

Armed attacks in Cabo Delgado

- Suspension of Total's Activities raises risks and uncertainties for Mozambique's economy

By: Inocência Mapisse*

1. Context

The Ministry of Mineral Resources and Energy, through the National Petroleum Institute (INP), made a public announcement on 26 April 2021, informing that due to the insecurity situation caused by armed attacks in the Afungi peninsula, District of Palma in Cabo Delgado Province, Total E&P Mozambique Area 1, Limitada (Total), concessionaire and operator of area 1 offshore the Rovuma Basin, has suspended contracts with a significant part of its partners citing a cause of “force majeure”.

According to the INP, the suspension aims to mitigate the negative effects arising from the implementation of the contracts and costs of goods and services that cannot be provided or used during the period in which the activities are suspended, a fact that would have negative effects on the overall cost of the Project whose investment is estimated at USD 20 billion.¹

A preliminary analysis by the Confederation of Business Associations (CTA) indicates that the armed attacks have affected at least 410 companies and about 56,000 jobs and generated a negative financial impact of about \$95 million, which includes destruction of equipment, delays in payments and goods in transit without certainty of delivery. This financial impact represents about 14 times the budget limit for Cabo Delgado Province in the framework of decentralized governance, set at 401.5 million meticais².

At the same time, Total issued a statement³ reinforcing that it is temporarily withdrawing from Afungi for reasons of force majeure and reiterates that it will return to activities as soon as the actions taken by the Government of Mozambique and its regional and international partners re-establish security and stability in Cabo Delgado, in a sustained manner.

This situation has negative implications and raises risks and uncertainties in the country as expectations of the contribution of gas exploration to Mozambique are high. On the one hand, the private sector has been preparing to actively participate and reap the dividends of natural gas exploration in Mozambique and, in this regard, ENH has been taking on debt to guarantee its participation in the gas business. On the other hand, the growth projections of the economy for the coming years are based significantly on the development of gas projects, with the Moz LNG project, led by Total, being the largest of them in the development phase.

In this context, the present analysis aims to present the implications of the temporary suspension of Total's activities in Cabo Delgado due to the armed attacks.

1 <http://www.inp.gov.mz/en/Noticias/TOTAL-Declara-Forca-Maior>

2 <https://www.mef.gov.mz/index.php/documentos/instrumentos-de-gestao-economica-e-social/orcamento-de-estado/oe-2021/1180--254/file?-force-download=1>

3 <https://www.total.com/media/news/press-releases/total-declares-force-majeure-mozambique-lng-project>

2. Analysis

2.1 Analysis of the implications of the Suspension of Total's Activities in Cabo Delgado

Economic Implications

- **Deficit in Tax and Parafiscal Revenue Collection** – the suspension of Total's activities in Cabo Delgado has a direct negative impact on revenue collection for the state coffers, currently valued at an average of 1.3 billion meticaís over the last 4 years (excluding capital gains), which contributes to the mega-projects having a 7 to 8% contribution to the state's annual revenue⁴.

Total considered resuming activities when security and stability conditions are re-established in Cabo Delgado and in a sustained manner. If these conditions are not guaranteed in at least 1 year, the fiscal contribution of megaprojects to the state budget may reduce by about 1 percentage point, to an average of 6%.

In addition to the drop in tax revenues, the temporary suspension of Total's activities will impact the parafiscal revenues (institutional empowerment fund, social project funds and institutional contribution) collected by institutions such as the National Petroleum Institute (INP), whose average annual amount paid by Total since 2016 stands at 236.4 billion meticaís⁵, corresponding to about 50% of these revenues.

- **Fall in Foreign Direct Investment (FDI)** – 2019 data show a slowdown in inflow by about 18% -to USD 2,211.7 million (14% of GDP), down from USD 2,692.3 million (18% of GDP) in the same period in 2018.⁶ In addition, the major projects made investments totalling USD 954.0 million. Among these, the final investment decision for the Golfinho Atum/ Mozambique LNG project, led by Total, stands out.

Therefore, the suspension of Total's activities threatens the volume of Foreign Direct Investment in the country, both in real terms and in terms of investment prospects that are based on the macroeconomic environment.

- **Deterioration of the private sector performance in Cabo Delgado** – the private sector is one of those most directly affected by the effects of armed attacks in Cabo Delgado and by Total's very recent decision to suspend activities and contracts with partners in the project.

Preliminary data from the Confederation of Business Associations indicate losses to the private sector caused by the armed attacks of around US\$95 million. It should be noted that a significant part of tax revenues, about ¼ of total revenues, is made up of Corporate Income Tax (IRPC), coming from companies. In 2020, the IRPC reached 58.2 billion meticaís, corresponding to the weight of 24.6% of total revenues.

In addition to the drop in revenues, in response to the suspension of activities of Total and the companies that are somehow focused on the Palma gas project, the departure of Total has an impact on the increased uncertainty in the market in Cabo Delgado in particular and in the country in general.

The country's economic environment has been deteriorating since the beginning of 2021. According to the National Institute of Statistics (INE)⁷, the economic climate indicator (ECI) worsened in January and February 2021, from 90.5 points in December 2020 to 89.4 in January and 89.14 in February 2021, despite the employment outlook and demand indicators indicating an upward trend for the following months. (See chart below)

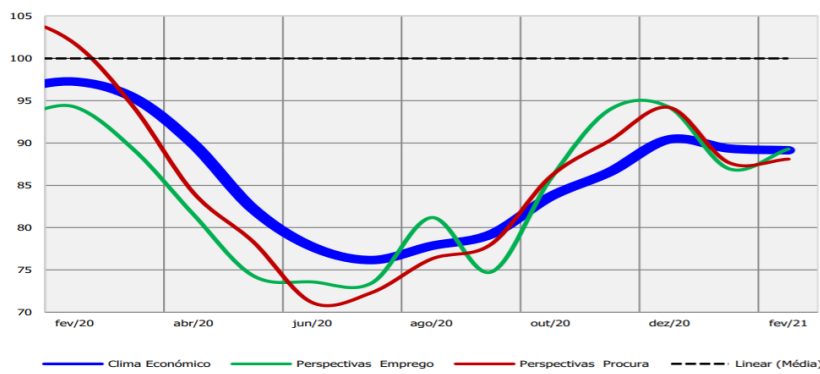
4 <https://www.mef.gov.mz/>

5 <http://itie.org.mz/index.php/download/nono-relatorio-itie/?wpdmdl=3092&refresh=5fdb4f87084921608208263>

6 https://www.bancomoc.mz/fm_pgTab1.aspx?id=73

7 http://www.ine.gov.mz/estatisticas/estatisticas-economicas/icce/indicadores-de-confianca-e-de-clima-economico-icce-fevereiro-2021.pdf/at_download/file

Chart 1: Business climate indicator



Source: INE, 2021

The unfavourable situation of the Mozambican economic environment was due to the negative assessment of the accommodation, restaurants and similar sectors, as well as the construction sector, thus supplanting the favourable assessments of the trade, industrial production and other non-financial services sectors.

Thus, the situation in Cabo Delgado may worsen the already deteriorated economic environment and contribute to an increase in the level of unemployment in the country.

- **Implications for economic projections (Medium Term Fiscal Scenario and State Budget)** - one aspect that cannot be overlooked is the impact that Total's indefinite suspension may have on economic projections. The budget documents indicated promising expectations for 2021, forecasting Gross Domestic Product (GDP) growth at 2.1%, based on positive growth in the extractive sector of about 1.5%. One of the arguments for this growth is the resumption of activities of the Moz LNG project (the largest gas project in the country that has already advanced with the final investment decision) after about 6 months of suspension due to the Covid-19 pandemic. Thus, Total's decision and the consequent suspension of contracts with companies under the project represent a risk increase in the economic projections initially made for the year 2021.

2.2 Implications for Empresa Nacional de Hidrocarbonetos (ENH)

Empresa Nacional de Hidrocarbonetos (ENH) holds a 15% stake in the project led by Total. In this context, in 2020, under the EPCC⁸, which is the model for participation of the state's business arm in the Rovuma basin gas projects, ENH has begun a road-show in South Africa to secure financing of about \$1.5 billion to ensure its effective participation in the development costs of the area 1 gas (Moz LNG) project, the Golfinho Atum fields, and the country's first natural gas plant.

The road-show comes after the Government issued an external guarantee in the amount of 2.2 billion dollars to cover the share of risk inherent to ENH's participation in the financing to be provided by the financiers of the Moz LNG project.

The issue of this guarantee to support ENH in the gas project, in addition to increasing the vulnerability of the public debt to exchange rate variations via an increase in the external debt, mostly denominated in foreign currency, simultaneously generates an increase in ENH's liabilities, forcing down the solvency ratio. It is important to mention that the solvency ratio and financial autonomy are currently below the recommendable level.⁹

These factors combined with Total's indefinite suspension of the Moz LNG project and the prevalence of attacks in Cabo Delgado put ENH in an increasingly high credit risk zone.

⁸ Contract model for gas exploration in the Rovuma basin

⁹ <https://www.mef.gov.mz/index.php/documentos/instrumentos-de-gestao-economica-e-social/relatorios-de-riscos-fiscais/930--232/file?force-download=1>

A credit risk analysis, prepared by the Ministry of Economy and Finance, shows that although ENH annually shows positive net results, currently estimated at 1.6 billion meticaís¹⁰, the company has a high credit risk (D)¹¹ and constitutes a large level of fiscal risk for the state.

- i. According to ENH's 2020 financial report, the financing of natural resource exploration assets stood at \$790 million and includes principal, interest and exchange rate differences representing all expenditures from 2006 to 2020. Therefore, the delay or abandonment of Total's project will have significant financial implications for ENH. These implications will ultimately be borne by Mozambican citizens, as ENH is a public company with the State as its shareholder.
- ii. **Conclusion and Recommendations**

The armed attacks in Cabo Delgado and the consequent temporary indefinite suspension of the activities of the French multinational Total in the Moz LNG project raise the risks and uncertainties for Mozambique's economy and this situation will tend to be more serious the longer it prevails.

This situation could negatively impact the annual collection of tax revenues by about 1 percentage point of the contribution of megaprojects in total revenues, reduction in payment of non-tax revenues by about \$236.4 billion, corresponding to Total's annual payment; fall in FDI; deterioration of private sector performance, and impact on economic projections.

The suspension of Total's activities also constitutes a high risk for ENH as it has been taking on debt to participate in the development phase of the Moz LNG project in particular, and gas projects in general.

As such, it is recommended that the Government act quickly to reach solutions to re-establish peace and stability in Cabo Delgado in a sustainable manner, this being a sine qua non condition for the resumption of the French oil company's activities in the country.

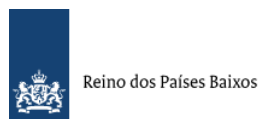
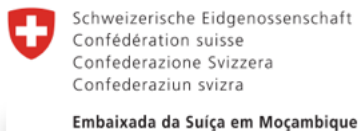
¹⁰ Empresa Nacional de Hidrocarbonetos (2020), Financial Statements: June 2019 – June 2020, Maputo

¹¹ The classification according to Altman's Z-score methodology ranges from A to D, where A represents lowest risk and D highest risk.



CENTRO DE INTEGRIDADE PÚBLICA
Anticorrupção - Transparência - Integridade

Parceiros:



Editorial Information

Director: Edson Cortez
Author: Inocência Mapisse

Peer review: Rui Mate, Estrela Charles, Baltazar Fael, Borges Nhamirre, Aldemiro Bande e Ben Hur Cavelane

Language Review: Samuel Monjane

Property: : Centro de Integridade Pública

Rua Fernão Melo e Castro,
Bairro da Sommerschild, nº 124
Tel: (+258) 21 499916 | Fax: (+258) 21 499917
Cel: (+258) 82 3016391
[f @CIP.Mozambique](#) [t @CIPMoz](#)
www.cipmoz.org | Maputo - Moçambique