EXPLORING INVESTMENT POTENTIALS IN ANGOLA & MOZAMBIQUE

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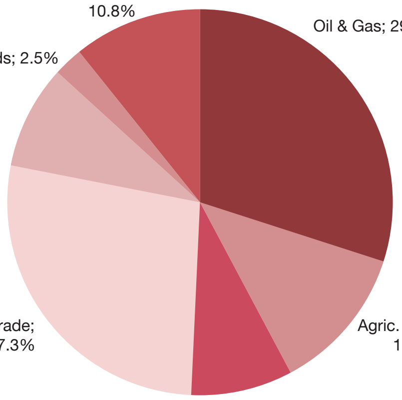
Insight into Angola's Prospects

The sharp drop in oil prices since mid-2014 has had a major impact on the Angolan economy. Real GDP growth is projected to have slowed to 2.9% in 2015 from 4.8% in the previous year. This is significantly lower than the average annual growth rate of 10.2% recorded during the decade of 2004-14 that made Angola one of the fastest growing economies in the world. The current slowdown in economic activity is attributable to a hard landing in the non-oil sector, which recorded the lowest growth rate since the end of the civil war (1.5% vs. 8.2% in 2014). The oil sector is projected to have expanded 6.3% (from a contraction of 2.6% in 2014). Overall, lower private consumption and public spending levels in an existing backdrop of more limited availability of foreign exchange in the local economy all led to a significant adjustment in the industry, construction and services sectors last year.

GDP Structure (2015E)

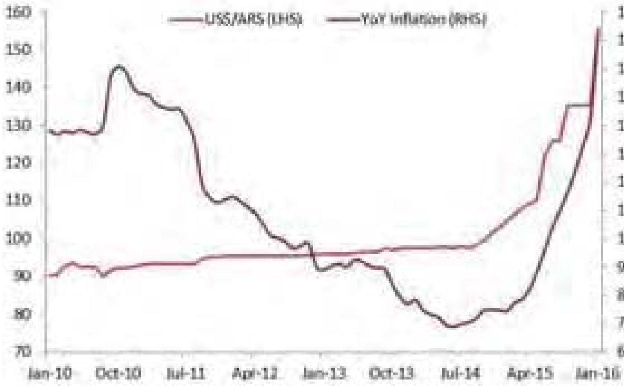


Source: Angolan authorities.

The Angolan authorities currently forecast a 4% growth rate for 2016. The oil sector is expected to advance 4.5% while the non-oil sector is projected to pick-up to 3.8%. Our real GDP growth assumption of 3.2% for 2016 is more conservative than the government's forecast though. We believe further downside risks could emerge and continue to weigh on economic activity, namely persistently low oil prices and a slowdown in some of Angola's main trading partners, particularly China.

Meanwhile, inflation has climbed back to double-digits in recent months, reflecting in large part the impact of the depreciation of the kwanza, which the BNA is trying to contain through tighter monetary policy measures. The central bank has used international reserves to defend the local currency and limit inflationary pressures, but has not prevented the kwanza from depreciating nearly 31% against the dollar in 2015 and a further 20% so far this year. It is worth noting that annual inflation had kept a downward trend in recent years and stayed in single-digits from mid-2012 until July 2015. However, it has reached 20.26% in February of this year, its highest level recorded since January 2006. This recently led the Angolan authorities to revise upwards their 2016 inflation forecast to 15.8% from 11% in the 2016 budget.

Exchange Rate vs. Inflation
Source: BNA.



International Reserves vs. Exchange Rate
Source: BNA.

On the fiscal front, the government is aware that in the current low oil price environment it remains crucial to rationalize public expenditure levels and imperative to accelerate the efforts to increase non-oil related revenues. This starts with reducing the public wage bill to levels more consistent with a new revenue reality. Another area is the reform of fuel subsidies, which started in September 2014. The lower international oil prices together with the several domestic fuel price increases since the reform began have reportedly led to the elimination of subsidies on most fuels while the ones still subsidized are done at much lower levels than in the recent past. The plan is to reportedly eliminate fuel subsidies completely by 2020. At the same time, the local authorities aim to improve social assistance to the poor in order to lower the impact of the gradual elimination of fuel subsidies. Moreover, public investment projects need to be better prioritized and their execution more carefully monitored.

There are several sectors that are likely to be on top of the local authorities' agenda going forward. The aim is to gradually diversify the economy away from the oil sector and reduce import levels. These are sectors that are likely to support real GDP growth in the future. However, the impact from these increased diversification efforts is going to take time to materialize.

First, agriculture is the second non-oil production sector and has resources that can make Angola one of the richest agricultural countries in Africa. Less than 10% of arable land is still exploited and very little of irrigation land is developed. Some of the country's most successful crops include coffee, bananas, timber, tobacco and sunflowers. Angola's climate is diverse and provides for the growth of both tropical and semi-tropical crops. The fishing sector has recently shown improvements but its full potential has yet to be realized.

Second, diamonds represent the lion's share of Angola's mining sector. The country also remains an extremely attractive target for the discovery and development of world class ore deposits such as iron, gold, copper, phosphate and even zinc. The government has created a new legislation for mining exploration and is assessing the best way possible to attract new investors into the sector.

Third, the post-war reconstruction boom and resettlement of displaced persons has led to high growth rates in the construction sector. Although the appetite for housing and large scale projects has recently slowed (in most part due to the fall in oil prices), it is worth noting that the expected strong population growth and increasing urbanization levels in the country should continue to support the expansion of the construction sector.

Fourth, the government remains committed to improving the country's energy facilities, namely hydroelectric, in order to improve and expand its power generating capacity and network grid. Solar and wind power energies are also at an early stage of development.

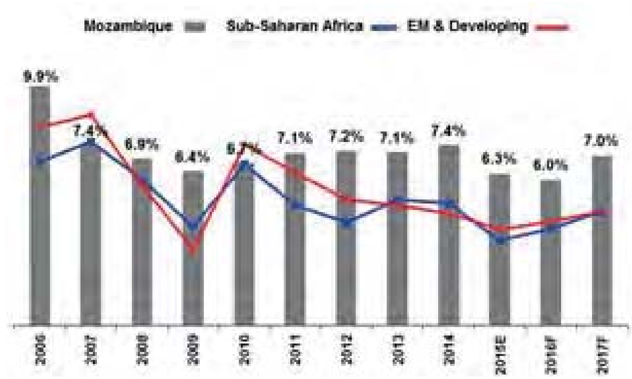
Other areas of interest are likely to come in the manufacturing, retail and services sectors such as telecoms and banking where Angola still remains underdeveloped. And finally, it is worth highlighting the potential of the country's tourism sector. The business segment is currently the main segment that visits Angola. However, there is still a long way to attract other types of tourists. Problems related to bureaucracy (visa requirements), lack of infrastructure, a weak focus on the visitor and no institutional marketing are critical for the development of the tourism sector of the country.

Mozambique's long-term prospects remain upbeat

Mozambique's latest GDP figures showed that economic activity in the country slowed to 5.6% YoY in the last three months of 2015 and that real GDP growth for the year stood at 6.3%, below the 7.4% in 2014 (which is near the average growth of the last decade). This slowdown was mainly due to the sharp drop in commodity prices, namely aluminium and coal (the country's main exports) and lower foreign direct investment (FDI) inflows. However, real GDP growth remained well ahead of the IMF's latest 3.5% average growth projection for Sub-Saharan Africa in 2015.

Real GDP Growth

Sources: Mozambican authorities, IMF and Eaglestone Securities.

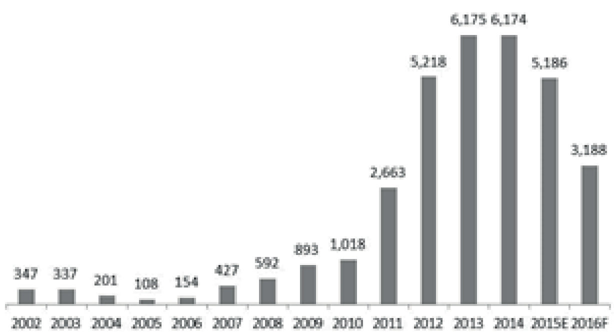


Inflation also picked up recently after recording a constant downward trend in recent years. Prices are expected to remain under pressure chiefly due to the sharp depreciation of the metical against other currencies like the US dollar and South African rand. Inflation is more than likely to remain above the official target of 5.6% this year.

The extractive industry has been responsible for a significant part of the FDI inflows in recent years (other inflows have gone to the transport, storage and communication sectors). Large investments have initially been made in the coal sector, but more recently attentions have turned to the vast natural gas reserves in the Rovuma basin, in the north of the country. This has boosted other sectors such as construction, utilities and real estate. Mozambique is nowadays a more diversified economy but remains highly dependent on the agriculture sector, which still accounts for nearly a third of its GDP.

Net Foreign Direct Investment (US$ million)

Sources: Mozambican authorities and IMF



Despite the recent slowdown in economic activity, the country's long-term prospects remain upbeat as a result of the natural gas projects expected to come on stream later this decade. Local officials reportedly expect more than US$ 30 billion will be invested initially in the sector, with the first exports of LNG due to start no sooner than in 2020. This is huge for a country whose GDP currently stands at more than half of that amount.

Real GDP growth could pick-up once again to nearly 8% in 2017-20 on the back of the anticipated investments in natural gas. The country is also expected to benefit from international loans like the ones recently agreed with the IMF (US$ 286 million over an 18-month period) to help bring some stability to the economy following the sharp drop in commodity prices and the European Union (US$ 740 million over the next five years) to support development projects.

Economic growth should also remain supported by the rehabilitation of the country's transport infrastructures (roads, railways, ports and airports), which is a strategic priority for the local authorities. The development of hinterland corridors also serving neighbouring countries is critical for the future of Mozambique, providing easy access to the sea for mineral projects, agricultural projects and industry.

Other areas of interest include agriculture and fisheries. Mozambique provides strong potential in a variety of crops, namely for the local market and export of cereals, fruits, flowers and vegetables. The Zambezi valley is a prime area for agriculture. Moreover, the country's vast coastline is very rich, as Mozambique currently exports prawns and the sector is being developed through local and foreign investors.

Meanwhile, the potential for hydroelectric power plants is considerable and the need for a reliable power transmission infrastructure urges. Mozambique also has the potential to explore renewable energy (wind, solar and photovoltaic). It is a capital intensive sector, but with several investment opportunities.

The telecoms market is also underdeveloped with relatively low penetration levels while a significant part of the local population does not hold a bank account. Telecoms and banking are two sectors where foreign players remain quite interested and hold strategic positions.

Finally, we also highlight the strong potential in terms of tourism. The ongoing investments in infrastructure development will allow access to new locations with touristic potential, also benefiting from the country's large coastline and natural parks.