Nigerian Oil Savings Fund Requires Strong Protections

To promote sustainable economic development, the government of Nigeria is considering the creation of a Sovereign Wealth Fund, a savings tool that could protect against the volatility of the country's main revenue source: oil. But, according to new analysis by the Revenue Watch Institute (RWI), Nigeria risks repeating patterns of weak economic governance and volatile spending unless its new Fund features certain safeguards.

Sovereign Wealth Funds enable resource rich countries to save windfall profits when commodity prices are high, and soften the negative impact of price volatility. As researcher and Nigeria expert Alexandra Gillies explains in the Revenue Watch analysis, if Nigeria's leaders are to create a Fund that is more effective than existing fiscal policies, the Fund needs a solid legal standing, binding rules regarding the inflow and outflow of funds, and strict transparency requirements.

"The politics of Nigeria call for a carefully safeguarded Fund," said Gillies. "Without strong and transparent governance, a new fund will end up as depleted as the current Excess Crude Account."

Nigeria's Excess Crude Account (ECA) was created to save windfall profits from periods of high oil prices. However, per-

missive governance structures have allowed extensive ad hoc withdrawals, reducing the ECA balance by almost 85%, or 16 billion dollars, in just 18 months. The account's depletion is among the reasons why Nigeria's National Economic Council and Ministry of Finance are considering alternative stabilization programs such as an SWF.

"If the Fund has a clearly-defined relationship to the constitution and operates transparently, Nigeria can avoid the longstanding challenges to savings that arise from competition for resources among the federal, state and local governments," said Gillies.

The RWI analysis was released today in partnership with Nigeria-based think tank Centre for the Study of Economies of Africa (CSEA). Menachem Katz, Director of CSEA said, "Stabilization of Nigeria's economy against oil price volatility remains a crucial priority and a precursor for development and economic diversification."

"Nigerians understand that we must diversify our economy and move past our unenviable legacy of oil dependence," said RWI Nigeria Program Coordinator Dauda Garuba. "This Fund can help us build a stronger economic future, but it will only succeed if it is aligned with the constitution and accompanied by a sound policy framework."

Iraq looks to spectacular oil boom to revive its political fortunes

Patrick Cockburn. The Independent.

What is being called the great Iraqi oil rush has gained momentum in the wake of BP's Gulf of Mexico disaster. THE MAP of the world's main energy suppliers is about to change as Iraq's oil output quadruples over the next 10 years according to new forecasts. Iraq will eventually displace Saudi Arabia as the world's biggest exporter, experts predict, giving Baghdad crucial influence over the future price of oil.

The rush to exploit Iraq's "super-giant" oilfields, of which it has the largest concentration in the world, has gathered impetus with unexpected speed in the wake of BP's disaster in the Gulf of Mexico which has raised fears over deep-sea drilling. Iraq's oil has the advantage of being both onshore and cheap to develop.

Iraq, by contrast, aims to raise its crude production from 2.5 million barrels a day today to 9.5 million in 2020 under contracts signed with the world's biggest oil companies over the last 12 months. This development should be feasible, experts believe, because the rise in production will come from improved exploitation of oilfields already discovered rather than from the discovery of new ones.

The outcome of what is being called "the great Iraqi oil rush" will inevitably transform the balance of power between oil-producing states with Iraq the winner. Dr Leo Drollas, chief economist of the London-based Centre for Global Energy Studies, who has produced the first comprehensive study of the impact of the new Iraqi contracts and the consequences of an accelerated oil rush over the coming years, predicts that "the evolution of Iraq's oil capacity over the next 10 years promises to be the most important issue confronting Saudi Arabia in particular and Opec and the oil industry in general."

Dr Drollas says: "Saudi Arabia will only meet its revenue needs if Iraq wholly fails to meet its production plans." Given that Opec has more capacity than it needs to meet demand, increased Iraqi output will drive down the price of oil.

The development of Iraqi oil at breakneck pace started when the Iraqi government awarded 11 service contracts in two rounds of bidding to international oil companies such as BP, Royal Dutch Shell and Exxon last year. At the first auction last summer many companies held back or had their bids rejected as too costly, but at a second round of bidding at the end of the year there was a rush to sign up by more than 20 companies. Much of the world's oil industry felt that Iraq's oilfields represent a once-in-lifetime opportunity they could not ignore.

At stake are some of the biggest oilfields in the world. Rumaila oilfield just north of the Kuwaiti border, for example, is expected to produce 1.85 million barrels a day, West Qurna 1, north of Basra, 1.84 million and Majnoon, in the salt marshes on the Iranian border, 1.3 million. Increased Iraqi output will total 7.5 million, far in excess of the expected increased production capacity of all of the rest of Opec.

The sums of money involved are also huge. This week Shell signed a $12.5bn natural gas production venture with Iraq. The companies developing Iraq's oil, for which they are paid a fee per barrel and do not get a share in production, will spend $100bn over 10 years according to Iraqi oil minister Hussain Shahristani. He adds that Iraq itself should benefit by $200bn.

It has long been known that Iraq has vast oil reserves, mostly in the south of the country around Basra, but these have been under-exploited because international oil companies were locked out of Iraq after the nationalisation of oil by Iraq in 1972. The Iraqi government did not have the resources to develop its own oil industry at a necessary pace in the 30 years of war and sanctions following the start of the Iran-Iraq war in 1980.

But staff from the giant oil companies have been pouring into Basra recently, establishing expensive headquarters in the city. Visiting diplomats said they were impressed with the speed with which the oil giants are moving to develop the Rumaila field in particular. At the heart of the current excitement is that there may be more oil under the sands of southern Iraq than almost anywhere else on the planet. The country has 115 billion barrels of proven reserves but there may be up to another 100 billion barrels under the Western Desert where there has been little exploration.

This is on top of oil and gas reserves already discovered. These include nine "super-giant" fields (over five billion barrels) and 22 known "giant" fields (over one billion barrels). The US Department of Energy, citing independent consultants, says the cluster of super-giant fields in south-eastern Iraq forms "the largest known concentration of such fields in the world and accounts for 70 to 80 per cent of the country's proven oil reserves". A further 20 per cent of Iraq's oil is around Kirkuk where it is a source of continuing dispute between the Kurds, the local Arabs and the government in Baghdad. Iraq badly needs more oil revenues which last year were around $60bn. This was underlined in June by riots and demonstrations over the lack of electricity as summer temperatures reached 50C. The Electricity Ministry says it needs $5bn a year to build new power stations and fix old ones but it gets a maximum of $1.2bn a year.

The rest of the Iraqi infrastructure is in the same state. For 10 years after 1980 Saddam's government spent all its money on weapons and from 1990 until its overthrow it did not have much money because of sanctions. No new hospitals were built after the early 1980s. Power stations grew so old that spare parts were no longer manufactured. Much of Iraq does without clean drinking water and raw sewage often goes straight into the Tigris or Euphrates. Restoring this derelict infrastructure will be costly.

Not that money alone will solve all of Iraq's problems. Government administration is dysfunctional and corrupt. Basic needs can often only be acquired by bribery. In one recent case, a pregnant woman who taught at a Baghdad university applied for a month's paid leave as was her right. The university administrators informed her that they would reject her request unless she paid them a month's salary.

The incapacity and corruption of government helps explain why so little has been done to rebuild Iraq seven years after the fall of Saddam. A significant proportion of state revenues are spent on salaries and pensions because the state acts as a giant patronage machine in which its supporters get jobs regardless of ability. This is one way of distributing oil revenues, though an unfair one, that is unlikely to change, so money for investment requires higher oil revenues.

Whatever happens politically in Iraq the development of its oil reserves can only gather pace. It is the one trump card held by the embattled government in Baghdad and it is bound to play it. Most of the oil discovered hitherto is in the Shia heartlands around Basra where there has been little fighting so continued violence in Baghdad and Mosul will not stop the oil rush.

Energy subsidies issue is heating up

By SYED RASHID HUSAIN | ARAB NEWS

The issue of energy subsidies is heating up. The cards are out, positions are being redefined and bargaining is in process. A concerted effort is on to get this anomaly to the maximum possible and the issue was mentioned at the just-concluded G20 summit in Toronto too.

The final communiqué at the end of the G20 summit in Toronto not only noted with appreciation the report on energy subsidies from the International Energy Agency, OPEC, OECD and the World Bank combined, but also welcomed the work of the finance and energy ministers "in delivering implementation strategies and timeframes, based on national circumstances, for the rationalization and phase out - over the medium term - of inefficient fossil fuel subsidies that encourages wasteful consumption, taking into account vulnerable groups and their development needs." The IEA, OPEC and the World Bank report on fossil fuel subsidies was prepared at the request of the previous G20 summit in Pittsburgh.

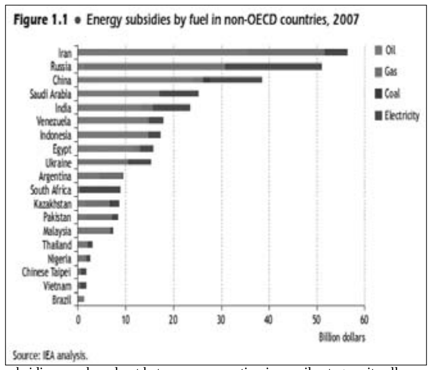
The G20 also encouraged, "full implementation of country-specific strategies," and insisted on continuing to "review progress toward this commitment at upcoming summits."

This "first exhaustive study of the financial assistance devoted to oil, natural gas and coal consumption" reported countries spend more than $550 billion in energy subsidies a year, about 75 percent more than previously thought. It emphasized that phasing out subsidies over the medium term, as agreed last year by the G20, would trigger vast savings in energy consumption and carbon dioxide emissions.

As per the report, in 2008 alone - the latest year for which data is available - 37 large developing countries spent about $557bn in energy subsidies. This represented a big increase from $342bn in 2007. The IEA says the 37 countries surveyed for the report, spent on average about 2.1 percent of their GDP on energy subsidies. Iran, Russia, Saudi Arabia, India and China were among the top countries spending on energy subsidies.

Fatih Birol, the chief economist at the IEA, believes removing subsidies was a policy that could change the energy game "quickly and substantially."

The IEA estimated that energy consumption could be reduced by 850 million tons equivalent of oil - or the combined current consumption of Japan, South Korea, Australia and New Zealand - if the



subsidies are phased out between now and 2020. The consumption cut would save the equivalent of the current carbon dioxide emissions of Germany, France, the UK, Italy and Spain. Subsidy critics say they encourage wasteful consumption, reduce global energy security, impede investment in clean energy sources and undermine efforts to deal with the threat of climate change.

They also claim that subsidies are a burden to national budgets, with spending on financial support to oil, natural gas and coal at times larger than education or health spending.

Interestingly Saudi Arabia is on the list of the countries that spend most on subsidies. Indeed Saudi Arabia can boast being a country with the cheapest petrol on earth and plays a definite role in keeping oil prices low for common consumers on the street. Riyadh has reasons for this, as it is one way of sharing the Kingdom's energy resources with the common masses - a considerable number of whom are definitely poor.

Then there are also economic reasons for keeping fuel prices low in the country. Low fuel prices keep inflation under tab. If petrol prices go up then inflation increases, something that affects the common masses as it does in other parts of the world. This is a social issue and cannot and should not be overlooked altogether.Yet one cannot deny fuel subsidies promote wastefulness and there are manifestations of it in society everywhere, something one cannot deny. Indeed, with public transport lacking in the real sense, people tend to depend on private vehicles, gas-guzzlers, something that is contributing to the skyrocketing demand pattern.

The Kingdom has also been increasingly burning crude oil to generate power, particularly in the summer months. The IEA classifies "direct crude" burnt for power generation in an oil category it calls "other products." Saudi consumption of other products rose by 58.7 percent last year, the agency noted.

According to revealed data, total Saudi domestic energy demand is expected to rise from about 3.4 million barrels per day of oil equivalent in 2009 to approximately 8.3 million barrels per day of oil equivalent by 2028 - a growth of almost 250 percent. Saudi Arabia has emerged as the second-biggest source of global oil demand growth after China.

This growing Saudi consumption is a cause of concern - conceded, highlighted and acknowledged by none other than Khalid Al-Falih - the czar of Saudi oil. This is a real challenge to planners here in Riyadh. Many in IEA strongly underline that subsidies promote wastefulness. It encourages inefficiencies too. Al-Falih acknowledges this warning that unless Saudi Arabia tackles inefficiencies in the way it uses energy, the Kingdom's availability of crude to export risks falling by as much as 3 million barrels by 2028 to 7 million barrels a day.But supporters, including some G20 members, who reluctantly signed the statement last year such as India, say subsidies are needed to help poor people in developing countries and control inflation.The issue is a divisive one. It exhorts emotions. It has it pros and cons. Inefficiency needs to be tackled. Wastefulness cannot and should not be encouraged yet social aspect could not be overlooked. This is imperative too.

The G20 has finally felt the need; allowing member countries to take into account "the national circumstances, needs of vulnerable groups and the development needs of the societies." The road to success is through compromise and bargaining only. One needs to strive for a middle point accommodating both views; one cannot help underlining at this stage.