PROGRAM INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

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Operation Name	Mozambique Eleventh Poverty Reduction Support Credit
Region	AFRICA
Country	Mozambique
Sector	Other Mining and Extractive Industries (20%); Central government administration (60%); General industry and trade sector (20%)
Operation ID	P154422
Lending Instrument	Development Policy Lending
Borrower(s)	GOVERNMENT OF MOZAMBIQUE
Implementing Agency	Ministry of Economy and Finance
Date PID Prepared	November 16, 2015
Date of Appraisal	October 28, 2015
Estimated Date of Board Approval	December 22, 2015
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Country and Sector Background

Mozambique's economy has grown rapidly since the end of the civil war in 1992. Annual Gross Domestic Product (GDP) growth averaged around 8 percent over the past two decades. Robust growth was made possible by sound macroeconomic management, a number of large-scale foreign-investment projects, political stability and significant donor support. However, there has been relatively little structural transformation in the economy. The share of manufacturing in the economy, which grew from 13 percent in the early 1990s to 16 percent in the early 2000s, had fallen to 10 percent in 2010-14. The share of the agricultural sector, which initially fell from 35 percent before the end of the war to 24 percent in the early 2000s, has increased again to 27 percent recently. In recent years strong growth has been supported by Foreign Direct Investment (FDI) inflows in extractive industries. Major discoveries of coal and gas may transform Mozambique into a significant player in global energy markets and the country's medium term reform agenda needs to focus on strengthening government capacity to better manage the country's extractive industries.

II. Operation Objectives

This programmatic series is designed to improve the country's business climate and increase transparency in the management of natural resources, strengthen social protection and enhance public finance management. The series supports reforms in key policy areas, including: (a) improving the business climate and increasing transparency in the management of extractive industries, by simplifying business regulations for promoting broad-based growth and enhancing the legal and institutional framework for the resource sector, (b) strengthening social protection, by reducing economic vulnerability through well-targeted social-protection policies, and (c) enhancing public finance management, by improving the management of public investments, debt and fiscal risks.

III. Rationale for Bank Involvement

Over the past decade rapid growth has not translated into significant poverty reduction. Strong economic growth led to a decline in the national poverty headcount by 14 percentage points between 1997 and 2003 to 56 percent, implying a growth elasticity of poverty reduction of 0.3. Poverty fell between 2003 and 2009 to 52 percent, implying a growth elasticity of poverty reduction of only 0.14. The weakened relationship between growth and poverty reduction is due to the changing pattern of growth, which in the past decade was driven by capital-intensive, import-dependent sectors. This pattern of growth is also reflected in labor markets, which continue to be dominated by low skilled labor in the agricultural sector; meanwhile, the rest of the economy is unable to offer better-remunerated jobs for the 300,000 new workers entering the labor force every year.

The PARP, Mozambique's third poverty reduction strategy paper, was developed through a broadly consultative process involving representatives from a range of government agencies as well as stakeholders from the private sector and civil society. During the development of the PARP the government held a series of meetings at the national and district levels and took steps to ensure that the strategy was informed by the international experience on effective development policy. The PARP was presented to donors and other stakeholders in April 2011 and endorsed by the council of ministers a month later. Its implementation period was originally intended through the end of 2014, but it has recently been extended until 2015 to allow the next government to design its own poverty reduction strategy. The policy reforms being supported, in line with the PARP, will contribute to a reversal of the weak poverty-growth relationship and to a more inclusive growth process.

IV. Tentative financing

Source:		($m.)
BORROWER/RECIPIENT		0
IDA Credit		35
Grant		35
Borrower/Recipient		
IBRD		
Others (specify)		
	Total	70

V. Tranches *(if applicable)*

	($m.)
Single Tranche	70
Total	70

VI. Institutional and Implementation Arrangements

The design of the proposed PRSC is aligned with the General Budget Support Program of budget support donors group in Mozambique. In order to reduce the administrative burden on the Government the Bank executes its supervisory role in cooperation with the Government's other development partners. In addition to two joint annual reviews, the implementation of the Government's program is monitored through monthly joint steering committee meetings held by the Government and budget support donors. Progress in each sector is overseen by sector working groups, which include representatives of the Government and its development partners. Bank staff actively participate in these meetings. In addition, the Bank participates in IMF missions to monitor progress on the implementation of the macroeconomic framework. Monitoring national poverty indicators is the responsibility of MEF and INE. INE is currently implementing the next round of the Living Standards Measurement Survey (the last round dates back to 2008/09), and first results are expected toward the beginning of 2016.

VII. Risks and Risk Mitigation

The risk to this operation is moderate. The principal risks to the objectives of this operation include macroeconomic shocks, institutional capacity constraints, political uncertainty with the change in administration, and vulnerability to natural disasters. These risks are presented below.

Mozambique's macroeconomic stance could be negatively affected by worsening current account deficits, rising external debt, or unpredictable external shocks such as commodity price and demand shocks. Macroeconomic risks are considered moderate. Sustainable internal and external macroeconomic balances depend on anticipated inflows of FDI, as well as external debt conditions and continued foreign assistance. Low commodity prices and a weak external environment increase the risks to the macroeconomic outlook, but the risks to the achievement of the operation's development objective are considered moderate. Weak commodity prices may affect investors' interest in Mozambique's natural resources, as can already be observed in the coal sector. Limited investor interest may affect the results expected in the first pillar regarding new contracts being signed under the revised regulatory framework for mining and petroleum. All other results are unlikely to be affected by macroeconomic instability (other than tail events which are unlikely). To mitigate macroeconomic risks, the National Assembly approved a 2015 budget that puts the country back on a sustainable path by significantly reducing public spending and narrowing the deficit. The 2016 draft budget prepared by the Government continues with a prudent fiscal policy, although further fiscal tightening may be needed if balance of payments pressures continue.

Weak institutional capacity may slow the implementation of reforms. Institutional capacity risks are considered substantial. Despite ongoing improvements in the capacity of the public administration, a lack of institutional resources could limit the pace and scope of the reforms supported by the proposed PRSC-11. Institutional changes in the new government (the merger of MPD and MoF into a single ministry) may also delay the pace of important reforms. To mitigate this risk the Bank is providing technical assistance in all areas supported by this operation. Despite this support, institutional capacity risks are regarded as substantial.

The inauguration of a new Government after the general elections in October 2014 could delay the pace of the reform program. Political risks are considered moderate. The political climate in the two years prior to the election was characterized by significant tensions between ruling party Frente de Libertação de Moçambique and opposition party RENAMO. These tensions led to violent confrontations between the army and RENAMO-backed guerrillas in the country's central region in 2013 and 2014. Political dialogue between the ruling party and the opposition has resulted in mutually agreed-upon revisions to election legislation and a cease-fire agreement, declaring the end of the violent confrontations. However, there are continued confrontations on a number of fronts. The start of a new administration could affect the pace of reforms, although there is significant policy continuity, as evidenced by the new PQG and continued engagement with development partners to gain support to the Government's economic reforms program. The likelihood of major policy reversals with this Government is therefore limited and political risks to the achievement of results are moderate.

Finally, Mozambique's inherent vulnerability to natural disasters and weather-related shocks represents a moderate and indirect risk to this operation. Natural disasters and weather related shocks are considered moderate. Mozambique is the only country in Africa considered to be at high risk from recurrent floods, cyclones and droughts. In the past 30 years, at least 14 percent of the population has been affected by a drought or flood/storm. Natural disasters present serious threats to public health, food security, and the Government's poverty reduction and human development goals since they tend to disproportionately affect the poor and vulnerable. The immediate necessity of responding to environmental shocks could draw scarce administrative resources away from the reform program and threaten its long-term continuity. The floods in early 2013 and early 2015 again highlighted the relatively large impact that natural disasters can have on the country's fiscal position and economic growth prospects. Large natural disasters could also lower returns to both public and private investment. The risk of major disruptions due to natural disasters and weather related shocks is mitigated by the Government's commitment to rapidly implementing many key policies supported by the proposed PRSC, while the ongoing dialogue on enhancing resilience to natural disasters is supported by the concurrent Climate Change DPO series. Emerging economic activity by mining industries is taking place in less vulnerable zones of the interior, with the potential to influence positively the risk exposure of the landscape. Coupling the benefits of risk based urban planning with expected increases in household incomes, the vulnerability of communities is expected to decrease.

VIII. Poverty and Social Impacts and Environment Aspects

The policies supported by this series are expected to have a positive impact on poverty and social indicators. Reforms to simplify business regulations and start up procedures will lead to increased productivity of the private sector and through it employment creation. Improving the business environment in general and more specifically simplifying business regulations has a positive impact on growth and employment. By reducing the time (and related costs) needed to start a business and obtain a license, this reform will lead to higher investment, productivity and increased employment creation. These reforms are also more likely to benefit smaller and medium enterprises that have fewer resources at their disposal to deal with an excessively onerous business environment.

The legal framework for environmental protection is relatively well developed in Mozambique, but implementation and enforcement capacity remains limited. The Law on the Environment (Law n° 20/97) is the basis for environmental regulations and applies to all public and private activities with potentially significant environmental consequences. These activities are subject to an Environmental Impact Assessment, which must precede any issuing of licenses or the approval of any new projects. The Ministry for Land, Environment and Rural Development (*Ministério para a Terra, Ambiente e Desenvolvimento Rural*) is the agency responsible for conducting Environmental Impact Assessments. The revised legislation for mining and petroleum sectors makes environmental impact assessments mandatory, refers to existing norms and legislation for environmental protection and includes provision for environmental management and the end of operations. The capacity of the government, however, is limited due to financial and technical capacity constraints.

The reforms supported by this PRSC series are not likely to have significant negative effects on the environment, forests, fisheries, wildlife habitats or other natural resources. The PRSC series supports policy actions designed to accelerate poverty reduction, which by themselves have no direct impact on the environment. Regular private and public investment activities which may result from a more enabling business climate could have an impact on the environment, but as mentioned above the domestic legal framework and regulatory mechanisms are judged to be fundamentally adequate to address them. Mozambican legislation requires that such effects would have to be identified as part of the preparation of the individual business projects, with credible evidence provided as to how the developer plans to manage potential environmental consequences.

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