The bad: Mozambique

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Despite tensions between the ruling party, Frelimo, which won the 2014 general election with just over 57% of the vote, and the main opposition party, Renamo, Mozambique remains one of the more attractive markets in sub-Saharan Africa, according to BMI Research's Mozambique Operational Risk Report. The government is also committed to developing its coal industry and generally welcome of foreign investment to do so.

Indeed foreign players – from Brazil's Vale to a recent influx of Indian investors – dominate the country's coal sector. Vale's Moatize mine and associated Nacala Logistics Corrider is by far the most advanced project in the country, despite Vale announcing in September 2015 that the ramp-up in metallurgical coal exports from Mozambique would be constrained for the remainder of the year due to disruption at the port of Nacala and on the railroad to the port. Its exports are expected to remain flat y/y at 3.2 million t, according to CRU – a fall on its previous forecast of 6.5 million t.

Overall, Mozambique exported an estimated 2.6 million t in 1H15, according to CRU, up 31% on the previous year, with its coal comparable to that coming out of Australia. Key export markets were India, Taiwan, China and Japan.

Yet despite the potential and the interest in Mozambique coal, infrastructure remains the biggest challenge to its development – a challenge that becomes harder to solve in today's low-price environment. "Mozambique's coal production growth will continue to be hampered by low global coal prices, high domestic start-up costs and inadequate infrastructure," BMR Research's Mitchell Hugers said – with agreement from CRU's Boyle.

"Rail and port infrastructure is probably the key cost factor influencing the seaborne metallurgical coal market," said Boyle. "In recent years, we estimate that transportation costs [for Mozambican coal] have been about US$50 – 60/t, a result of operating on an inefficient multi-cargo rail line and also a result of using a less than ideal port solution, whereby coal is shipped 40 km offshore using handymax ships, then transhipped to panamax vessels. This transportation inefficiency has been adding about US$20/t to operating costs."

That is starting to change with the development of the Nacala-a-Velha coal terminal, which opened in mid-July 2015. "It's definitely going to be positive as its development will provide an alternative route to the transportation of coal from Tete," said Hugers.

Away from transportation, Hugers also highlighted the lack of a sufficient power supply as a major downside risk, preventing companies from reaching their maximum output. And as with South Africa's mining industry, ESKOM may again be to blame: "An inability [by ESKOM] to meet domestic demand will curb electricity exports to other members of the Southen African Power Pool," explained Hugers. "South Africa is the most developed power market in sub-Saharan Africa and a failure to export electricity to Botswana and Mozambique in particular will hurt these economies."

Outlook: the bad comes good?

Over the longer-term, however, the outlook for Mozambique's coal industry is more upbeat as the infrastructure challenges are worked through – though they will cast a shadow over the country's growth prospects for a while yet. "We are quite positive on Mozambique's coal production – strong single digit growth," said BMI Research's Hugers. "Although I'm saying single digit growth; it won't be double digit because this sector is going to face some significant challenges."

CRU's Boyle takes a more positive view, however: "Beyond 2015, we expect exports from Mozambique to rise quickly as Vale's export volumes from Moatize ramp up. However, we have assumed a slower pace of export growth than our previous forecasts, given the problems at the Nacala port. Between 2016 and 2019, Mozambican metallurgical coal exports are forecast to grow at a CAGR or 21% to reach 14.8 million t – which is significant growth over just a few years. Mozambique is forecast to account for 5% of metallurgical coal export in 2018, compared to 2% in 2015."

Vale will be responsible for most of this growth – but Indian firms could also start to play a significant role in developing Mozambique's coal assets. With the acquisition of Rio Tinto's coal assets in 2014 for US$50 million, International Coal Ventures joined India's state-owned mining company, Coal India, and Jindal in investing in the country.

Nor might that interest be confined to Indian companies: "We believe that Indian firms will increasingly be joined by other Asian firms over the coming years as other countries look to secure long-term access to resources of metallurgical and other types of coal," said Hugers, citing the example of Japanese trading house, Mitsui, who bought a 15% stake in Vale's Moatize coal mine and 35% in the Nacala Logistics Corridor for US$313 million in December 2014.

There has also been some Chinese investment in the country with Ncondezi Energy signing a joint development agreement with Shanghai Electric Power (SEP) in January 2016 to develop an initial 300 MW coal-fired power plant in Tete Province. The agreement will see SEP, which is majority owned by Chinese state utility, State Power Investment Corp., invest up to US$25.5 million for a 60% stake in a new holding company for the power project, Ncondezi Power Co.

The project, which also includes development of a captive coal mine, to be developed by Ncondezi Energy independently of SEP, aims to develop the power plant in 300 MW phases until it reaches a final capacity of 1800 MW.

New entrants will have to overcome the significant cost challenges involved in constructing a mine and related transport infrastructure in a low-cost coal environment, however. As a result, CRU does not anticipate significant volumes from these companies before 2019, "despite numerous plans for significant capacity additions."

"Capital costs to develop the assets have increased relative to the original plans," concluded Boyle. "While operating costs are also less favourable."

Note: This article first appeared in the February 2016 of World Coal as part of a report on southern Africa's coal industry. Read the rest of the report below:

- The good, the bad and the ugly: southern Africa's coal industry
- The good: Botswana
- The ugly: South Africa

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