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Country Study

GROWTH, POVERTY AND INEQUALITY IN MOZAMBIQUE

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COUNTRY STUDY PUBLISHED BY THE INTERNATIONAL POVERTY CENTRE

GROWTH, POVERTY AND INEQUALITY IN MOZAMBIQUE*

Pekka Virtanen** and Dag Ehrenpreis***

ABSTRACT

Mozambique has experienced more than a decade of sustained economic growth based on two sectors, agriculture and industry. Absolute poverty has fallen rapidly. The main factor in the reduction of poverty since the mid 1990s has been increased production in agriculture, the main source by far of livelihoods in the country. However, this growth represents only a 'bounce-back' to pre-war levels of agricultural production, without any substantial improvement in productivity, which remains very low even when compared regionally. Growth in industrial production has been the main driving force behind Mozambique's rapidly growing exports. Based on a few mega-projects, this growth has, however, created few jobs while its contribution to public revenue has been marginal when compared to its value of production. Due to the enclave character of such projects, the spillover effect in terms of technology transfer or skills development has been minimal. External aid provides a major part of all foreign exchange available to Mozambique, and it has thus far had a positive effect on growth without major negative impact on the real exchange rate. Aid must be allocated now to crucial services for creating globally competitive agricultural production capacity, including rural infrastructure, in order to promote sustainable livelihoods and enhance labour productivity.

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1 INTRODUCTION

This Country Study examines poverty, inequality and economic growth in Mozambique since the acceleration of the market economy reforms after the end of the armed conflict in 1992 and the shift from one-party state to multi-party democracy. It first reviews recent economic developments in terms of GDP growth and its changing sectoral composition, and follows with an assessment of the impact on poverty and inequality, and on other dimensions of human development, viz., education and health.

The study then turns to the issue of the role of foreign capital investment, followed by an analysis of agriculture as a source of pro-poor growth. Given the magnitude of foreign aid in Mozambique, a major section is devoted to the importance of aid and trade for economic growth and poverty reduction, with recommendations for a significant shift in the country's development strategy. A concluding section summarises the main findings of the study.

2 RECENT ECONOMIC DEVELOPMENTS

After a period of structural adjustment accompanied by large foreign aid and the first democratic national elections, Mozambique benefited from two rounds of international debt relief for Highly Indebted Poor Countries (HIPC) in 1999 and 2001. This substantially reduced the country's external debt.

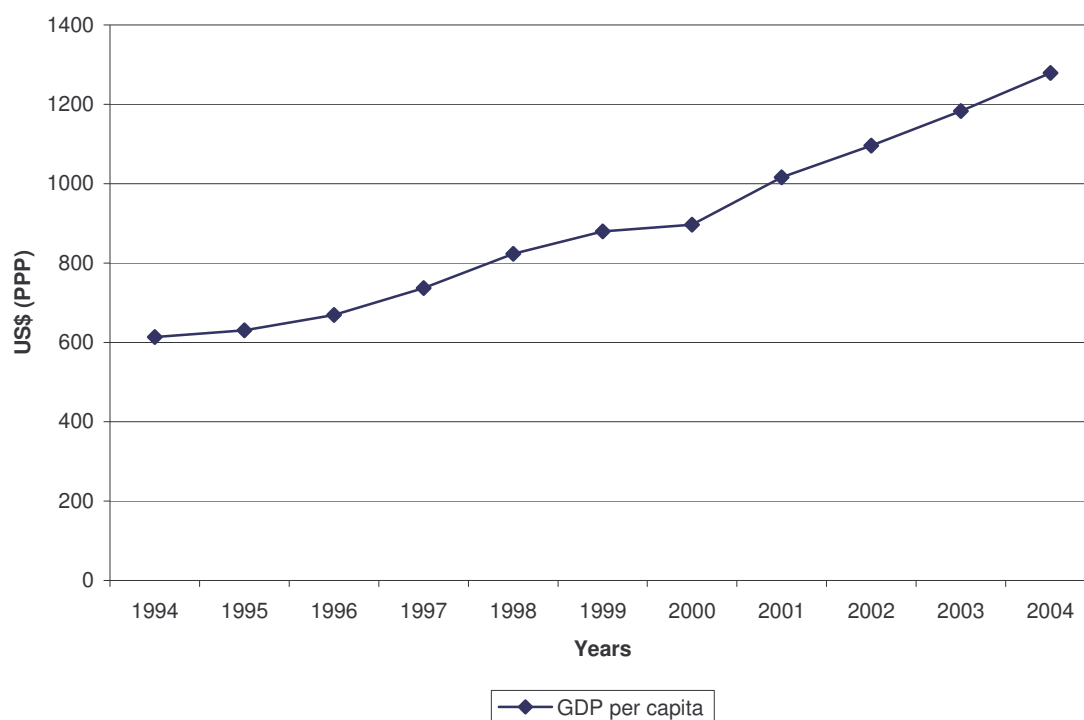
The first national poverty reduction strategy¹ (known by its acronym PARPA) was elaborated for the period 2001-2005. The document is based on the notion that lack of economic growth is the key cause of poverty, setting an average annual economic growth rate of eight per cent as the key target for the period. The strategy focused on the development of physical and human capital, notably by reconstruction and development of transport and other infrastructure as well as social services—mainly health and education.

While these sectors were already emphasised in the previous government plans, the priority for investment in human capital reflects a major change in the policy recommendations of the principal International Finance Institutions (IFIs), as compared to the 1980s structural adjustment strategies. The change has also been reflected in aid flows: assistance to social sectors increased from an average of seven per cent of total aid for the period 1985-1989 to 26 per cent for the period 2000-2004.

The policy of market liberalisation and privatisation in the context of relative political stability led to high economic growth and a profound structural change in the economy. The GDP per capita doubled between 1994 and 2004 (Figure 1). The real annual growth rate has remained steadily above seven per cent except for the year 2000, when it fell below two per cent due to catastrophic floods. The growth has been driven mainly by mega-project² construction, investment from neighbouring countries, a high level of donor support and the post-war recovery of the agricultural sector.

The mean annual growth in agricultural production between 1995 and 2003 was 5.2 per cent, while the fishing sector practically stagnated. Growth in the agricultural sector was thus substantially lower than the overall mean GDP growth rate of 8.6 per cent. High rates of growth (above 10 per cent) in construction (12.8 per cent), electricity and water (43.1 per cent), and finance and insurance (10.4 per cent) resulted essentially from the mega-projects that generated high growth rates in manufacturing (18.9 per cent) and mining (16.2 per cent), and to a lesser degree from growth in the tourism industry (World Bank 2005).

FIGURE 1
GDP Per Capita in Mozambique, 1994-2004



Source: IMF 2006.

Diverging sectoral growth rates caused a relatively rapid structural change in the economy, at least in terms of output. In terms of employment, the change has been much less radical. In 2003, approximately 80 per cent of the economically active population were still employed in agriculture and fishing. The service sector employed 15 per cent of the work force, while manufacturing industry employed only five per cent. Further, if the mega-projects are excluded, the growth rate in manufacturing falls to below ten per cent, with considerably lower growth rates after 2000.

3 POVERTY AND INEQUALITY

At the time of the first national household survey in 1996-97, Mozambique was considered one of the world's poorest countries (UNDP 2000). The mean consumption per capita was actually below the absolute poverty line, making the need for economic growth indisputable as redistribution alone would not be enough to reduce the levels of poverty. In the period 1996 to 2002, the economy grew by a cumulative 62 per cent while consumption per capita grew by a cumulative 50 per cent. The poverty headcount figure fell from 69 per cent in 1996-97 to 54 per cent in 2002-03, representing a reduction of about 15 percentage points (Table 1).³ Whilst the trend is encouraging, it is important to note that over one half of the population (nearly ten million people) continue to live in absolute poverty. This highlights the continuing importance of poverty reduction in Mozambique's development policy (James et al. 2005; Massingarella et al. 2004).

While the provincial surveys involve some problems with respect to data reliability and consistency,⁴ they are indicative of general geographical trends. Poverty incidence has declined remarkably (28 percentage points) in the central region, but also considerably in the north (11 percentage points). In the south, there has been very little change (less than one percentage point): the headcount poverty measure has actually increased in Maputo City and Province, while there was only a marginal reduction in Inhambane and Gaza provinces.

The poverty gap index, which measures the magnitude of poverty,⁵ shows these regional differences even more clearly. Except for Gaza, which shows a slight improvement, all the southern provinces have suffered from a substantial increase in poverty. The results are consistent with other research findings using different welfare indicators, such as quality of habitation and possession of durable goods (bicycles and radios), as well as locally perceived changes in well-being (Massingarela et al. 2004; Mate et al. 2005).

TABLE 1

Incidence and Magnitude of Poverty in Mozambique, 1996-97 and 2002-03

	Incidence of poverty (%)			Poverty gap index		
	1996-07	2002-03	Change	1996-97	2002-03	Change
National average	69.4	54.1	-15.3	29.3	20.5	-8.8
North	66.3	55.3	-11.0	26.2	19.5	-7.1
Centre	73.8	45.5	-28.3	32.7	16.0	-16.7
South	65.8	66.5	+0.7	26.8	29.1	+2.3
Niassa	70.6	52.1	-18.5	30.1	15.8	-14.3
Cabo Delgado	57.4	63.2	+5.8	19.8	21.6	+1.8
Nampula	68.9	52.6	-16.3	28.6	19.5	-9.1
Zambézia	68.1	44.6	-23.5	26.0	14.0	-12.0
Tete	82.3	59.8	-22.5	39.0	26.3	-12.7
Manica	62.6	43.6	-19.0	24.2	16.8	-7.4
Sofala	87.9	36.1	-51.8	49.2	10.7	-38.5
Inhambane	82.6	80.7	-1.9	38.6	42.2	+3.6
Gaza	64.6	60.1	-4.5	23.0	20.6	-2.4
Maputo Province	65.6	69.3	+3.7	27.8	31.1	+3.3
Maputo City	47.8	53.6	+5.8	16.5	20.9	+4.4

Source: Massingarela et al. 2004.

The geographical pattern of the growth process has contributed to a reduction in regional disparities in Mozambique. In 1998, the national human development index (HDI) was 0.285, ranging from 0.605 in Maputo City to 0.176 in Zambézia Province. The difference between the south (0.427), centre (0.267) and north (0.212) in the immediate post-war period was indeed substantial (UNDP 2000).⁶ In parallel with improving inter-regional equity, intra-regional inequality has, however, increased in all provinces except Nampula and Manica (Table 2).

In 2002-03, inequality was lowest in the north and centre, with estimated Gini coefficients of approximately 0.39. The level was much higher in the southern region (Gini coefficient 0.47), driven in part by the increase of inequality within Maputo City from 0.44 in 1996-97 to 0.52 in 2002-03. This is a cause for concern, especially considering that the poverty headcount has remained essentially flat in the capital city between the two sample periods despite the increase in mean consumption. Moreover, the Theil entropy measure value for the City increased from 0.41 to 0.60. The results show a sharp rise in the consumption growth of the

richest households in the midst of a large impoverished population. This would seem to indicate that the benefits of economic growth in the city in recent years are not reaching the poorer sections of society.

TABLE 2

Regional Changes in Inequality Between 1996-97 and 2002-03

	Mean consumption ¹	Increase in real consumption ²	Gini ³		GE(1) ³	
			1996-97	2002-03	1996-97	2002-03
National average	1.28	32	0.40	0.42	0.31	0.37
<i>North</i>	1.22	20	0.38	0.39	0.29	0.35
<i>Centre</i>	1.40	63	0.37	0.39	0.27	0.31
<i>South</i>	1.15	4	0.43	0.47	0.37	0.50
Niassa	1.29	45	0.35	0.36	0.22	0.26
Cabo Delgado	1.27	8	0.37	0.44	0.27	0.62
Nampula	1.18	20	0.39	0.36	0.30	0.24
Zambézia	1.35	44	0.32	0.35	0.20	0.23
Tete	1.06	49	0.35	0.40	0.21	0.30
Manica	1.41	22	0.41	0.40	0.36	0.30
Sofala	1.81	207	0.40	0.43	0.32	0.41
Inhambane	0.77	-1	0.38	0.44	0.31	0.40
Gaza	1.24	12	0.38	0.41	0.27	0.38
Maputo Province	1.01	-6	0.42	0.43	0.35	0.36
Maputo City	1.69	10	0.44	0.52	0.41	0.60

Notes: 1. Proportion of poverty line, 2002-03;

2. From 1996-97, per cent;

3. The Gini and GE(1) (General Entropy or Theil entropy measure) reflect the dispersion of a distribution, 0=absence of inequality.

Source: James et al. 2005.

The national level of inequality measured by the Gini coefficient increased moderately from 0.40 in 1996-97 to 0.42 in 2002-03, which is still a low level in the regional context of southern Africa. This reflects the fact that the rapid economic growth has been relatively broad-based, with consumption per capita in all percentiles of the population growing by at least three per cent per year. However, even though the mean consumption per capita for the entire population increased from 97 per cent of the poverty line in 1996-97 to 128 per cent in 2002-03, the mean consumption in the poorest quintile was still less than 40 per cent of what is required to meet basic needs. This is because average consumption in the highest quintile was eight times that in the poorest quintile, while the growth rate in the highest quintile was 36 per cent, compared with 23 per cent in the lowest.

In absolute terms this means that 57 per cent of the total increase in consumption took place in the richest quintile, against only eight per cent in the poorest. Data from household income surveys reflects an even more skewed distribution of growth in rural areas: over 70 per cent went to the top income quintile, while less than three per cent went to the poorest (Boughton et al. 2006). Using the definition of pro-poor proposed by Kakwani and Pernia (2000), the recent economic growth in Mozambique cannot, therefore, be considered pro-poor.

4 HUMAN DEVELOPMENT

In the first years of independence in Mozambique, primary education and basic health care services were extended to cover most of the African population. The growth in coverage was facilitated by a substantial increase in the number of schools and health facilities in rural areas. A fundamental role was given to literacy and adult education, which were seen as prerequisites to eradicating poverty and increasing production and productivity. In the health sector, a network of community health workers was created to support the expanded provision of primary health care (PHC) services.

Due to the armed conflict (1977-1992) and economic destabilisation, many of these progressive social sector policies were, however, never fully implemented, while the physical infrastructure suffered heavily from rebel attacks. By 1992, nearly 60 per cent of the primary schools had been destroyed and/or were closed. Of the 1,373 health centres and posts in operation in 1982, one third had been destroyed by 1987 (UNDP 2000; UNICEF 1994).

The decline in the social services was not, however, caused solely by the acts of war. Despite relatively high allocation for social services in the state budget, the expansion relied on a high number of rather poorly trained human resources possessing little if any material means to operate. In primary education, for example, wages made up 99 per cent of recurrent costs in the late 1980s. Several health posts and primary schools actually ceased to function due to lack of operational resources and staff well before the war reached the area.

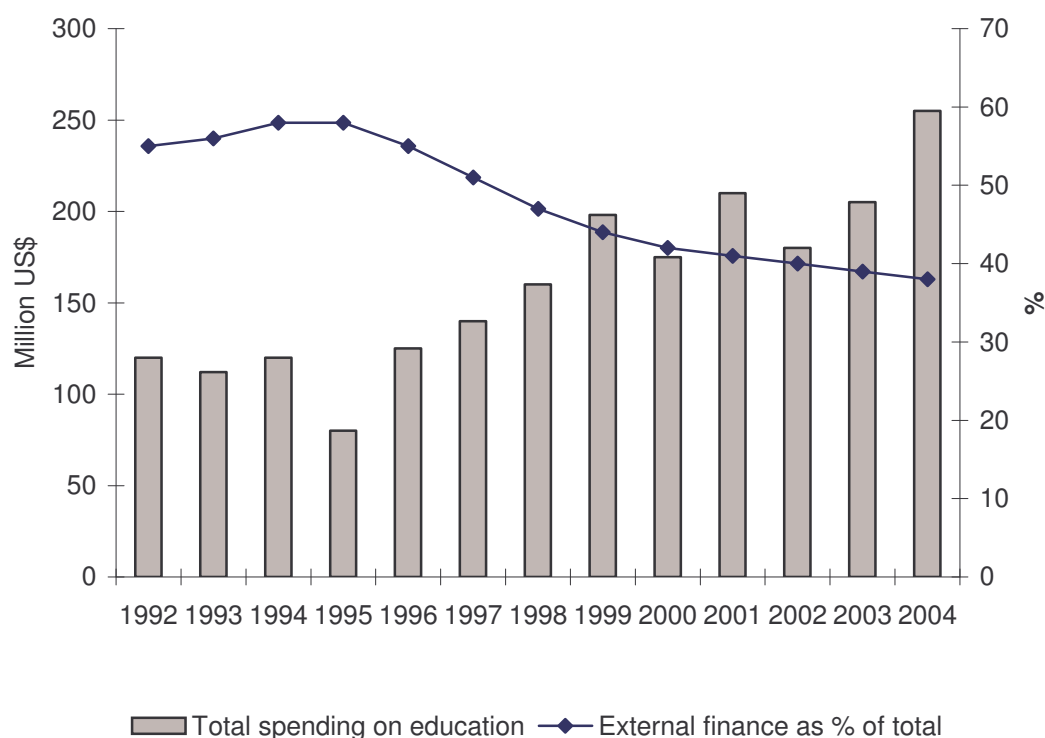
At the same time the continuing southern bias in resource allocation tended to perpetuate the regional inequality inherited from the colonial era. For example, specialised hospitals in the capital accounted for almost one half of health-service running costs in 1991, leaving very little to spend on drugs, staff and maintenance in over one thousand rural and provincial PHC facilities. In education, Maputo City received over 60 per cent of all investments in the early 1990s (UNICEF 1994).

4.1 EDUCATION SECTOR

Investment in education has grown substantially in the government budget since the early 1990s. Total public spending on education doubled between 1992 and 2004, growing steadily from 1995 to 1999 and again from 2002 to 2004 (Figure 2). This growth was made possible by external financial support, which constituted on the average almost 50 per cent of the education budget (Arndt et al. 2007).⁷

With increased funding, relatively good progress has been made in the education sector since 1997 (Table 3). Between 1992 and 2004, the number of primary schools increased from 3,556 to 9,489. Better coverage of the educational infrastructure was also reflected in literacy rates, and indirectly in the labour force. While approximately 86 per cent of the economically active working population had no educational qualifications in the early 1990s, the proportion had fallen to 77 per cent in 2004. It has been estimated that the contribution of education to economic growth in the period 1999-2004 was close to 14 per cent, which represents a relatively high return to education for a developing country (Jones 2006; Simler et al. 2004).

FIGURE 2

Total Spending and Share of External Finance in Education, 1992-2004

Source: Arndt et al. 2007.

TABLE 3

Indicators of Education Level in Mozambique, 1997 and 2003 (%)

	1997	2003
Net enrolment rate in primary education	44	69
Primary education (EP1) completion rate	22	39
Literacy rate of 15-24 year-olds	52	58
Literacy rate in population above 15 years	40	46

Source: Republic of Mozambique 2005.

The overall level of education, however, remains very low despite recent improvement in the provision of primary education. According to a recent study, only 15 per cent of students entering the system completed seventh class (EP2), and at grade 12 the percentage had shrunk to one. This means that more than 60 per cent of primary school-age children are likely to leave the system without appropriate skills in reading, writing and numeracy. The situation is aggravated by continuing problems in the efficiency and quality of education, which have either improved only marginally or deteriorated. For example, the pupil per teacher ratio has increased from 53 in 1992 to 59 in 2004, while repetition rates and absenteeism remain high (Arndt et al. 2007; Republic of Mozambique 2005).

The average figures hide substantial geographical and gender disparities. For example, the Net Enrolment Ratio (NER) was only 53 per cent in Nampula Province, while it was 66-78 per cent in the other provinces, and above 96 per cent in Maputo Province and City. Similar differences were registered in the literacy rate, which varied from 71-85 per cent in the south, to 39-55 per cent in the centre and only 32-36 per cent in the north. The regional disparity is partly explained by the higher share of the urban population in the southern region, as this population has higher average literacy levels than the rural population (70 per cent compared to 34 per cent). Despite substantial expansion in the EP1 and EP2 networks, access to school is still limited in peripheral rural areas (Republic of Mozambique 2005).

While the gender gap in the enrolment ratio has gradually decreased, girls remain disadvantaged: in 2003 the NER for girls was 66 per cent compared with 72 per cent for boys. The literacy rate (above 15 years) remains highly skewed towards men, only 31 per cent of women being literate compared to 63 per cent of men (Republic of Mozambique 2005). This is a significant factor in terms of economic development, as it reduces the employment opportunities available to women.

Currently women constitute about 54 per cent of the total labour force. However, almost 90 per cent of women work in the agricultural sector (mainly small-scale), where they make up more than 62 per cent of the labour force. Men constitute over 90 per cent of the labour force in manufacturing, construction and transportation, 75 per cent in government service, 65 per cent in service industries, and almost 60 per cent in commerce. Of the occupied female labour force, less than five per cent had a secondary school or higher level of education, while the proportion for men was 15 per cent (Republic of Mozambique 2006).

Due to the increasing coverage of primary education, the number of workers without any education has been falling in absolute terms during the post-war period. However, the extent of secondary schooling remains low in rural areas; thus agricultural workers with some education had attended mainly the primary level. In the other sectors, the contribution to growth attributed to skilled labour has been increasingly driven by secondary-level education, suggesting that further expansion of education at this level and beyond will be necessary to support future employment needs and demands of modern technology (Jones 2006; cf. Republic of Mozambique 2006).⁸

This conclusion is supported by studies from the more industrialised South Africa, which show that with increasing access to primary education, secondary education is rapidly becoming a basic requirement for entering labour markets (Leibbrandt et al. 2007).

4.2 HEALTH SECTOR

Similarly to the education, the health sector has been highly dependent on external financing.⁹ Since the late 1980s, aid has financed 60-70 per cent of total spending in the sector, and approximately 80 per cent of all capital investment. In the post-war period, external and internal funds have grown at similar rates. Subsequent rapid increases have financed extensive rehabilitation and construction of the health service infrastructure in the 1990s. The number of public health centres grew from 162 in 1994 to 683 in 2004, while the total number of beds increased from approximately 9,000 to 17,000 during the same period (Arndt et al. 2007).

Increased service coverage has had some concrete effects in terms of reduced child mortality. In the period 1997 to 2003, infant mortality declined from 147 to 124 (per 1000 live

births), while under-five mortality decreased from 219 to 178. There are, however, huge differences between provinces; from 241 in Cabo Delgado to 108 in Maputo Province and 89 in Maputo City. The nutritional status has not improved much; the prevalence of under-weight children under five years of age, has remained high. It was almost twice as high in rural (27 per cent) as in urban areas (15 per cent) in 2003 (Republic of Mozambique 2005; cf. Simler and Ibrahimo 2005). Among other factors, the geographic differences in health indicators reflect continuing unequal allocation of resources. For example, Maputo City receives four times the average funding per person, and has three times the average number of beds per person (Arndt et al. 2007).

5 FOREIGN CAPITAL INVESTMENT

During the last decade there has been a rapid increase in Foreign Direct Investment (FDI), especially in manufacturing, mining and energy, contributing to a very rapid rise in exports and deepening integration in global markets. However, if we look at the regional pattern of poverty incidence and compare it with the distribution of productive investment in Mozambique, we note a negative correlation. Between 1990 and 2003 the City and Province of Maputo absorbed 75 per cent of FDI and 60 per cent of total private investment in the country. The other two southern provinces of Gaza and Inhambane together absorbed another 15 per cent of total FDI and 17 per cent of total private investment (Castel Branco 2004).

While the southern region has thus consumed approximately 90 per cent of FDI and 77 per cent of total private investment, it is the only region where the incidence of poverty has actually increased, especially in Maputo City and Province—exactly where the majority of the new investments were made (See Table 1, Page 4). We also note that the two provinces with the highest headcount poverty ratios (81 per cent in Inhambane and 70 per cent in Maputo Province) are in the south, while even in Maputo City the poverty ratio is just barely below the national average.¹⁰

This apparent paradox can be explained by the current pattern of economic growth and the changing role of Mozambique in the regional economy. The southern part of Mozambique was historically integrated in the South African economy, and especially in the South African Mining and Energy Complex (MEC) as a labour reserve and transport corridor. The dominant position of the MEC and recent changes in its structure provide the major explanation of the weak development effect of the industrialisation process taking place in Mozambique. The Mozambican dimension of MEC consists of a few mega-projects in core industries (aluminium and energy, natural gas, heavy and mineral sands), which are exploited by very large South African-based multinational corporations in collaboration with international capital and IFIs.

After independence the volume of income from migrant labour and transport decreased rapidly. The number of migrant labourers working in South Africa fell by more than 60 per cent between 1975 and 1977, while railway transport through the port of Maputo decreased initially more gradually, but then fell drastically by 70 per cent (in volume) between 1982 and 1984 as the armed conflict intensified (Castel-Branco 2002).

While the reduction in railway traffic was not reflected directly in employment figures as the state-owned ports and rail corporation (*Caminhos de Ferro de Moçambique*, CFM) did not lay off workers, the reduction in migrant labour was immediately visible in the increasing number of unemployed, and indirectly in radically decreasing investment in agriculture and

other productive activities. However, even with reduced employment potential these sectors constituted, at least up to the late 1990s, the major mechanism whereby the Mozambican economy benefited from the South African MEC, notably as an important source of investment capital for the small-scale agricultural sector in the southern part of the country.

The system suffered a further setback in the late 1990s as a result of structural changes in the South African and Mozambican economies. In South Africa, the restructuring and increasing mechanisation of the gold mines, including the closure of some, caused a further reduction in migrant labour, which was reflected in a 40 per cent decline in migrant workers' remittances to Mozambique between 1997 and 1999.¹¹ At about the same time the privatisation process in Mozambique had moved to utilities, with a focus on the management of port and railway services. While the privatisation of CFM had some positive economic effects, such as an increase in transport revenue (in foreign currency) from less than US\$ 60 million in 1998 to US\$ 100 million in 1999, it also implied a substantial decrease in the labour force.

While the MEC continues to dominate the economic linkages between South Africa and Mozambique, it has suffered some major changes as a result of the globalisation process. The key issue is that trade and FDI have become South Africa's main instruments for regional domination.

Practically all investment in technologically advanced industries and services in Mozambique since 1994 has taken place in the context of Spatial Development Initiatives (SDIs), planned and managed from South Africa, mostly in the context of the South African-dominated MEC. Almost 80 per cent of investment in the transport infrastructure takes place around the three SDI corridors, with emphasis on the Maputo Development Corridor, and close to 90 per cent of total private investment in the manufacturing industry in Mozambique takes place in the capital region.

Regional control over production sites, trade and capital flows—typically in the context of Spatial Development Initiatives and other joint public-private strategies—has become more important than access to cheap migrant labour and transport services. South Africa has been remarkably successful in attracting international finance capital and know-how to mega-projects located in neighbouring countries conveniently close to major export outlets, and in tying host government resources to supporting physical infrastructure. However, the local development impact of these highly capital-intensive projects has been minimal.

With the exception of sugar, none of the major South Africa-driven industrial projects located in Mozambique has provided substantial numbers of job opportunities beyond the initial construction period. While a few projects have stimulated the emergence and growth of small and medium enterprises in South African regions bordering on Mozambique, linkages between South African and Mozambican firms are few and tenuous. Overall, the mega-project based development strategy relying on market opening has lost more jobs than it has created.

While the change in South African industrial strategy, which lies behind the current pattern of investment in southern Mozambique, has created a small number of highly productive and relatively well-paid jobs, its overall impact has arguably been to increase poverty.¹² Most observers agree that the contribution of mega-projects to local employment has been at best marginal, while the tax contribution has also been very limited, about 0.4 per cent of revenues in the case of Mozal. Replacement of migrant labour with FDI has, therefore,

practically eliminated the key mechanism for distributing the benefits from Mozambique's participation in the MEC to those affected by the change.

At the same time, the concentration of private and public investment in large capital-intensive projects with little impact on poverty has drained financing from other, potentially more poverty-reducing projects, e.g. rural infrastructure. Increased demand has also created localised pressure on market prices, which—in the context of increasing economic inequality—has driven many poor inhabitants of the capital and surrounding provinces into poverty.

The poverty situation is especially serious in Maputo and Inhambane provinces, but also in Gaza. Except for a few localised areas of high productivity, such as parts of the Lebombo highlands and the Chokwe irrigation scheme, the agricultural potential in the southern provinces is very low. As discussed above, this has historically been compensated by access to remittances from migrant labour to South Africa, which was the main source of investment capital and livelihood support for the rural population.

The radical decline of this revenue, and failure to compensate for it with salaried work in Mozambique, has drastically increased the incidence of poverty and vulnerability to drought in the region. In the predominantly rural provinces of the south, increasing poverty is closely linked to falling agricultural production. In Inhambane, for example, large-scale capital investment in the natural gas project and tourism industry in Bazaruto Islands has brought relatively few benefits to the local population, while the production of most basic food crops has decreased substantially (see, for example, Mate et al. 2005).

6 AGRICULTURE: THE KEY TO PRO-POOR GROWTH

Agriculture provided the second most important sectoral contribution to GDP growth (after manufacturing) between 1996 and 2003, accounting for 1.7 out of 8.6 percentage points. Furthermore, its contribution to poverty reduction was the largest: no less than 11 of the 15 percentage points in total reduction of poverty incidence were due to households whose heads worked in agriculture (World Bank 2005).

The prominent role of agriculture in reducing poverty is due to its dominant position in the structure of employment: some 70 per cent of the entire population have agriculture as their main occupation. Small-scale farmers (with an average farm size of 1.4 ha) constitute 99 per cent of the farming community and cultivate 95 per cent of the total cultivated area. This means that no significant increase in agricultural output and no significant reduction in poverty can be achieved unless the small-scale sector is made a priority.

Agriculture is important also from the gender perspective: in 2003 more than 88 per cent of women worked in agriculture. They made up 59 per cent of all unskilled labour in the sector, while men accounted for about 75 per cent of skilled agricultural labour (Table 4). This unequal division has a direct implication for gender differences in the incidence of poverty, since unskilled agricultural labour gets the lowest wages, by far.

Researchers and policy analysts broadly agree that the post-war growth in agriculture in Mozambique resulted mainly from the recovery of smallholder subsistence food crop production through an expansion of the area under cultivation and a higher labour input.¹³

The area under cultivation expanded by 3.3 per cent annually during the period 1992-2001, while the labour input grew by 1.7 per cent.

TABLE 4

Skill and Gender Composition of the Mozambican Labour Force, 2003

	Gender shares by skill, per cent		Skill shares by gender, per cent			Wage index
	Female	Male	Female	Male	Total	
Unskilled agricultural labour	59.0	41.0	88.2	67.0	78.1	100
Skilled agricultural labour	25.3	74.7	2.4	7.8	5.0	164
Unskilled non-agric. labour	30.1	69.9	7.1	18.0	12.3	430
Skilled non-agric. labour	25.2	74.8	1.8	5.8	3.7	1,474
Highly-skilled non-agric. labour	25.3	74.7	0.4	1.4	0.9	3,509
Average/Total	52.2	47.8	100	100	100	225

Source: AfDB/ADF 2006.

The increase in factor inputs was particularly substantial in the central region, where the cultivated area expanded by seven per cent and labour input grew by four per cent annually. A 45 per cent increase in the mean cultivated area per capita (adult equivalent) in the central region was recorded between 1996 and 2002. But the growth in cultivated area was only ten per cent in the north, while the southern provinces (excluding Maputo City) suffered an eight per cent decline.

The problem is that this 'bounce-back' effect in agriculture cannot be repeated. The growth rates of the production of such staple food crops as maize, sorghum and cassava have fallen from their 1990s levels, and the same is visible in traditional cash crops such as cashew. Recovering pre-war production levels with well-known and previously applied technology did not demand much innovation or investment, but now this option for growth has largely been exhausted.

At the same time, there was little increase in market integration and the use of productivity-enhancing inputs. For example, about 90 per cent of farmers still prepare their land by hoe. Consequently, the yields of basic food crops in the smallholder sector have remained essentially flat over the last decade. In rural areas, subsistence agriculture provides about half of total income, the rest coming primarily from sales of agricultural produce and animal products, supplemented by non-agricultural activities, mainly natural resource extraction.

6.1 AGRICULTURAL DEVELOPMENT STRATEGY

The current challenge is to transform the present system of subsistence agriculture, which is characterised by geographical dispersion, small units and low productivity, into an efficient commercially oriented system. According to the national poverty reduction strategy (PARPA), "the agricultural development program must be oriented toward: (i) assistance to small family farms during their gradual transition to commercial operation; and (ii) assistance to commercial farmers, encouraging them to boost their production, productivity, and competitiveness, thus ensuring satisfaction of basic needs and higher incomes in rural areas, coupled with the establishment of agroindustries that will add value to farm products for both the domestic and export markets".

Commercial agriculture and agroprocessing are widely identified as the areas in which Mozambique has comparative advantage on the global markets, due to favourable agro-ecological conditions, low demographic pressure and relatively cheap labour costs. However, investment in agriculture remains extremely low.

This can at least partly be attributed to weak government performance. Despite years of preparation, the recently launched national rural development programme (Proagri II) lacks a concrete strategy as to how input and output markets and financial services (particularly for smallholders) should actually be implemented. Various observers have noted that little effective change can be observed in the Ministry of Agriculture, which remains heavily overstaffed at the central level, but suffers from lack of human and financial resources at district and lower levels (see, for example, Birgegård 2006; Coughlin 2006; Weimer et al. 2004).

With dozens of sub-sectoral strategies and no overarching development vision or adequate mechanism to prioritise, link and co-ordinate activities, the government's approach to rural development has been fragmented and based on poorly integrated analyses. Government initiatives, especially in key export sectors such as cotton and cashew, have been inconsistent and sometimes contradictory—not least as a result of donor interventions. This has discouraged investment and caused stagnation in producer prices. In terms of economic growth and poverty reduction, the results have clearly been far from optimal, especially for agriculture and agro-processing.

Investment of external financial resources in economic infrastructure, which is important to smallholders and rural entrepreneurs, as well as in basic health care and primary education services, can do much to promote growth and reduce poverty when it creates livelihoods for the poor and enhances their labour productivity. However, the atomistic supply structure and the length of supply chains from dispersed smallholder producers and artisanal fishermen creates a major obstacle to the creation and maintenance of cost-efficient linkages with export markets. In these sectors weak absorption capacity in the public sector, combined with relatively low public revenue collection capacity, seem to set the limits to further cost-efficient investment of external resources.

6.2 TRANSITION TO COMMERCIAL AGRICULTURE

Most observers agree that achieving the transition to a commercially oriented agriculture depends on investment in rural trade networks, agricultural extension, micro-credit, transport and processing services. Currently credit is available to only three per cent of rural households, while less than five per cent of farmers participate in farmers' associations, and extension services reach only 14 per cent of farmers. The government cannot realistically be expected to provide these services on a nation-wide scale: at present, for example, less than one third of extension agents are in government service, the rest being NGO and private sector employees. Some kind of joint public-private approach is thus called for.

However, the lack of infrastructure (especially rural roads and electricity), combined with the geographical dispersal of producers, creates strong disincentives to expansion of the private service network and processing industries in rural areas far from the main markets and/or transport corridors. As a result, commercial margins for agricultural products are very high, especially for primary products, while access to improved agricultural inputs (seeds, fertilizers, pesticides) is limited and prices elevated.

With the ongoing high rate of investment in construction and rehabilitation of rural and district roads and the expansion of the electricity network, the coverage of the commercial network is likely to expand in the near future. The question is: which of the alternative rural development strategies (or combinations thereof) would most likely contribute to pro-poor growth that is also sustainable?

In collaboration with the private sector, improvement in agricultural service delivery can be achieved either by vertical integration of the agro-industry or through contract farming arrangements. In the period 2000-2004, five major agricultural products (cotton, tobacco, sugar, cashew and timber) accounted for approximately 40 per cent (in value) of agricultural exports. Of these, tobacco and sugar have grown rapidly with the support of foreign investment and know-how, while the production of cotton and cashew has stagnated or even declined as a result of inconsistent government policies and conflicts within the sector.

Timber exports have grown rapidly but suffer from inconsistent government policy and a relatively high incidence of illegal (unsustainable) harvesting and contraband. A sixth product group with good export potential is horticultural products. It should, however, be kept in mind that traditional food crops, such as maize, millet, cassava, beans and fruits, still constitute the bulk of national and even regional trade- though it is often informal and thus unregistered. This provides a third alternative.

6.3 CONTRACT FARMING

Contract farming provides a strategy that can, at least in theory, stabilise the rural population within the smallholder framework by creating remunerative agricultural self-employment through product-specific contracts with private firms, which provide the necessary inputs and services (credit, extension, seeds and tools) to smallholders for the right to buy the produce. In Mozambique the system has traditionally been used for producing cotton, but recently also tobacco.

Processed commodities, such as cotton and tobacco, require a great deal of coordination to be produced, processed and marketed competitively. Since most farmers in Mozambique require credit to access the needed inputs, one of the key challenges is to ensure timely access to and use of appropriate inputs, and subsequently to recover the credit. Due to widespread credit market failure experienced during recent years, a combination of public and private action is needed to resolve the endemic credit market failure, acquire and diffuse technical innovations, and ensure the necessary co-ordination to meet the quality requirements of global markets.

However, contract farming tends to favour the more affluent farmers who have the better resource base—including education and social capital—and higher risk-bearing capacity. The latter is an important factor: due to low farm-gate prices for crops, the application of expensive modern inputs is risky and not always lucrative, especially for the poorest farmers. In the cotton and tobacco sectors, for example, contract farming has proved profitable for those farmers who have been able to plant on a relatively large scale, while those with small areas under cultivation have actually incurred losses (Benfica et al. 2005). Contract farming tends to operate most efficiently in relatively concentrated high-potential agricultural areas, and thus it tends to increase rather than reduce regional and sub-regional inequality in terms of service accessibility.

The impact of contract farming on the poorest groups and on women in particular is, therefore, at best indirect. Nevertheless, in the context of the widespread rural poverty, improving the income-generating capacity of even the middle strata could make a major difference for reducing poverty.

6.4 WAGE LABOUR

It has been argued that in the context of a high incidence of poverty, decently remunerated rural wage-earning opportunities can have a dramatic effect on reducing poverty, especially among poor women, such as widows, without access to sufficient land. In the classical growth model, the increase in wage labour (either farm or non-farm) is the main factor that makes growth pro-poor and there are some indications that such growth has taken place in a few African countries that have managed to gain access to international food markets, e.g., Kenya in European horticulture markets.

In Mozambique, however, agricultural wage labour currently represents a decreasing source of income for the rural poor. While the share of wage labour in total rural household income increased rapidly from two per cent in 1995-96 to nine per cent in 2001-02, the increase took place in the highest income quintile while its share among the poorest groups actually decreased. Even though seasonal agricultural wage labour is one component (along with much more important natural resource extraction) of a typical diversified livelihood strategy of the poor, its role remains secondary (Boughton et al. 2006). Pro-poor policies and institutional arrangements must, therefore, be implemented in order to link smallholder development to the expanding large commercial farming sector and to ensure a substantial employment effect for the rural poor.

6.5 MARKETING FOOD CROPS

Among the rural poor, agricultural production is concentrated in traditional food crops. According to the agricultural sample survey, crop production contributed 80 per cent of income for the poorest 60 per cent of rural households in 2001-02 (Boughton et al. 2006). Maize is particularly important for smallholder households in the central and northern inland regions, where it occupies more than one half of cultivated land. Even though less than 20 per cent of maize is sold on the market according to official statistics, informal trade with neighbouring countries is actually an important source of revenue for smallholders, especially in the border districts.

In Zambézia and southern Nampula, smallholders produce rice as a cash crop by rain-fed methods on low-lying land. Smallholders also grow fruit and cultivate various horticultural crops using traditional techniques, partly for cash and partly to complement their own food supply. Some of the products have already found markets in the neighbouring countries, notably South Africa and Malawi.

In the food crop sector, where the national research effort on seeds and pest control has been relatively strong, active dissemination of higher-yielding, drought-tolerant and disease-resistant crop varieties could make a major impact on food security and cash-earning opportunities for the majority of semi-subsistence smallholders, even in the context of otherwise weak service provision.

7 AID, TRADE AND GROWTH IN MOZAMBIQUE

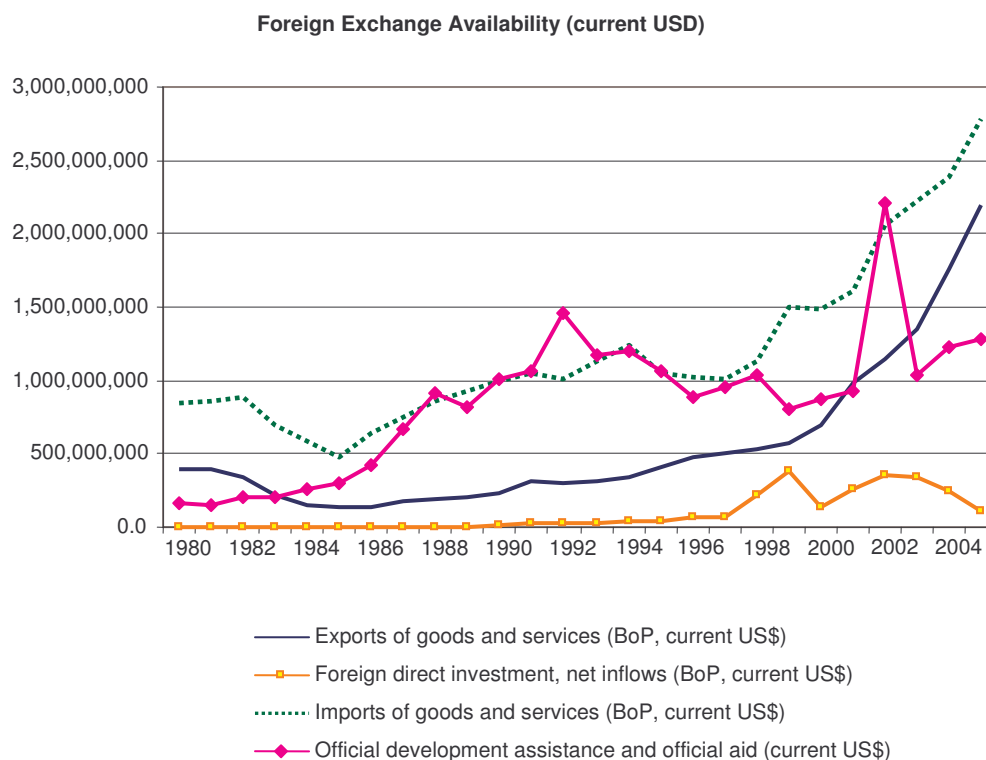
External aid provides a major part of all foreign exchange available to Mozambique—over 65 per cent between 1986 and 1995 (Figure 3). Total official development assistance (ODA) was larger than export revenues over the whole period 1984-2000.

Since then, exports have accelerated extremely rapidly through mega-project production, while aid also increased. At the same time, imports have also increased rapidly as a result of the mega-project construction and operation. Thus the export boom so far has not contributed as much to the availability of foreign exchange for development expenditures as the growth of export revenues indicates. However, by 2005 export revenues from mega-projects had increased to more than three times the value of related imports; this balance is projected to remain at least as large. Meanwhile, FDI has also become an important source of foreign exchange over the last 10 years or so, mainly related to the construction of mega-projects (World Bank 2001, 2006b, 2007; Government of Mozambique 2007).

Total export value has in recent years been consistently higher than ODA, except for 2002, when massive debt relief in the form of payments to foreign creditors was accounted for as an extraordinary increase of aid to Mozambique. Although, consequently, the debt relief did not increase the immediate availability of foreign exchange for development expenditures, it did so substantially in the following years, when a large part of gross aid no longer had to be used for debt service payments.

FIGURE 3

Foreign Exchange Available to Mozambique, 1980-2005¹⁴



Source: World Bank 2006b, 2007.

The fast increase of aid after 1985 followed the structural adjustment policy agreement between the government and the Bretton Woods institutions. The aid volume peaked briefly after the end of the war in 1992, and then receded somewhat during the rest of the 1990s, while maintaining levels well above those before 1985.

This was a period of international aid fatigue and decreasing aid. ODA to sub-Saharan Africa started to fall in the early 1990s, decreasing from US\$ 16,900 million in 1994 to US\$ 11,600 million in 1999. In the ten-year period after 1987, 12 of the 19 main bilateral donors providing aid to the region reduced their aid, including France—by far the largest provider of aid to sub-Saharan Africa—the European Commission, Belgium and the Nordic countries; these major donors all cut their aid to the region by ten per cent or more. This trend was reversed in 2000, with ODA to the region reaching a new high point of US\$ 17,700 million in 2002. The increase is primarily driven by France and the USA (Addison et al. 2005). Aid to Mozambique also increased sharply from 2001, as indicated in Figure 3.

Gross aid (including debt relief grants) to Mozambique from the DAC member countries averaged over 40 per cent of GNI in per capita terms after 1985, with a peak of 93 per cent in 1992. In the late 1980s over 50 per cent of gross aid was being used to pay debt obligations. As a result of the HIPC initiatives and Paris Club programmes since the late 1990s, net external funding effectively available to support government expenditure has increased substantially from an average of US\$ 555 million during the 1980s to US\$ 825 million in the 2000-2004 period.

Since 1985, such external financing has been about equivalent in value to overall government investment, and approximately to one half of total government expenditure. As these figures exclude off-budget expenditures financed from external sources, Arndt et al. (2007) have estimated that the total value of external finance, including off-budget payments, corresponds to around 55-60 per cent of total government expenditures. According to government data, net ODA has amounted to around 31 per cent of GNI in the post-war period.

There has been a major change in the type of assistance to Mozambique. During the period of armed conflict, the majority of aid went to humanitarian relief and other kinds of direct impact aid, such as various forms of balance of payment support (commodity aid, import support, debt relief and budget support). Since the 1992 aid peak there has been a shift into slower-disbursing project and programme funding with a more long-term impact, such as assistance to social-sector development. At the same time, loans have largely been replaced by grant-based financing, which by 2004 comprised 71 per cent of aid flows compared to less than 20 per cent in the early 1980s. An increasing proportion of aid (about 40 per cent of gross aid in the government budget) has more recently been provided in the form of direct budget support or sector-wide programme support instead of being tied to specific projects.

7.1 THE RELATIONSHIP BETWEEN AID AND ECONOMIC GROWTH

Sub-Saharan Africa receives currently a historically unprecedented volume of aid, which is even likely to increase in the future. Is that likely to promote or restrain economic growth? That would depend on a number of factors, such as the purposes of aid in each case, what kind of aid is actually provided, how predictable and consistent the aid flows are, how effectively aid from a large number of donor agencies is coordinated and harmonised with recipient

country plans and administrative structures, and how conducive recipient policies and institutions are to enhancing the growth impact of aid.

It is important to take into consideration the fact that economic growth is sometimes less important than other concerns (e.g., humanitarian relief, social protection, environmental conservation and donors' commercial and political motives) as the most important objective of aid. Yet, the single most common result of recent empirical aid-growth studies is that aid has a positive impact on per capita growth. At the same time, aid is by no means a panacea for growth and poverty reduction (Tarp 2006).

Critical aid analysts tend to emphasise the potential negative economic and institutional impacts of increasing volumes of aid and have suggested that the proposed increase might be better spent on other types of assistance than traditional bilateral aid (Moss et al. 2006).

The basic critical macroeconomic argument is that large volumes of aid can affect the real exchange rate and thus undermine the competitiveness of the export sector, and indirectly economic growth. This effect is known as the 'Dutch disease'. However, there has been scant evidence of strong negative effects on recipient economies other than an expected short-run real exchange rate adjustment to accommodate the higher demand for national currency. In the medium-term, aid is likely to impact on the supply side through an improvement in productivity and output capacity, hence stimulating economic growth and employment (Adam and Bevan 2005).

Furthermore, central banks have several policy tools that can be employed in order to manage exchange rate appreciations and mitigate the pernicious effects on competitiveness. Nevertheless, the management of the real exchange rate is arguably rendered more difficult by ODA volatility, which can cause serious inefficiencies. This is because aid is often less predictable than domestic fiscal revenues, and its volatility lessens the positive effects of aid on recipients (Addison et al. 2005; Lensink and Morrissey 2000). Aid volatility thus contributes to macroeconomic instability, which complicates public policy making, and directs public spending toward consumption rather than investment (Aiyar et al. 2005; Foster and Killick 2006; Moss et al. 2006).

However, various studies show that aid has contributed positively to growth in sub-Saharan Africa due to its positive effect on the volume of investment and related income and employment benefits. In the case of Mozambique, increased ODA appears to have had a positive effect on growth while it has not appreciated the real exchange rate. The criticism that aid generates 'Dutch disease' and leads to structural distortions seems, therefore, to be unfounded in the case of Mozambique, at least up until now.

Some observers even see the Mozambican experience as a shift from a vicious to a virtuous cycle, marked by the end of armed conflict and the emergence of sustained growth supported by external aid. According to this view, sustained aid at high level was crucial for managing the transition process: establishing peace smoothly, managing the challenge of post-war stabilisation, and carrying out widespread reconstruction (Arndt et al. 2007).

It is, however, important to note that upsurges of ODA can be a major source of growth volatility. Externally financed investments in public and social infrastructure tend to generate fiscal pressures. In Mozambique, the rate of return from such investment was particularly high in the early post-war period due to the very low base from which they were made. Nevertheless, problems in meeting recurrent costs without prejudicing the quality of the services offered

make sustaining such high rates in the future unlikely. As constraints in absorptive capacity reduce marginal returns to increases in public investment, the feared structural distortions may appear in the future (Arndt et al. 2007; cf. Foster and Killick 2006). It is thus important to ensure that aid-funded investments are well targeted to sectors that are able to boost the productive capacity of the country (e.g., infrastructure and education).

7.2 THE IMPACT OF ODA ON PUBLIC INSTITUTIONS

According to recent studies, out of 22 low income countries with ODA inflows equivalent to at least one half of total government expenditure, 16 are in sub-Saharan Africa. Out of 12 poor countries where the ratio of ODA to government expenditure is 75 per cent or more, 10 are African. For example, in Malawi and Zambia aid has funded more than 40 per cent of government expenditure for nearly 20 years (Bräutigam and Knack 2004; Moss et al. 2006).

Statistical data show that higher aid levels are associated with lower tax effort. In the mid 1970s tax revenue in both middle income and low income countries was about 17 per cent of GDP, but by the late 1990s it had increased to 21 per cent in the middle income countries while in the low income countries it had fallen to 14 per cent. The latter receive much higher levels of ODA (Bräutigam and Knack 2004). However, one needs to take into account the impact of IFI advice (i.e., conditionality) during that period on trade reforms (lower trade taxes) and downsizing of government and the public sector. In the case of Mozambique, the level of tax revenue has stagnated at the level of 12 per cent of GDP.

The basic critical argument is that a large and sustained volume of aid tends to focus accountability on the relationship between the executive branch of government and aid donors rather than between state and society, thus weakening the role of domestic political institutions in governance. Various studies show that countries that rely on a substantial proportion of revenue from natural resources, such as oil, will tend to be less democratic and have less effective institutional mechanisms for providing accountability.

Aid can have many of the same dysfunctional effects as natural resources since in both cases governing elites are insulated from the need to ensure the support of citizens and the assent of their legislatures in order to raise revenues. According to this argument, reliance on citizens for raising public revenues, as opposed to income via natural resource extraction or ODA, is an essential ingredient to establishing accountability between the state and society (Moss et al. 2006). However, the tax base in poor developing countries is relatively small, since a large share of the population live from subsistence farming.

In Mozambique, foreign aid currently finances approximately 50 per cent of the government budget (AfDB/OECD 2006). Combined with very high reliance on FDI in the private sector, the high level of aid dependence has facilitated the persistence of a highly centralised development approach. Following in the footsteps of the centralised colonial administration and the subsequent Marxist-Leninist party/state apparatus, the government continues to operate through mega-projects put together by top political leadership and respective donors and/or private investors with very little public consultation or transparency.

The post-war period has been characterised by a number of centrally initiated large projects in agriculture and tourism, including failures such as the Mozagrius project in Niassa Province, the Blanchard project in Maputo Province, and arguably the cotton joint venture companies in Nampula Province. The current approach of Spatial Development Initiatives and

related industrial mega-projects seem to follow the same approach, even though their economic sustainability (at least for the foreign owners) is likely to be better. According to Söderbaum and Taylor (2001, p. 687), "what is emerging is not a partnership between state and capital in the service of public good, but rather a deal between political elite and transnational capital, supported by the IFIs and the donor community".

7.3 TRADE CAPACITY BUILDING AND FOREIGN AID

According to OECD (2003) guidelines, trade capacity building seeks to enhance the ability of policymakers, enterprises and civil society in developing countries to (i) collaborate in formulating and implementing a trade development strategy embedded in a broader national development strategy; (ii) increase the volume and value-added of exports, diversify export products and markets and increase foreign investment to generate jobs and exports, and (iii) participate in, and benefit from, the institutions, negotiations and processes that shape national trade policy and the rules and practices of international commerce.

While trade capacity building is typically presented as a technical exercise, it should be noted that especially the first and third of the above activity areas are essentially political processes that should be driven by developing country institutions. The OECD guidelines emphasise that ensuring local ownership of trade and development strategies is a key objective of trade capacity building. The role of technical assistance from donor organisations should be limited to strengthening domestic policy analysis and formulation, and elaborating the technical rules and regulations needed to operationalise the trade policy choices made by domestic political authorities. Instead of imposing selected trade policies as the only possible or rational options available for developing countries, trade capacity building should encourage domestic political debate over trade issues.

The type of investments in institution building required for full adherence to WTO agreements on, say, customs valuation or intellectual property rights may not be the first order of business for low income countries with more urgent needs. Since human resources, administrative capacity, and political capital are scarce, especially in low-income countries, policy makers need to have a good sense of priorities. An implication of this line of reasoning is that we should think of the trade regime and WTO rules as being at the service of developing countries' institutional needs, and not vice versa (Rodrik 2002).

In the case of sub-Saharan Africa, it is not only its limited negotiation capacity that has prevented gains from multilateral trade talks from materialising, but perhaps rather the comparatively small size of African economies that leaves them with little say at the negotiation table. In Mozambique, institutional capacity building for trade should arguably focus on addressing the numerous supply constraints that the economy faces.

Mozambique is well endowed with resources and geographically positioned to export agricultural products to surrounding markets. This comparative advantage should be used effectively to both guarantee national-level food security and develop increasingly competitive commercial agricultural export capacity.

Production and trade strategies (contract farming or wage-labour based production for export markets, independent production of food crops for local markets) are by nature complementary. In the medium term southern African and neighbouring regional markets

and related production linkages can serve as a springboard for integration in global supply chains of high-value agro-industrial products, which are likely to provide the most promising means to access the lucrative global markets in the long term.

Significant advances in packaging and transport technology over the past two decades have opened up new opportunities for agricultural trade, with fresh food products becoming a significant part of the global agro-food trade (OECD 2003). At the same time, however, the new agro-food chains are characterised by the dominance of strict process-based quality conventions, which transfer the quality control function upstream to the producing company or exporting country government. Increasing attention must thus be paid to different kinds of non-tariff barriers to trade, such as sanitary and phytosanitary (SPS) regulations in the importing countries.

For a country such as Mozambique, which suffers from a serious lack of both human and social capital, increasing demands with respect to quality control systems operated by the public sector and covering most highly dispersed smallholder producers can quickly become an insurmountable barrier. The problem becomes even more obvious if we include the provision of other services that are crucial for creating globally competitive agricultural production capacity, such as agricultural research, extension and marketing services. These constitute also some of the supply side constraints that institutional capacity building for trade should address.

8 CONCLUSION

Mozambique has experienced more than a decade of sustained economic growth. This growth is based on two sectors, agriculture and industry. Concurrently, absolute poverty has fallen rapidly.

The main factor in the reduction of poverty since the mid 1990s has been increased production in agriculture, which is overwhelmingly the main source of livelihood in the country. However, this growth represents a 'bounce-back' from the catastrophic war years to previous levels of agricultural production without any substantial improvement in productivity, which remains very low even when compared regionally.

Growth in industrial production has been the main driving force behind Mozambique's rapidly growing exports. Based on a few mega-projects, this growth has, however, created few jobs while its contribution to public revenue has been marginal when compared to the value of production. The new FDI-financed industries rely on imported inputs, and are closely linked to the South African mining and energy complex. Due to their enclave character, the spillover effect in terms of technology transfer or skills development has been minimal.

While increased agricultural production in the centre and north has helped to even out inter-regional disparities, intra-regional inequality has increased. The changing regional pattern of poverty seems counter-intuitive given the distribution of investment: poverty has increased in the south, where most of the new investments were made. This paradox is explained by the current pattern of economic growth and the changing role of Mozambique in the regional economy. The loss of jobs in transport and migrant labour in South Africa has not been compensated by job creation in the new industries, and this has disturbed the traditional basis of livelihoods in the south.

The Mozambican economy suffers from three crucial handicaps: (i) Both domestic savings and national investment are very low—because financial institutions are inefficient; (ii) Market oriented agricultural production is hampered by sparse population and poor infrastructure; while monopsonistic markets and high transport costs make inputs expensive and keep producer prices low, discouraging investment in agriculture; (iii) The level of human development is extremely low despite considerable improvements after independence and especially since 1994. Combined with a drastic lack of social capital, the competitiveness of export production outside of the capital-intensive enclave sectors remains very low.

External aid provides a major part of all foreign exchange available to Mozambique, and it has thus far had a positive effect on growth without a major negative impact on the real exchange rate. As externally financed investments in public and social infrastructure tend to generate fiscal pressures, such as on recurrent expenditures, it is important to ensure that aid-funded investments are targeted to sectors that are able to boost productive capacity.

Commercial agriculture and agroprocessing are widely identified as the sectors where Mozambique has a comparative advantage in global markets. Investment of aid resources in services that are crucial for creating globally competitive agricultural production capacity, such as quality control systems, agricultural research, extension and marketing, is, therefore, essential. Other key sectors are transport and communications infrastructure, basic health care and primary education services in rural areas, which can reduce poverty by promoting sustainable livelihoods and enhancing labour productivity.

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NOTES

1. Republic of Mozambique 2001: Action plan for the reduction of absolute poverty, 2001-2005 (PARPA).
2. The concept of mega-project refers to large capital intensive projects, operating typically in the minerals and energy sector and financed almost entirely by FDI. Currently there are three operational mega-projects, namely the Mozal aluminium smelter in Maputo Province, the Cabora Bassa hydroelectric plant in Tete Province, and the Sasol gas project, which extracts natural gas in Inhambane Province and exports it to South Africa via pipeline. Two mining projects (mineral sands extraction) are currently under construction in Nampula and Gaza provinces.
3. The poverty analysis is based on two nationally representative surveys (1996-97 and 2002-03) containing detailed information on expenditure for 8,274 and 8,700 households, respectively. A cost of basic needs approach was employed to construct time- and region-specific poverty lines for each survey, with the same spatial regions used in both studies. A change in the definition of urban and rural areas between the two surveys, however, makes interpretation of the rural-urban aspect somewhat more complicated. The poverty gap index measures the average distance (in percentage points) of poor households from the poverty line (Datt et al. 1998; Massingarela et al. 2004).
4. The main problems relate to Sofala and Cabo Delgado. It is generally agreed that the 1996-97 data from Sofala reflect the effects of the unusually destructive seasonal floods that occurred during those years, and are thus not representative of the overall situation in the province. Cabo Delgado, on the other hand, has suffered from serious sampling problems in both surveys (Massingarela et al. 2004). For some of the intricate conceptual and practical problems involved, see Tarp et al. 2002.
5. This measure of the magnitude of poverty considers both the number of poor people, and how poor they are. The Poverty Gap Index is the combined measurement of incidence of poverty and depth of poverty.
6. While caution is needed when using development indicators (notably GDP per capita) calculated at the level of sub-national units such as provinces (Rolim 2002), they do provide indicative figures on general trends.
7. Sector-wide support is based on Education Sector Support Plans (1999-2003 and 2005-2009). A joint Education Sector Support Fund was established in 2002 to coordinate donor funding.
8. Despite recent growth, in 2004 only about five per cent of adults were educated above primary school level (Arndt et al. 2007).
9. Support is based on a Health Sector Strategic Plan (2001-2005). A Health Sector Support Fund has been established to coordinate donor funding.
10. While an increase in inequality in the main urban centres is common in the process of economic transition, it does not automatically cause an increase in poverty. For example, in Dar es Salaam (Tanzania) recent rapid growth has resulted in a larger than average reduction in the incidence of poverty (United Republic of Tanzania 2005).
11. While the number of legal migrant workers outside the MEC is insignificant (less than two per cent), most of the illegal migrant workers are found outside of the MEC, mainly in agriculture (Castel-Branco 2002).
12. Similar conclusions have been reached on the basis of East Asian data, which indicate that reliance on FDI has an adverse effect on income distribution (You 1998).
13. See, for example, Republic of Mozambique 2006; World Bank 2006a. Labour input in agriculture increased despite virtual stagnation in the total number of people active in agriculture, forestry and fisheries. This was probably due to more intensive use of available labour.
14. Figures for 2005 are from the World Development Indicators (WDI) database, April 2007, while previous data are those published in WDI 2006.



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