FALLING CRUDE OIL PRICES: SILVER LINING FOR ROBUST FISCAL MEASURES IN AFRICA?

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There is no doubt that oil producing countries are reeling under extreme pressure to reconcile spending with revenues as crude oil prices continue a nose dive; reaching an 11-year low in January 2016. Demand for oil remains low relative to supply on account of a slowing Chinese economy. US gasoline stockpiles grew by 10.6 million barrels at the beginning of January 2016 - the biggest weekly build since May 1993 - and distillate supplies rose by 6.3 million barrels. Iran is expected to increase oil production by another 500,000 barrels daily and could go up to a million barrels, following lifting of sanctions on the country. This throws price expectations very wide; and the implication for this is predictable.

African producers are the worse hit by the oil crush due largely in part to their less diversified economies, over-dependence on oil revenues, lower tax effort, fiscal indiscipline and corruption among others. In spite of the lower benchmark prices of between US$50 to US$60 per barrel used by most of the countries in the 2016 budget, they are now compelled to make difficult fiscal adjustments which are not only going to be unpopular with their people, but also affect their macroeconomic outlook. The question that confronts these governments is simple – Does lower oil price provide a silver lining for introducing tough fiscal measures?

Nigeria, the leader of the pack in its 2016 Budget outlined a number of measures to address some of the challenges that plaque the country amidst the oil crush. For example, the government expressed its plan to prioritize agriculture as a way to diversify the economy away from oil, widen the tax net, and remove fuel subsidies. Ghana has already imposed new taxes and levies on petroleum products and electricity, and withdrew subsidies from petroleum. Other producers like Angola, Equatorial Guinea, and Gabon are still faced with policy dilemmas whilst their economies are suffocating from the oil squeeze. There is cause to believe that some of the fiscal measures are unpopular with the people. Ghanaian Labour Unions have already held a march to protest the new taxes and levies on petroleum, whilst making demands for increase in salaries.

The economic environment created by the oil crush is both a blessing and a curse. It is a blessing because; consumers of petroleum products now enjoy lower prices of petroleum products as demonstrated in Nigeria and Ghana where pass-through prices have favoured downward price adjustments. Also, the reduction in the petroleum import bill for these countries who although produce crude oil, import large quantities of petroleum products, has been significant, bringing desirable improvements on their terms of trade. The governments also now have basis to remove subsidies from petroleum products.

It is however a curse because savings from subsidies are unlikely to finance the deficits from lower oil prices. Government's can also introduce or increase taxes on petroleum products reducing the benefits of price over-recoveries to consumers. Further, these countries are compelled to cut spending, which adversely affects social welfare.

It is therefore not surprising that oil-producing countries are taking tough fiscal measures to raise additional revenues to meet budget targets. For example, the Government of Ghana will raise incremental revenue of about US$800 million annually from new taxes and levies on petrol, diesel and LPG alone.

Key policy issues arising from the oil price crush in producing countries however remain unanswered, which could undermine the positive effects of any fiscal measures introduced.

1. The stabilization mechanisms through Sovereign Wealth Funds (SWF) are weak and poorly funded. With the exception of Libya and Algeria, the rest of the oil producers by the end of 2015 had very lower balances in their Funds (Angola – US$5 billion; Nigeria – US$1.4 billion; Gabon – US$400 million; Ghana – US$250million; Equatorial Guinea – US$80 million). This throws into doubt the efficacy of the Funds in fulfilling their primary objectives of providing inter-temporal stabilization, diversification and risk adjusted investment.
2. The economies of most oil producing countries are not diversified from oil dependence. Oil exports constitute about 40-50% of GDP for countries such as Gabon, Angola and the Republic of the Congo, and 80% for Equatorial Guinea. Also, oil accounts for 75% of government revenues in Angola, Republic of Congo and Equatorial Guinea.
3. Tax efforts in most of Africa's oil producers are lower than their non-oil producing counterparts. For instance, non-oil tax efforts in these countries according to the African Economic Outlook are – (0.39 in Angola; 0.42 in Republic of Congo; 0.53 in Algeria; 0.08 in Equatorial Guinea; 0.28 in Chad; 0.58 in Sudan; and 0.52 in Gabon). Tax effort of less than 1 shows that these countries are not collecting taxes relative to the potential of their economies.
4. Governance challenges relating to fiscal integrity such as fiscal discipline, tax administration, corruption and wasteful spending remain a dominant feature in these countries. Also, most of these countries that are introducing new taxes and levies to raise additional revenues do not have accountability measures to govern

the utilization of the money. They will merely be spent through the Consolidated Funds without strong parliamentary scrutiny - using their parliamentary majority and weak parliamentary structures to have their way.

As a result of these challenges, adoption of tough fiscal measures in addressing the effects of lower oil prices will therefore not only amount to window-dressing the problems but is also unsustainable.

Africa’s oil producing countries must not adopt a hand-to-mouth fiscal policy for spending their oil revenues in spite of the shortfalls. Even in these difficult times, they must exercise fiscal restraint and encourage savings as was done by Chile to its Copper Stabilization Fund. To diversify their economies, they should invest in agriculture by increasing agricultural spending to at least 10% of the national budget in line with the Maputo Declaration. They should also invest in infrastructure to promote manufacturing. They can do these by promoting market friendly reforms to attract foreign investments as well as through public-private-partnership. Tax effort must be increased. New taxes as well as higher taxes can only increase the tax burden of the current profile of taxpayers; and could tax them out of the economy. Tax effort requires the widening of the tax net as well as improvement in the efficiency of tax collection. Most important is the troubling issue of corruption and poor public accountability in these countries. The recent corruption perception index shows that the performance of Africa’s oil producers is deteriorating, a disturbing trend undermining economic development.

As OPEC expects to recover its power through consensus on production cuts, which have become ineffective though, non-OPEC producers are more willing to increase production to raise more revenues. Whether Saudi’s strategy to hold its market share succeeds or not is another issue. Meanwhile, the Chinese economy is still in comma. All these factors increase the uncertainty about a significant oil price recovery. This also puts to test the effectiveness of robust fiscal measures African oil producers are introducing, which are mostly shot-term by form. Eventually, only policies that are forward looking culminating in economic diversification, savings, and good governance, can support Africa’s oil economies to gradually adjust to sustained equilibrium.