



Examining Mozambique's Liquidity And Fiscal Vulnerabilities

S&P Global
Ratings

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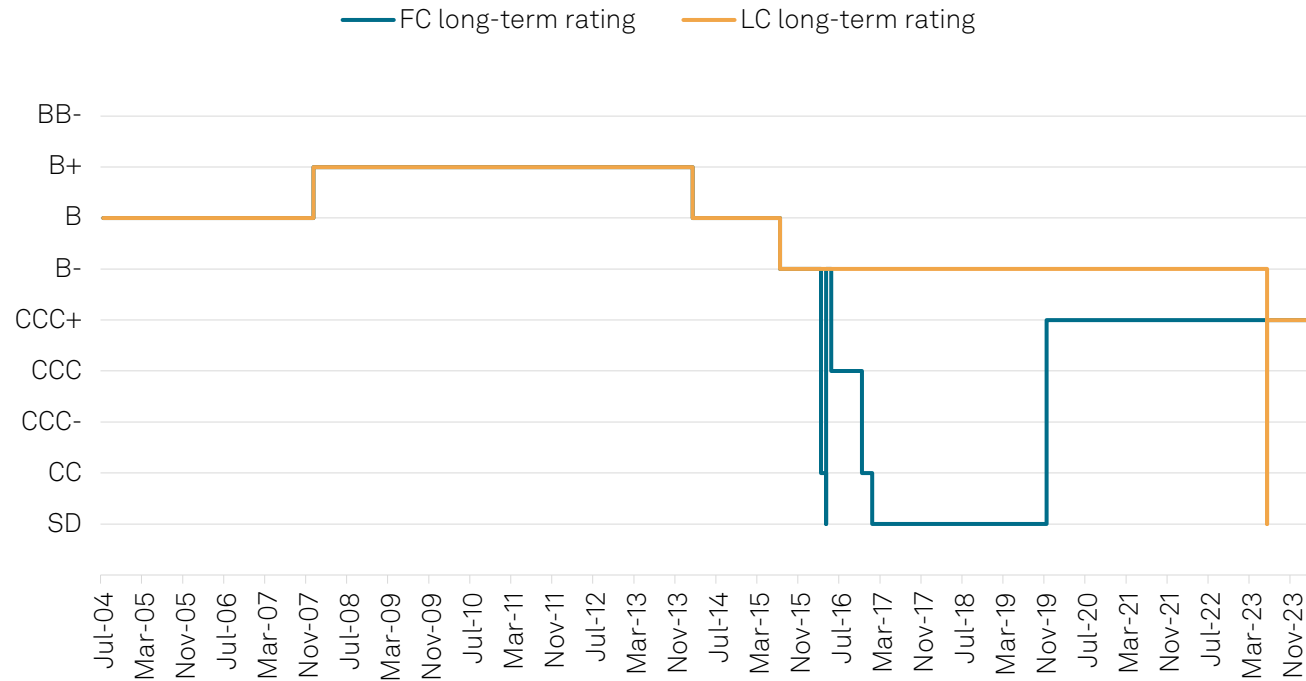
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Key Takeaways

- **Mega gas projects will provide significant upside in the 2030s, supporting longer-term improvements in economic growth and debt sustainability:** Mozambique could become a major global producer of liquefied natural gas (LNG). However, delays to projects mean production could only ramp-up materially in late 2028 or early 2029. Windfall government revenues are only likely to materialize by 2030, creating fiscal policy challenges for the sovereign in the interim.
- **Risks of delayed payments on sovereign obligations will therefore remain high until production ramps up substantially:** On April 19, 2024, we affirmed our 'CCC+' long-term local currency (LC) and foreign currency (FC) sovereign ratings on Mozambique. The outlook remains stable, and it balances weak public financial management and a poor track record in repaying debt against gradual gains from reforms aimed at improving the fiscal position and upside from large gas projects.
- **Fiscal challenges weigh on creditworthiness:** Government spending continues to outstrip revenue resulting in significantly wider budget deficits and the re-accumulation of arrears to contractors and suppliers (which we estimate at 3% of GDP in 2023).
- **Refinancing risk on LC commercial debt remains high, and FC commercial debt repayments will rise sharply from 2028:** The government has used more expensive LC debt to plug large fiscal shortfalls and its maturity profile is large. Its only outstanding Eurobond will begin amortizing from 2028, before the start of production at mega gas projects.
- **External imbalances and exchange rate misalignment pose further risks to government liquidity:** Mozambique has some of the weakest external metrics among all sovereigns rated by S&P Global Ratings. High external indebtedness, strained useable reserves (which cover just 2.2 months of foreign currency payments), high external financing needs (despite large foreign direct investment inflows), and strong appreciation of the real effective exchange rate compared with the nominal exchange rate, pose risks of a sharp correction.

Solid Growth Prospects Ahead But Fiscal Management Is Weak

Mozambique has defaulted three times on commercial debt since rating inception



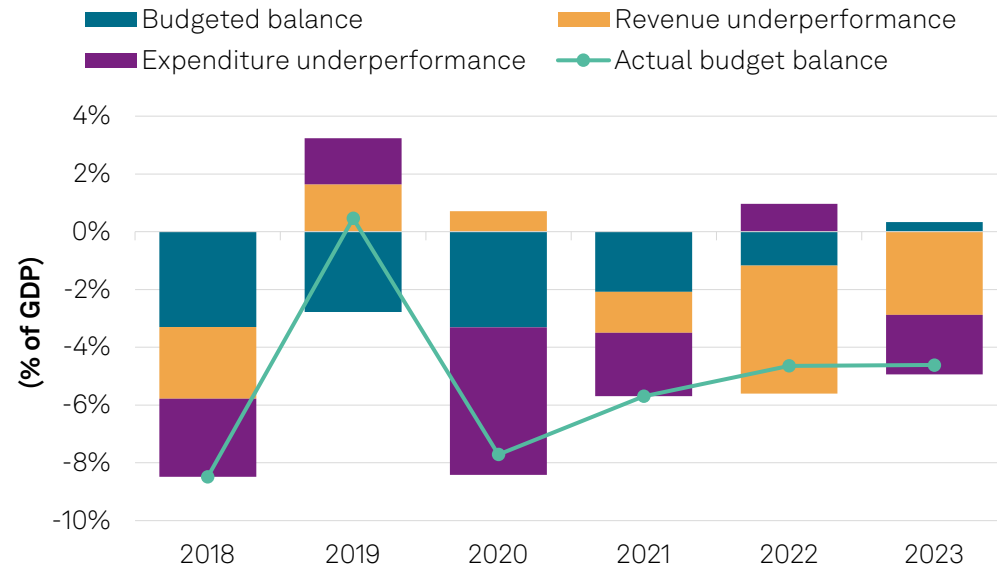
FC--Foreign currency. LC--Local currency. SD--Selective default. Source: S&P Global Ratings.

- We forecast average GDP growth of 5.5% between 2024 and 2026 as construction starts on mega LNG projects.
- However, public financial management remains weak. This has resulted in multiple defaults and restructurings on commercial debt, including in 2016 and 2017-2019 on FC debt, delayed payments on LC debt in 2023 (which we considered selective defaults), and late payment of some bilateral and multilateral creditors in the past 18 months.
- The government is slowly resolving the overhang from its 2016/2017 undisclosed debt scandal. It agreed on an out of court settlement for \$522 million relating to state-owned ProIndicus' debt owed to Credit Suisse (now owned by UBS).
- Fiscal reform to reduce fiscal vulnerabilities is ongoing, guided by an IMF program, however, liquidity challenges have risen sharply over the past year.

Persistent Fiscal Slippages Cause Liquidity Pressure

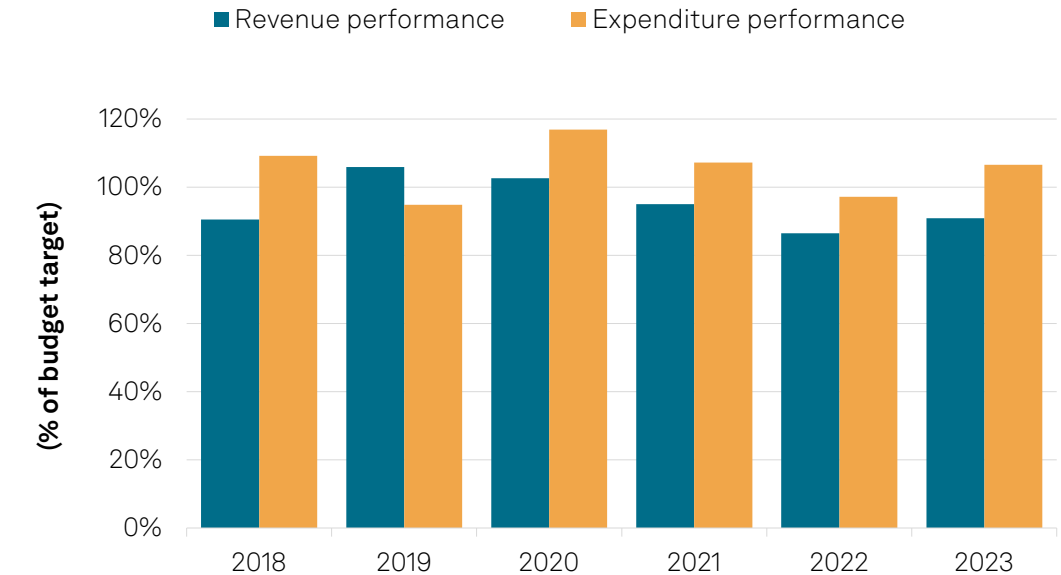
- The budget deficit has on average been 3.1% of GDP wider than initially budgeted since 2018 due to fiscal slippage (left chart).
- Significant slippage is attributed to higher execution of spending relative to revenue performance, creating larger fiscal gaps (right chart). Wage bill overruns, despite wage reforms, rising debt service costs and overly ambitious revenue projections are key drivers of weak fiscal outcomes.
- Salaries, wages and interest spending together make up 67% of total expenditure, straining Mozambique’s fiscal flexibility.

Breaking down Mozambique’s fiscal slippage



Source: Ministry of Economy and Finance, S&P Global Ratings.

Budget targets are consistently missed by large margins

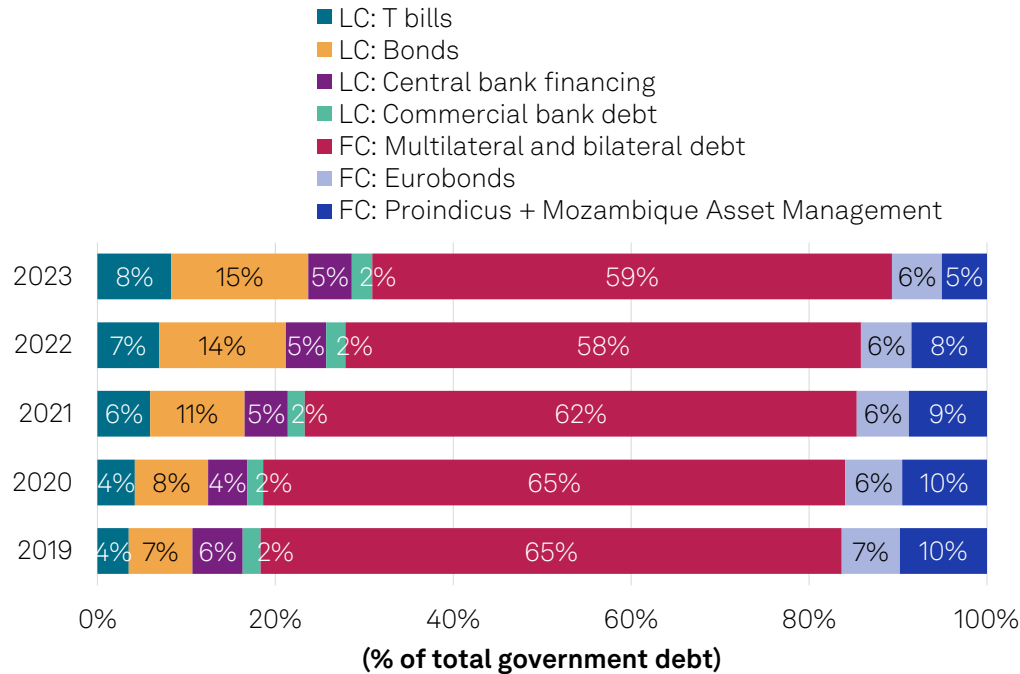


Source: Ministry of Economy and Finance, S&P Global Ratings.

Fiscal Gaps Are Plugged By Expensive Domestic Financing

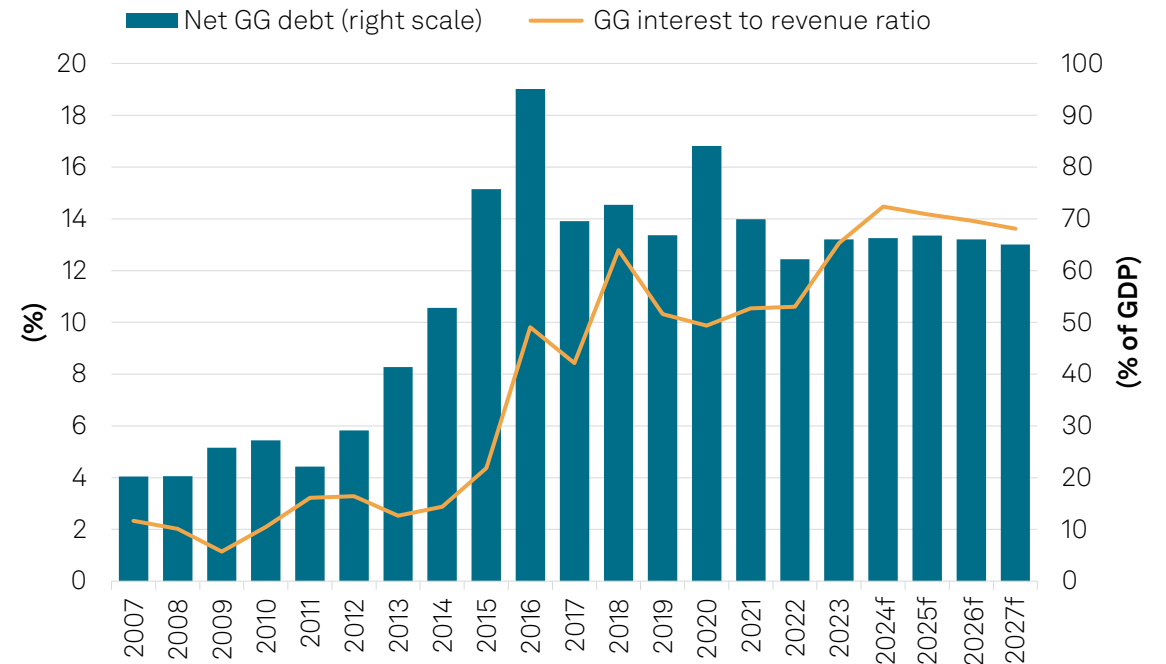
- Treasury bills and LC bonds have risen sharply to around 23% of general government (GG) debt currently, from 11% in 2019 (left chart).
- Interest costs will remain elevated as interest rates, particularly on LC debt, remain higher compared to the past decade (right chart).
- The government also funded fiscal gaps in 2023 by drawing down MZN 105 billion (\$1.6 billion or 8% of GDP) of its liquid assets.

LC debt has provided the government key financing



FC--Foreign currency. LC--Local currency. Source: S&P Global Ratings.

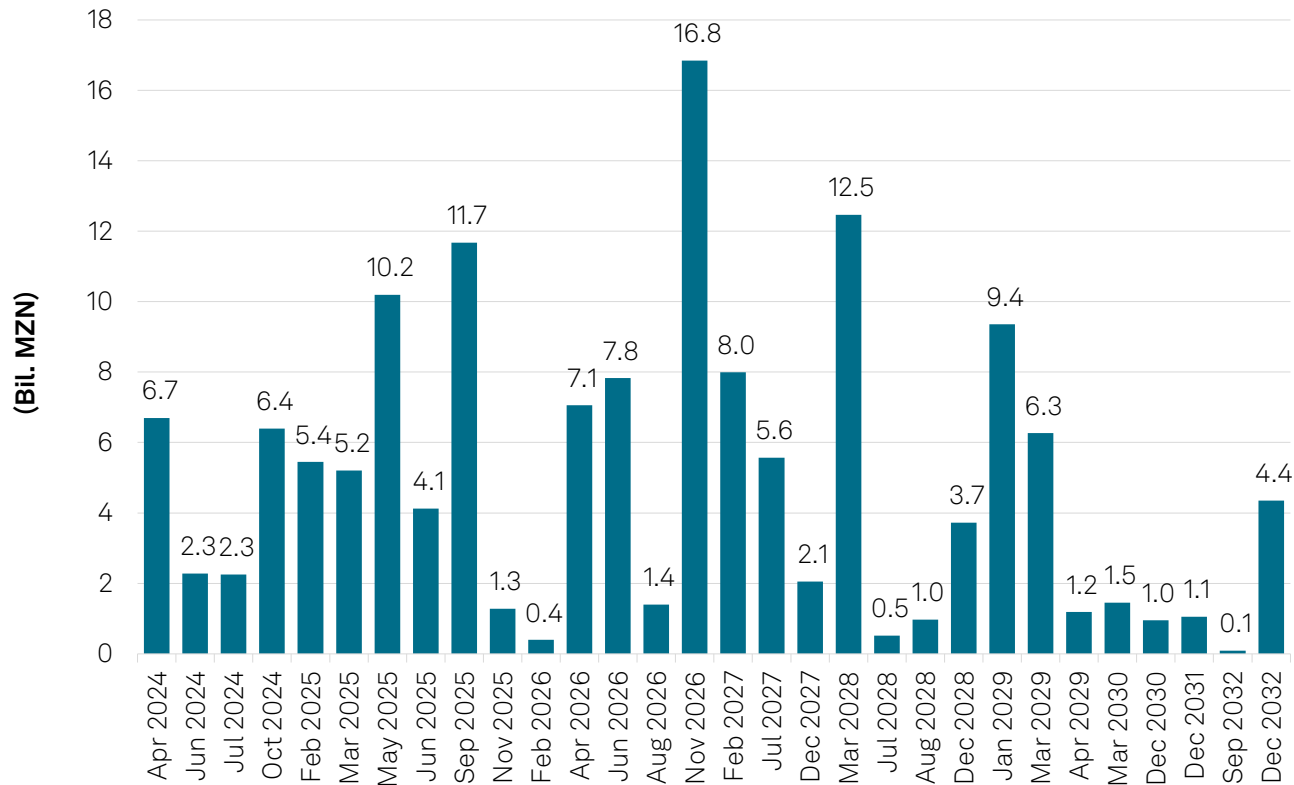
Interest costs will rise, weakening fiscal headroom



f--Forecast. GG--General government. Source: S&P Global Ratings.

Implications For Further Defaults On LC Debt

Mozambique's LC bond redemption profile is sizeable through 2029

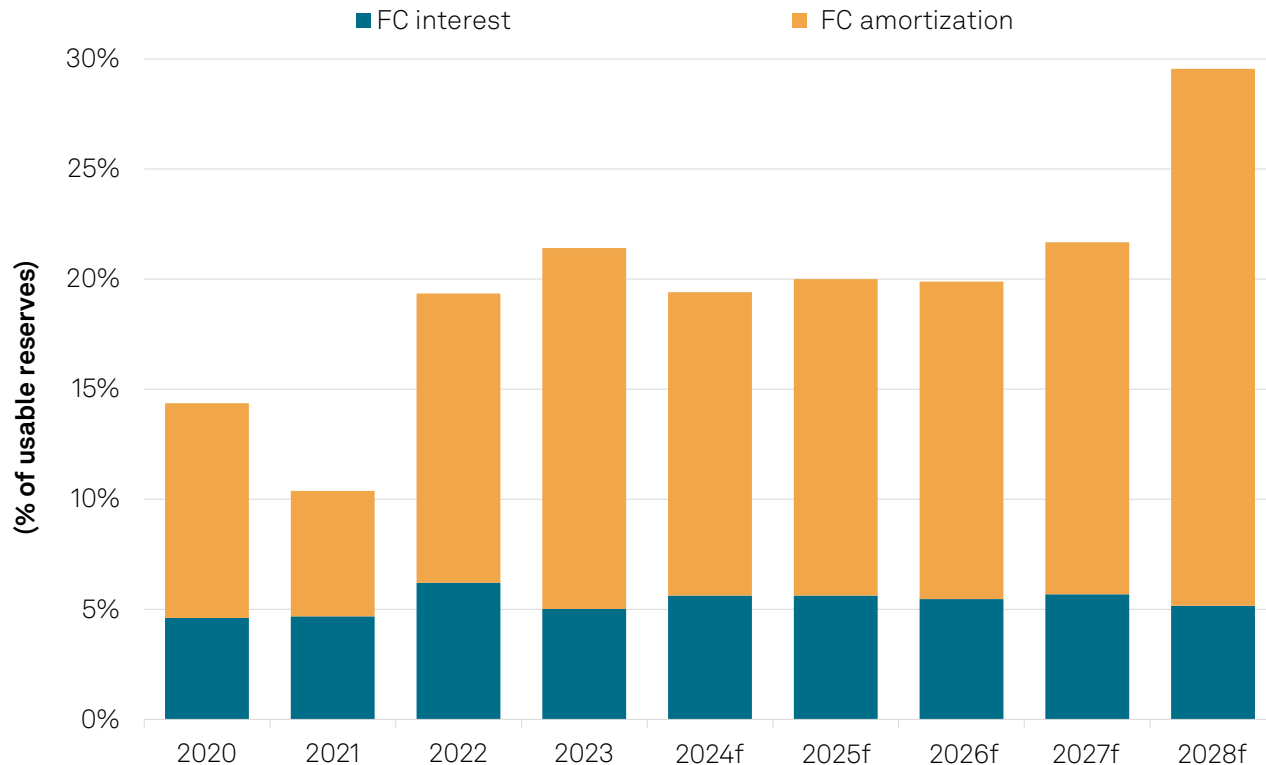


MZN--Mozambican metical. Source: S&P Global Ratings.

- The government made delayed payments on LC bonds in the first half of 2023 and has reportedly fully repaid arrears to LC bondholders.
- The risk of additional payment delays, or of a distressed exchange or restructuring, remain high due to persistent liquidity pressures.
- Maturing LC bonds will peak at 2.4% of GDP in 2025, up from 1.7% in 2023, moderating to about 1% thereafter.
- Local banks still have some capacity to absorb government debt issuances. However, exposure to the sovereign is already high, averaging close to 24% of total banking sector assets since 2017.

Implications For Further Defaults On FC Debt

FC debt service costs are currently manageable, but will rise from 2028



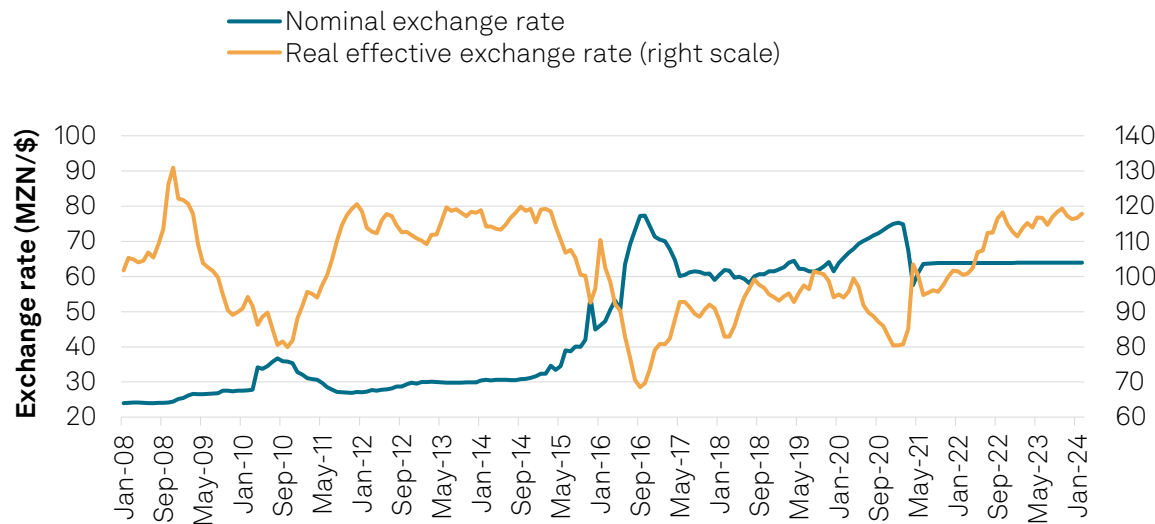
f--Forecast. FC--Foreign currency. Sources: IMF, S&P Global Ratings.

- The government remains current on its sole outstanding 2031 Eurobond, but its ability to service this over the long-term relies on future revenues from large LNG projects, in our view.
- Eurobond payments currently amount to \$81 million per year for coupons only, but amortization will begin in 2028 at \$225 million per year until 2031.
- The risk of delays to FC bilateral and multilateral creditors remain elevated. The government made delayed payments on LC bonds in the first half of 2023 and to bilateral and multilateral creditors over the past 18 months.

Sizeable External Imbalances Pose Significant Risk

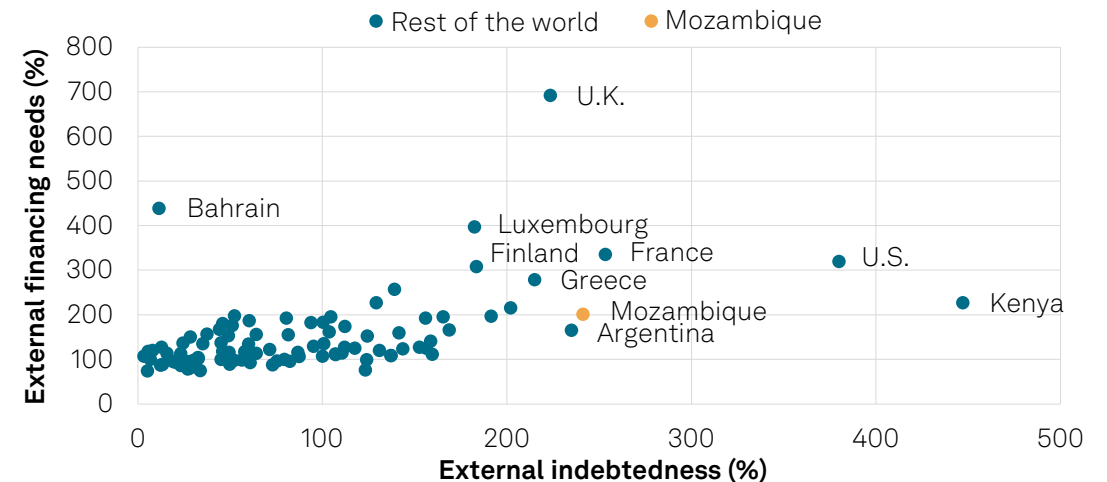
- The risk of an exchange rate shock is rising as the nominal exchange rate and real effective exchange rate movements have decoupled following almost three years of exchange rate rigidity (left chart).
- This has significant implications for the sovereign as this could further exacerbate its weak fiscal position, reduce the government's liquidity, and worsen debt metrics as 69% of total public debt is denominated in FC (right chart).
- The return of concessional external financing from the IMF in 2022, alongside financing from the World Bank and other multilateral institutions, could provide some liquidity relief for the government via cheaper financing.

Risk of disorderly exchange rate adjustment is rising



MZN--Mozambican metical. Source: S&P Global Ratings.

Mozambique's external ratios are among the weakest of all our rated sovereigns globally



Note: External indebtedness -- narrow net external debt/current account receipts. External financing needs -- gross external financing needs/(current account receipts + usable reserves). Source: S&P Global Ratings.

Are Mega Gas Projects The Silver Bullet For Mozambique?

We do not believe that gas revenues will offset the government's liquidity pressures over the short to medium term (before 2029).

- **ENI's floating LNG platforms:** The Coral South platform started production in November 2022 and has peaked at 3.4 million tons per annum (mtpa). Government revenues are estimated at 0.3%-0.4% of GDP annually. ENI is planning a second floating LNG project and aims to reach final investment decision (FID) by end-2024. This could add a further 0.3%-0.4% of GDP to revenues by 2026, absent any project delays. This will support public finances but will not resolve significant fiscal pressures.
- **TotalEnergies Area1:** We anticipate gas production could begin in late 2028, or early 2029 and has capacity to produce 13.1 mtpa. The project remains under force majeure after insurgent attacks in 2021. The government could benefit indirectly through increased taxes, which accompany large FDI from 2024 onwards, but this benefit will be limited.
- **Exxon Mobil Corp.'s Area 4:** FID on the 15.2 mtpa project is delayed and we do not expect FID to be reached before the neighboring TotalEnergies Area 1 project recommences fully. ExxonMobil is looking to draw synergies from TotalEnergies' project in terms of security and onshore infrastructure.

Are Mega Gas Projects The Silver Bullet For Mozambique? (Cont.)

Fiscal and economic prospects will only benefit over the long term (from 2029 onward).

- The longer-term fiscal and economic prospects are positive. The government estimates LNG exports could reach \$90 billion over the life of the projects and the government could receive \$1 billion per year in revenue from about 2035 onwards. The government expects to receive \$750 million on average per year but the payments will only start materializing from the 2030's onward.
- The government passed its sovereign wealth fund bill in December 2023. During the first 15 years 60% of gas revenues will be allocated to the budget while 40% will be put toward the sovereign wealth fund for savings. Thereafter, the split will be 50:50. This fiscal rule is encouraging for long-term gas revenue management.

Related Research

- [Mozambique Ratings Affirmed At 'CCC+/C'; Outlook Stable](#), April 19, 2024
- [Mozambique LC Ratings Raised To 'CCC+/C' On Resumption Of Debt Repayments; 'CCC+/C' FC Ratings Affirmed; Outlooks Stable](#), June 21, 2023
- [Mozambique LC Ratings Temporarily Lowered To 'SD' On Delayed Payments; 'CCC+' FC Ratings Affirmed](#), June 20, 2023
- [Sovereign Ratings List](#), May 17, 2024
- [Sovereign Ratings Score Snapshot](#), May 7, 2024
- [Sovereign Risk Indicators](#), April 8, 2024
- [S&P Global Ratings Definitions](#), June 9, 2023

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