to engage in conflict with other actors and survive, as well as the power to enforce the existing rules (Behuria et al. 2017; Dietsche 2018a). This approach is important if we are to identify specificities of the empirical reality we are analysing, where there is a high level of informality and where manifestations of a Weberian state and impersonal institutions are not the norm (Khan 2010; North et al. 2009). An example of the application of the political settlement framework to natural resources investment is the creation of pockets of effectiveness (PoE)—organizations with high performance in a context of a generally inefficient public sector (Roll 2014)—in the gas sector in Africa generally (Hickey 2019; Hickey and Izama 2017) and in Mozambique particularly (Macuane et al. forthcoming).

To operationalize the framework, we adopt Baldwin et al.’s idea that ‘Institutional analysis comprises a suite of approaches for understanding the various ways in which formal laws and informal social or organizational norms shape policy actors’ behaviour’ (Baldwin et al. 2018: 2). A challenge of the institutional analysis is the difficulty in empirically operationalizing its variables (Baldwin et al. 2018; Siddiki et al. 2019). In operational terms we adopt the multi-level institutional analysis proposed by two of the principal exponents of the field, Williamson and Ostrom (Baldwin et al. 2018; Dietsche 2018a; Ostrom 2005; Siddiki et al. 2019; Williamson 2000), the levels being (i) the social level—socially embedded norms; (ii) the institutional environment or policy level—formal rules of the game; and (iii) the governance level—the operation of the rules of the game. This means that we will analyse the formal rules and policies, how they are implemented, their interface with the informal rules, and their outcomes. The analysis also has to be sensitive to the role of external actors. This is particularly relevant in the context of Mozambique, where high dependence on external resources is a key element in its political economy.

In the case of Mozambique, where the contribution of the recent boom in natural resources to economic transformation is yet to be seen, the argument will be forward looking. However, some past and present dynamics are important in building up the argument. In this regard, we look at the following elements: (i) institutional environment and performance—i.e. formal rules/legislation, policies, their implementation, and outcomes in relation to the structural transformation of the economy; (ii) the history of the contribution of natural resources to the economy; (iii) the role of natural resources in economic transformation, namely policy and institutional choices and their effects; (iv) the underlying dynamics of policy and institutional choices and their economic transformation effects, with a focus on the relation between actors, institutions, and outcomes.

3 Policies and institutions

In the last two decades, with the increasing importance of the extractive industries in the economy, Mozambique has passed extensive legislation in the extractives sector, with a focus on the mining and O&G sector and its respective tax regime. Concerns over the governance of the sector, along

with demands for more accountability on the management of natural resources revenues, led Mozambique to join the Extractive Industries Transparency Initiative (EITI) in 2009 and become a compliant member in 2012.⁷ Since then, Mozambique has produced eight reports, and improved its transparency, making the contracts of the natural resources' concessions publicly available. Reforms in the sector have included the creation and strengthening of administrative, regulatory, and accountability institutions, combined with the increasing participation of civil society in the debate on the contribution of natural resources to the country's development.

Whilst these reforms have improved the governance of the sector and responded to some of the challenges of its increasing importance, their effect on the country's economic transformation is more difficult to quantify. Not only is the importance of natural resources a relatively recent phenomenon in the economy, whose effects are still to be seen, but, as we have seen, economic transformation is underlain by a complex web of institutions, policies, actors, and dynamics. In this section, we describe some of these, as the background to assessing the role of institutions in the emerging resources economy of Mozambique, and the dynamics of economic transformation more broadly. In this regard, we analyse the NDS, which is the government's main instrument for presenting a vision of the contribution of natural resources at the macro level. We also assess the key structuring policies for economic transformation and the normative instruments of the extractives sector itself.

3.1 National Development Strategy

Mozambique has a set of long-term and mid-term instruments that are the framework of government policy and plans. The main long-term document is Agenda 2025 (Comité de Conselheiros 2013). The Vision was originally defined in 2003 and revised in 2013 to align it with emerging challenges. According to Agenda 2025, development must be endogenous, prioritizing the national market through the widening of the production base of small and medium enterprises (SMEs).

In 2014, the country adopted the National Development Strategy (NDS) 2015–2035, based on the general lines of Agenda 2025. The main objective of the NDS is to improve the living conditions of the population 'through structural transformation of the economy [and] expansion and diversification of the production base' (República de Moçambique 2014b). Thus, industrialization is at the core of the programme, and both agriculture and the extractive industries are aligned with the objective of structural transformation of the economy. The NDS acknowledges that the national economy generally and the rural economy particularly depend heavily on the exploitation and use of natural resources. The strategy further includes the creation of an Investment and/or Stabilization Fund from the surplus revenues and resource windfalls resulting from the extraction of natural resources (República de Moçambique 2014b: 20). The linkage of the mineral resources sector with industry will be through vertical integration of minerals production—coal, gas, ore, and mineral sands—assuring their transformation into industrial goods for national and international markets. In the area of the extractive industries, the strategy includes (i) the establishment of a partnership between national and foreign enterprises in the exploitation of resources; (ii) the involvement of national enterprises in the provision of services; and (iii) the creation by the state of public–private partnerships (PPPs) for the provision of goods and public services (República de Moçambique 2014b: 37).

⁷ The EITI is a global standard for the transparent and accountable management of natural resources, to which countries adhere voluntarily. To be considered compliant, a member country must complete steps defined in the Standard. For more details see <https://eiti.org/document/eiti-standard-2019> and <https://eiti.org/mozambique>.

In the extractive industry—especially coal, gas, and heavy sands extraction—the main challenge posed by the NDS is the need for domestic transformation—a process which, according to the strategy, may address the problems related to primary commodity export dependency.

Considering natural resources as fundamental for economic growth and structural transformation, the NDS points out that sustainable management is, among other factors, key to their success. This strategic vision supports, at least partially, the established argument that ‘resource-based accumulation is not an end in itself, but a means or stage(s) within a dynamic process of industrialization and economic transformation’ (Castel-Branco 2011: 2). However, how resource-based accumulation should translate into industrialization and economic transformation is not systematically explained in the strategy. Nor does the NDS set out how the revenues generated from the country’s natural resources will finance the policies for transformation.

The NDS does not mention explicitly the role of FDI, but inferences can be drawn about the role of FDI in development from the assertion of the need for the state to avoid investing in areas where the private sector can perform better, and from its encouragement of national companies to establish partnerships with foreign enterprises and, through them, potentially mobilize funding. The resources for the project of economic transformation will hypothetically come from the country’s strategic and operational instruments of planning and budgeting, at the government and sectoral levels, and potentially from the above-mentioned Investment/Stabilization Fund. Thus, for the NDS to attain its stated objectives, macroeconomic policies (fiscal and monetary), industrial policies, and relevant sector policies, especially related to the extractives, should define and determine the instruments for economic transformation. The following sections analyse the extent to which those instruments are consistent with the goals stated in the NDS with regard to the contribution of the extractives sector to structural transformation.

3.2 Macroeconomic and sector policies

A set of policies creates an environment in which different economic and social actors can operate to generate structural transformation. These are the macroeconomic policies and key sector policies, but with a structural impact as the industrial policy. Macroeconomic policies (monetary and fiscal) play a central role in defining the conditions and directions of structural transformation. Their management is a major institutional factor determining the way the resources sector can effectively contribute to such a transformation. A major and widely discussed issue related to macroeconomic policy management in the context of extractives is how to avoid the adverse impacts of resource dependency, resulting, for instance, from a sudden increase in foreign exchange inflows—‘Dutch disease’. Mozambique is no exception, and major challenges regarding macroeconomic policy management are still to be addressed. These concern not only the role monetary and fiscal policy play in preventing Dutch disease, but also, and fundamentally, their role in creating the conditions for structural transformation.

As it is argued in the most recent Industrial Policy and Strategy (2016–2025), productive linkages between domestic SMEs and megaprojects, particularly in the natural resources sector, are seen as a way to strengthen the domestic private sector (República de Moçambique 2016). These processes require commitment to the creation and improvement of institutional capabilities, in both the state and the private sectors, and at various levels (political, economic, organizational, and financial). However these commitments are set up and whatever particular institutional and organizational capabilities are needed, the role of the state and the private sector in providing, through investment, the incentives to make them effective is central.

Complementary to the debate about industrial policy has been the discussion about local content (the participation of the national companies in the natural resources investment projects). This was

initiated in 2007, but only in 2019 did the government approve a legislative proposal to be submitted for enactment by parliament. Discussions between the government and national private companies about how and to what extent Mozambican enterprises would benefit from the new developments in the extractive sector are the most contentious. Emphasis and interest, especially from the domestic private sector, have been particularly on the upstream sector of the resources industry (i.e. the supply of goods and services relevant to the operations of the gas projects).⁸ The debate over the development of linkages is related to the fact that the main multinational corporations (MNCs) operating in the O&G sector in Mozambique have already approved their production plans for the next few decades, some of them including FIDs. FIDs for the projects in the northern Cabo Delgado province have created a set of expectations regarding the benefits of the gas exploitation to the country's development, including the business opportunities for domestic private enterprises (Muianga 2019a, b). However, most of these companies control global value chains (GVCs) within the industry and impose high international standards on their suppliers that local companies can hardly match. This poses the question as to how the natural resources projects can create opportunities for linkages that can contribute to the transfer of know-how and technology for a sustainable diversification and structural transformation of the economy. The institutions and policies designed to respond to this question are described in the next section.

3.3 Policy and institutional environment of the extractive industries sector

As mentioned before, the extractives sector considered here comprises large-scale mining, and the O&G sector. Reforms in this sector have included the separation of the policy, commercial, and regulatory functions previously lumped together in one entity, such as the national oil company (NOC), a ministry, or agency. In the case of the gas sector, this was part of the so-called new institutional arrangements (NIA), following the Norwegian model, which was considered an example of good governance (Thurber et al. 2011). In Mozambique these reforms were reflected in the redefinition of the functions of the Hydrocarbons National Company (ENH), the NOC, which maintained the commercial functions but saw its former regulatory functions being allocated to the National Petroleum Institute (INP), as a result of pressure from the World Bank—Norwegian cooperation, the long-time donors to the sector (Macuane et al. forthcoming). The implementation of these reforms was more a strategic choice in a context of a country dependent on external resources than part of an internal agenda. In this regard, reforms were stimulated by increasing demands for the accountability of the sector in the international arena, embodied in the EITI, and by the need to attract FDI, which implied complying with international standards, to respond to pressures from donors and investors (Macuane et al. forthcoming). The disproportionate influence of external factors and actors' interests in the reforms to some extent explains the weak performance of institutions in this area, stemming from the limited commitment of the ruling elites to the process (Macuane et al. forthcoming). Specific reforms in the gas and mining sectors are presented below.

Institutional reform in the gas sector

Well before these recent developments, Mozambique had set up new legislation and revised existing legislation, policies, and institutions for the 'promising' gas sector. The main policy instruments in the gas sector are the legal framework and the Natural Gas Master Plan (República

⁸ There has been little discussion on the possibility of the development of the downstream sector, although, with respect to the O&G industry, policy discourse has emphasized the importance of this, especially in the NDS, discussed in the previous section, and the current industrial policy and strategy, 2016–2025 (República de Moçambique 2016). This may be explained by the fact that gas production has not yet started in the Rovuma basin. However, the possibilities of developing such downstream production appear to be very limited if we look at the structure of the gas industry, which consists essentially of primary commodity exporters.

de Moçambique 2014a), which regulate investment in and governance of the sector. Due to its specificity this area has a specific legislation regime for investment, embodied in its core laws and regulations.

Recent legislative changes can be traced back to 2001, when the Oil Law was approved. Among its many initiatives, this introduced the direct participation of foreign enterprises and defined the mechanism of state participation in the sector. In 2004, the government approved the Regulations of the Oil Operations (Decree 24/2004) and, within this legal framework, a model concession contract was designed. In the same year, the National Petroleum Institute (INP) was created. This took over the role of regulator (under Decree 25/2004). Two additional regulations were subsequently approved: for the licensing of premises for oil activities (Ministerial Diploma 272/2009) and the Environment Regulation for Oil Operations (Decree 56/2010).

This legal framework prevailed until the recent discoveries of gas, which made the existing laws obsolete. Under pressure from investors, the government proposed, and parliament approved, a new Oil Law, 21/2014, on 18 August 2014. Parliament also approved a law authorizing the government to enact specific legislation on LNG in order to address the legal void for future investments in the Rovuma basin (Areas 1 and 4). Additional legislation was approved in 2014 and 2015, including regulations specific to the projects of the Rovuma basin (Law 25/2014 of 23 September 2014), the petroleum fiscal regime (Law 27/2014 of 23 September 2014, revised as Law 14/2017 of 28 December 2017), on the taxation and tax benefits of petroleum operations (Decree 32/2015 of 31 December 2015), and on the Environmental Impact Assessment (Decree 54/2015 of 31 December 2015). Subsequently, in 2017, additional legislation was approved. The fiscal legislation allows companies to recover part of the costs of their investments, and it is the responsibility of the INP to certify these costs to prevent companies from inflating them, hence reducing the revenues to be collected. The 2014 Petroleum Law includes provisions on local content, which consists of the participation of the ENH in all concessions and the involvement of local companies and markets in the procurement of goods and services for petroleum operations. The main concern relates to the weak capacity of the local companies to provide goods and services in terms of both scale and quality to meet the demands of the international companies involved in large-scale petroleum operations.

The Natural Gas Master Plan is consistent with the NDS concerning industrialization and linkages. In this regard, it includes the development of an industrial zone with integrated support services in Nacala, Palma, and Pemba, a fertilizer plant, and a power plant. The Gas Master Plan promotes increased industrialization of the country through the emergence of SMEs linked to the megaprojects.

A set of policy, regulatory, and administrative institutions operate in this area: (i) the Ministry of Mineral Resources and Energy, responsible for government policies; (ii) INP, the sector regulator; (iii) the public-owned company ENH, which participates in all O&G projects with a share ranging from 10 per cent to 25 per cent, and is the main shareholder of the Mozambican Hydrocarbons Company (CMH, a subsidiary of the ENH), which participates in the Pande and Temane gas ventures; (iv) Mozambique's Tax Authority (AT), responsible for fiscal revenues collection; and (v) the Administrative Court (TA), which plays the role of the auditor general and is responsible for the external audit (compliance and performance) of the whole public sector.

The INP is the entity responsible for coordinating the bidding process for the oil and gas concessions. It is therefore the main entry point for investments in this sector. The Ministry of Mineral Resources and Energy is responsible for policies related to natural gas (and mining) as well as the rest of the energy sector. It therefore coordinates the potential linkages between gas and coal extraction and power generation projects. The AT is the entity responsible for the taxation of

gas operations, and in 2017 it created a specific unit to deal with extractive industries taxation. Finally, the TA is the entity responsible for auditing oil contracts and all operations related to revenues, including the revenues from natural resources received by public entities.

Legislation, policies, and institutions of the mining sector

The Strategy and Policy of Mineral Resources approved by the government in December 2013 states that mineral resources must above all benefit Mozambicans. Among its objectives is to make mineral resources one of the main contributors to industrialization and country development, diversification, and economic transformation, as well as to the improvement of the balance of payments (Resolution 89/2013, article 4, a). It also aims to ensure the implementation of corporate social responsibility (CSR) in the business sector involved in oil and mining activities and the attribution of benefits and special compensations to the communities where mineral extraction occurs.

As in the gas sector, investments in this sector are regulated through a specific law, the mining law (Law 20/2014 of 18 August 2014), which defines specific contracts for the different phases of the mining process, from prospection to exploitation. The law also regulates the different scales of mining (from big investments to artisanal mining) and licences for the trading of mineral products. As in the gas sector, there is a specific fiscal regime for the mining sector approved on 23 September 2014 (Law 28/2014) and revised on 28 December 2017 (Law 15/2017). AT and the Administrative Court exert the same mandates regarding taxation and auditing as in the gas sector.

The 2014 mining law created two entities, namely the High Authority for the Extractive Industry (HAEI) and the National Mines Institute (INAMI). The HAEI is a mixture of a regulatory and oversight body comprising representatives of government, the National Assembly, and civil society. In the commercial area there is a state-owned (85 per cent) company, the Mozambican Company for Mineral Exploration (EMEM), created in 2009 with the objective of defending the interests of the state in the mining sector, manage the state's shares in mining investments, ensuring the participation of local companies, and promoting local content in the sector.

The institutions of both the mining and the petroleum sectors, apart from the HAEI, are under the tutelage of the Ministry of Mineral Resources and Energy, which plays the coordination and policy role.

This institutional setting, comprising a set of legislation and policies, and the actors—MNCs, donors, public entities, organizations, and political actors—operating within it is key to understanding the contribution of natural resources to structural transformation. Consequently, it is important to analyse the performance of these institutions in interaction with the actors that operate within them, to understand their role in the process of economic transformation.

4 Natural resources, institutional framework, and economic transformation

The institutional setting (policy and legislation) of the extractives includes various elements with the potential to promote economic transformation, among them the involvement and promotion of local companies and markets and the promotion of national industrialization. However, despite the existence of a clear vision in the NDS, at the operational level there is no instrument that brings all the relevant elements together. Moreover, the instruments that do exist provide neither a clear plan of resources mobilization for the diversification of the economy, nor broad and structuring macroeconomic and strategic sectoral policies linked to the demands of structural transformation.

This section shows how the institutions identified in the previous section are performing in the context of the natural resources economy and the implications of that performance for structural transformation.

4.1 Macroeconomic policies

Macroeconomic policy is key to setting the conditions for and directing structural transformation. Mozambique's high level of external dependence in a context of an emerging resources economy poses a challenge to macroeconomic management—namely, how to avoid Dutch disease. The challenge is due to the inconsistency between fiscal and monetary policies, which is manifested in the way they have been addressed over the past two decades.

On the one hand, monetary policy in Mozambique has been geared towards achieving single-digit inflation. This goal has been set in an economy that is highly dependent on imports for the majority of consumer goods (especially food) and suffers from a chronic current account deficit, and where the major sources of foreign exchange are concentrated and volatile—about 90 per cent of exports are concentrated in few primary products, including mining and other natural resources (Castel-Branco 2017; Chivulele 2017). Given this, the focus of monetary policy is on managing liquidity so as to guarantee the value of the national currency relative to the main global currencies and thus maintain the capacity to import basic goods and services. The Central Bank therefore defines the direction of monetary policy in terms of the exchange rate and the level of foreign capital inflows and international reserves.

On the other hand, fiscal policy in the context of the natural resource boom has become geared towards expanding public expenditure, especially public investment in infrastructures to support the growing extractives sector of the economy. These investments have been funded essentially by external and domestic debt, which puts more pressure on the state budget to service the debt (Massarongo 2016). For example, between 2014 and 2019, external debt financed more than 20 public investment projects accounting for almost US\$6 billion (see Table 1). Of these public investments, 10 were major infrastructure projects in the energy, transport, and communications sectors (see highlighted projects in Table 1). Domestic public debt has also increased, having been intensively used to finance short-term public expenditure over the past decade. Domestic debt servicing has increased continuously between 2009 and 2019, from almost less MT1 billion (US\$14 million) in 2009 to more than MT150 billion (US\$2 billion) in 2019 (Ibraimo forthcoming).

Table 1: Public investment projects

Public investment project	US\$ million
Maputo Ring Road Project and Maputo–Katembe Bridge	982
Development and expansion of Nacala Port-Phase II, Nacala Special Economic Zone, Nacala Free Trade Industrial Zone and Beluluane Industrial Park	868
Road constructions: Mueda–Negomano, Nampula–Nameti; construction and rehabilitation of road infrastructures; Rovuma River bridge; management and maintenance of roads and bridges	727
Upgrade and extension of the national electricity power network in the northern region; power transmission line Chimuará–Nacala; Temane; Niassa rural electrification, Phase II; improvement of power network in Maputo and Matola and peripheral zones	687
Moamba major dam study and construction	329
Maputo gas project, technical assistance for large scale power and gas investment; Ressano Garcia thermal power plant	237
Digital migration project	156
Beira and Angoche fishing port construction and rehabilitation	152
Acquisition of carriages, wagons, locomotives, and railway equipment for Mozambique Railway Company (CFM) and Beira container terminal	126
Maputo International Airport rehabilitation and navigation infrastructure improvement	79
EMATUM – Mozambican Tuna Fish Company	850
Rural water supply for Manica, Sofala, Zambézia, Nampula, and Maputo provinces	216
Financial assistance for emergencies in the central and northern regions of Mozambique	178
Drainage system project in Maputo city and construction of Maputo and Matola landfills	120
Construction of the Department of Geology of Eduardo Mondlane University; Nampula Agrarian Polytechnic Institute; Maputo Health Sciences Institute	115
Olympic Games Infrastructures	100
Lumbo Hospital construction, Quelimane (supplementary area); emergency ambulance acquisition; tuberculosis and health system support	59
Combined cycle development project	44
Forestry investment	28
Aquaculture and artisanal fishing	12
Acquisition of equipment for the Public Rescue Services (SENSAP)	5
Total	6,060

Source: adapted from Ibraimo (forthcoming).

Chivulele (2017) noted that, given the current dynamic of the economy, which has shaped policy management, macroeconomic policies had become inconsistent, both among themselves and consequently with the objective of structural transformation. Such inconsistencies are present within monetary policy, between monetary policy and the real economy, and between monetary policy and fiscal policy. The inconsistencies between monetary and fiscal policy and the real economy are principally due to the weak responsiveness by the financial sector to expansionary and restrictive policies such as the significant reductions in reference interest rates by the Central Bank. For example, between 2011 and 2015, the permanent lending facility (FPC) was reduced by 55 per cent and the permanent deposit facility (FPD) by 70 per cent. These reductions were followed by a timid reduction of interest rates charged by commercial banks—from 24 per cent to 21 per cent in the same period. However, when the Central Bank increases interest rates, commercial banks react more quickly. The increase by the Central Bank of the FPC rate between 2015 and 2016 from 7.5 per cent to 23.25 per cent was immediately responded to by an increase in the commercial interest rate of about 50 per cent. Although the percentage change of the reference rate is higher than that of the commercial interest rates charged by commercial banks, the important aspect to highlight is how quickly commercial banks react to an increase in reference rates as compared to a decrease.

The continual resort by the state to treasury bills, associated with a reduced and highly speculative financial market, has created pressure to increase commercial interest rates, making it difficult for monetary policy to stimulate the economy (Ibraimo forthcoming). Expansionary monetary policies, which are supposed to expand credit for financing the productive sector towards a more diversified economy, are abruptly interrupted by these dynamics, reflecting the structure of dependency of the economy and the increasing reliance of the government on domestic public debt (Castel-Branco 2014). The activity of the financial sector is then geared towards financing the infrastructure supporting the extractive core of the economy, and the issuance of public debt, consumption of durable goods and the real estate sector with speculative prices. This tendency to speculation is partly explained by the higher demand and short-term profitability of these assets, as the increasing investment in extractives has prompted an emergence of a middle income strata with access to higher salaries from the extractive sector. By concentrating its financing capacity in such activities, the financial sector diverts resources that should be used to finance productive investment in the country, a process that may allow the achievement of a more diversified productive domestic capacity and hence build the basis for the structural transformation of the economy.

4.2 Dependence and structural economic transformation in Mozambique

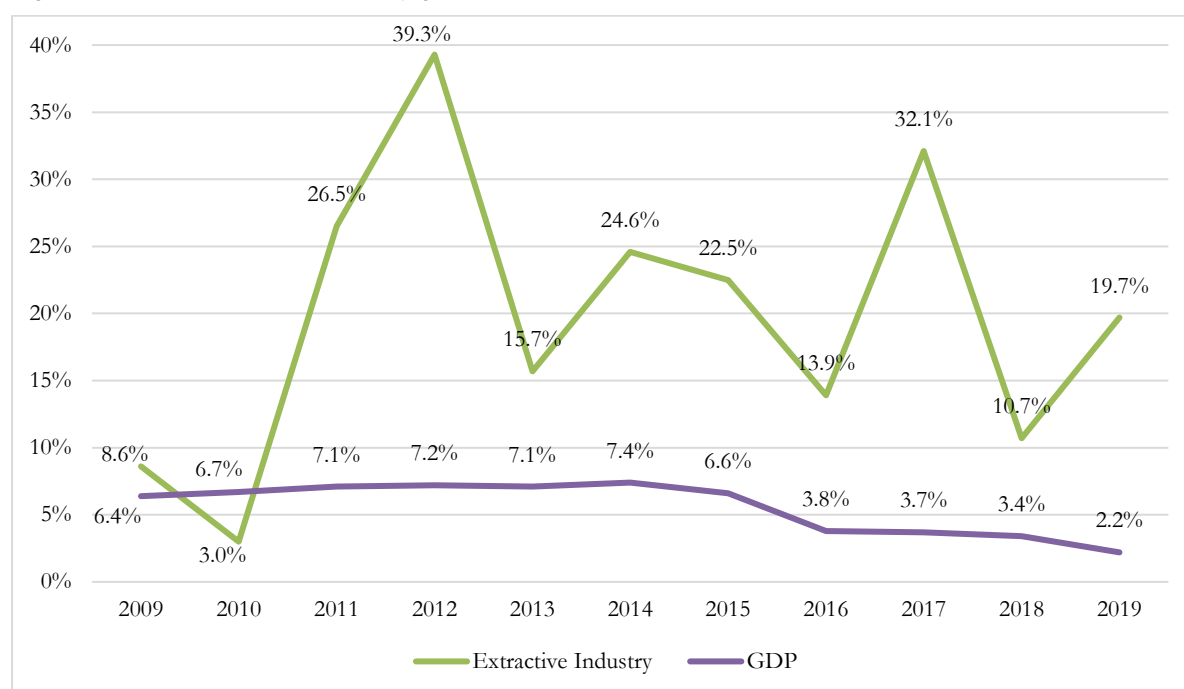
The past and recent history of Mozambique is that of a highly and structurally dependent economy, which has implications for its economic transformation. In the economic and social dimensions, dependence on foreign capital inflows—both public (foreign aid) and private (FDI, concessional and commercial loans from the international financial system)—is, along with resource extraction, the main structural feature of the country's dependence.

With respect to private capital inflows, the dependence on FDI, especially in the extractives sector and related activities, is the dominant feature of the pattern of economic growth and one of the fundamental elements of the 'dominant political economy of Mozambique' (Castel-Branco 2010, 2014).⁹ Over the past two-and-a-half decades, Mozambique has presented a pattern of dependence on natural resources extraction similar to those of several resource-dependent developing countries. Between 2000 and 2009 (the period before gas discoveries in the Rovuma Basin in Cabo Delgado), the resources sector, especially mining, represented 43 per cent of total FDI inflows, followed by the manufacturing sector with 28 per cent (of which 92 per cent corresponded only to the Mozambique Aluminium Smelter Company MOZAL). From a total FDI of US\$1.4 billion that the sector received over this period, megaprojects in the extraction of heavy sands and coal contributed 53 per cent (US\$580 million and US\$171 million, respectively). In terms of exports, the resources/extractives sector in general or the mineral energy complex (aluminium, gas, coal, energy) represented, on average, about 64 per cent of the total value of exports between 2000 and 2016 (Langa 2017). By 2012, after the gas discoveries, the sector had increased its share to 72 per cent. It continued to do well until 2014, despite lower commodity prices after 2012 (Roe 2018). The effect of the dependence on natural resources hit hard in 2015, when prices of Mozambique's main export commodities (especially coal, gas, and aluminium) fell drastically, affecting the country's economy, with GDP growth decelerating to 6.6 per cent and subsequently dropping as

⁹ 'the dominant political economy of Mozambique is focused on three fundamental and interlinked processes, namely the maximization of inflows of foreign capital – FDI and commercial loans – without political conditionality; the development of linkages between these capital inflows and the domestic process of accumulation and the formation of national capitalist classes; and the reproduction of a labour system in which the workforce is remunerated at below its costs of subsistence' (Castel-Branco 2014: S29).

low as 2.2 per cent, after a mean value of over 7 per cent in most of the period since 2000. Figure 1 shows the growth of the extractives sector in relation to GDP growth between 2009 and 2019.

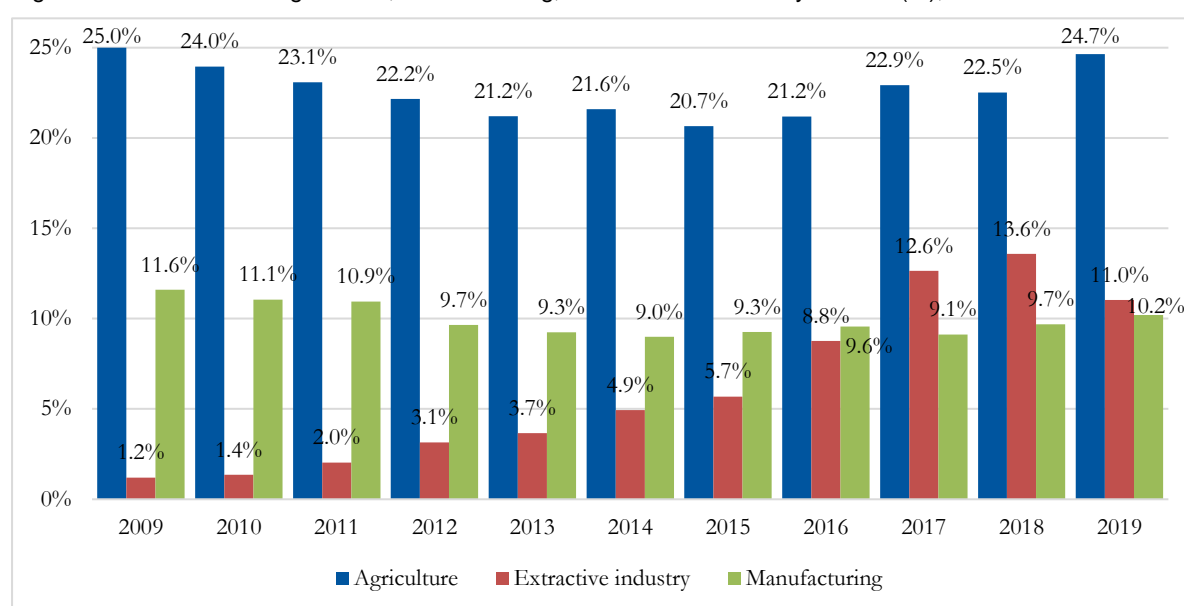
Figure 1: GDP and extractive industry growth (%), 2009–2019



Source: Statistics National Institute (INE).

As Figure 2 shows, the contribution of the extractives sector to GDP increased from 1.2 per cent in 2009 to 13.6 per cent in 2018, and it is expected to contribute substantially over the next few years, as the production of gas in northern Mozambique starts. Manufacturing declined from 2009 to 2014, when it started a slight increase up to 2019, but it is still below the share of the GDP of 2009. Agriculture remains the main sector, contributing 24.7 per cent in 2019 to GDP, but the extractives sector has been the fastest growing sector over the past decade.

Figure 2: Contribution of agriculture, manufacturing, and extractive industry to GDP (%), 2009–2019



Source: INE.

Current economic dynamics, supported by the discoveries and recent FIDs in the gas sector, and the set of expectations over future FDI, revenues, and linkages, point to an increasing dependence of the country's economy on natural resource exploitation, consolidating the country's structural dependence. As Langa (2017: 165) argues, under such conditions 'Mozambique is following an opposite trajectory to economic [structural] transformation', in the sense that the dependence on primary commodities has been expanding, at the same time that 'a process of premature deindustrialization [defined as the increasing underdevelopment of the existing manufacturing sector] has been underway, constraining the possibilities of multiplication and intensification of productive linkages within the economy'.

Tendencies towards deindustrialization are confirmed by research on the manufacturing sector, which shows that from 2011 to 2017 there was a reduction in the number of companies in the sector, of the labour force, and of turnover (CEEG et al. 2018). Whilst there has been some mobility of the labour force from agriculture to other sectors (services and manufacturing), the productivity of the labour force in these areas has been lower (Jones and Tarp 2015). These results cannot be directly linked to the emerging resources economy, but the consistency of the downward trend in manufacturing as well as of the labour force suggests that economic growth is heading in the opposite direction to structural transformation.

Despite the government's approval of the local content bill in 2019 (to be submitted to parliament for its enactment as an Act), prospects of local companies making linkages with the gas projects of the Rovuma basin are still uncertain. National companies lack the capacity to match the quality standards of the O&G industry and the national business class poses a high reputational risk to international companies due to its excessive reliance on political lobbying.¹⁰ These factors are contributing to the resistance to local content policies from the international companies leading the investments in the gas sector.¹¹ Total's signing of all financing contracts in July 2020, following EXIM Bank's decision to back American suppliers to LNG development in Mozambique, together with the imminent approval of US\$1 billion from UK Export Finance (see Introduction) may mark a turning point towards the start of the LNG production, but at the same time they signal the difficulties national companies will have in establishing linkages with the gas projects. Despite the provisions in the local content policy to promote linkages with national companies, this will be a more complex issue than expected. Power dynamics have played a central role in providing the conditions and the direction of public policy for local content. More specifically, the power that MNCs have in controlling the GVCs of their production, including the suppliers of goods and services to their industry, may define the possibilities and outcomes of local content initiatives. In fact, the dynamics and structure of natural resources extraction reflect the dependence of the natural resources sector upon FDI for financing development projects, thus justifying the relative power that MNCs have in influencing local content policies and resource extraction in a capital and (industrial) capability scarce economy. This puts MNCs in a position to determine the direction of policy.

Policies that promote structural transformation through diversification of the economy and the establishment of linkages between local companies and the natural resources projects will more likely be supported by internal actors than by FDI. This makes domestic resource mobilization an

¹⁰ See interviews with the Head of Local Content of the National Business Association (CTA) https://macua.blogs.com/moambique_para_todos/2019/02/h%C3%A1-um-l%C3%B3bi-contra-a-lei-do-conte%C3%BAdo-local-em-mo%C3%A7ambique.html, and <https://www.rfi.fr/pt/mocambique/20190823-lei-de-conteudo-local-tem-de-ser-atractiva-para-o-investimento>.

¹¹ https://www.africaintelligence.fr/petrole-et-gaz_strategies-etat/2020/07/16/contenu-local--total-eni-et-exxonmobil-font-de-la-resistance,109243877-ar1.

alternative to external resources—which is in fact the idea of using natural resources revenues to promote the diversification and economic transformation presented in the NDS.

4.3 Extractives sector contribution to revenue mobilization

As mentioned, the natural resources area has experienced a set of reforms in the last two decades, which were accelerated by the increasing importance of natural resources in the Mozambican economy. Most of these institutional reforms have been either directly or indirectly linked to the generation of natural resources revenues, and they have led to the creation of regulatory agencies in the petroleum sector (INP), in 2004, and mining (INAMI), in 2014. Besides, in response to the growing importance of the extractive industries in the economy, the AT created a specific unit to deal with the sector in 2017. The results of these reforms are mixed, with implications on revenue generation.

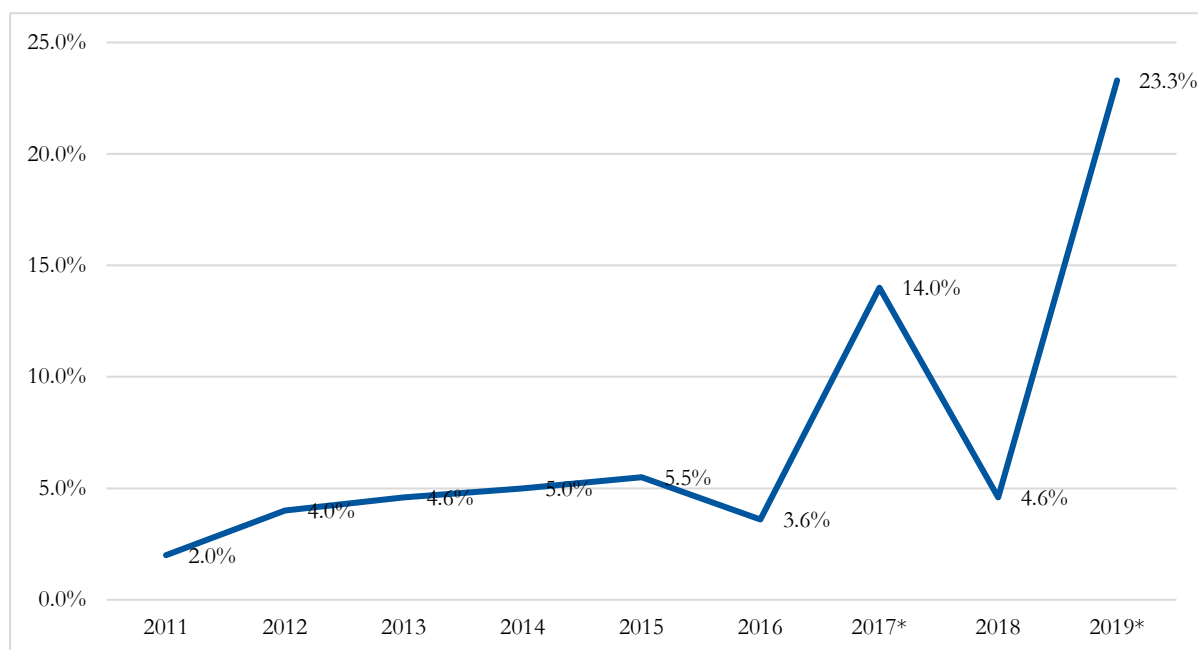
There has not been a systematic assessment of the performance of key institutions related to natural resources. The most relevant is the Resource Governance Index (Natural Resource Governance Institute 2017), which covers three indicators: value realization, revenue management, and enabling environment. Scores range from 0 to 100, higher values referring to higher performance. In the last assessment, carried out in 2017, Mozambique's overall score on resources governance was 50 (average) and on value realization 66—which is satisfactory due to good performance in taxation—but its scores on revenue management and enabling environment were poor: 42 and 43, respectively. The enabling environment is related to governance indicators, voice and accountability, government effectiveness, regulatory quality, rule of law, control of corruption, political stability, and absence of violence.

Revenues from natural resources derive from a series of standard taxes and fees, including value-added tax (VAT), income tax (corporate (IRPC) and individual (IRPS)), royalties, and production taxes (República de Moçambique 2018). Specific revenues are collected by the regulatory agencies, INP and INAMI, including for their capacity development. Public-owned companies (ENH, CMH, EMEM) in the sector must provide dividends to their shareholders when they are profitable.

Figure 3 shows the share of fiscal revenues from megaprojects in the mining and oil sectors in total state revenues. The fiscal contribution of extractives increased over the first half of the last decade, from 2 per cent of total revenues in 2011 to more than 5 per cent in 2015. This increase reflects the boom in production—especially of mineral coal, as prices were high. However, the commodity prices drop since the end of 2014 has prompted a decline in regular extractives revenues.

The higher contribution of the sector in 2017 and 2019 is explained by the extraordinary revenues—capital gains taxes (CGT) of about US\$350 million and US\$880 million, from oil asset transactions between ENI and Exxon Mobil, and between Occidental (which took over the concession and assets of Anadarko) and Total, respectively. Without CGT, the contribution of the extractives would fall to 5 per cent and 3.7 per cent of the total revenues in 2017 and 2019, respectively. This would confirm the downward trend that began in 2015. Despite the fact that the legislation is clear about the rate of 32 per cent and the mandate of the AT to collect CGT, this revenue has been embroiled in intense debate and 'interpretations' on its calculation, with suspicions that MNCs have negotiated politically to pay less than what is due. Presidents Guebuza and Nyusi were directly involved in the ENI and Total deals, respectively, to some extent bypassing the existing institutions, especially the AT (Macuane et al. forthcoming). In the case of the negotiations with ENI, part of the payment agreed was in kind—the construction of a coal power plant, which was never delivered, fuelling suspicions of corruption (Macuane et al. 2018).

Figure 3: Fiscal contribution of megaprojects in the mining and oil sector to total state revenues, 2011–2019



Note: * includes capital gains taxes.

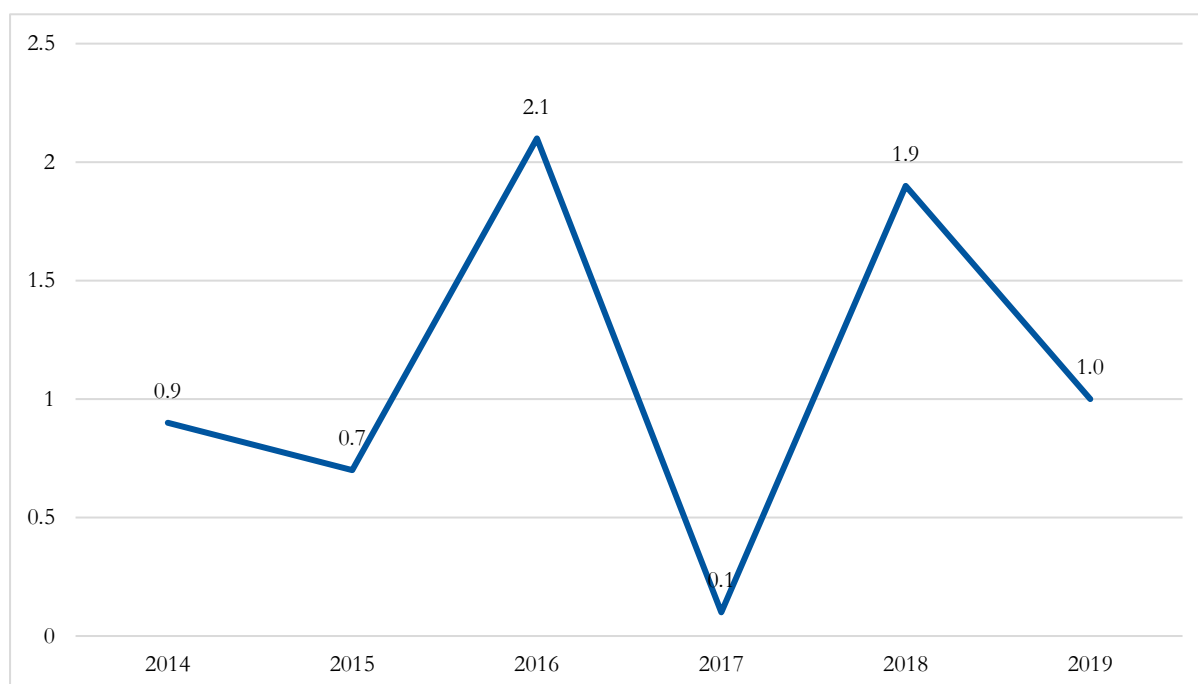
Source: State General Accounts, 2011–2019.

Despite progress in creating capacity to implement the tax regime, there are still institutional weaknesses in revenue collection, among them the capacity to audit companies to define the taxable amount and, in the case of oil and gas projects, the recoverable costs. Moreover, discrepant information on natural resources for revenue collection purposes is an institutional inefficiency that has been persistent over time and systematically reported by the Administrative Court analysis of public accounts. The successive country EITI reports show discrepancies in the revenues declared by the companies and by the Revenue Authority, although the differences are reducing (EITI Mozambique/I2A Consultoria e Serviços 2020; Tribunal Administrativo 2017, 2018). Part of this improvement is due to the increasing scrutiny that the sector has been subject to from civil society organizations, which also participate in the secretariat of the EITI. To some extent, demand for transparency in the sector is contributing to the increasing collection of revenues.

Despite the growing importance of the extractives in total state revenues and the institutional reforms made to strengthen institutions of revenue collection, the contribution of the sector (when CGT is not included) is low. It is therefore not an alternative to FDI and foreign aid for public investment in areas to stimulate structural transformation. The regular bypassing of the institutions where CGT is concerned also suggests that natural resources revenues are vulnerable to appropriation by political leaders and use for clientelist purposes.

The gas sector has been the principal source of another revenue stream, dividends paid to the government by the natural resources public enterprises (ENH and its subsidiary CMH), INP, and companies with state shares (Mozambique Gas Pipeline Company (CMG)), but this has accounted for less than 1.5 per cent of state revenues in most of the 2014–2019 period (Figure 4).

Figure 4: Extractives dividends as % of total revenues



Source: State General Accounts, 2014–2019.

The contribution of the extractives sector's public enterprises to public revenues is still modest. However, in the case of the gas sector, specifically in the SASOL projects of Pande and Temane, these companies have been a source of rents for national business elites linked to the ruling party, in down- and mid-stream projects such as gas distribution and electricity generation (Salimo et al. 2020). The participation of the public companies in these gas projects did not make a visible contribution to the promotion of linkages with local companies, and the lead company SASOL has been criticized for its limited contracting of local companies in its supply chain. In sum, the model so far adopted, of participation by public companies in the extractives, has neither been a good source of revenues to public coffers nor visibly contributed to the structural transformation of the economy.

Extractives revenues, apart from the extraordinary CGT payments, have not played any significant or transformational role in public expenditures. This is partially attributable to the size of the revenues so far, but it is also due to the lack of a specific regime to earmark its contribution for broader or defined economic goals. The discussion over creating an SWF, which would go some way in that direction, has so far been restricted to a limited group. To some extent, this is a continuation of the uncertainty and lack of transparency that have characterized the use of CGT revenue so far. The use of CGT to cover budget deficits has been recurrent (for example, in the last transaction of assets between Occidental and Total in 2019, the President announced that part of the revenues would be used to finance the deficit resulting from the elections), but there is no specific mechanism of accountability for this.

5 Underlying causes

The NDS is a resource-led economic transformation strategy, whose main objective is to promote industrialization for the diversification of the economy, using the country's natural resources as the catalysers of this process. However, despite the growing importance of the extractives' dynamics in the economy and institutional reforms to improve the sector's governance, both its

impact and its prospects for structural transformation are limited. Two underlying factors explain these dynamics: the nature of the NDS as a coordination policy instrument, and the country's structural dependence. These factors are developed below.

Since its elaboration, the NDS has never been formally adopted as the country's strategy by a broad-based coalition or legitimated by the key decision-making institutions, such as parliament. This renders its implementation less binding and its role as a coordination mechanism of the various actors towards structural transformation limited. Despite its being referred to in many sector programmes and strategies, there is no explicit integration of this instrument with a broader framework of structural transformation. Fragmented decisions and responsibility for implementation across uncoordinated organizational mandates have created a weak context for the effectiveness of the economic transformation strategies embodied in the NDS. Strategic decisions about the use of natural resources revenues have not been linear and are vulnerable to changes in the leadership of the country.

The lack of broad-based participation in the decisions of key actors in the sector is another critical factor. For example, the creation of the SWF has been delayed and the discussions related to it have been carried out by a limited set of actors and institutions, and in secrecy, which limits its analysis. The discussion about the role of the local content policy in promoting industrialization has been undermined by the disproportionate power dynamics and interests, including those of foreign investors, which do not have incentives to contribute to national long-term goals and would rather favour the use of their GVCs, which are more efficient. Moreover, the existence of an economically weak entrepreneurial class, undercapitalized and much prone to use its political influence for rent-seeking, prevents the creation of a strong coalition of national actors pushing for institutions that can enable a sustainable economic transformation.

There is no acknowledged set of ideas informing institutional choices and actions, which is reflected in the fragmentation of interventions and the lack of linkages between ideas and actions to make natural resources contribute to broader economic and social change. From an institutional point of view, this means that the NDS does not have the status of a widely accepted set of norms that can intermediate relations between and influence the behaviour of the key actors in the sector and those that might contribute to structural transformation. This is evidenced by the limited impact that the increasing contribution of the extractives to the GDP and of the natural resources revenues have had on the fiscal policy. The way natural resources revenues, especially through CGT, have been negotiated and managed is a good example. The country's top political leadership taking over the process and bypassing existing institutions and processes denotes the existence of inconsistencies between the objectives of economic transformation and policy actions, which affects fiscal policy management. It also denotes the weakness of the existing policy instruments in influencing political actors' behaviour with respect to broader development goals.

The recent developments related to the FIDs in the gas sector have created new expatiations and pointed to an even greater dependence of the country's economy on natural resource exploitation. It is therefore important to bear in mind that dependence should not be reduced only to the inflows of FDI that the country has received over the past decades and might receive in the decades to come. Instead, the ability of these foreign capital inflows to effectively structure the general dynamics and conditions of production and reproduction (or sustainability) of the economy should be acknowledged. Particularly important here is how the country's economic policy and macro-policy management in general are set through, and shaped by, the dynamics of foreign dependence at various levels (investment, production, and consumption). This includes, for instance, the development of productive linkages and the role of macroeconomic and sectoral policies in addressing relevant questions of economic transformation.

A fundamental problem in the case of Mozambique is that the dependence of the economy on resource extraction and the corresponding foreign capital inflows has become a dilemma, since domestic capital accumulation is strategically promoted through these capital inflows, which at the same time provide the main opportunities for industrialization and diversification of the economy. Hence, diversification of the economy cannot be conceptualized outside the aforementioned core dynamics of dependence. However, in the context of dependence it cannot be expected that Mozambique will receive significantly large FDI into the manufacturing and agricultural sectors compared with what it currently receives in the extractives sector, which is much more attractive to the foreign investors. In fact, given that external financing of the non-resources sector is limited, it is expected that the country will have to rely on its own domestic savings to finance diversification. However, productive domestic investment has usually been crowded out by a debt-financing government expenditure policy, through the issuance of treasury bills, which are more attractive and less risky for the domestic financial sector (Castel-Branco 2014; Massarongo 2016). This creates limitations for the implementation of a sustainable industrial policy that can stimulate diversification and create linkages with the natural resources projects that promote the transfer of technology and know-how to the broader economy.

6 Conclusions and perspectives

Mozambique's National Development Strategy hinges on the structural transformation of the economy through industrialization and diversification, catalysed by the growing importance of the extractives sector. In this context, the country has carried out institutional reforms to respond to the increasing importance of the natural resources sector in its economy. These reforms are resulting in the growing contribution of the resources sector to the economy. However, underlying dynamics undermine the prospects of the resources sector contributing to economic transformation, namely: (i) the absence of a strong institutional setting expressed in a resource-based strategy that plays the role of a binding set of norms and references for coordination of the various actors; (iii) the different strategies pursued by the political and economic actors, especially the political leadership and the government, the national entrepreneurial class (undercapitalized and more reliant on its political linkages), and the MNCs with less incentive to invest in other areas than the extractives; and (ii) the structural dependence of the country on external resources, particularly FDI and its role in shaping the relations between international and domestic actors and influencing macroeconomic policies, especially monetary and fiscal policies, in ways that contradict the objectives of economic transformation.

In order to make a contribution to structural transformation, the sector needs to influence institutional and policy dynamics in two ways.

The first is to activate relevant policy actors, especially the government and the private sector, and improve coordination, as defined in the National Development Strategy and reflected in its various policy instruments. Activating such relevant policy actors and processes implies the mobilization and alignment of the agendas of the government and the domestic entrepreneurial class in the context of the increasing role of the extractives sector in the economy. In this regard there must be a clear alignment between the industrialization strategy and the relevant sector policies, particularly the local content policy, in which the domestic private sector has to play a role. One way to improve coordination is through a fiscal regime and institutional mechanism that define the scope of public expenditure in areas related to structural transformation, especially industrial policy, and domestic and human capability development. This could be combined with a mechanism to aggregate sector policies—for example local content and industrial policy—as part of a broader development strategy.

The second way in which the sector needs to influence institutional and policy dynamics is to confront the conditions of dependence that influence macroeconomic policy management. This implies, for instance, addressing the existing conflicts and tensions between fiscal and monetary policies with the objective of structural transformation. In other words, this implies untying macroeconomic policy management from the logic of dependence, and subordinating it to the agenda of economic transformation, as a central instrument for the promotion of industrialization and economic diversification. Thus, fiscal policy must clearly define strategically how natural resources revenues must be used within a broader development framework that addresses central aspects of economic transformation. This means that, instead of financing recurrent public deficits indiscriminately, as has been the case so far, these resources must selectively finance public expenditures directly linked to industrialization and the diversification of the economy. Among them are those related to the promotion of local content in the extractive industries and beyond. It also demands the existence of more effective rules to bind and influence behaviour of relevant political and economic actors, which can be attained through the approval of a more consensual resource-led economic transformation strategy by parliament.

Such a strategy has to be defined through a broad consultation process, involving different government sectors, the private sector, civil society, and parliament. This is important to allow the instrument to be more binding—not only because it is enacted by the legislature, but also because it has been approved by a broader coalition that will contribute to its continuous scrutiny throughout the implementation process. Regarding monetary policy, it must be ensured that it is more aligned with the challenges of mobilizing resources for the domestic financing of a strategy of economic transformation, in a context of limited financial resources. This means a more coordinated approach between the monetary authorities, the domestic private financial sector and the government. Such a coordination approach should aim not only to avoid adopting policies that crowd out productive investment from the domestic private sector, but also to promote much more flexible access to financial resources to fund initiatives in line with the strategy of industrialization and diversification of the economy that is assumed in the NDS.

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