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COMPETITIVENESS IN LIGHT OF MOZAMBIQUE'S RESOURCE BOOM

TRIP REPORT

DRAFT

October, 2013

COMPETITIVENESS IN LIGHT OF MOZAMBIQUE'S RESOURCE BOOM

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USAID SUPPORT PROGRAM FOR ECONOMIC ENTERPRISE DEVELOPMENT
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J.E. AUSTIN ASSOCIATES, INC.

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BACKGROUND

Martin Webber, Competitiveness Expert, worked in Mozambique from August 2-17, 2013. The focus of the assignment was to begin to identify how sector competitiveness in Mozambique is likely to be affected by Mozambique's resource boom.

The consultant greatly appreciated the support and collaboration of the Confederação das Associações Económicas de Moçambique (CTA) and the SPEED project, and especially Mr. Hipolito Hamela and Dr. Antonio S. Franco.

MAIN ACTIVITIES

A. Purpose and Objectives

The objective of this study and mission was to contribute to an understanding of and assist in developing consensus around the opportunities and challenges to Mozambique's economic competitiveness and growth as a result of the current resource boom. The mission identified competitiveness and growth challenges and issues, and prepared draft scopes of work for further research on competitiveness and growth in Mozambique in the context of potential "*Dutch Disease*".

B. Summary of Activities and Results

The consultant met with businesspeople, public sector officers and others to discuss perceptions regarding the impact of resource revenues on other economic sectors, particularly tradable commodities. In the course of these discussions, the team narrowed the focus to several indicative sectors – agriculture, manufacturing and tourism, and also the impact on labor costs and availability.

In examining these sectors through discussion and document review, the team developed several hypotheses about the impact of resource revenues on the three sectors (agriculture, manufacturing and tourism). The consideration of these hypotheses will be the core of the proposed follow-on research and analysis. They are described briefly in this report.

The consultant was invited to present and respond to questions at a breakfast meeting hosted by CTA. The meeting was well attended, with about 75 participants.

A briefing was also provided to USAID (Tim Born).

Antonio S. Franco of SPEED and Martin Webber worked closely together, and held various side discussion and planning sessions. SPEED and CTA took the lead in identifying and organizing meetings, in coordination with the consultant.

The annexes to this report include:

1. Example of the banana sector
2. Schedule of meetings
3. Bibliography
4. Terms of reference for this assignment

C. Prospects For Competitiveness In The Context Of Mozambique's Resources Boom

Two visits to Mozambique by well-known economist, Tyler Biggs, were organized by CTA and SPEED in 2011 and 2012. During these visits, Dr. Biggs highlighted the economic risks facing Mozambique from “Dutch Disease” and the “Resource Curse”. These two linked and widely studied phenomena result from structural changes and management of revenues arising from a boom led by extractive resources exports (or, for that matter, from any large and extended influx of revenues, such as from international aid). Dr. Biggs suggested that certain tradables sectors (he cited agriculture and tourism in particular) in Mozambique were at risk of facing negative pressures as a result of a resource boom, that would impact their sustainability and competitiveness.

In discussing competitiveness, focus may be on the competitiveness of:

- A business
- A value chain
- A region or municipality
- An economy
- The business environment

Ultimately, all competitiveness is business competitiveness.

These patterns are determined by factors such as an appreciating exchange rate, increases in wages especially for skilled labor, and scarcity of skills. They are symptomatic of local prices being “bid up”, and a movement of resources towards the economic sectors – the non-tradables – whose prices are determined within local, rather than competitive global, markets.

Consequent expectations or concerns therefore include:

- Extractive resources will provide substantial revenue (that can be invested, saved or spent), consumption from investment or higher incomes will increase prices.
- Labor costs will increase, especially in respect of persons with skills or in locations that are proximate to megaprojects and other centers of investment and economic activity.
- The Metical will suffer pressures to appreciate against other currencies because of increases in prices of non-tradables versus tradables (spending and resource movement effects).
- There will be tendency for labor to migrate to cities (and corridors) if rural areas do not provide jobs and wealth, and if work opportunities are seen as better or only potentially available in the cities.
- There will be a tendency for labor to migrate to non-tradable sectors, meaning that tradable sectors, if these do not see improved productivity, will face serious sustainability issues.
- Imports will become relatively inexpensive.

These outcomes are not inevitable. The government can take actions to mitigate these outcomes. On the other hand, there is reason to expect that these outcomes will occur. They have occurred in many other countries.

Debate around this issue needs to be properly informed, and discussed in a transparent manner. While it would be misleading to suggest that these issues have not yet been considered in Mozambique, the consultants had the impression that the resource curse and Dutch Disease impacts were not being widely and openly discussed, that potential impacts on competitiveness were not being informed by well-researched, comparable data, and that many stakeholders are assuming (hoping) that exchange rates will not dramatically appreciate and that labor costs will remain low because there is a large available pool of rural unskilled labor.

It is also important to note the anecdotal stories the consultant was told about businesses and investments that are doing well – presumably because of their good strategies and

operational management, and perhaps because of sound entrepreneurial behavior, small markets, and close to uncompetitive market powers exercise by these companies. It would be very informative to understand these businesses' strategies; they will perhaps provide good models for sectoral competitiveness in the face of resource-induced pressures.

Underpinnings of Mozambique's Competitiveness

The focus of this assessment is on the growth and sustainable competitiveness of non-extractive tradables sectors in the Mozambican economy. It is thus worthwhile discussing what we mean by competitiveness, particularly in the Mozambican context.

Leading thinkers and strategists have developed core concepts of competitiveness, perhaps foremost amongst them being Prof. Michael Porter of the Harvard Business School. Competitiveness has been the subject of discussion in Mozambique already, and numerous analyses and consultants have focused on the country's competitiveness.

At the core is the difference between comparative and competitive advantage. Comparative advantages help to generate competitiveness only if they are used to build competitive advantages. Mineral resources are a comparative advantage – they do little for an economy or the population unless the revenues from their sale are used to build competitive strengths – stronger comparative advantages or sustainable competitive advantages.

The following table, adapted from a recent study on urban competitiveness¹, describes types of comparative and competitive advantages:

Comparative Advantages	Competitive Advantages
Land availability; land costs	Labor productivity
Arable land; fertility	Process efficiencies
Taxation	Quality of product, service
Labor costs	Skills base
Raw materials	Technology
Business environment	Research and development (R&D)
Transport	Knowledge base; core competencies
Proximity to markets	Differentiation
Scenery, beaches, etc.	Social capital/trust
Economies of scale	Market knowledge
Collaborative advantages	

¹ Adapted from Chloe, K. and Brian Roberts, *Competitive Cities in the 21st Century*, Cluster-Based Local Economic Development, Asian Development Bank, Manila 2011. <http://www.adb.org/publications/competitive-cities-21st-century-cluster-based-local-economic-development>

Minerals or gas or beaches or fertile land or labor are not competitiveness. The value that is added from such resources is competitiveness.

Comparative resources are hugely important in helping countries to gain footholds in global markets; for example, where businesses use comparative resources in the form of low-cost labor or proximity to markets as a basis for garment assembly manufacturing. These comparative resources are helpful, and provide a basis for building competitive advantage. But without value added through productivity, there is no growth in competitiveness. And other countries will often be able to compete with the same or better comparative strengths.

Competitiveness is measured largely by productivity, which in turn is measured by value addition. Competitiveness is seen when businesses and value chains are able to sell products and services at higher prices and greater profits (which assumes that the market is willing to pay and that competitors cannot easily imitate and thus force prices down) than competitors, or than previously. A competitive economy builds wealth for businesses, workers and economic stakeholders – and this wealth can be used to increase incomes, or to reinvest in creating even more competitive advantage (e.g. investing in better education and skills).

To be able to continue to (or begin to) sell in the context of an appreciated exchange rate, economic sectors need to be increasingly productive, or to offer unique advantages in terms of quality, differentiation, location or other factors.

Companies, value chains and sectors have to continually improve their competitiveness; they have to stay ahead of competitors who try to imitate or beat the quality, productivity or service associated with goods or services. The same applies to countries and regions, which of course are composed of these businesses, value chains (VCs) and sectors.

Productivity of investment is a useful concept relating to competitiveness, and is of course attractive to the investor. Some businesses, value chains and economies are more able than others to achieve productivity from new investment².

Countries and regions want to build the competitiveness of their economies and the businesses (including farmers) that form the economy because:

- It attracts investment;
- It allows companies to pay employees more;
- It allows companies to invest in their employees' capabilities;
- It generates national income, which can pay for social services, further investment, education, and other desirable factors; and
- It is easier to defend against competition from a position of strength.

Diversification is also an important element of the sustainable competitiveness of an economy. In theory it's possible for a business, value chain or economy to be highly competitive through competitiveness in a single product or sector. But it is also risky to do this. Risks include downturns in prices, accidents of nature, disruptive innovations, or goods or services becoming outdated as demand shifts in line with increasing incomes. An example is Detroit, in the U.S., a location that depended too much on one sector (the automotive industry), and failed to develop other competitive advantages.

² This is measured by an index called "ICOR".

Competitiveness and the Business Enabling Environment

The weak business and investment environment has been highlighted in Mozambique for many years. The current environment – regulations, procedures, availability and quality of services – fails to provide most business and investors with the services that they need. The current business environment imposes unnecessary costs and inefficiencies and risks on business and investors. Businesses, therefore, are unable and unwilling to plan and invest for the long term, or to, in some cases, make investments that would lead to world-class productivity. It is a principle that any aspect of the national economy or bureaucracy that adds costs or risk to investment or business operations is impeding competitiveness, and may be limiting job creation by permitting impediments to business formation and sustainability.

To the extent that domestic actors are always making choices about whether to invest further, and international investors have a choice of whether to invest in Mozambique or somewhere else, the quality of the country's business environment is a competitive factor.

Businesspeople in Mozambique are preoccupied with issues in the enabling environment. The immediacy of these issues may partly explain why business hasn't fully turned its attention to the potential competitiveness impacts of resource boom.

Using low cost labor to develop Mozambique's economy

Low labor costs can be attractive to labor intensive industry, if the business environment, services, location and other elements offer satisfactory (and ideally superior) services, low operating and logistics costs, and low transaction costs. Many countries³ have used low-cost labor as a first step towards building their competitiveness.

Low cost labor typically means that there are large populations of unemployed or underemployed, which bid down wage rates. Wages can also be low in global terms in situations of a depreciated currency. Low cost labor can be a comparative advantage. But low cost labor (and the low levels of skills that that generally implies) is not a long term competitive advantage. Relying on cheap labor, other than as a way to get a foothold, means that an economy and its labor intensive businesses will have an interest in keeping wages low, and therefore will not have incentive to invest in the education and skills of its people, and will likely therefore be stuck with low levels of productivity which, over the medium- and long-term will be a serious impediment to growth.

The Economist⁴ quotes Bernard de Mandeville⁵: *[It is] "manifest, that in a free nation ..., the surest wealth consists in a multitude of laborious poor"*. That perspective suggests that countries should want to keep its labor low-paid. It is sad but common to see countries touting their low labor costs as a virtue.

There is need for a legitimate debate about whether, despite a potential Resource Curse, Mozambique can offer low cost labor as an advantage, and thus attract light manufacturing such as garments assembly, or labor-intensive agro-processing. Such manufacturing is likely to locate where infrastructure, logistics and services are superior – that is, at locations that

³ Japan, South Korea, Ireland, Honduras, Costa Rica, Indonesia, Georgia and Mauritius are but a few.

⁴ The Economist, Free Exchange, Penury Portrait - The consensus on raising people out of poverty is surprisingly recent Jul 27th 2013. <http://www.economist.com/news/finance-and-economics/21582233-consensus-raising-people-out-poverty-surprisingly-recent-penury/print>

⁵ A 17-18th Century Anglo-Dutch political economist and philosopher.

will attract many of the support services for megaprojects, hence at precisely the locations where labor prices are bid up the most. However there is a tremendous labor resource that could satisfy labor-based manufacturing, especially if urban migration were encouraged. However, legislation in Mozambique obliges a minimum wage of about \$70/month - not a comparatively low wage when productivity is low.

A focus on low-cost labor would typically imply relatively unskilled labor, and possibly limited investment in developing skills. In Mozambique's economy, skills are scarce, and skilled personnel are able to command increasing wages, often higher than those in countries elsewhere in the Southern African region. A competitive economy is one that becomes more complex and service oriented over time, and hence one that requires more people with high-level skills. With respect to labor, then, Mozambique will need to understand and plan for both changes in labor costs and the impact of scarcity of skilled employees.

D. A Three Sector Focus

The discussions and investigations undertaken in this initial mission, and the proposed work program going forward, emphasize 3 broad industries: agriculture, manufacturing and tourism – recognizing that there are many subsectors within these. These sectors were selected because they are currently large contributors to the economy and generators of livelihoods (agriculture), are considered national priorities (tourism and manufacturing), are or could be large-scale employers (and hence would be exposed to changes in labor costs), and are tradables with strong export components and global market exposure (and hence are potentially exposed exchange rate appreciation). Each has a strong stake in the country's comparative advantages, but also can benefit from strategies that build competitiveness.

Suggested Research Topics

Four research topics are suggested. These are briefly described below.

To illustrate the proposed type of cost structure analysis, Annex 1 presents data for a prototypical banana enterprise, and several considerations that it would be important to investigate.

This mission has developed several hypotheses of how labor (as a factor of production) and subsectors within each of the three industries will be affected by appreciating exchange rates, increasing labor prices, labor scarcity and other factors. Transport costs, costs of material inputs, costs of power and other factors are likely to change, perhaps dramatically, in Mozambique's economy. The proposed research will examine and test these hypotheses, providing stakeholders with perspectives and insights to inform their debates and decision-making.

It is important to recognize that the possible developments, and their impacts, are "broad strokes". Individual businesses, with excellent strategies, market linkage or operations, always have the opportunity to be successful. Indeed, during the discussions and meetings held for this assignment, various anecdotes were recounted about businesses that are successful or are investing in subsectors that are nonetheless hypothesized to come under competitive pressures.

1. Research Topic: Prospects for traditional agricultural export value chains in the context of Mozambique extractive resource boom

Hypothesis

Traditional value chains include sugar, cotton, tobacco, coconut, and cashew. These crops/products are globally traded commodities, and prices are thus set globally – Mozambique can do little to influence the global prices. Per unit revenues in Metical terms will be reduced because of appreciating exchange rate. However, appreciating exchange rates will lower the cost of imports, so the import component of production will also be reduced. Labor demand from businesses in the extractive industries and an increasingly robust service sector will likely bid up wages, particularly for employees with skills; increasing labor costs in the tradeables sector will pressure margins. Small farmer incomes will be squeezed, and the farmer will switch crops if s/he can.

Producers supplying the local market will tend to receive higher prices, because demand will increase; this may in turn trigger greater production and moderated prices.

An appreciating exchange rate will reduce costs of imported inputs. The cost of locally sourced inputs, on the other hand, will rise.

Mozambican smallholder agriculture has to dramatically improve its productivity, market access, and expansion of productive areas. Continued agricultural competitiveness will rely heavily on Mozambique's ability to substantially improve productivity in the agricultural sector.

Key perspectives and data points to investigate

- Examine the value chains' pricing structures and risk mitigation measures (Take into account the substantial price fluctuation in agricultural products). How will these stand up to pressures?
- What options are available for increased productivity? How are firms preparing for this?
- Price or profit advantage can be obtained by quality improvements (a form of productivity). What would it take to achieve this? What would be the potential impact of quality/price improvements on the cost structures?
- Benchmark subsector cost structures against those in other countries.
- Is there/how much flexibility is built into the system because of transfer pricing arrangements? Will that provide some buffer to relieve sourcing price pressures?
- How have other producer countries fared and reacted in the face of such pressures?
- What's the counterfactual – what pressures/investments/evolutions would have been expected in the industry in the absence of these pressures?

Note on increasing productivity via commercialization of agriculture: Mozambicans interviewed are aware of the need to increase productivity in agriculture and upstream agribusiness, and “commercialization” seems to be a “mantra”. “Commercialization” does require definition, however. In the Mozambican context, “commercialization” refers to farm-to-market systems that include scale economies, exposure to and transmittal of market-based incentives and pressures, and market access through downstream intermediaries. Greater commercialization of agriculture is viewed as a mechanism to promote greater productivity and consequently, both competitiveness of agricultural value chains and increased rural incomes. Competitive Mozambican agriculture will need to respond to

pressures developing from the resource boom by substantially increasing agricultural productivity, at the producer level and throughout the value chain.

Detailed examination of the possible improvement of agricultural productivity may be beyond the scope of SPEED's analysis. However, it is worthwhile emphasizing that understanding several factors will be important to assessing the evolution of the competitiveness of Mozambique's agricultural sector. Examples include: yields, value added, profitability of the value chain and actors in the value chain, prices received and quality. Greater productivity will require strong and self-sustaining producer-buyer linkages that facilitate transmission of incentives, information and inputs. How will these be affected by exchange rates and labor costs?

2. Research Topic: Tourism development – achieving a national priority in the face of Mozambique's extractive resource boom

Hypothesis

Tourism development is a national priority, and hence requires specific attention. Mozambique possesses comparative advantages (natural assets) that could provide the basis for the country to develop a destination (leisure, adventure, cultural, wildlife, etc.) tourism industry. But much investment will be needed to further establish the industry.

Mozambique's tourism industry requires lots of imported goods, both for investment and ongoing operations. Mozambique will most likely be slow to replace such imports with locally produced products. Much tourism is paid for in foreign currency as part of a package arrangement, and this may dampen the cost advantages of imports in a situation of an appreciating exchange rate.

As a labor-intensive industry, tourism will face not only general rising labor costs, but rising costs for skilled labor. And unless Mozambique can establish itself in a part of the market that is not price sensitive (presumably high end tourism), or perhaps as an add-on to regional tours⁶, then this part of the tourism market will be inaccessible in the near and medium term.

There is growing demand for business related tourism services – e.g. transport, hotels, restaurants, entertainment, and purchases – for personnel linked to investment and operations in the extractive sectors. This market will also provide demand for easily accessed leisure tourism. There is a sequencing opportunity – i.e. using leisure tourism for business tourists as a step towards developing facilities and services needed for high value regional and international leisure tourism.

With increasing incomes, Mozambicans will also be interested in domestic tourism opportunities. The infrastructure that caters to domestic tourism will have appeal to some elements of the regional and international market as well.

In this analysis, it will be important to recognize that tourism is not yet a firmly established sector; and in particular, skills and services are still weak.

⁶ A rationale that was expressed in several meetings would be that Mozambique offers a "different" destination than the mature, established locations such as South Africa and Kenya, and that Mozambique would be an excellent "add-on" destination.

Key perspectives and data points to investigate

- Describe the main tourism segments pertinent to Mozambique.
- How will each of these be affected by exchange rates and labor costs? Which cost elements will change?
- Identify in particular the labor component of various tourism businesses, and how changes in the labor market will impact tourism affordability and profitability.
- What will be the impact on the costs of locally imported goods? How will this change the attractiveness of the tourism industry for Mozambique? How will it impact the possibility of Mozambican producers increasing their supply of inputs to the industry?
- Examine the experience of other countries affected by resource booms. How have they been affected? What strategies have been successful?

3. Research Topic: There are several potential manufacturing subsectors – which can be successful in the context of Mozambique’s extractive resource boom?

The analysis will consider several types of manufacturing– e.g. light manufacturing, resource-based manufacturing, agro-processing and agro-industry, and manufacturing for regional markets.⁷

Hypotheses

Light manufacturing and more capital intensive manufacturing for export would most likely depend on importing materials or components and exporting assembled or processed products. If manufacturing is based on assembling or transforming imports for re-export, the advantages of lower costs of imports would not be strong, because the import component is just re-exported. Labor costs would increase, however, and this would have particular impact on the profitability of labor-intensive light manufacturing.⁸

Manufacturing that depends on a natural resource (e.g. local power and minerals) will more likely be insensitive to labor availability or costs. Appreciating exchange rate may put Mozambique at a comparative disadvantage to other resource-rich locations – but scarcity of such resources may be a strong mitigator.

Manufacturing for the region may hold promise, if transport service and availability is robust. On purely geographic terms, southern Tanzania, Malawi, Zambia and perhaps Zimbabwe all offer opportunities of proximity, particularly if South African transport infrastructure is overstretched and its labor costs are high. However the business model would have to be robust to overcome South Africa’s head start in terms of skills, manufacturing infrastructure and logistics. Mozambique’s labor may be low cost compared to that of South Africa but the impact of transport costs and efficiencies, such as through corridor linkages, would be an important driver of a region-focused subsector.

Agro-processing, adding value to Mozambique’s own-grown products, or regionally-produced products, has a strong logic, as long as agricultural productivity and processing

⁷ Manufacturing based on high levels of skills or knowledge is another category. But this is unlikely to be an immediate priority opportunity for Mozambique.

⁸ That is assuming infrastructure, services, procedures and transport costs are all supportive of streamlined logistics and other processes, allowing Mozambique to compete on a cost basis against countries with such efficiencies.

productivity are strong and continue to improve. It would bring forward natural value chain processes. Transport costs would be minimized in terms of distance. There would be a strong logic to FDI as well as domestic investment.

Key perspectives and data points to investigate

- Develop the cost structures of various value chains and enterprises. Compare costs of various production factors with international benchmarks.
- Perform a cost analysis from a competitiveness perspective that highlights costs impacted by labor and exchange rate.
- Discuss the availability of infrastructure – possible “competition” for infrastructure availability with extractives along corridors.
- There are some instances reported of fairly recent garment industry investments. What is their strategic/financial rationale and are they competitive?
- Sensitivity analyses to highlight impact of exchange rates and labor costs.

4. Research Topic: Impact of rising labor costs on several value chains

This topic examines the expected impacts of labor costs across several sector and business models.

This topic will also provide understanding of the likely response of rural populations to new opportunities in non-tradable industries, and hence the cost and availability of labor for agriculture and manufacturing.

Hypothesis

Rising labor costs will put pressure on the costs of goods and services, in particular in labor intensive sectors such as non-mechanized agriculture, tourism, labor intensive manufacturing, construction, etc. Businesses will have to absorb these extra costs (reducing unit profits), achieve greater labor or other productivity – or go out of business. Many businesses (and value chains) will not be able to vary their prices in the face of global prices or imports.

An alternative hypothesis is that rural labor will be largely insulated from these higher-wage labor markets, and hence agricultural production should not face significant labor-related pressures, and low cost labor will continue to be available for labor-intensive manufacturing. However, labor entering the manufacturing sector will be paid minimum wage that is comparatively high and that will rise over time - real wages are rigid downwards and possibly too high in comparison to other countries.

Key perspectives and data points to investigate

- Early value added investment in developing countries is very often based on the availability of low-cost labor. Such investment will be inhibited in Mozambique. That will apply to FDI as well as domestic investment.
- Examine the labor cost component of several value chain/business cost profiles. Which sectors are likely to be heavily affected?
- How does the labor component in Mozambican subsectors compare to that of competitor countries?
- Which sectors are more robust by being able to increase prices? How will they respond to labor scarcity and labor price increase?
- Labor costs will have already increased in some regions of the country. What has been the sector experience in those regions? What responses are already being seen?
- What responses have been seen in other countries that have experienced labor price increases?
- What are the available options to increase productivity in the affected sectors?
- Which policy options are available to address these issues?

E. A Concluding Note

Four research topics are proposed to further examine the likely impacts of Mozambique's resource boom on the competitiveness of tradables sectors in the country's economy. The information and hypotheses were developed by the consultant on the basis of available reports and detailed discussions with Mozambican stakeholders.

Many factors other than the resource boom will affect the competitiveness and success of Mozambique's tradable economy. Of particular importance will be the quality of the underlying business enabling environment, policies that specifically impact each sector, Mozambique's success in attracting globally competitive private investment, and the quality of the strategies adopted by businesses individually and collaboratively. While not specifically directed to these additional factors, the proposed research will also contribute to improved understanding of these factors.

Annex 1

Example of the Banana Sector

The following cost structure is a simplified presentation of the estimated revenue, costs and profit of a model commercial banana farm, producing for export. The numbers are adapted from a model developed by TechnoServe.

This model is presented to demonstrate the types of issues that will emerge by developing subsector cost structures and evaluating their sensitivity to possible impacts associated with a resource boom – such as appreciating exchange rate, increased labor costs and greater scarcity, and changes in service costs.

	USD	%
Selling price	8.50	100.00
Variable costs, of which:	5.74	67.53
Labor	0.43	5.04
Transport and loading	1.90	22.35
Materials	3.04	35.79
Electricity	0.17	2.03
Other	0.20	2.32
Fixed costs, of which:	0.87	10.24
Labor	0.75	8.88
Other	0.12	1.35
Maintenance and Capex	0.17	2.00
Total Operating Costs	6.77	79.65
Operating profit	1.72	20.35

Important impacts to understand include:

1. Revenue per box of \$8.50 – this is likely to be a price fixed by global markets and competition, and is unlikely to change. If denominated in dollars, the business would receive fewer Meticals, because of currency appreciation.
2. Labor costs comprise 13.92% of the sales price. If labor costs increase, margins will be squeezed.
3. Transport-related costs are significant- 22.35% of the sales price. It will be important to understand how transport-related costs will change as the result of the resource boom, as the impact on margins could be significant.
4. Materials costs are also significant – 35.79% of sales price. Imported materials should become less expensive in Metical terms.

Annex 2

Schedule of Meetings

MEETING SCHEDULE -- MARTIN WEBBER		
Week/day	Time	Description
Week 1		
Monday - 5 Aug 2013		Work at SPEED office, meetings with Brigit, Maria Nita, Tomas and Antonio, revision of schedule, data gathering and preparation of mission
	11:00AM	Mr. Hipolito Hamela and Mr. Eduardo Sengo, CTA
	9:00 AM	Mr. Mubarak, Pintex (paiting), CTA
Tuesday - 6 Aug 2013	10:00 AM	Mr. Luis Siteo, SPEED's Adviser to Minister of Agriculture, MINAG
	2:00 PM	Mr. Carlos Henriques, CEO MozFoods -- agricultural producing and exporting company
	10:00 AM	Mr. Tim Born, USAID
Wednesday - 7 Aug 2013	11:00 AM	Mr. Fausio Mussa and Mr. Carlos Madeira, Standard Bank
	2:00 PM	Meeting with CTA, Pelouros -- Mr. Gomes (producing bananas, tomatoes)
	3:30 PM	CEPAGRI - research centre at Ministry of Agriculture, Eng Mavie
	08:00AM	Mr. Antonio Sousa Cruz, Lecturer
Thursday - 8 Aug 2013	10:00 AM	Mr. Carlos Mate, NORAD/Norway
	12:00 AM	Mr. Harun Mohamed, Tourism -- Perola or Sabores
		Mr. Jake Walter and Ms. Jane Grob, TechnoServe
Friday - 9 Aug 2013	8:30 AM	
Week 2		
	08:30AM	Mr. Lourenco Sambo, CEO Investment Promotion Centre (CPI)
Monday - 12 Aug 2013	10:30 AM	Dr. Rafael Uaiene, MSU/IFPRI
	12:00 PM	Jake Walter and Jane Grob, TechnoServe
	2:00 PM	Mr. Julio Revilla, Lead Economist, Mr. Enriques Armas, The World Bank
	9:00 AM	Mr. Frade, CEO -- SuperSteel -- Across street from Shoprite
Tuesday - 13 Aug 2013	Evening	Jim Lafleur - Agrofuturo
	8:30	Bruce Chapman, Southern Sun
Wednesday - 14 Aug 2013	12:30 PM	Michael Jordan, USAID
Thursday - 15 Aug 2013	3:30 PM	Meeting with USAID -- preliminary findings and recommendations
	6:00 PM	Tourism sector meeting - Southern Sun
Friday - 16 Aug 2013	8:00 AM	Business Breakfast -- Presentation and discussion of preliminary findings to key stakeholders
	4:00 PM	Correia Goncalo, Syngenta

Annex 3

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Terms of Reference for assignment

SPEED PROJECT

TECHNICAL INSTRUCTIONS

CONTRACT No. EDH-I-00-06-00004-00, TASK ORDER 13

Study on Mozambique's Competitiveness and Growth

Position Title:

Competitiveness Specialist

Level of Effort Days:

17 days, on a 6-days week

Period of Performance:

From April to May 2013, including 1 mission

Name:

Martin Webber

Objective:

The objective of this study is to contribute to an understanding of and consensus on the opportunities and challenges to Mozambique economic competitiveness and growth. This mission will identify competitiveness and growth challenges and issues and will determine a scope of work for further research on competitiveness and growth in Mozambique.

Background:

Mozambique is rapidly turning itself into a resource-rich economy. Significant discoveries of coal and natural gas are being found and confirmed every year and exports could increase tremendously, and growing in importance in terms of the size of the economy. The mineral resources sector will generate huge inflows of foreign exchange that, once they begin flowing to the economy, can rapidly transform the country. These resources when properly and ingeniously used will increase productivity and incomes, and will improve the country's competitiveness.

Massive inflows of foreign exchange can, however, place unwanted pressures on the economy. For example, the exchange rate could appreciate in real terms causing pressures on economic competitiveness and growth of tradables in particular. Mozambique is an economy in which about three-quarters of the population gets their incomes from agriculture and have to produce surpluses to generate incomes and overcome poverty. An appreciating exchange rate with stagnant agriculture productivity could cause unbearable consequences in terms of poverty and the incomes of the large majority of Mozambicans.

The business environment in Mozambique is weak and tending to get worse as per the Doing Business report from the World Bank. If competitiveness falls due to an appreciating exchange rate that lowers the price of imports in parallel with a cumbersome and impairing

business environment, job creation, diversification of the economy and linkages with the mega-projects could be an almost mission-impossible for policy makers.

Looking into competitiveness and growth is imperative. This study will examine which challenges could be important for Mozambique as it turns into a mineral-rich economy in terms of competitiveness and growth. The consultant will prepare a short trip report about key challenges and issues to be addressed, and will prepare a draft scope of work for a research study/paper on competitiveness and growth in Mozambique.

Tasks:

The consultant(s) for this activity shall:

1. Prepare for the mission by reading background documents, and discussing potential meetings and agendas with SPEED.
2. SPEED will set up a program of individual and group meetings to discuss priority challenges and opportunities relating to Mozambique's competitiveness. 2-3 meetings will be scheduled per day for the first 5-6 days of the mission.
3. During these meetings the participants will discuss Mozambique's competitiveness priorities and the consultant will introduce options and information/ideas from international experience and good practice.
4. The consultant will prepare a draft Scope of Work for research, investigation and discussion of priority themes and ideas.
5. The draft SOW will be discussed with SPEED and USAID. It will be presented during a briefing with USAID through a PowerPoint presentation.
6. The consultant will prepare a revised SoW, taking into account the feedback received.

Deliverables:

1. A Scope of Work to research and discuss key issues relating to Mozambique's economic competitiveness and to suggest actions/initiatives to address Mozambique's economic opportunities and challenges. This will be done using a PowerPoint presentation to USAID and SPEED.
2. A brief (5-10 pages) trip report, including the PowerPoint presentation as an annex.
3. A workshop to present main economic competitiveness issues. Communicate how competitiveness is evolving in Mozambique, what could be the impact of the resource boom on competitiveness and present main research proposals.

Annex 5

PowerPoint slides presented at the CTA breakfast workshop



Impact of Mozambique's Resource Revenue Boom on the Competitiveness of Business Sectors

Martin Webber
J.E. Austin Associates, Inc.

August 16, 2013



Competitiveness

- Competitiveness has been a theme for a long while
- What we mean by competitiveness
 - Business
 - Value chain
 - Region
 - Economy
 - Business environment



Objectives

- Define competitiveness issues for existing sectors
- Prepare Terms of Reference for research
- Provide information for debate and discussion



Competitive and comparative advantages

Comparative Advantages	Competitive Advantages
Land availability; land costs	Labor productivity
Arable land; fertility	Process efficiencies
Taxation	Quality of product, service
Labor costs	Skills base
Raw materials	Technology
Business environment	Research and development (R&D)
Transport	Knowledge base; core competencies
Proximity to markets	Differentiation
Scenery, beaches, etc.	Social capital/trust
Economies of scale	Market knowledge
	Collaborative advantages

Source: ADB and JAA



Definitions

- Resource curse
 - Inferior rates of growth
- Dutch disease
 - Changes in the structure of the economy
 - Contraction of the tradables sector



Expectations

- Labor prices rise
- Skills are scarce
- Exchange rate appreciates

What are the consequences?

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Sectors to consider

Principally:

- Agriculture
- Tourism
- Manufacturing

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Agriculture

- Traditional export commodities
- New exports
- Subsistence and smallholder agriculture

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Impressions

- Few seem to have looked at these issues
- Assumption that exchange rates won't appreciate
- Many anecdotes of good business models and strategies
- When businesses discuss these issues, they discuss their core strategies

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Agriculture - hypotheses

- World prices limit what exporters can earn
- Costs of imported items (in meticals) will decline:
 - Competition for those producing for the local market
 - Reduces costs of some inputs
- Many local inputs and service costs will rise
- Small farmer will be squeezed – will switch crops if s/he can

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Sector hypotheses and research

The research will examine impacts of exchange rates and labor prices.

Competitive sectors will also require – supportive business environment, market linkage, ...

Banana for Export (per box, USD)
Profitability at risk

	USD	%
Selling price	8.50	100.00
Variable costs, of which:	5.74	67.53
Labor	0.43	5.04
Transport and loading	1.90	22.35
Materials	3.04	35.79
Electricity	0.17	2.03
Other	0.20	2.32
Fixed costs, of which:	0.87	10.24
Labor	0.75	8.88
Other	0.12	1.35
Maintenance and Capex	0.17	2.00
Total Operating Costs	6.77	79.65
Operating profit	1.73	20.25

Source: Adapted from TNS

**Banana for Export (per box, USD)
Profitability at risk**

Metical Component of Revenue per Box	
	%
Labor	13.92
Electricity	2.03
Transport and Loading	22.35

Source: Adapted from DNS

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- ### Manufacturing - hypotheses
- Light manufacturing
 - Labor (and other) costs will be prohibitive
 - Capital intensive manufacturing
 - Prohibitive - Will require startup and skills
 - Manufacturing for the region
 - Might piggyback on corridor, transport, power advantages
 - Agro-processing/agro-industry
 - Conceptually attractive, if it can compete against imports and global pricing.
 - Resource-based industry
 - Conceptually attractive, if it can compete against imports and global pricing

And for comparison, an example of road transport (data is only indicative)

Road Transport per Container	
	%
Revenue, of which:	100.0
Destination	85.0
Backhaul	15.0
Costs, of which:	
Fuel	22.0
Labor	5.5
Other operating costs	17.5
Fixed costs	8.0
D&A	17.0
Profit	20.0

Source: Author's estimates from industry discussion

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- ### Manufacturing – to research
- Investigate the strategic/financial rationale for current investments – are they replicable?
 - Cost structures of selected businesses and value chains
 - Benchmark the cost structures against international models
 - Sensitivity analyses to highlight impact of exchange rates and labor costs
 - How have other producer countries adapted to similar pressures?

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- ### Agriculture – To research
- Value chain cost structures (overall value chain and individual actors)
 - Impact of quality/price improvements on the cost structures
 - Benchmark value chain cost structures vs. comparator countries
 - Sensitivity analysis
 - Flexibility due to transfer pricing
 - How have other producer countries adapted to similar pressures?

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- ### Tourism - hypotheses
- Overall:
 - Labor will be increasingly expensive and skills will be scarce
 - Local inputs (for investment and operation) will be increasingly expensive
 - Imported inputs (especially from RSA), will continue to be attractive

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Tourism - hypotheses

- International (high end) leisure
 - Leisure tourism serving customers from overseas will lose cost competitiveness
 - Will need to operate in price insensitive market segments
- Domestic and regional
 - Rising Mozambican incomes will improve affordability
 - Regional interest will continue, but with cost sensitivity
- Business-related
 - Both for business and add-on leisure
 - Package opportunities through big companies
 - This segment may not be price sensitive

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Tourism – to research

- Profitability of various tourism business models
- Cost structure of tourism businesses – especially the labor costs, and costs of imported and locally-procured goods and services.
- Tourism strategies that have been successful elsewhere.
- How have other producer countries adapted to similar pressures?


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Impacto da Expansão dos Recursos Naturais na Competitividade da Economia e Empresarial

Martin Webber
 J.E. Austin Associates, Inc.

17 Agosto 2013


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Competitividade

- Competitividade tem sido assunto de discussão a longo prazo
- O que pretendemos dizer com competitividade
 - Negócios e economia empresarial
 - Cadeia de valor
 - Região
 - Economia
 - Ambiente de negócios


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Objectivos

- Definir competitividade para os sectores existentes
- Preparar Termos de Referência para pesquisa
- Providenciar informação para debate e discussão de matérias de competitividade


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Competitividade e vantagens comparativas

Vantagens comparativas	Vantagens Competitivas
Acesso a terra; custos com terra	Produtividade laboral
Terra arável; fertilidade	Processos eficientes
Impostos	Qualidade do produto, serviços
Custos de trabalho	Base de conhecimentos
Materias primas	Tecnologia
Ambiente de negócios	Pesquisa e Desenvolvimento (P&D)
Transportes	Competências principais
Proximidade de mercados	Diferenciação
Paisagem, praias, etc.	Capital social/confiança
Economias de escala	Conhecimento de mercados
Vantagens colaborativas	

Fonte: ADB and JAA


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Definições

- Maldição de recursos
 - Taxas de crescimento menores
- “Dutch disease”
 - Mudanças na estrutura da economia
 - Contração do sector de transaccionáveis (produtos que competem com importações ou exportações e fazem face a preços definidos mundialmente)


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Expectativas

- Aumento dos custos de trabalho
- Competências profissionais tornam-se escassas
- Taxa de cambio aprecia

Quais são as consequências?

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Sectores a considerar

Principalmente:

- Agricultura
- Turismo
- Manufactura

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Agricultura

- Mercadorias/bens tradicionais de exportação
- Novas exportações
- Agricultura de subsistência e pequena escala

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Impressões

- Poucos tem olhado para estes assuntos de competitividade
- Assumir que a taxa de cambio não apreciará
- Muitas histórias/exemplos de bons modelos de negócios e estratégias
- Quando as empresas discutem estes assuntos, elas discutem as suas estratégias básicas

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Agricultura - hipóteses

- Preços mundiais determinam os ganhos dos exportadores
- Os custos de bens importados diminuirão (em meticais) provocando:
 - Maior competição para aqueles que produzem para o mercado interno/local
 - Reduz custos de inputs
- Muitos dos inputs locais e custos de serviços aumentarão
- Pequenos produtores agrícolas serão apertados e poderão mudar para outras culturas se o conseguirem

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Hipótese de sectores e pesquisa

A pesquisa deverá examinar os impacto da taxa de cambio e custos laborais

Sectores competitivos requerem: ambiente de negócios que estimule crescimento, ligação a mercados, ...

Exportação de Banana (por caixa, USD)
Rentabilidade em Risco

	USD	%
Preço de venda	8.50	100.00
Custos variáveis, dos quais:	5.74	67.53
Trabalho	0.43	5.04
Transporte e manuseamento	1.90	22.35
Materiais	3.04	35.79
Electricidade	0.17	2.03
Outros	0.20	2.32
Custos fixos, dos quais:	0.87	10.24
Trabalho	0.75	8.88
Outros	0.12	1.35
Manutenção e Capex	0.17	2.00
Custos Totais de Operação	6.77	79.65
Lucro de operação	1.73	20.25

Fonte: Adaptação de DNS

**Banana para Exportação (por caixa, USD)
Rentabilidade em Risco**

**Componentes em Metical da Receita
por Caixa**

	%
Trabalho	13.92
Electricidade	2.03
Transporte e manuseamento	22.35

Source: Adapted from FNS



Manufatura - hipóteses

- Indústria ligeira
 - Custos de trabalho (e outros) serão proibitivos
- Indústria de capital intensivo
 - Proibitivo – Requer grandes injeções de capital e competências profissionais
- Produzir para a região
 - Possivelmente usando corredores, transporte, vantagens em energia
- Agro-processamento / agro-indústria
 - Conceptualmente atractiva, se poder competir contra importações e preços mundiais
- Indústria na área dos recursos
 - Conceptualmente atractiva, se poder competir contra importações e preços mundiais

**E para comparação, um exemplo de
transporte rodoviário (informação indicativa)**

Transporte Rodoviário por Contentor

	%
Receita, da qual:	100.0
Destino	85.0
Retorno	15.0
Custos, dos quais:	
Combustível	22.0
Trabalho	5.5
Outros custos operacionais	17.5
Custos fixos	8.0
D&A	17.0
Lucro	20.0

Fonte: Estimativas do autor após discussão com o sector



Manufatura – para pesquisar

- Investigar a razão estratégica e financeira dos investimentos actuais – podem eles ser replicados?
- Estrutura de custos de negócios/empresas seleccionadas e cadeias de valor
- Comparar a estrutura de custos contra modelos internacionais
- Análise de sensibilidade ressaltando o impacto da taxa de cambio e trabalho
- Como outros países se adaptaram a pressões semelhantes?



Agricultura – Para pesquisar

- Estrutura de custos da cadeia de valor (cadeia de valor completa e actores individuais)
- Impacto de melhorias de qualidade/preço na estrutura de custos
- Estrutura de custos da cadeia de valor vs. países comparativos
- Análise de sensibilidade
- Flexibilidade derivada da transferência de preços
- Como outros países produtores se adaptaram a pressões semelhantes?



Turismo - hipóteses

- No geral:
 - Custos laborais tornar-se-ão mais altos e as competências profissionais serão mais escassas
 - Inputs locais (para investimento e operação) serão crescentemente mais caros
 - Inputs importados (especialmente da RSA, continuarão a ser atractivos)

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Turismo - hipóteses

- Internacional (principal fim) lazer
 - Terá que operar em segmentos de mercado não sensíveis a preços
 - Turismo de lazer servindo clientes estrangeiros poderá perder competitividade
- Doméstico e regional
 - Rendimentos moçambicanos crescentes permitirá o desenvolvimento do turismo
 - Interesse regional continuará, mas será sensível ao custo
- Turismo relacionado com negócios
 - Ambos para negócios e prazer
 - Oportunidade de pacotes através de grandes empresas
 - Este segmento pode não ser sensível ao preço

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Turismo – para pesquisar

- Rentabilidade dos diferentes modelos de turismo
- Estrutura de custos dos negócios de turismo – especialmente os custos laborais e os custos de bens e serviços importados e localmente adquiridos
- Estratégias de turismo que tenham tido sucesso algures
- Como outros países se adaptaram a pressões semelhantes?