

COUNTRY REVIEW

Angola



5 August 2010

ANALYST: Andrew Atkinson

EULER HERMES COUNTRY RISK GRADE: C

Country Risk Grades are on a scale of AA, A, BB, B, C, D
where AA is the lowest and D the highest risk.

Strengths

- Legislative elections in September 2008, although not without logistical problems, were conducted relatively peacefully and the results accepted by opposition forces, thereby assisting the country's progress in entrenching political stability
- Despite bordering DR Congo, there are no significant threats to security from external forces
- The country rivals Nigeria as the leading Sub-Saharan African oil producer (the position depends on uncertainties relating to Nigerian output because of production disruptions), with reserves calculated to provide almost 21 years of further output at current rates of extraction
- The status of the country's oil sector was enhanced by its membership (as of January 2007) of OPEC and Angola chaired the organisation in 2009
- In addition to hydrocarbons, Angola possesses significant natural resources through its mining (particularly diamonds) and agricultural sectors

Weaknesses

- An estimated 70% of the population survives on less than USD2 per day and food aid from UN and NGO sources will continue to be required
- Ongoing process of re-housing and employing four million displaced citizens following the civil war
- Rebuilding and reconstruction of economic and social communities requires considerable resources
- With crude oil accounting for 96% of export revenues, the economy is susceptible to volatility in global markets and to potential collapse of oil prices
- Corruption, particularly in relation to the lack of transparency in oil accounts, has limited local confidence in the country's leadership and prevented full IFI support and investment from the western world in the non-oil sectors
- Provision of macro-economic and other data is generally poor

Key Risks

- Collapse of global energy demand and international oil prices

Country Risk Assessment

Ratings	Angola		Median		Peers	
	Latest	Previous	Grade D	Grade C	Niger	Turkey
Systemic Political Risk:	P3-	P3-	P3-	P2-	P4	P3-
Systemic Economic Risk:	E5	E6	E6	E5	E6	E5
ME rating:	ME4	ME4	ME6	ME5	ME6	ME5
<i>Structure</i>	5.7	6.0	6.0	5.9	6.0	4.0
<i>Policy</i>	5.2	5.2	5.6	5.2	6.0	5.6
<i>Solvency</i>	2.0	3.3	4.3	3.0	4.2	4.3
<i>External Liquidity</i>	2.8	1.9	4.3	4.8	4.8	6.0
SBE rating:	SBE5	SBE6	SBE6	SBE4	SBE6	SBE3
COUNTRY GRADE:	C	D	D	C	D	C

Nomenclature:

Political Risk Ratings are on a scale of P1 (lowest risk), P2+, P2-, P3+, P3-, P4 (highest risk).

Economic Risk Ratings are on a scale of E1 (lowest risk), E2, E3, E4, E5, E6 (highest risk).

ME (Macro-Economic) ratings are on a scale of ME1 (lowest risk), ME2, ME3, ME4, ME5, ME6 (highest risk).

The constituent parts of the ME rating are on a scale of 1.0 (best) to 6.0 (worst).

SBE (Structural Business Environment) ratings are on a scale of SBE1 (best), SBE2, SBE3, SBE4, SBE5, SBE6 (worst).

Country Grades are on a scale of AA, A, BB, B, C, D where AA is the lowest and D the highest country risk.

Source: Euler Hermes Country Risk Unit

ECONOMIC STRUCTURE

Country Profile	
Capital city:	Luanda
Population:	18.5 mn (2009)
GDP:	USD 88071 mn (2009)
Currency:	Kwanza (AOA)
Form of state:	Republic
Head of government:	President José Eduardo dos Santos
Next elections:	Legislative by September 2012; presidential (abolished)

Major Industries (% of GDP at market prices, 2009e)	Global Assumptions	2010f	2011f	
Agriculture	12.0%	World GDP grth (% yr/yr)	3.3	2.9
Oil & gas sector	40.0%	Inflation (% , average)	1.2	1.4
Construction	8.0%	Dated Brent oil (USD/b)	75.0	70.0
Manufacturing	7.0%			
Commerce	23.0%			

Main Exports (% of total, 2009e)	Main Imports (% of total, 2009e)		
Crude oil	96.0%	Machinery	18.0%
Diamonds	2.0%	Vehicles	15.0%
		Iron & steel products	11.0%
Lead Export Markets (% of total exports, 2009)	Lead Import Markets (% of total imports, 2009)		
China	34.0%	Portugal	18.0%
US	25.0%	China	17.0%
France	8.0%	Brazil	11.0%
Brazil	6.0%	US	8.0%

Basic indicators

Selected economic indicators	2007	2008	2009	2010f	2011f
Nominal GDP (USD mn)	59,263	84,945	88,072	93,504	114,719
Population (mn)	17.56	18.02	18.50	18.98	19.46
GDP per capita (USD)	3,375	4,714	4,761	4,926	5,897
Real GDP growth (% yr/yr)	20.3	13.0	-2.0	7.5	6.5
Inflation (% , average)	12.3	12.4	13.8	13.0	11.5
Fiscal balance (% of GDP)	9.9	9.7	0.7	7.0	5.8
Current account balance (% of GDP)	17.2	7.5	-1.0	4.3	3.9
External debt/GDP (%)	19.4	17.8	18.2	19.6	17.0
External debt/Exports of goods & services (%)	25.4	23.4	39.1	31.6	32.5
Debt-service ratio (%)	9.8	2.5	9.8	6.0	6.7
Foreign exchange reserves (USD mn)	11,197	17,869	13,238	16,250	17,000
Import cover (months)	3.8	3.7	3.8	3.7	3.7
Exchange rate assumption, AOA:USD (av)	76.7	75.0	79.3	92.0	90.0
f: CRU central forecast					

Sources: Central Bank, IMF, World Bank, Euler Hermes Country Risk Unit

Political Stability

The peace accord signed in 2002 following the violent death of Jonas Savimbi, the leader of União Nacional para a Independência Total de Angola (UNITA), brought to an end the **civil war that displaced approximately 4mn people and severely limited economic development for over 25 years**. Elections for the country's legislature—which had been delayed by the slow pace of voter registration and the poor physical infrastructure (roads and rail network) destroyed by civil war—were held in September 2008; the first national poll since 1992. The **ruling Movimento Popular de Libertação de Angola (MPLA) led by President dos Santos won the elections convincingly**—now commanding 191 seats out of 220 in the National Assembly—and the opposition UNITA leader Isaias Samakuva conceded defeat, following initial demands for a partial recount. The relative success of the elections has allowed a **period of political consolidation**. Under a **new constitution adopted by parliament in January 2010**, the president is no longer elected by a popular vote and is the leader of the party with most parliamentary seats. In addition, with the abolition of the post of premier, the government is now nominally headed by a vice-president. This new presidential-parliamentary system is comparable with that in South Africa. However, it can be seen as **further consolidating the position of dos Santos—re-elected as MPLA leader in December 2009—as the constitution effectively allows him to remain in power until 2022, at least**.

UNITA is now a formal political party and constitutes the main parliamentary opposition to the MPLA. Significantly, the civil war had begun by the time of independence and, accordingly, until 2002 the country had not experienced a period of stability in which to build political and civil institutions. Without a track record of governance, political and social advancement has been slow. It is likely that **the inner circle around the presidency will continue to mould the political system to suit its own ends and narrow-based vested interests**. Nevertheless, following the September 2008 elections, relative political stability has ensued and there has been consistent policymaking, permitting improvements in economic and social development.

Although Dos Santos has outwardly promoted economic reform—partly in an attempt to improve relations with the international investor community—there are **doubts about the commitment to liberalisation and openness**. The country has a **reputation for corruption** (see also Structural Business Environment) and Human Rights Watch Report alleged that between 1997 and 2002 an estimated USD4.22bn of USD17.8bn in oil revenues was "unaccounted". Improving the country's image will be difficult in the short term even if reforms are instituted, but it is essential if the government is to mobilise global support and promote inward investment in the non-oil sectors.

The **country is physically divided in two**, with the province of Cabinda separated by DR Congo's access point to the sea. **Political tensions are high in some areas of Cabinda** as separatist groups demand a greater share of the oil wealth (largely generated in Cabinda) and espouse independence claims. This situation is not as severe as that experienced by Nigeria in the Niger Delta state but, nevertheless, represents a considerable problem requiring mediation. The government claimed to have established a peace deal with Cabindan rebels in 2006 but separatist movements have continued to operate within the territory. The **government is highly unlikely to offer complete independence for the oil-rich province**. Accordingly, Cabinda will continue to represent a risk of potential instability.

Regional relations focus on commercial links with South Africa, which is increasing investments in the country. As a member of the Southern African Development Community (SADC), Angola's elections were monitored by officials from that grouping and were found to be broadly acceptable (and certainly more effective than recent experience in Kenya and Zimbabwe), although below international standards of transparency and fairness. **International relations will reflect an increasing link with China—that country accounts for over one-third of export revenues**—which is attempting to secure future energy supplies through operations in smaller oil producing countries. Until recently, Angola had not required a full IMF lending facility but it currently has a Stand-By Arrangement (SBA) in place until February 2012. The SBA improves the country's international image as it signifies a relatively increased openness in economic affairs.

Economic Stability

Angola is the 23rd largest country in the world (covering an area larger than South Africa) and it possesses **substantial natural assets, including oil and gas reserves, mining resources (particularly diamonds—around 10% of total world supply), hydroelectricity potential** (Norsk Hydro is investigating the feasibility of a dam that would enable electricity capacity to double) **and rich agricultural land**. However, the protracted civil war devastated the country's development, caused a

misdirection of financial and other resources and generated macro-economic instability. Although annual average per capita incomes are now over USD5,000 and the economy is thereby categorised as “upper middle income” under World Bank terminology, oil wealth has benefited only a relatively small elite and **poverty remains pervasive** in a population of around 19mn, with an estimated 70% living on less than USD2 per day.

Annual average real GDP growth was only 0.6% 1990-99 but **around 13% 2000-2008**, reflecting recovery from a very low base and expansion in the oil sector. **We forecast annual growth will be around 6-7% this year and in 2011, following outright contraction of around 2% in 2009.** However, economic growth will depend on the sustainability of the global recovery and its feed through to energy markets, particularly as Angola’s current round of hydrocarbon-related investment has probably peaked.

The economy is highly dependent on the **oil and gas sector, which accounts for around 40% of the country’s GDP and approximately 90% and 96% of government revenues and export earnings, respectively.** In 2007, the country became OPEC’s newest member and in 2009 it chaired that organisation. Angola is one of Sub-Saharan Africa’s leading oil producers and, given sustained disruptions to supply from Nigeria’s oilfields, can sometimes claim to be the region’s largest. According to OPEC data, Angola’s crude oil output was 1.77 million barrels per day (mbpd) in July 2010, compared with 0.75mbpd in 2000 and 1.79mbpd in 2009. Although Angola is not yet subject to official production ceiling allocations, **an OPEC quota of 1.95mbpd is under consideration and strict imposition of this could prevent output reaching recent medium-term projections of 2.1mbpd.** Angola is on schedule to become an exporter of liquefied natural gas (LNG) by early 2012. Most of the country’s oil fields are located offshore in the Cabinda area, part of the country physically separated from the rest of the country by a narrow strip of the Democratic Republic of Congo.

Transparency in the country’s fiscal accounts has been a recurring problem. Substantial budget deficits (averaging an annual 6% of GDP in 2000-04) reflected high defence expenditure and misappropriation through bogus or undisclosed accounts at that time. While some of these problems of recording financial flows have eased through more effective controls and a period of higher oil prices have turned the budget account to (large) **surplus in most years (averaging over 9% of GDP in 2005-08)**, fiscal reporting will continue to be a concern. For some time, Angola has raised finance through oil-backed facilities. The latter are not recommended by the IMF and are condemned by NGOs as they use expected future oil production earnings as a means of collateral for the loans and have provided problems of transparency.

In the early part of the last decade, rapid growth in money supply resulted in domestic price pressures, with annual inflation almost 100% in 2002-03. Stronger fiscal accounts from 2004 have helped moderate inflationary pressures (down to an average of 12-14% in 2007-09 and latest of 13.7% yr/yr in July 2010) and inward FX flows have supported the kwanza, thereby limiting the effects of imported inflationary pressures. Currency support has also derived from the official exchange rate policy, which permits central bank intervention in the foreign exchange market. **We forecast inflation to average 13% in 2010 and around 11.5% in 2011 and the kwanza to stabilise in H2 2010**, after a rapid depreciation in H1 2010, and in 2011.

A strong external position in most years since 2003 reflects a sustained period of high international oil prices combined with increased output from the energy sector. A significant boost to export receipts allowed the current account (in deficit prior to 2004) to register a surplus equivalent to over 17% and 7% of GDP in 2007 and 2008, respectively, although weaker oil prices through most of 2009 are likely to have resulted in a deficit in that year. With a recovery in benchmark oil prices to USD70-90/b, we **forecast the current account surplus will be equivalent to around 4% of GDP in 2010 and 2011.** There is some uncertainty relating to the outlook for the global economy and therefore for international commodity markets and Angola’s high dependence on the oil sector makes it **vulnerable to large falls in oil prices**, which would limit FX generation. **Import cover remains below 4%—comfortable but requiring build-up.** Our central forecast envisages further expansion in oil production—spurred by strong investment flows from Chinese interests, with Angola having overtaken Saudi Arabia as China’s principal source of crude oil—and, against this background, export revenues and the current account surplus are projected to remain positive.

In 2006, Angola settled long-standing disputes relating to overdue interest payments on loans with creditor countries under the Paris Club arrangement and this resulted in an improved relationship with the international financial community. Annual foreign debt servicing is now around 7% of FX earnings,

down from 10% in 2007, and other **foreign debt ratios are also manageable, although repayments of such obligations necessitate a redirection of financial resources away from productive use in the domestic economy.** Some additional foreign obligations have been taken on as part of oil production deals and are probably not included in the official figures. Other indicators of external sector activity have also improved, but **foreign exchange reserves currently provide 3-4 months of import cover and need to be rebuilt.** There is some doubt that all export revenues appear in officially published accounts and, in general, the **supply of macro-economic and other market data remains poor.**

Structural Business Environment

The **business environment is well below average** for the overall group of countries we assess. It remains below average for the Sub-Saharan African region and also for the upper-middle income group.

The UN's Human Development Index (HDI) ranks the country 143 out of 182 countries assessed, with a life expectancy at birth of less than 47 years, an adult literacy rate of 67% and only 49% of the population has access to a source of improved water supply. Overall, Angola is categorised by the HDI as "medium human development" and ranks below Yemen, Pakistan and Swaziland but above Nepal, Madagascar and Bangladesh. The latest World Bank's Doing Business report (2010) indicates that Angola ranks **among the three worst countries in the world in terms of enforcing contracts** and is one of the worst in terms of starting a business, registering property, closing a business and trading across borders, although **investor protection is generally above average.** Overall, Angola ranks 169 out of 183 countries analysed by the World Bank in terms of ease of doing business, above Equatorial Guinea, Cameroon and Benin but below Togo, Mauritania and Côte d'Ivoire.

A broad measure of the institutional environment in which businesses may or may not flourish is the Heritage Foundation's Index of Economic Freedom (IEF). Angola was not graded in the IEF 2000-05 and **the 2010 IEF classifies Angola as "repressed" (the worst category of the Index)** and ranks the country 154 out of 179 countries assessed, above Lesotho, Seychelles and Sierra Leone but below Equatorial Guinea, Central African Republic and Guyana. The IEF indicates that Angola scores relatively well in terms of fiscal freedom and moderately positively in relation to trade and size of government but in all other measurements it receives negative scores. In particular, the IEF notes that **inconsistent and confusing regulations limit private business investment and make entrepreneurial activity costly and difficult.**

Although the **banking sector is open to foreign investment,** state-owned organisations retain substantial influence and the regulatory environment remains weak and large areas of the country have rudimentary (at best) access to finance. It is estimated that **less than 10% of the population has a bank account.** Furthermore, government regulations are a severe hindrance to business and most independent assessors quote **corruption as a major deterrent to corporate involvement** with the country. In this respect, Transparency International's Corruption Perceptions Index for 2009 ranks Angola 162 out of 180 countries reviewed (along with Republic of Congo, Venezuela and Guinea-Bissau), above Burundi, Equatorial Guinea and Guinea but below Central African Republic, Laos and Tajikistan.

Andrew Atkinson

London: +44 (0)20 7860 2577

Charts

