

Angola

## *Growing Up Fast* – Analysing the Downstream Petroleum Market in Angola

July 2013

### Summary

Angola is a young country, having gained independence from Portugal in 1975. Like many former colonies in sub-Saharan Africa, it began life with low levels of economic development yet vast amounts of natural resources, primarily oil. Its development since independence has been painful but explosive. At one point in the mid-2000s Angola's economy was growing at a breakneck 20% on an annualised basis. Much like other speed freaks, Angola's progress was fuelled by large quantities of oil, which it has an abundance of.

However, whilst Angola is one of the top three exporters of crude oil in Africa, its downstream refining industry is underdeveloped. Its production of petroleum may be high, but its consumption has been historically low. Bargate asks: is this state of affairs likely to continue?



### In this report

Summary	This page
Backdrop	1
Troubled Childhood	2
Petrol Head	2
Signs of Maturity	4
Bargate's View	5

In short – no! The statistical data shows that Angolan consumption of petroleum products is rising, despite the global slowdown of 2009. Bargate believes that Angola's downstream market is likely to grow and develop, particularly if its refining capabilities are expanded in the near future.

## Backdrop

One could say that Angola is a rare example of an oil industry with a country attached to it, rather than the other way around! The oil industry dominates the Angolan economy, making up 40-50% of GDP as of 2011. However, there is evidence from the World Bank that both the manufacturing and financial sectors, though small, are growing quickly. Since its infancy Angola has relied on the quick and easy growth it could squeeze out of its oil wells. However the finite nature of petroleum and the heap of well documented negative impact of an economy's over-reliance on petroleum revenues mean that an evolution in Angola's economy will have to happen at some point.

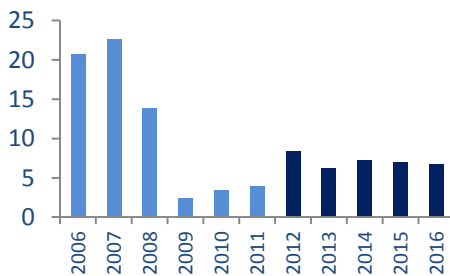
### Angola at a glance

Population: 19.6 million

GDP (current prices, 2012 est.): US\$118.7bn

#### Annual GDP Growth (%)

(Source: IMF; 2012 onwards estimated)



### Why are we doing this?

The aim of this report is to assess if the downstream petroleum market in Angola is a growth market or not. In 2012, Angola's recoverable reserves of petroleum were estimated as being 13.5 billion barrels, or 21 years of current production. There is therefore no gainsaying that Angola needs to diversify its economy, both to ensure further growth should the oil run out, but also to insulate itself from any negative commodity price shocks.

### What's our plan of attack analysis?

The plan is to first analyse the effects of Angola's long civil war (1975-2002) on the country. Then, we will look at its economic performance since the end of the civil war, with particular attention to the upstream oil industry. Finally we will assess the downstream oil industry and judge whether it is likely to develop in the near future.

### A bit of a disclaimer

While we are confident that our analysis is based on internally consistent parameters, our views are based entirely on the data we have independently sourced and verified where necessary.

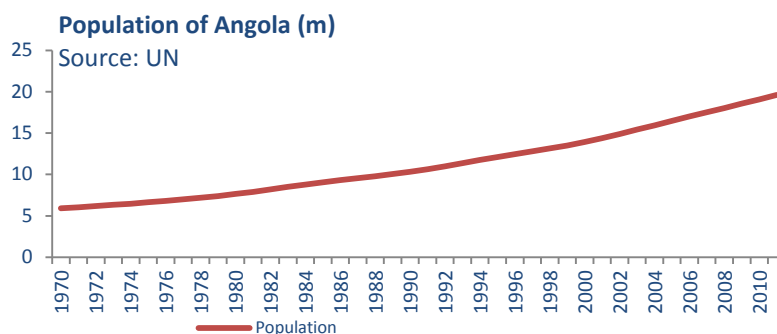
### Did you know?

Angola accounts for over 40% of Portuguese wine exports and the market is growing at 16.8%. In 2012 Angola bought more than 680,000 hectolitres of wine from Portugal – not all of it for use in mass!

<http://www.macauhub.com.mo/en/2013/07/03/angola-accounts-for-over-40-pct-of-portuguese-wine-exports/>

## Difficult Childhood

Angola's first 30 years were turbulent, to say the least. The civil war between the People's Movement for the Liberation of Angola (MPLA) and the National Union for the Total Independence of Angola (UNITA) claimed between 500,000 and 1.5m lives with many millions more displaced or maimed. During the war the median age of the population fell from 19.4 years in 1950 to 16.7 years in 1980. Despite this, the population continued to grow over the period.



The Angolan Civil War has held the country back. However it has made immense strides since 2002.

The war left deep scars on both the people and the country. Millions of landmines are still spread over farmlands, roads and even in residential areas. Land mine injuries account for 20% of medical operations performed within the entire country every year.

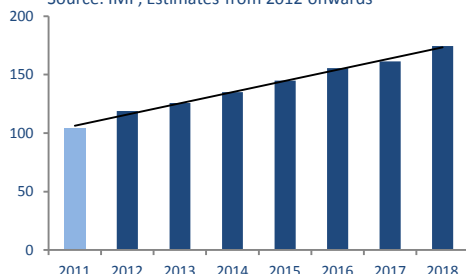
The war also meant that economic development was held back. According to the UN, 58% of the population lives below the poverty line. The destruction of agricultural land is believed to be the main cause of this disturbing statistic. However, despite such grim data, there is reason to believe Angola is making up for lost time by speeding ahead with economic growth since 2002.

In the space of ten years (2002-2012) Angolan GDP has more than quintupled.

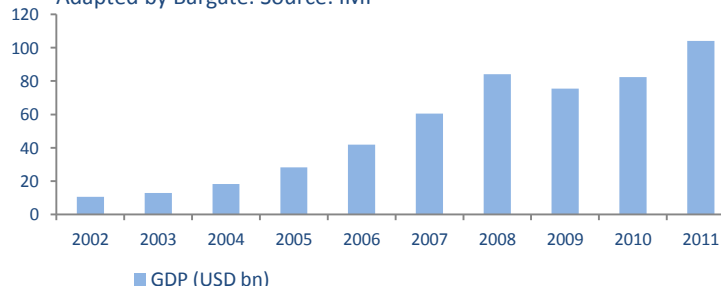
## Petrol Head

One look at the GDP figures, both absolute and growth, tell you that Angola has experienced a frenetic boom in the last decade or so. In the space of ten years (2002-2012) GDP has more than quintupled. Since 2002 Angola's economy has averaged growth of around 11% per annum – most of this was fuelled (pun intended) by oil exports.

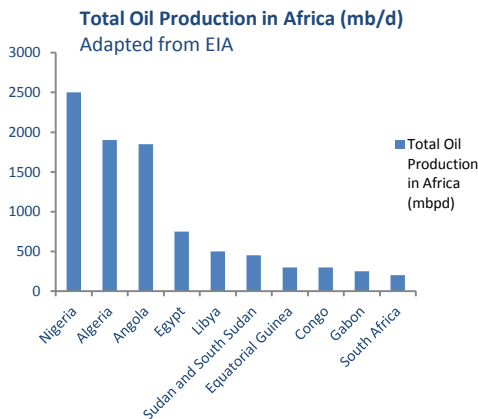
**Angolan GDP (USD 000s)**  
Source: IMF; Estimates from 2012 onwards



**GDP (USD bn)**  
Adapted by Bargate. Source: IMF

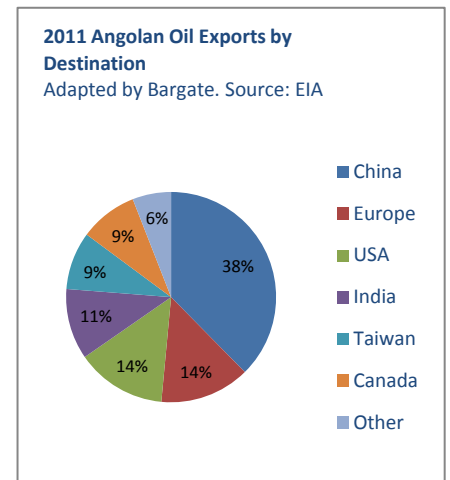
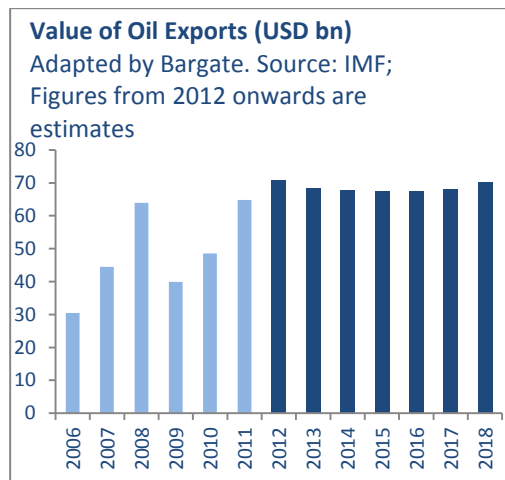


**How does Angolan oil production compare with the rest of Africa?**



More than 90% of all oil produced in Angola is exported, mainly to China and North America. According to the US Energy Information Agency, oil exports accounted for over 98% of Angolan government revenues. In 2012 oil production averaged 1.871mb/d, up from less than 1.6mb/d in 2011.

The Angolan oil industry is overseen by Sonangol, a state run oil company created in 1976 as the sole concessionaire in all oil and gas exploration in Angola. All foreign companies operating in the Angolan oil industry had historically done so under joint venture operations with Sonangol. However, since the enactment of the Petroleum Activities Law (2004) these have increasingly been replaced by production-sharing agreements (PSAs).



Angolan Oil Exports are expected to maintain their value into the near future

Limited processing capacity means that downstream petroleum market is underdeveloped

Having taken a hit in 2009-10, the value of oil exports is predicted to stabilise at around \$65bn over the next few years. Despite the recent hullabaloo about shale gas killing off the market for oil, the IMF believes the value of Angolan exports will hold up, mostly due to increased demand from India and China.

However, despite being an oil producing country, Angola has only one small refinery located in Luanda. The refinery, built in 1955, historically only had the oil processing capacity of 39,000 b/d (although this is being increased to full capacity, which is 65,000 b/d in 2012). Because of its shortage of processing power, Angola annually imports about US\$ 250 million of oil derivatives – despite being the third largest oil producer in Sub-Saharan Africa.

Among developing nations, Angola has comparatively low rates of fuel subsidies. In August 2010, Luanda partially removed subsidies on gasoline and diesel - in line with an IMF demand for market deregulation and for Sonangol to be freed of its quasi-government functions, which included providing subsidised fuel prices. Angola appears committed to freer markets, which is encouraging.

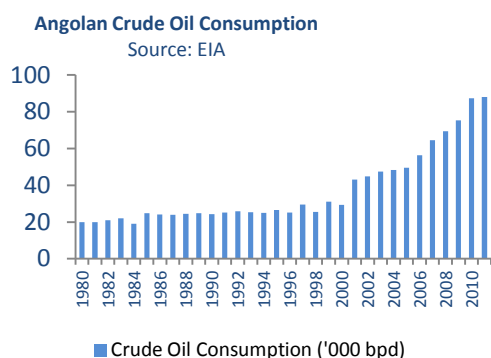
## Signs of Maturity

Signs that Angola's consumption of petroleum is increasing as the country gets richer

### Total Crude Oil Consumption (2011):

79,430 b/d

(Source: CIA World Factbook)

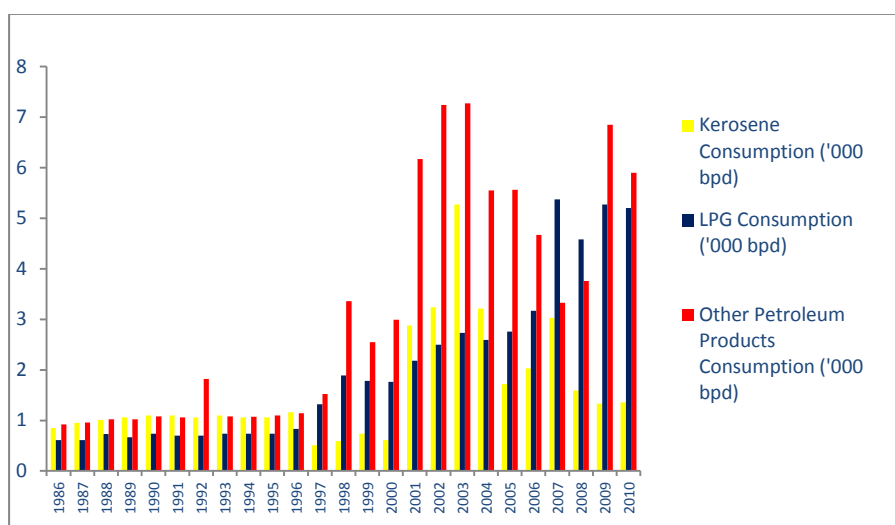


Recent economic data has suggested that Angola is shifting away from just producing petroleum towards producing and consuming it. Domestic oil consumption in 2012 was 85,000 b/d, with a strong upward trend. In terms of development, increasing fuel consumption is the economic equivalent of hairs on the chin and a broken voice! Overall, the data suggests that Angola is becoming a more developed economy. Economic growth is predicted to slow from its hair-raising average of 10-11% from 2002-2009 to a more leisurely 5-6%.

Angola's consumption of both crude oil and refined products is increasing, albeit from a low base. There has been a recent shift away from consumption of kerosene towards consumption of LPG and other kinds of petroleum products. However, most of the energy consumed in Angola is from solid biomass rather than from petroleum. The statistical evidence suggests that Angola is moving towards greater consumption and fewer exports. This diversification and maturation of the economy is likely to result in moderately fast but stable rates of growth in the next decade or so.

As we can see from the chart below from the US Energy Information Agency, Angolans are consuming more petroleum-based products than ever before. It shows an overall upward market trend.

Increasing consumption of LPG and other petroleum products – shifting away from kerosene

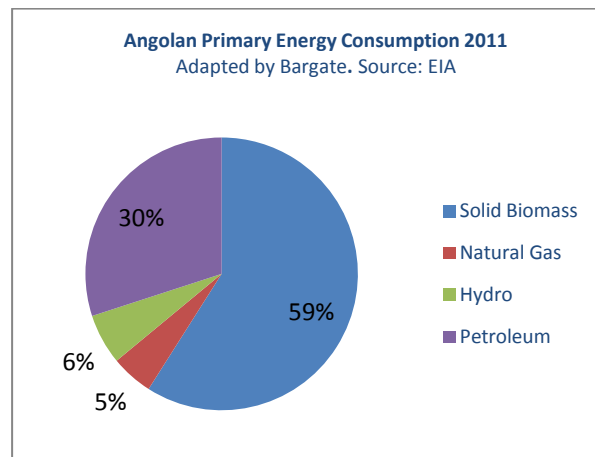


### New Investment in refinery capabilities

To meet the national demand, Sonangol has now started the construction of a new and modern refinery, Sonaref, with the objective of having complete integration of oil production and refining activities. The new refinery is set to open at Luanda in 2015 and is expected to have a crude distillation capacity of approximately 200,000 b/d. Angola has taken the mature decision to start producing more of the refined products it wants. Whether or not it is a commercially sound decision remains to be tested by Bargate. We are confident that it would be fun finding out.

Petroleum currently makes up a minority share of the total energy consumed in Angola

However, the petroleum market remains underdeveloped in Angola. Nearly two-thirds of all energy consumed in Angola comes from solid biomass (i.e. wood). Despite being rich in petroleum, Angolans have hitherto been too poor to enjoy the fruits of their own resources.



Important economic drivers suggest the downstream market is likely to grow in the future

However, there are signs that the downstream market may be a growth market. Positive signs include:

- **Growing Private consumption:** Private consumption grew by 14.7 % in 2012, up from a weaker 1.6 % in 2011. Angolan consumption is set to become a more important driver of growth in the long term.
- **Falling Inflation:** in 2012 the headline inflation rate fell to single figures (9%) for the first time in 20 years and is forecast to stay low. This is likely to increase the spending power of consumers in the future as per capita incomes increase.
- **New Refinery Capacity:** Along with the new refinery at Luanda Sonaref is to expand the capacity of the existing refinery at Luanda to 100,000 b/d and to have an export refinery at Soyo with a capacity of 200,000 b/d. For the latter plant, Sonangol is seeking a qualified IOC to be a partner.
- **Establishment of a Sovereign Wealth Fund:** the Fundo Soberano de Angola (FSDEA) is designed to maintain macroeconomic stability by insulating the annual budget from volatile oil-revenue inflows. The initial size of the fund will be US\$5 billion, with the funds to be invested both internationally and domestically.
- **Exploitation of Natural Gas:** The planned commencement of LNG production in 2013 could boost growth by 2% annually. Angola's projected LNG production capacity will be 5.2 million tons per year, or 7.2 billion cubic meters of LNG for export - the equivalent of 45 million barrels of oil.

Currently Angola is moving away from the teenage years of economic development – (volatile swings in prices, miraculous growth) towards a more confident, mature economic model.

## What is Bargate's View?

Our view is that the downstream oil market in Angola will represent an important growth area in the long term

Bargate's view is that the downstream petroleum market in Angola is expected to grow by an annual average of about 7% to 2016. We consider this growth to be conservative. This growth will be driven partly by growing domestic demand for LPG and motor gasoline, which is forecast to remain strong.

Ordinary Angolans may finally be reaping the benefits of the long boom period in the 2000s. They are likely to respond like we all do when our income increases – by buying more cars and driving more!

As a caveat, we cannot guarantee that various market shocks or bad government decisions may wreck this development, but *ceteris paribus* (as economists like to say) Angola's development will continue strongly.

## So, what next?

Bargate is happy to provide a more detailed analysis (including short, medium and long term forecasts) of the domestic market for Angola's downstream petroleum market on request.

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