

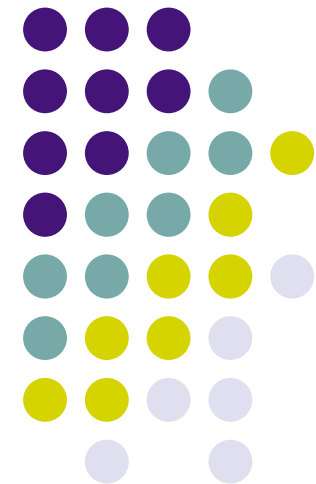
Appropriate Fiscal and Macroeconomic Policy Responses to Resource Revenue Management

Enhancing the Development Impact of Resources Industries Through the Effective Use of Revenues and Corporate Social Responsibility Investments

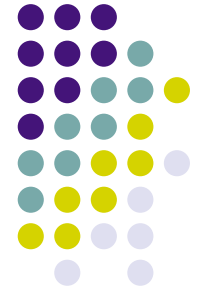
Maputo, Mozambique, March 25, 2009

Teresa Dabán
Fiscal Affairs Department
International Monetary Fund

The views expressed herein are those of the authors and should not be attributed to the IMF, its Executive Board, or its management.



Outline of the Presentation



Part 1

- The specific advantages and challenges of resources revenues: the “resource curse”
- The policy prescriptions to prevent the resource curse
- Difficulties in preventing the resource curse.
- A Public Financial Management Framework for Resource Revenue Management

Part 2

- Response of oil-producing countries to the recent oil boom and sharp fall in oil prices.

The specific advantages and challenges of resource revenues



Advantages: the “blessing”	Challenges: the “curse”
<ul style="list-style-type: none">●A “gift from nature”: discovery of a non-financial asset●Improve the government’s net worth and financial envelop●No conditionality●Enclave nature: independent of the country’s economic, political, and institutional processes (e.g. Angola, Colombia).	<ul style="list-style-type: none">●Large foreign-currency denominated inflows●Volatility and uncertainty●Depletion of a non-renewable, temporary, exhaustible asset●Excessive dependence on resource revenues

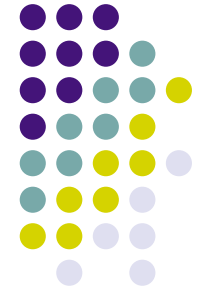
If the large, uncertain and volatile resource revenues lead to increases in spending...



Dutch disease ► if mainly spent on domestic goods and services: inflation, RER appreciation, erosion of competitiveness, etc (e.g. Nigeria, Equatorial Guinea, etc)

Waste ► frequent and sudden upward and downward adjustments of expenditures would put pressure on the country's administrative capacity.

Excessive borrowing ► government difficulties to cut expenditures during busts; countries tendency to over-borrow during booms (e.g. Mexico, Angola, Nigeria)



Non-renewable, temporary, and exhaustible resource revenues could also lead to...

Sustainability ► resource revenues would not last for ever; there is a need to adopt an “exit strategy” and build a “resource buffer”.

Intergenerational equity ► resource revenues are derived from depleting the country’s net wealth; they could be allocated to other forms of capital (physical, human, or financial).



An excessive dependence on resource revenues could give rise to...

Rentier mentality ► resource-rich countries tend to become unaccountable to their citizens and less prone to political competition (Moore, 2004).

Inefficient redistribution mechanisms ► large wasteful and “prestige” investment projects, inefficient public enterprises, low-quality spending programs (e.g. subsidies to failing industries) and overstuffed civil services.

Lack of incentives to build or preserve strong institutions ► such as tax administration, business regulation, supervision, relationships with international community, and political competition, etc (e.g. Saud Arabia).



What are the policy prescriptions to prevent the “resource curse”?

Prudent fiscal policy ► sustainable path for the non-resource deficit over the medium-term according to the country’s absorptive capacity (macroeconomic and administrative).

Sustainable long-term fiscal strategy ► alternative compositions of the non-resource deficit overtime: frontloading spending, cutting taxes, paying back debt, building financial assets, etc

Development of a sound institutional framework

► a robust Public Financial Management (PFM) framework including sound budget procedures and robust accountability, transparency mechanisms.



A few successful stories...

USA, Australia, Canada, Scandinavia ► efficient governments, robust political institutions, and strong positive spill-over from the resource to the non-resource sector.

Botswana, Namibia, Chile, Ghana, South Africa, Trinidad e Tobago, Indonesia, Malaysia ►

- (i) sound pre-existing institutions
- (ii) predictable legal framework
- (iii) effective medium-term hard-budget constraints
- (iv) government effectiveness

Why the prevention of the “resource curse” is so difficult?



Unfavorable pre-existing economic and institutional conditions of some resource-rich countries ►

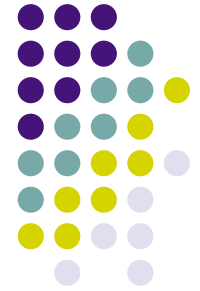
- Weak separation of powers
- Lack of an effective political competition
- Absence of a robust PFM system and a sound public administration
- Huge expectations
- High and persistent resource dependence, reflecting low non-resource revenues, poorly diversified economy, etc.



Why the prevention of the “resource curse” is so difficult?

Proliferation of “parallel” off-budget and rule-based mechanisms for the management of resource revenues ►

- Earmarking frameworks (fragmentation of budget)
- Special “parallel” budget and treasury procedures
- Non-realistic rules (complex, procyclical, difficult to enforce).
- Ill-defined oil funds (as an institution, separated account, etc)
- Separated investment and oversight committees (difficult to staff and are not really independent)
- Convoluted resource-revenue legal frameworks.



What is the rationale of adopting “parallel” management mechanisms?

The need to...

- crystallize public support for policies, especially in countries with weak institutional framework.
- bypass the existing institutional framework, by implementing quickly a set of “parallel” management mechanisms
- carve out a space within the public sector in which the appropriate budgetary mechanism could be put to work on a highly visible way.
- start reforms in a stand-alone separate body or procedure, instead of reforming the whole PFM system.



What are the risks of using “parallel” management mechanisms?

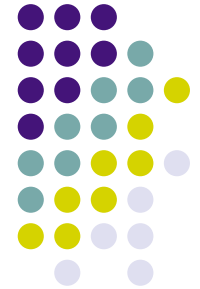
Increased opportunity of misappropriation and mismanagement, especially in countries with high concentration of power.

Fragmentation and delay of the budget process, especially in countries with poor sharing-information practices

High administrative costs, reflecting the differentiated and sometimes privileged bureaucracy of the “parallel” bodies.

Lack of incentive for reforming existing budgetary institutions, with which the “parallel” bodies compete

A PFM framework for the management of resource revenues



- **Transparent budget formulation.** Realistic revenue projections, sustainable long-term fiscal strategy, a realistic medium-term fiscal framework, and the emphasis on the non-resource deficit as the main fiscal policy anchor.
- **Sound budget execution.** Flexible and transparent transfers from the Treasury Single Account to finance the non-resource deficit, unified and integrated budget execution process, and a sound cash-management mechanism.
- **Sustainable and integrated asset-liability management strategy.** e.g. consistency between oil buffer and debt policy
- **Reinforced transparency and accountability mechanisms.** EITI, IMF's Guide on Resource Revenue Transparency, special selected reporting and auditing mechanisms.

The 2003-2008 oil boom—“...haven't we seen this movie before?”

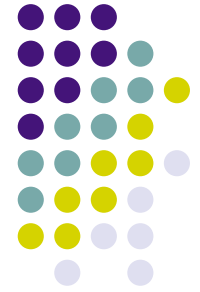
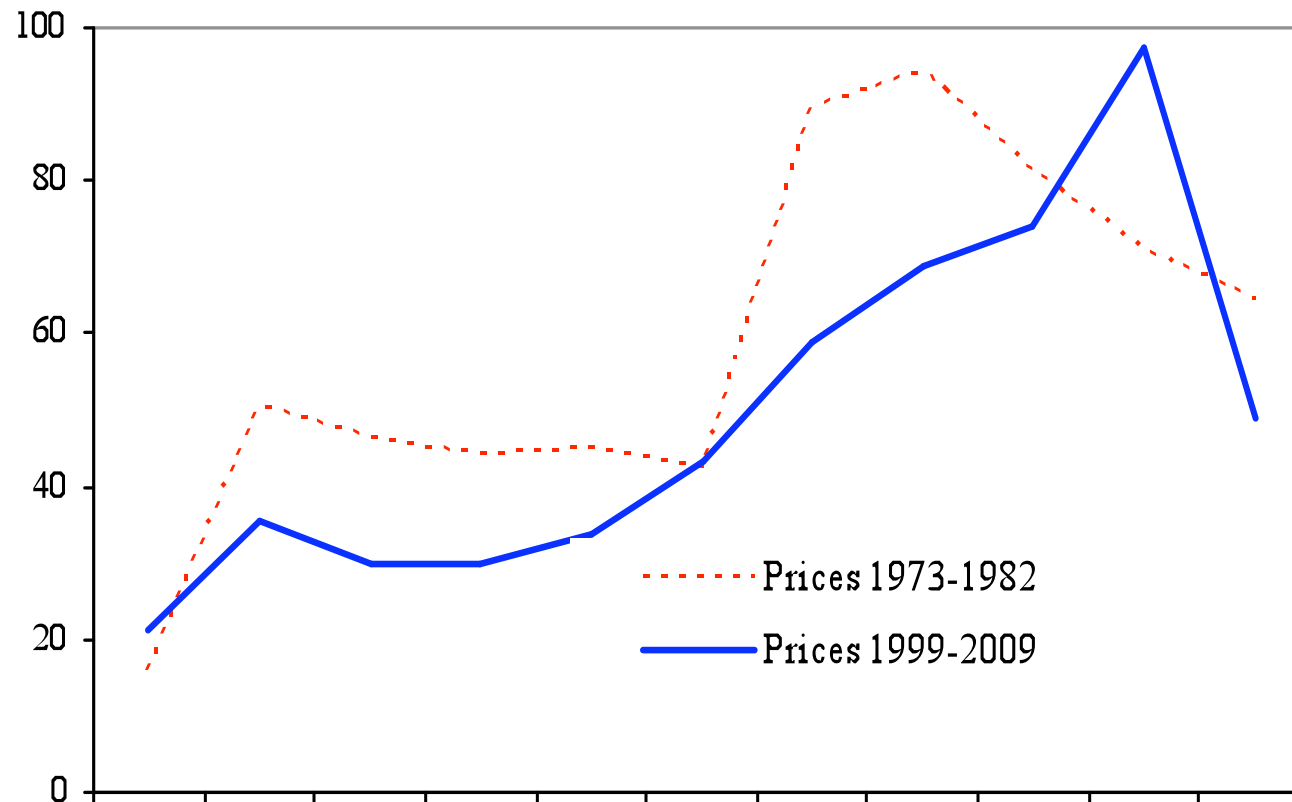


Figure 1. Real Oil Prices
(US\$ per barrel at 2008 prices, IMF WEO basket)



Overall fiscal balances have improved...with some differences

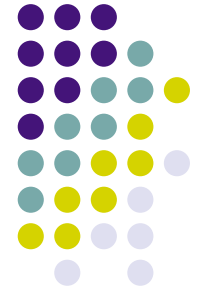
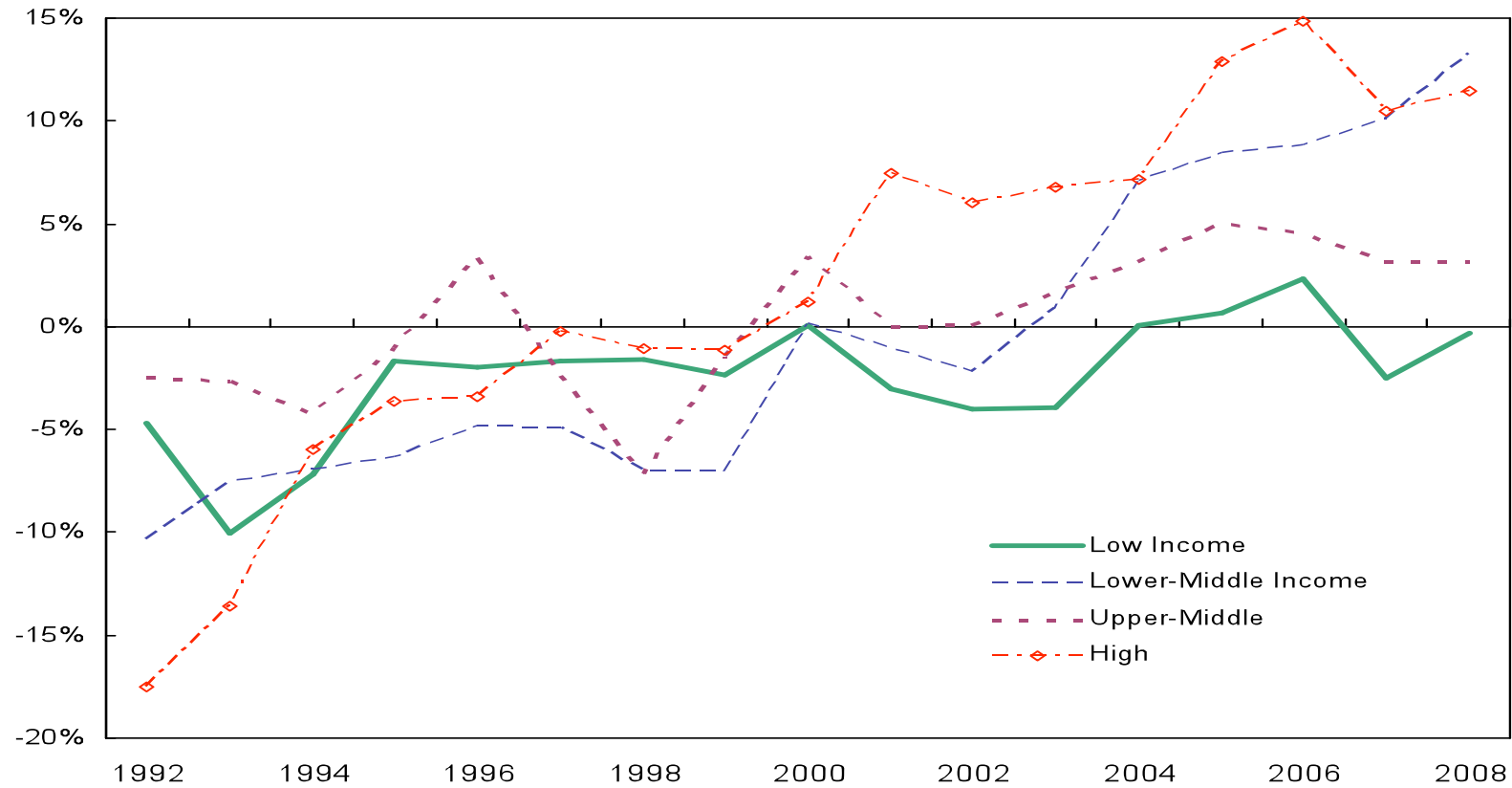
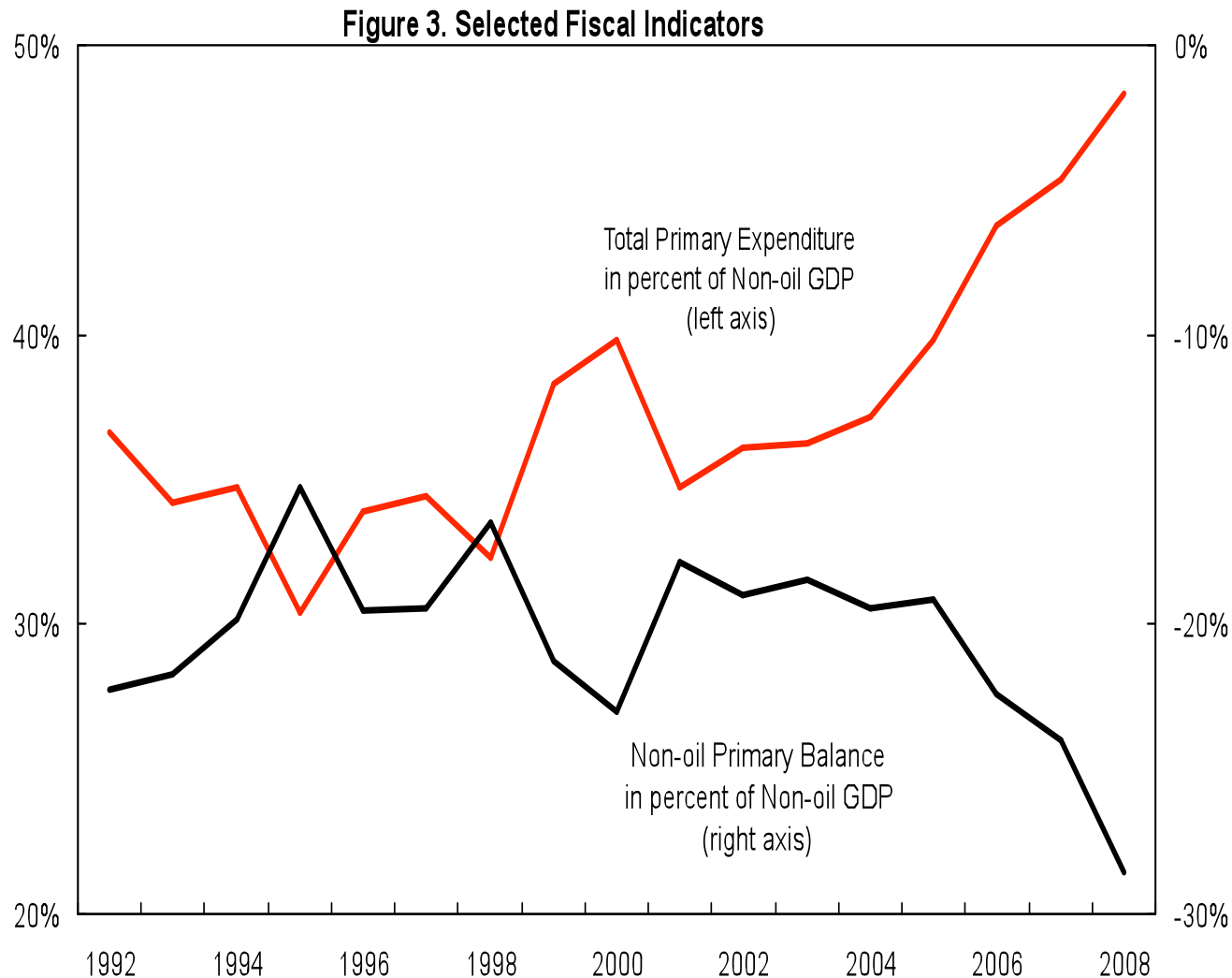


Figure 2. Overall Balance in percent of GDP, by Income Classification



The oil boom has led to higher spending and non-oil deficit



How the oil boom has been spent? Capital spending has accelerated

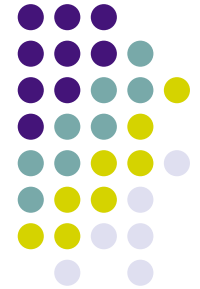
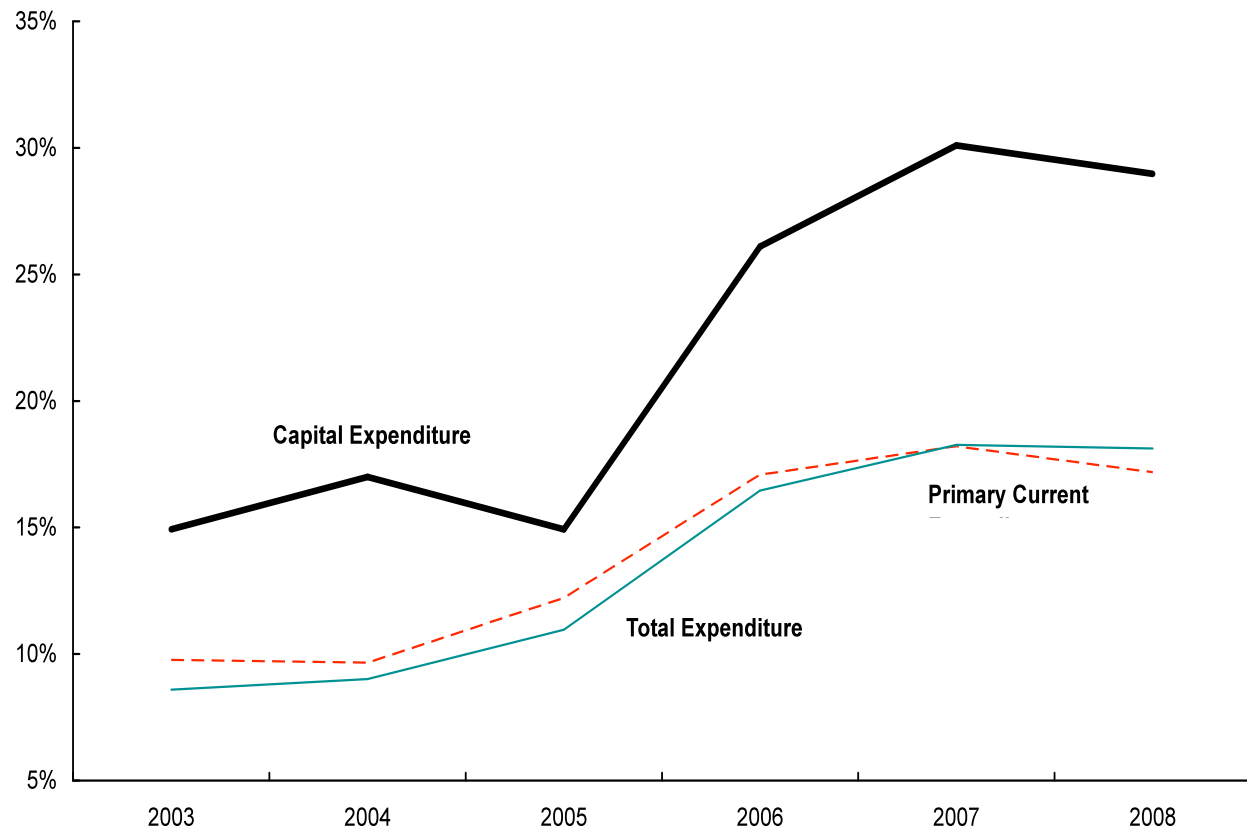


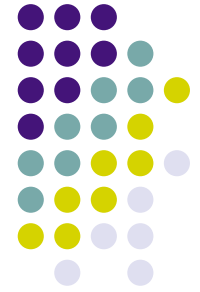
Figure 4. Total, Primary Current and Capital Expenditure
(Rate of growth in real terms, three-year moving averages)

However,

- Quality?
- Sustainability?
- Vulnerability?



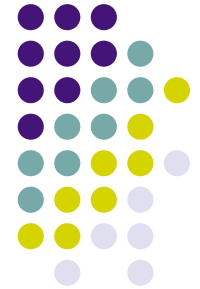
Sources: IMF country documents and Fund staff estimates.



Are countries adjusting to the recent fall in oil prices? Not much...

- **No adjustment** (Algeria, Congo)
 - Draw-down of reserves; domestic borrowing
- **“Wait-and-see”** (Angola, Azerbaijan)
 - Some very initial consideration of cutting *capital investment*
- **Revenue sharing as “adjustment”** (Nigeria, Sudan)
 - Outcome depends on how subnationals react
 - Lack of transparency / predictability may be a concern
- **Major adjustment in some vulnerable countries** (Chad, Yemen)

Looking forward, ...most countries would need to adjust to ease pressures on reserves and domestic financing



Clear and credible adjustment plan (with country-specific *pace and composition*)

Expenditure adjustments (in a medium-term context)

- Wage restraint (*possibly reversal*)
- Action on fuel pricing/subsidy regime
- Strict prioritization of capital spending (*ongoing & new projects*)

Efficiency-enhancing improvements to non-oil revenue regime

Growth-enhancing (non-oil) structural reforms

Exchange rate adjustment (*in some countries*)

...with support from the Bank and Fund



Thank you!