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THE IMPACT OF OIL PRICE HIKE

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Voices of the South on Globalization is a monthly newsletter intended to inspire a meaningful North-South Dialogue by raising awareness for global interdependences and by offering a forum for voices from the South in the globalization debate. Each edition will present short analyses or commentaries from a Southern perspective on one particular issue of the globalization process.
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GOOD NEWS WITH A TINGE OF CAUTION

The steep rise in oil prices over the past three years has had little impact on some of the world's poorest countries. But they will come under pressure if oil prices remain at current levels or go up this year and beyond, according to research by a team of IMF economists.

"A puzzling feature of the large increase in world oil prices since 2002 is the seemingly limited macroeconomic impact on low-income countries (LICs)," the economists say in a working paper titled '*Weathering the Storm So Far:The Impact of the 2003-05 Oil Shock on Low-Income Countries'*.

The research paper by Paolo Dudine, James John, Mark Lewis, Luzmaria Monasi, Helaway Tadesse and Joerg Zeuner was released earlier this month. The economists point out that the global context has helped mitigate the impact.

The increase in world oil prices has been more gradual and smaller in percentage terms than during 1970s and 1980s, while global growth and trade have been higher, consistent with the demand-side pressures that characterize this shock. This has given countries time to adjust, which many did as petroleum import volumes contracted in reaction to the pass-through of world oil prices to domestic retail prices.

At the same time, exports picked up in many low-income countries, in large part due to higher world prices, driven by strong world demand. On average, the rise in exports offset the portion of the oil shock that was not offset by lower import volumes.

Also, current account deficits widened as a result of rising non-oil imports by LIC oil importers in 2003-05, indicating that countries did not adjust to the oil shock through a compression of other imports. Instead, more positive capital account developments -- reflecting foreign direct investments (FDI), debt relief, and other capital inflows -- helped cover the wider current account deficits. Some countries reduced reserve coverage moderately to finance the remaining gap.

In this setting, there was not an increase in demand from LICs for IMF (International Monetary Fund) resources. This demand would have been seen through requests for increased access or "augmentation" under an existing Poverty Reduction and Growth Facility (PRGF) programme covering 78 countries, requests for access under a new PRGF, or requests for support under the Exogenous Shocks Facility (ESF).

The economists point out that to date there have been no requests under the ESF and few requests for PRGF augmentations, while overall PRGF commitments and disbursements have fallen even as oil prices have risen. Moreover, while IMF programmes over this period have been designed with the impact of the oil shock in mind, there has not been an increase in waivers in IMF programmes as a result of financial targets being missed due to the oil shock. **[More on page 6]**

ANXIETY CLOUDS BANGLADESH'S FUTURE

Dhaka – Bangladesh is unlikely to be affected immediately by the recent international oil price hike because it has a considerable quantity of petroleum products in the pipeline from contracts signed with suppliers earlier.

But there is great concern over things to come if the oil price that has touched a record high of 78 dollars a barrel continues to hike.

"We are worried and watching closely the global oil market situation," said Energy and Mineral Resources Advisor Mahmudur Rahman middle of the month. The state-run Bangladesh Petroleum Corporation (BPC) will incur a loss of 300 million taka, which is equivalent to about 4.4 million dollars, in the current fiscal year due to the excessive hike in oil prices in the international market.

Since the government has increased its fuel prices recently to offset the loss to some extent, it is reluctant to raise fuel prices further. However, sources at the Energy Ministry said the government will have no alternative but to increase fuel prices once again if oil prices cross 80 dollars a barrel.

According to Rahman, the BPC will have to spend an additional amount in line with increased international fuel price for any future deal. "The increased fuel price will automatically be adjusted from the next shipment," he added.

BPC officials said the current international price will not affect Bangladesh immediately, as the country has bought high speed diesel (HSD) and crude as per the rate set in the contract signed between Bangladesh and Kuwait. The current contract will expire in December.

The BPC's different depots across the country are said to have adequate stocks of fuel to meet the local demands. "Currently, we've nearly 150,000 tonnes of stock at our different depots across the country. Some 100,000 tonnes are in the pipeline," a BPC official said.

Sources said the energy and mineral resources division (EMRD) recently received funds worth 200 million dollars from the Islamic Development Bank (IDB) for fuel imports. The EMRD hinted that another 50 million dollar IDB fund might be released in August. Bangladesh might also receive 250 million dollar credit from the Standard Chartered Bank to foot the oil import bills.

But impoverished Bangladesh needs much more: 10 billion dollars in investment over the next 10 years to alleviate its massive power shortage, according to the World Bank.

The country faces an average daily shortfall of 700 to 800 megawatts as demand rises due to fast economic growth. But this shortfall can peak as high as 2,000 megawatts when ageing plants are shut for maintenance.

"To improve the situation, an estimated investment, both public and private, of 700 billion taka or roughly 10 billion dollars will be needed over the next 10 years," the World Bank said in a statement mid-July.

The bank announced a 275-million-dollar soft loan for construction of a gas-fired power plant near Dhaka, the capital. The plant, to be run by an international power company, would add 300 megawatts of power. The estimate of the country's power investment needs followed a recent World Bank mission's visit to Dhaka to discuss ways of financing the sector.

The country requires "a comprehensive reform plan" to pave the way for private investment and donors' support for the power sector, the bank said. "Addressing power sector problems requires time," it added.

Just 40 percent of the 140 million population has access to electricity. In those rural areas with electricity, power lasts a maximum of six hours a day. Even in Dhaka there are regular power cuts lasting five to six hours a day.

The shortages have led to protests. Some 17 people were killed in northern Chapainawabganj district earlier this year when police shot at farmers trying to storm electricity offices to demand power for irrigation pumps.

Following the violence, a senior bureaucrat said the country was headed for more such confrontations as there was no way the situation could improve swiftly.

"This is a war-like situation. The supply scenario is so grim that we have to manage the load as it is done during wartime," B.D. Rahmatullah, whose office advises the government on power sector reforms, told AFP.
- Nabil Iftekar

OIL PRICE HIKE A "TAX BONANZA" FOR NEW DELHI?

New Delhi – Oil price hike in global markets has triggered a war of words in India between Finance Minister P Chidambaram on the one hand and the opposition Left parties on the other. At times even some ruling Congress Party legislators in both Houses of the Indian Parliament -- the Lok Sabha and Rajya Sabha – have been joining the fray.

The verbal war began when the Communist Party CPI (M) Rajya Sabha MP Brinda Karat said in a letter to Finance Minister P Chidambaram: "I reiterate my demand to reverse the increase in petrol and diesel prices in tune with the recommendation of the Standing Committee to change ad valorem component of tax/duty to specific, as was the practice till 1994."

Karat cited the high revenues being collected by the central government in New Delhi and the states from the petroleum sector. She said the revenue earning from the sector had jumped from 206 million dollars in 2002-03 to 272 million dollars in 2005-06.

She said that the ad valorem component of the tax duty means more tax revenues for the Government when the basic price of crude and petroleum products increases. The Parliamentary Standing Committee on Petroleum and Natural Gas had recommended that the ad valorem component in the existing mix should be replaced by a single specific component.

The allegation that the rise in crude oil price was a "tax bonanza" for the Government has been repeated in Lok Sabha, the lower house of the Indian Parliament too. But Chidambaram has termed the accusation a "misconception".

"Contrary to popular perception, we didn't even meet our target...we did not get any tax bonanza last year nor do we expect to get it this year," Chidambaram said. He pointed out that in 2004-05, the total collection from Customs and excise duties on petroleum products stood at 121 million dollars.

In 2005-06, against the budgeted target of 139 million dollars from these duties the government could collect 135 million dollars only, a shortfall of 4 million dollars.

Chidambaram said that the figures he gave were correct and asked the communist party MP Karat the source of the figures she was quoting.

In an obvious move to calm the tempers India's Petroleum and Natural Gas Ministry ruled out a further increase in the prices of petrol and diesel even as global crude prices were near all-time highs. "No price hike is intended," Petroleum and Natural Gas Minister Murli Deora said. He said under recoveries of oil marketing companies in the last two weeks of July were expected to be around 13.8 million dollars. India's crude basket was priced at 73.96 dollars a barrel on July 14, significantly higher than the average of 66.80 dollars in June. The government recently said state-run oil marketing companies could revise the retail prices of petrol and diesel on the last day of each month if the monthly average price of the country's crude oil basket crossed 70 dollars a barrel, The Business Standard newspaper said.

Asked how the government would deal with rising prices, the Minister maintained that they would take a call when the problem emerges.

"To bridge the demand and supply gap in natural gas we have a big contract with Iran. There are some problems in execution and we are trying our level best that Iran fulfils the conditions of that contract," Deora said adding that the problem was in the contract itself and efforts were on to sort them out.

According to an expert committee report on Integrated Energy Policy 2005, the share of natural gas in energy consumption is expected to increase from 9 per cent to 23 per cent in next 25 years.

Petroleum Ministry Secretary M S Srinivasan said production and consumption of natural gas in the country will easily cross 250 million cubic metres per day by 2012 and the launch of future trading in the commodity was timely.

The latest price rise also comes at a bad time for Asia's hard-charging economies. Asian governments have begun cutting back costly subsidies that sheltered consumers and businesses from higher energy prices.

Thailand and Indonesia began shaving subsidies last year. They have been joined this year by Malaysia, Taiwan, India and China, which are relaxing price controls and letting state-owned oil companies pass on some cost increases to customers.

"It's a double whammy in that past oil prices are starting, with a big lag, to feed through into these economies; and on top of that, you've got oil prices continuing to rise," says Robert Subbaraman, Hong Kong-based senior economist with Lehman Brothers Asia Ltd.

It also comes as countries in the region struggle to contain inflation. China, India and South Korea increased interest rates this year in attempts to cool their economies.
– **Sushil Parwar**

NO RESPITE FOR GHANAIANS - APPARENTLY

Accra - It was another breathtaking moment for Ghanaians as the National Petroleum Authority (NPA) announced new prices for petroleum products -- bringing to three, the number of fuel price increases this year alone.

Market watchers say this new development makes the New Patriotic Party administration the first in Ghana's history to sell petrol at about 5 dollars per gallon, three times higher than the minimum wage of many Ghanaians.

Some members of the public who spoke to 'Public Agenda', the Ghanaian weekly independent newspaper, said they were unhappy about the failure of the NPA to factor in the plight of ordinary Ghanaians before increasing the prices.

Many people are angry that announcing price increases without pre-planning with stakeholders in the oil industry, such as the Ghana Private Road Transport Union (GPRTU) of the Trades Union and the public, leaves room for arbitrariness in the determination of transport fares and the exploitation of the travelling public by drivers.

As a prelude to announcing the new prices, the Executive Secretary of the NPA, Dr. John Attafuah appealed to the public on Ghana TV's evening news to accept the new price hikes. He said the increment had become necessary because, international crude oil prices had risen close to 80 dollars per barrel, outstripping local retail prices by several percentage points and thus necessitating an upward adjustment.

But even before Dr. Attafuah's explanation, his counterpart at the Ghana Energy Commission, Dr. Ofosu Ahenkorah had predicted in May this year that because of the political wrangling in the Middle East and the U.S. tango with Tehran, oil prices could record an all time rate of 100 dollars per barrel before the year closes, the Public Agenda newspaper said.

The oil price hike in Ghana needs be viewed against the backdrop that levies which are currently in place include Debt recovery levy, Road Fund levy, Energy Fund Levy, Exploration levy, Strategic Stock levy, Social Impact Mitigation Levy, Cross subsidy levy. It is these levies, which have been the bone of contention between the NPA and the New Patriotic Party administration on the one hand, and the Committee for Joint Action (CJA) on the other.

According to the CJA, if these levies are lifted, fuel prices need not go further beyond about 3.2 dollars a gallon. The group agrees though, that because Ghana imports all its crude oil requirements, rising oil prices would have adverse consequences on Ghana's balance of payments and the economy. But it thinks there are options.

The immediate option available to Ghana; according to the group, is for the country to be efficient in the use of petroleum products. Over 75 percent of vehicles in Ghana are private cars and consumers can positively impact the situation if they change their consumption habits. Vehicle maintenance and adherence to speed limits have immediate impacts.

The use of mass transport will also contribute to a reduction in fuel consumption nationwide as more people can use the same bus or train to get to places as compared to the use of individual vehicles.

In the medium to longer term alternative fuels such as bio diesel and alcohol should be developed for use in the transport sector. The most promising alternative fuel is Compressed Natural Gas (CNG) which can be developed as quickly as 2007 when natural gas from Nigeria becomes available through the West Africa Gas Pipeline, the Public Agenda newspaper said.

The newspaper pointed out that in the face of rising oil prices, Ghana will have to find more dollars to purchase the same quantities of oil from exporters. "This will surely bring stress on our foreign exchange earnings. The limited revenue generated will have to be distributed fairly among development projects," the Public Agenda said.

The Ghanaian Chronicle newspaper quoted U.S. billionaire Jim Rogers -- a former partner of the internationally respected billionaire philanthrop George Soros -- stating that the commodity would not drop any lower for the next decade at least, meaning that countries like Ghana which is not an oil producing nation would be buffeted by more shocks.

"We're going to have high oil prices for a very long time. The surprise is going to be how high it goes," Rogers said. Repeating his comments, he noted "It will be much more than 100 dollars before the bull market is over." In London, Brent North Sea crude for August delivery slid 23 cent to 73.75 dollars per barrel in electronic trading. Rogers has predicted the commodities bull run has at least 15 years to run.

"It's a major long-term bull market as far as I'm concerned," he was quoted as saying. Aside from the bullish impact of tensions, described by Rogers as temporary, over Iran's nuclear ambitions and North Korea's missile tests, he said oil was drawing long-term support from the lack of large scale finds. **– Kofi Danso**

ENJOYING BOOM – WITH RESTRAINT

Doha - The Middle East is in the midst of an oil boom evocative of the 1970s and 1980s, but this time, instead of spending most of their profits, oil producing countries are managing the windfall with restraint.

A new World Bank report finds that oil producers are increasingly turning finite oil wealth into longer-term revenue streams. They are also showing fiscal restraint by building up savings, paying down debt, and setting up oil stabilization funds, says a new World Bank report, *'MENA Economic Developments and Prospects 2006: Financial Markets in a New Age of Oil'*. The report is the second in a new series of annual reports on economic developments in the Middle East region.

The oil producers' behaviour differs from that of previous oil booms, when they built up debt and banked on continued high oil prices to fuel their expansion. When the oil price declined, many were caught with large debts. This time, "there's a realization that they can't do things as before," says Jennifer Keller, Senior Economist in the Office of the Chief Economist for the Middle East and North Africa Region and principal author of the report.

Saudi Arabia, for instance, has reduced domestic debt from 97 percent of GDP in 2002 to 41 percent by the end of 2005. Over the same period, it turned a fiscal deficit of almost 6 percent of GDP to a fiscal surplus of 8.4 percent of GDP by 2005, according to the report.

The report notes increasingly close ties between the price of oil and the growth outcomes among the oil-rich, labour importing countries, a fact that was not always the case in prior oil booms. Because countries are adopting largely similar development strategies, they are now experiencing a "common growth effect."

Oil exports of oil-rich, labour-importing countries -- Saudi Arabia, United Arab Emirates (UAE), Kuwait, Qatar, Libya, Oman, and Bahrain -- more than doubled in the last three years, growing from 186 billion U.S. dollars in 2002 to 440 billion dollars by 2005.

At the same time, their economies grew by an average 7 percent in 2005, boosting the region's growth rate to 6 percent, up from 5.6 percent in 2004, and 3.5 percent in the late 1990s, says the report. The economies of oil-rich, labour abundant countries -- Algeria, Iran, Syria and Yemen -- also had healthy growth rates of between 5 and 6 percent.

But the boon to oil producers did not fully translate to resource-poor economies in the region, says the report. Egypt, Djibouti, Jordan, Lebanon, Morocco, and Tunisia averaged 4 percent growth, with Morocco's growth rate falling from 6.3 percent in 2004 to 1.5 percent in 2005, and Lebanon's economic growth collapsing to 1 percent from 6 percent in 2004. Compared with past oil booms, the resource-poor economies are not enjoying as many spill over effects from the high price of oil. In fact, the report finds that the relationship between economic growth of these countries and the price of oil has weakened substantially.

The reasons include less aid from oil-rich countries, fewer job opportunities for Arab laborers in the Gulf, and less money flowing from oil rich countries to resource-poor countries. In addition, the resource-poor countries are using more energy than they did 20 or 30 years ago, and must import greater amounts of more costly oil. And like all countries in the region, they maintain oil subsidies that keep the price of gas and diesel well below market prices.

The cost of oil subsidies in Jordan, for example, doubled between 2004 and 2005 -- from 3.1 percent of GDP and 11.3 percent of total expenditures, to 5.8 percent of GDP and 19 percent of current expenditures, according to the report.

"Oil subsidies are a drain on all the economies of the Middle East region, but are often politically difficult to abandon," says Mustapha Nabli, Chief Economist for the Middle East and North Africa Region.

"And rising oil revenues seem to be delaying plans to reform subsidy systems in several countries," he notes, including Saudi Arabia, which recently cut the price of gas and diesel by 30 percent to offset the effect of equity market declines.

Reform in other areas, however, is progressing throughout the region, the report says. The resource-poor countries reformed their business and regulatory environments and now rank in the 63rd percentile in those areas worldwide. These countries also took steps to liberalise trade, notes the report.

The region as a whole is making progress in reforming governance structures to be more accountable and inclusive. In fact, over the 2000-2005 period, it ranked in the 64th percentile in terms of progress, though the region remains at the bottom internationally in this area, the report says. Bahrain, Oman and Qatar, in particular, have taken steps to allow greater participation in public policy, notes the report. Progress on the governance front is important, says Keller, "because it has implications for the overall reform effort." **– Najeeb Hamdi**

PRICE HIKE DOUBLES GULF STATES' RESERVES

Dubai – Much to their satisfaction, the six Gulf States -- UAE, Saudi Arabia, Kuwait, Qatar, Bahrain and Oman -- have accumulated reserves worth about 145.1 billion U.S. dollars because of a sharp increase in oil prices in the past five years.

This was a boost of 70 billion dollars on 75.1 billion dollars by the end of 2000. Latest data show that the bulk of the reserves are controlled by the UAE and Saudi Arabia while the remaining members also reported large increases.

From nearly 14.5 billion dollars at the end of 2000, the UAE's cash reserves soared to a record 23 billion dollars at the end of 2005 while in Saudi Arabia the reserves jumped from 46.2 billion to 101.1 billion dollars during the same period.

The reserves swelled from 8.8 billion to 9.5 billion dollars in Kuwait; 1.3 billion to 4.9 billion dollars in Qatar; about 2.7 billion to 4.1 billion dollars in Oman and 1.6 billion to about 1.7 billion dollars in Bahrain, according to a report in the Gulf News.

The surge followed a sharp rise in the oil export revenues of six countries that form the Gulf Cooperation Council (GCC) because of higher production and a rally in crude prices, which averaged about 52 dollars a barrel in 2005 compared with 36 dollars in 2004 and 25 dollars in the previous three years, the UAE's Gulf News daily reported.

According to the Organisation of Arab Petroleum Exporting Countries (OAPEC) located in Kuwait, the GCC's oil revenues climbed to one of the highest levels of about 252 billion dollars in 2005 from nearly 115 billion dollars in 2000. The oil proceeds are expected to go up further to a record 300 billion dollars this year as crude prices are projected to average above 60 dollars a barrel and member states are pumping at near capacity.

A sharp decline in oil prices in the mid-1990s combined with heavy payments for the liberation of Kuwait in 1991 depressed the GCC's financial reserves to one of the lowest levels of less than 30 billion dollars. Saudi Arabia was the main victim as its financial reserves tumbled to about 5 billion dollars at the end of 1995.
– Jyotindra Srivastava

Coffers				
Saudi Arabia and UAE dominate (Figures in billion dollars)				
Country	**2000-02**	**2003**	**2004**	**2005**
UAE	14.5	15.1	18.6	23
Saudi Arabia	46.2	59.8	86.8	101.1
Kuwait	8.8	7.7	8.4	9.5
Qatar	1.3	2.9	3.4	4.9
Oman	2.7	3.6	3.6	4.1
Bahrain	1.6	1.5	1.7	1.7

Source: Gulf News

[Continued from page 1]

Analysing the country situations in detail, the paper points out:

- For 16 countries -- close to 30 percent of PRGF importers -- there was a decline in the oil import bill relative to GDP owing to what appears to have been a particularly sharp contraction in the volume of oil imports. The oil price rise did not lead to an adverse impact on the balance of payments for this set of countries, as they saw improvements in both the current and capital accounts during 2003-2005 that translated into a strengthening of the reserve position.
- Another 12 countries faced higher oil imports, expressed in relation to GDP, but benefited from substantial current account offsets in the form of improved exports, services, and/or grant receipts. Together with gains in the capital account, this subgroup also saw a strong overall improvement in the reserve position.
- For a third category of 12 countries, they faced both higher oil imports and a worsened current account, but a substantial improvement in the capital account allowed for a net improvement in the reserve position.
- The remaining 22 PRGF importers benefited from neither current account nor capital account improvements sufficient to offset the oil shock and thus saw a deterioration in their overall reserve position. Within this group, however, a majority of cases maintained relatively comfortable reserve coverage levels and could thus accommodate the drawdown in reserves.

Only in seven countries did reserves fall to very low levels: two of these (Bangladesh and Madagascar) requested a PRGF augmentation; three (Cambodia, Djibouti, and Tajikistan) are in the process of moving towards a PRGF arrangement; and the remaining two (Kiribati and Zimbabwe) have no PRGF prospects at present.

Looking ahead, the economists warn that the impact of bigger oil price hike in 2006 will be more adverse than in the past three years: "In particular, there may be little room for further compression of import volumes of petroleum products without some negative impact on growth. At the same time, if countries do not adjust, and higher imports of petroleum products lead to a loss of reserves, additional countries could be more vulnerable."
– Ramesh Jaura

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