

Grand corruption and the SDGs

Grand corruption is a serious threat to the 2030 Agenda for Sustainable Development. This series of case studies prepared by Transparency International illustrates how corrupt schemes across the globe have repeatedly implicated high-level officials and resulted in the gross misappropriation of public funds. As a direct result, education, health and other development priorities remain underfunded; the natural environment is ravaged; and fundamental human rights are violated. Those who suffer the consequences are ordinary citizens, and particularly those most left behind.

The visible costs of Mozambique's hidden debts scandal

1 NO
POVERTY



4 QUALITY
EDUCATION



At the start of the 2010s, there was real optimism that newly discovered resource wealth could help Mozambique overcome its acute development challenges. Much of this optimism has been undone by the hidden debts scandal. In collaboration with employees in an international bank, a group of senior Mozambican government officials secured US\$2.2 billion in off-budget loans. Ostensibly intended to build a fishing fleet and fund maritime security, large amounts of these funds were instead diverted to private pockets.

The discovery of the scandal contributed to an economic downturn in 2016 and has set back efforts to reduce persistent poverty and inequality. Funds that should have been available for investment in the SDGs, such as education and support to small-scale fishing communities, have instead been squandered. The burden of servicing unsustainable levels of debt will additionally have long-term negative implications for financing Mozambique's development needs.

In numbers:

- **US\$200 million:** estimated losses in bribes and kickbacks as part of the scandal, sixteen times more than the annual amount allocated to the Direct School Grants Programme.
- **US\$2.2 billion:** the amount in off-budget loans secured between 2009 and 2014, equivalent to two-thirds of the 2018 budget allocation to social priorities such as education, health, infrastructure and rural development.
- **US\$58.6 million:** the amount invested in the Artisanal Fisheries Promotional Project since 2011, as opposed to **US\$350 million** squandered on EMATUM.



Grand corruption and the SDGs: Mozambique

Grand corruption in Mozambique

While Mozambique is ranked 180th out of 189 countries on the 2018 Human Development Index, efforts to address the country's development challenges have been systemically undermined by high levels of corruption. One study has estimated that the average annual cost of corruption for ten years from 2004 to 2014 was up to US\$ 4.9 billion, equivalent to 60% of the country's 2015 budget¹.

Grand corruption, a feature of Mozambique's political economy, accounts for a large proportion of these costs. The governing political party, the Frente de Libertação de Moçambique (Frelimo), has ruled the country since the end of a 15-year civil war in 1992. This has allowed elite groups to monopolise the political arena and the economic opportunities that have arisen over the last three decades, particularly those related to the country's mineral wealth and the discovery of substantial offshore natural gas reserves in 2010.

These problems have periodically come to light in the form of different scandals. In the 1990s and early 2000s, it was the privatisation of two state-owned banks that created an opportunity for funds to be embezzled and cost the state in excess of US\$ 400 million². In the late 2000s, Mozambique was again thrust into the international spotlight after a key Frelimo funder sheltered in the country, Mohamed Bachir Suleman, was named by the US as a narcotics trafficker and drug kingpin³. More recently in 2013 to 2014, the construction of a ring road around the capital Maputo, awarded without tender, is believed to have been hugely overpriced, resulting in losses of government funds of between US\$ 40 and 50 million⁴. Collectively, these scandals point to the institutionalised and

What is grand corruption?

Transparency International identifies three main features of grand corruption: a corruption scheme; involvement of a high level public official; and serious harm caused, which may take the form of large-scale misappropriation of public resources or gross violations of human rights.*

seemingly intractable nature of grand corruption in Mozambique.

The hidden debts scandal

The hidden debts scandal nonetheless surpasses all previous cases in terms of the damage wrought to the Mozambican economy and the development implications for the country's citizens. It is also a textbook example of how grand corruption operates: the scheme built on long-established elite networks underpinned by corruption, capitalised on government decision-making behind closed doors, distorted public policymaking and involved the complicity of international businesses.

The scandal centres on three state-owned companies that secured loans from international lenders between 2009 and 2014 on the prospect of future revenues from natural gas. The first of these, the *Empresa Moçambicana de Atum* (EMATUM, Mozambique Tuna Fishing Company), obtained a US\$ 850 million loan (later restructured into a full sovereign bond) to build a tuna fishing fleet⁵. Two other companies, ProIndicus and Mozambique Asset Management (MAM), obtained loans of US\$ 622 million and US\$ 535 million respectively to provide maritime security for the offshore oil and gas industry and build a shipyard for the maintenance of vessels⁶.

* This is an abridged summary. TI's full legal definition with explanatory notes is available upon request from gdell@transparency.org

Of these loans, only the one to EMATUM was publicly disclosed. Together with further loans negotiated bilaterally by the government, the country incurred off-budget expenditure of around US\$ 2.2 billion between 2009 and 2014, equivalent to just over a quarter of the country's budget for 2015⁷. The loans were arranged by the international banks Credit Suisse and VTB, which were each paid US\$ 199.7 million in fees and are deeply implicated in the scandal⁸.

The ultimate destination of a large proportion of these funds remains unclear. The *Serviço de Informação e Segurança do Estado* (SISE), Mozambique's intelligence service, owned stakes ranging from 33% to 98% in the three companies⁹. An independent audit commissioned by the Office of the Public Prosecutor (PGR) in 2017, found inconsistencies of at least US\$ 500 million regarding how the loan proceeds were actually used, as well as an unexplained payment of US\$ 53 million from an off-book EMATUM account.

EMATUM, ProIndicus and MAM additionally appear to have paid vastly inflated prices for assets, potentially overpaying more than US\$ 700 million, including for vessels purchased from Privinvest, a global shipbuilding group based in the United Arab Emirates¹⁰. The three state-owned companies were not operational at the time of the auditor's report and, according to several accounts, the assets acquired still lie idle¹¹.

What has become increasingly clear is that a large proportion of these funds ended up in private pockets. An indictment filed by the US Department of Justice in New York in late 2018 alleged that at least eight individuals received bribes and kickbacks of over US\$ 200 million from the maritime projects¹². Among those implicated are three senior Mozambican government officials, namely António Carlos do Rosário, the head of the SISE, Manuel Chang, the country's then minister of finance, and Teófilo Nhangumele, who acted on

behalf of the Office of the President of Mozambique and played a key facilitating role in the scandal¹³.

Three investment bankers holding senior roles at Credit Suisse were also named in the indictment and had an important role in channelling funds to bank accounts in several countries¹⁴. Email correspondence included in the indictment suggests that one government official, Nhangumele, referred to bribes as "chickens" while kickbacks to the bankers were labelled as "consultancy" or "dividend" payments¹⁵.

Consequences of the scandal

The US investigation into this case is ongoing as of November 2019. To date, the three investment bankers at Credit Suisse, who together may have received up to US\$ 50 million in kickbacks, have all pled guilty to corruption¹⁶. In Mozambique, where around US\$ 150 million in bribes appear to have been dispersed to officials, the government indicted 20 individuals on charges of corruption and money laundering in February 2019 including Ndambi Guebuza, the oldest son of the country's former president Armando Guebuza¹⁷. Manuel Chang, the former finance minister who signed off on the loans, has been arrested in South Africa and is currently fighting a legal battle against his extradition to Mozambique or the US¹⁸. It is unclear whether any of these individuals will ever face justice in Mozambique. There is a long history of impunity for senior government officials involved in grand corruption.

The repercussions of this scheme go far beyond the funds lost in bribes and kickbacks. A Parliamentary Inquiry Commission and the Attorney General's Office determined that the loans were in violation of the country's budget law and the sovereign guarantees provided by the ministry of finance were illegal¹⁹. The loans were obtained without the knowledge of the country's key lenders, the International Monetary Fund (IMF) and World Bank. The former took the decision to suspend a

standby credit facility of US\$ 283 million in 2016 with the institution's then head, Christine Lagarde, stating publicly that the Mozambican government was "clearly concealing corruption"²⁰. In May 2016, the G14, a group of Mozambique's largest international donors, also suspended budgetary support of US\$ 300 million to the government²¹. The scandal has grievously harmed Mozambique's reputation in the eyes of key development partners. Rebuilding trust and credibility will likely take years, time Mozambique can ill afford if it is to meet the 2030 development targets.

An additional pernicious effect of the scandal has been to push Mozambique's debt levels to unsustainable levels. The decision by donors to withdraw support triggered a collapse in Mozambique's currency, which lost more than a third of its value in 2016, and led the country to default on its sovereign debt in early 2017. The IMF considers Mozambique to be in a position of debt distress and the country remains in talks with lenders about restructuring the three problematic bonds²².

Impact on the SDGs

The sheer volume of funds involved in the hidden debts scandal mean that this scheme has already had a severe negative impact on Mozambique's capacity to meet the 2030 SDG targets. The impact can be seen both in terms of the direct costs – what the funds lost to corruption could otherwise have been spent on – and the knock-on macroeconomic repercussions which undermine long-term development objectives in Mozambique.

The direct costs

The U.S. Department of Justice estimates the funds lost in bribes and kickbacks in this scheme to be in the region of US\$ 200 million. The damage of these losses is stark when compared to spending on SDGs, as can be seen with reference to the goals on improving education and reducing hunger.

SDG 4: Quality Education.

This is a critical goal for Mozambique given that the country's literacy rate for those aged 15 and over is a mere 50.6%. In 2018, children in Mozambique could also only expect 9.7 years of schooling, compared to a global average of 13.2 years²³.

US\$ 200 million equates to just under a quarter of the country's education budget in 2018²⁴. In a context where public resources for development are under intense strain, widespread corruption restricts the government's ability to fund its ambitious plans to increase school enrolment figures to levels needed to meet SDG target 4.1. US\$ 200 million is, for example, nearly 50 times the US\$ 4.2 million investment budget in 2018 for textbooks, classroom construction and technical vocation projects and 17 times as much as the US\$ 12 million allocated in 2018 to the Direct School Grants initiative. The latter programme provides direct funding to primary schools to enable them to purchase basic learning materials such as pencils, pens, notebooks and additional reading materials²⁵.

SDG 2: Zero hunger

Citizens dependent on the country's fisheries sector could have benefited from the US\$ 350 million that the government claims to have invested in EMATUM, the tuna fishing business which remains non-operational²⁶. Approximately 850,000 households, or around 20% of the population, rely on fisheries for part of their income, and the sector is also significant for food security in the country²⁷. In total artisanal fishing contributed US\$ 6.2 million to the country's gross domestic product in 2018, less than 2% of the funds made available to EMATUM.

Supporting these fishing communities is crucial to Mozambique meeting SDG target 2.3, which requires doubling the productivity and incomes of

small-scale producers. The Artisanal Fisheries Promotion Project, which has received US\$ 58.6 million in funding since 2011 from development partners and the government, less than a fifth of the amount invested in EMATUM, provides a comparison of how the funds might have been spent. This project has to date benefited 382,552 people through training, rehabilitation of economic infrastructure and nutrition programmes²⁸.

The broader effects

The macroeconomic effects of the scandal have a far-reaching impact on the overarching goals of reducing poverty and inequality across the country, as measured by SDG targets related to the reduction of poverty (SDG 1.2) and inequality (SDG 10.1).

SDG 1: no poverty

In 2018, 62.9% of the population lived below the international poverty line of US\$ 1.90 a day²⁹. The US\$ 2.2 billion in off-budget loans is equivalent to over two-thirds of the US\$ 3.2 billion allocated in the 2018 budget to social priorities, including education, health, infrastructure, agricultural and rural development, transport and employment spending³⁰.

While the poverty rate declined in Mozambique between 2008 and 2014, the World Bank has estimated that a spike in food prices caused by the economic downturn in 2016 may have increased poverty rates by 4 to 6 percentage points. Alongside a period of drought, the hidden loans scandal was a key driver of the economic recession, whose impact was most keenly felt in Mozambique's poorest provinces.

SDG 10: reduced inequalities

That the economic effects of these issues were felt unequally continues a trend of entrenched inequality in Mozambique, which is reflected in the

country's Gini coefficient of 54.0, the seventh highest in sub-Saharan Africa³¹.

From 2008 to 2015 the wealth of the top quintile grew almost three times faster than that of the bottom 40% of the population³². By bringing large amounts of capital under the control of self-serving political elites, high-level corruption is undoubtedly contributing to the growing wealth gap in Mozambican society, stymieing progress towards SDG target 10.1.

The burden of servicing the debts incurred as a result of the grand corruption scheme can already be shown to have affected development spending, and may well be the longest-lasting impact of this affair. As the scandal broke and the currency plunged in value, the government was obliged to introduce an emergency budget in 2016 which cut expenditure by up to 40% to keep up with debts held in foreign currency³³. Figures available for the 2018 budget show that the amount made available for debt servicing (MZN 75.4bn) was almost as much as that provided for education and health spending combined (MZN 79.2bn)³⁴.

Regardless of whether Mozambique succeeds in restructuring its three problematic bonds, the damage to the perception of the country in the eyes of external lenders and investors will see the country pay more to borrow in the future. When combined with the harm already caused to Mozambique's relationships with international development partners, this will mean more public funds tied up in debt servicing and less available for spending on the country's development goals.

Recommendations

National level

The government of Mozambique should:

1. Introduce reforms to the constitution to reduce the executive powers of the office of the

President, particularly its ability to nominate and dismiss the Attorney General without consulting parliament.

2. Take robust measures to guarantee independence in the judiciary and eliminate political interference. Removing the power of the President to appoint the Presidents of the Administrative Court, the Supreme Court and the Constitutional Council would be an important first step.
3. Introduce a dedicated asset recovery law.
4. Improve the financial disclosure system to enhance public scrutiny of officials' asset declarations.

Global level

To help support the accomplishment of the SDGs, States parties to the United Nations Convention against Corruption (UNCAC) should:

1. Explicitly recognise grand corruption as a threat to the achievement of the 2030 Sustainable Development Agenda.
2. Prioritise the prevention of and responses to grand corruption (as prescribed in the Oslo statement) due to its developmental consequences.
3. Initiate discussions about a definition of grand corruption and an Optional Protocol to the UNCAC on Grand Corruption.
4. Commit to further research on the impact of grand corruption on sustainable development to identify effective strategies to counter this problem, and convene an Expert Group Meeting on this subject.

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