



# Angola and the oil price shock

**Angola Field Group, February 5, 2015**

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# Remember

**Angola is not rich**

**It is a post-conflict country that is rapidly extracting its limited (known) oil reserves**

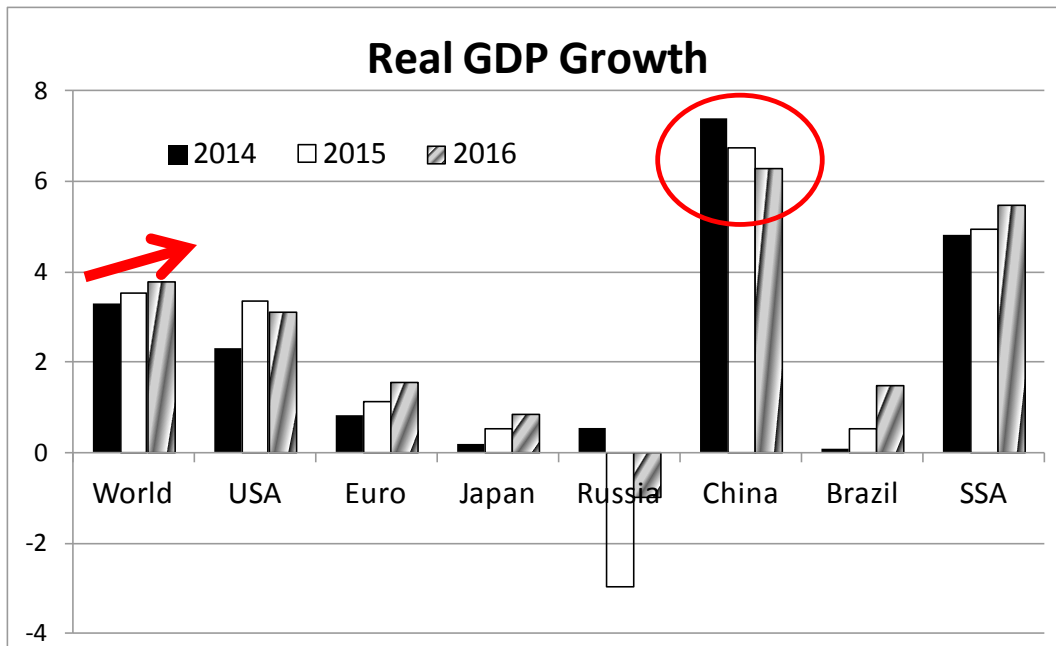
**It faces the challenges of both**



# External environment

# World growth slower than expected

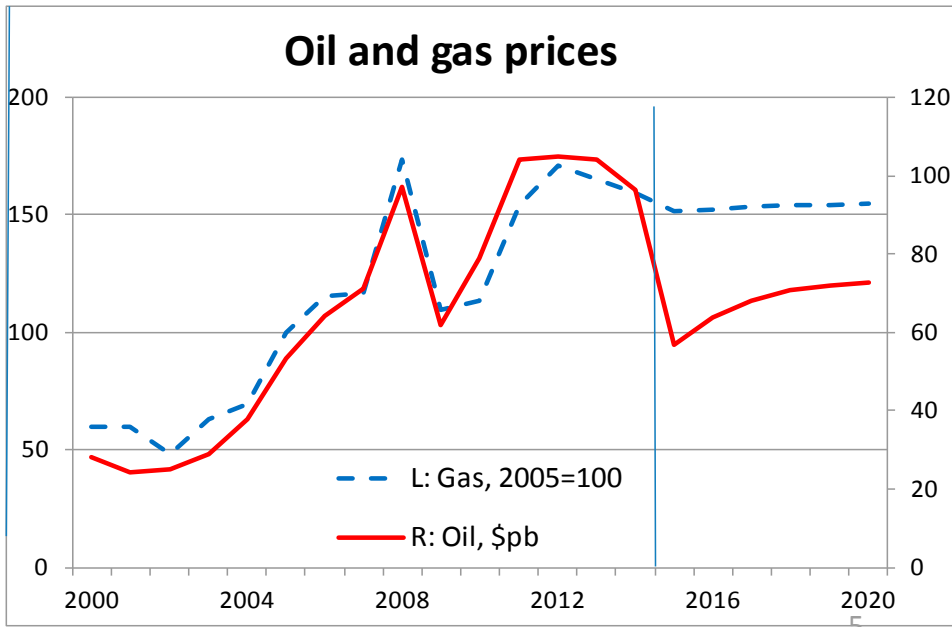
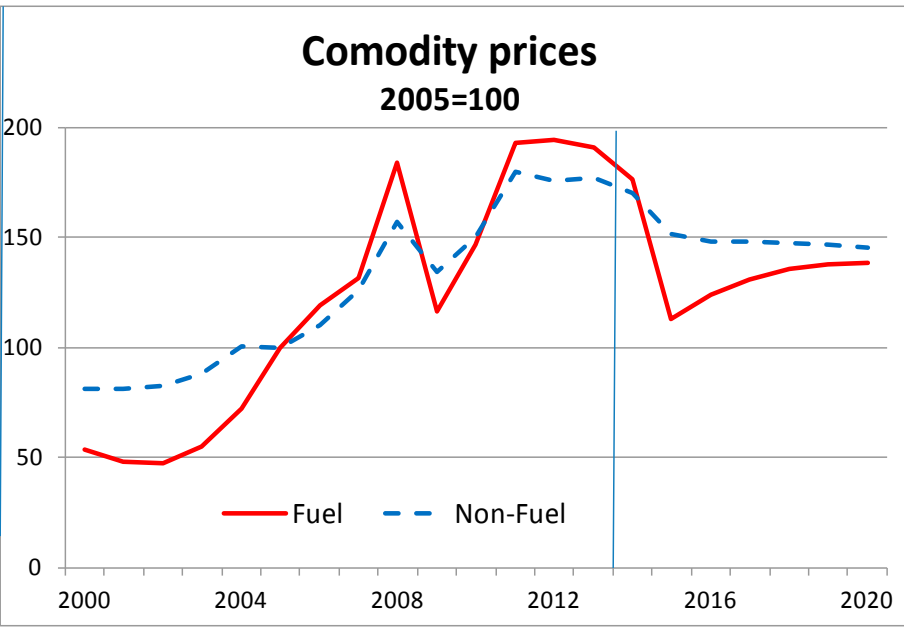
- ❑ US economy stronger than expected, but Euro area remains weak and China slowing down.
- ❑ Global growth projected to accelerate, but more slowly than expected.
- ❑ Growth projections keeps being reduced.



	2014	2015	2016
Apr-13	4.0		
Oct-13	3.6		
Apr-14	3.6	3.9	
Oct-14	3.3	3.8	
Jan-15	3.3	3.5	3.8

# Pushing down commodity prices

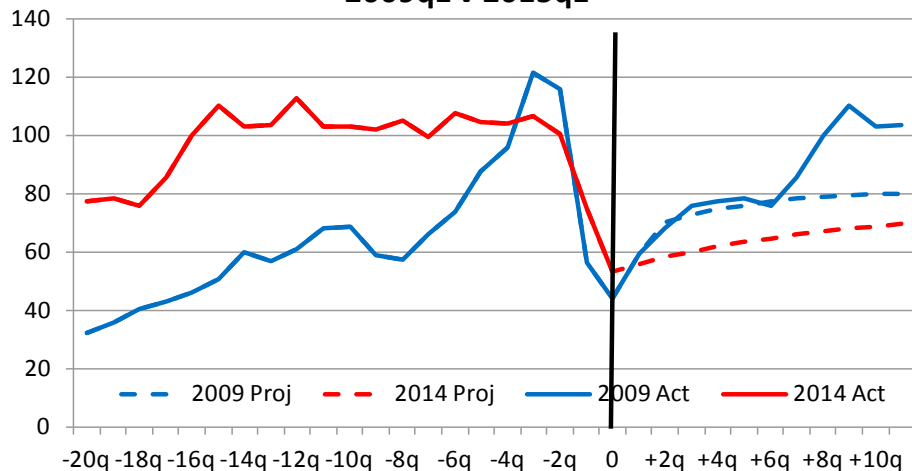
- ❑ **Demand:** Slow global growth is pushing down commodity prices.
- ❑ **Supply:** Fuel prices also affected by expansion of US fuel production and cycle of geopolitical tensions.
- ❑ **Price:** Oil price fell to \$45 p/b. IMF projects \$60 p/b in 2015 rising to \$75-\$80 p/b in medium term.



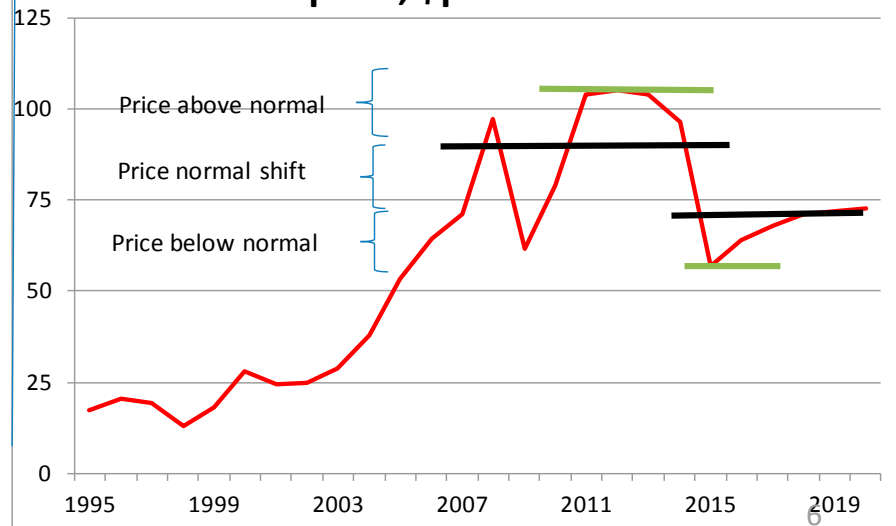
# Short v long term price shock

- ❑ Current shock differs from 2009 demand shock because of structural supply shock. But price rebound after 2009 was unexpected.
- ❑ Oil supply price shocks persist longer than demand shocks. Large explanatory residual suggests market over-reaction.
- ❑ Oil prices have probably overshot:
  - Decline in 'normal' from, say, \$90 to \$75-\$80 p/b.
  - Temporary decline below new 'normal'.

**Oil price projections at the trough**  
2009q1 v 2015q1



**Oil price, \$per barrel**





# Oil flows



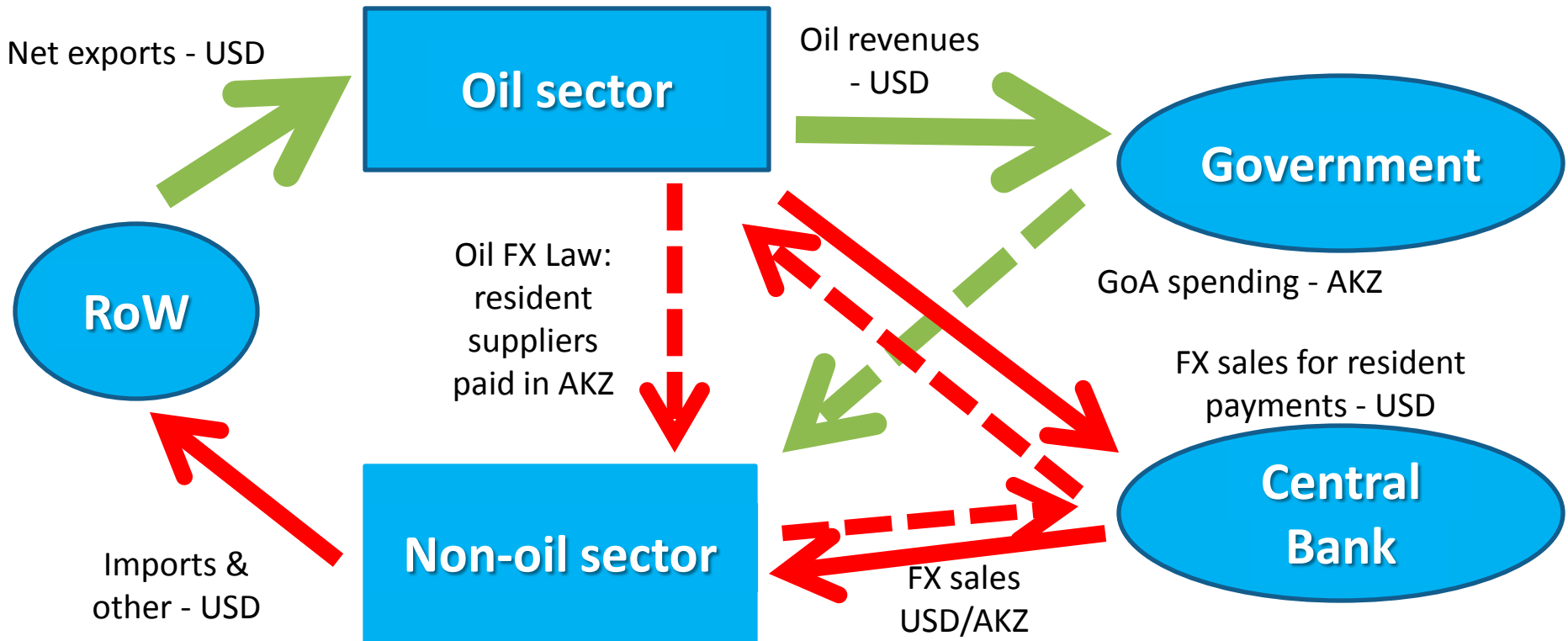
# Absorbing oil resources

- ❑ USD oil earnings are a claim on foreign resources – these resources are either consumed via imports of goods and services or saved as foreign reserves/deposits.
- ❑ Oil resources preferably used to import productive capital rather than consumer goods.
- ❑ Domestic AKZ spending is not a use of USD oil resources until it generates imports.
- ❑ Government receives USD oil revenues. But Government spending is only a use of USD oil resources when used to finance imports.



# Financial flows

- Oil resources enter non-oil sector through spending by GoA and oil firms. BNA now sole supplier of USD to non-oil sector.
- Two 'USD cycles' – budget cycle via GoA and FX market cycle via BNA.





# Impact of lower oil price

# Impact on exports and revenues

- Price shock is foremost a shock to **external balance**: fall in 2015 export receipts by around \$27 billion.
- Also **fiscal shock** because of lower oil revenues and financing constraints: fall in 2015 budget oil revenues by about \$17 billion.

Direct impact of oil price decline  
Assuming 2014 oil production

	2014 price	Rev	Difference
Oil price	104	60	44
Oil production	1.66	1.66	0
Oil export receipts	63	36	27
Oil budget revenues	31	14	17

# Policy buffers

**Angola better prepared to face oil price shock in 2014/15 than in 2008/09**

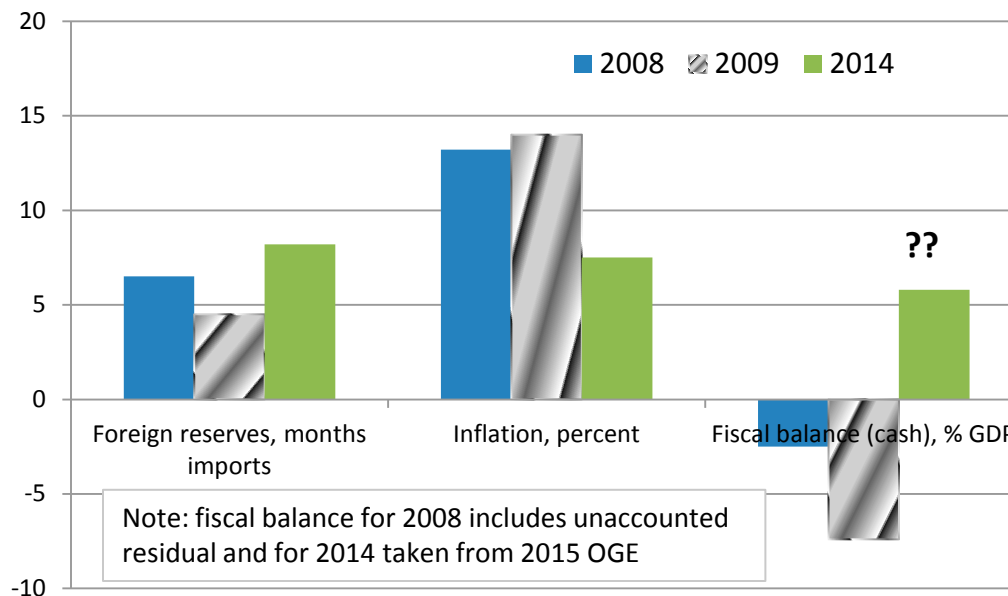
---Higher foreign reserves

---Lower inflation

---Stronger fiscal balance ??

And stronger policy coordination

**Policy buffers 2008/9 and 2014**





# Policy options

**Foreign reserves (savings) can and should be used to smooth the adjustment, but only temporarily.**

**External imbalance:** need to cut use of foreign exchange (imports) by:

- Price adjustment: depreciate FX rate plus higher interest rates.
- Demand adjustment: cut fiscal spending or raise taxes to suppress import demand.

**Fiscal adjustment:** need to restrain fiscal deficit by:

- Lower spending or higher taxes.
- Adjustment constrained by availability of domestic and foreign financing
- Impact on economic activity.

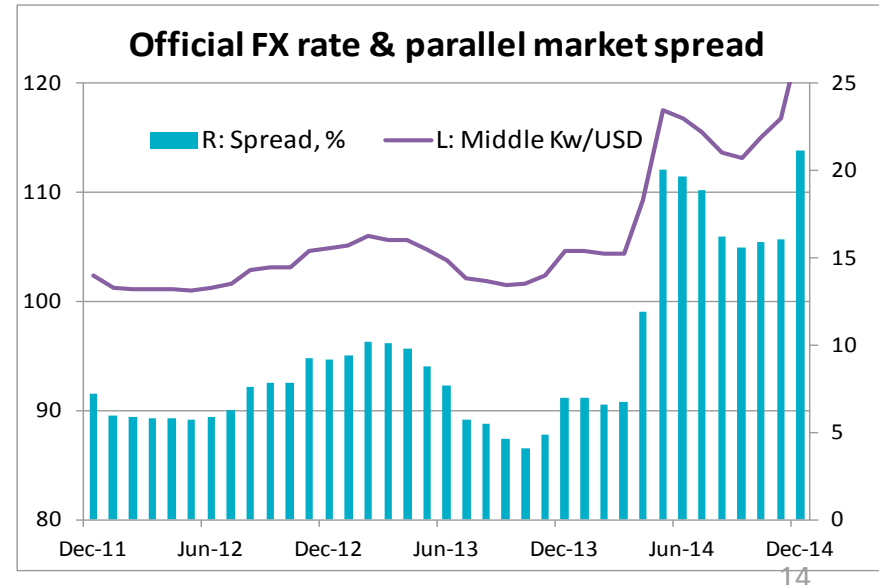
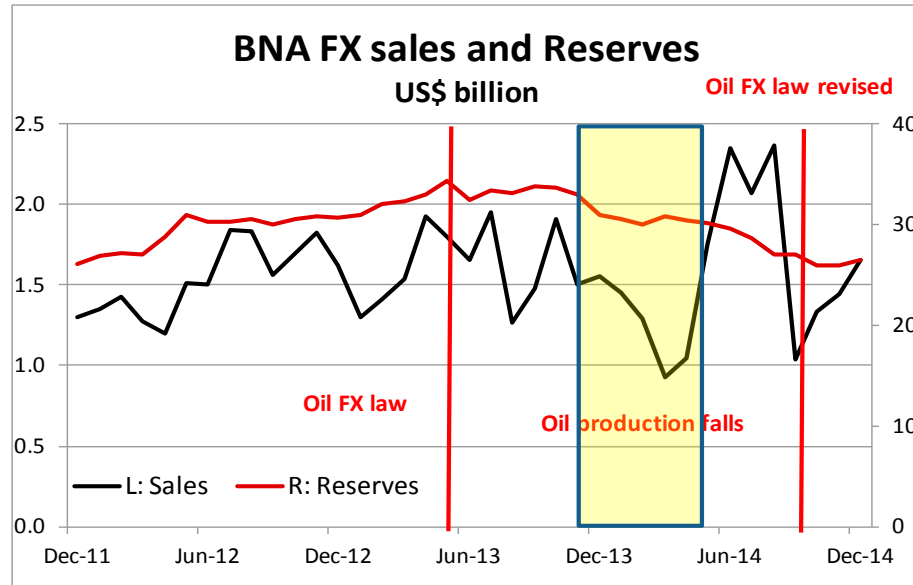
**What is the residual adjustment?**

**External:** quantity constraints on access to FX and import quotas

**Fiscal:** delayed payments.

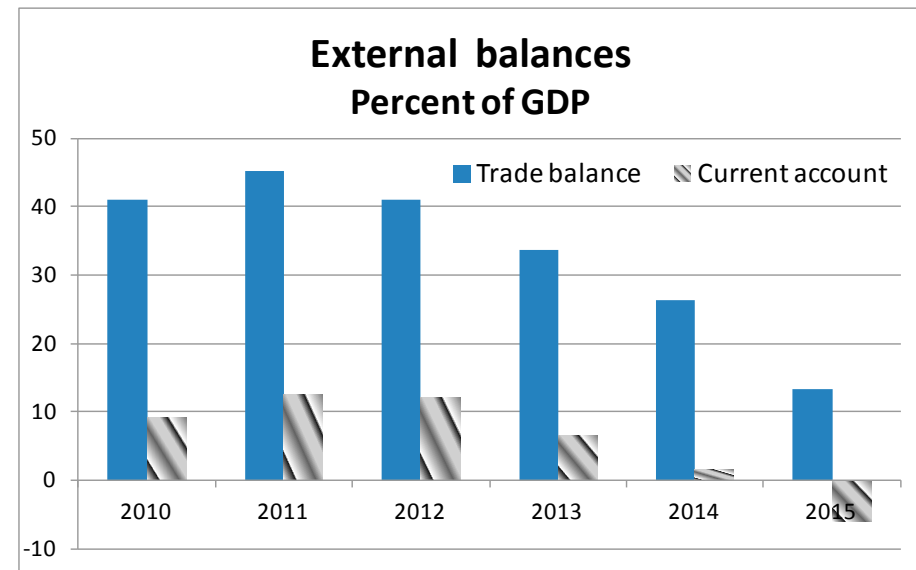
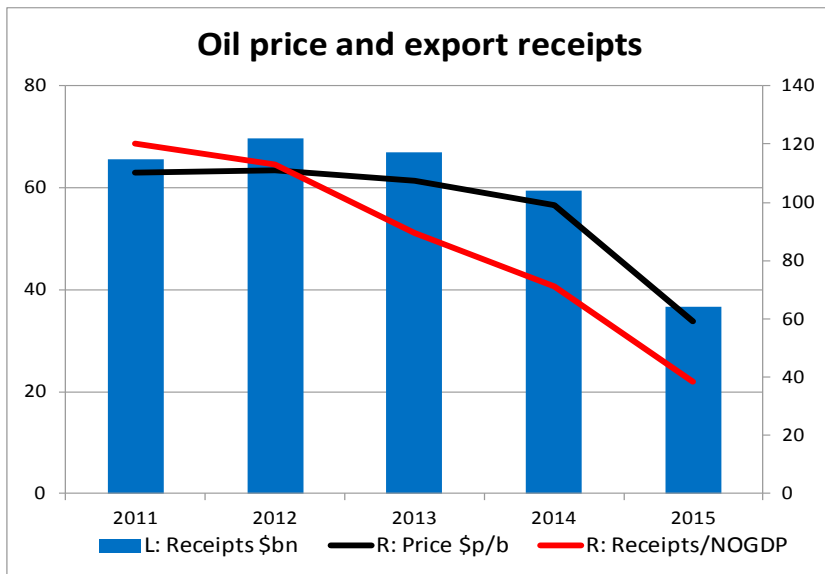
# Impact on FX market

- ❑ FX shortages already evident: FX rationing and import quotas. Widening FX spreads.
- ❑ FX depreciation about 7 percent since September. Further depreciation constrained by impact on inflation, fiscal costs, and banks' balance sheets. Need for higher interest rates?
- ❑ Fiscal adjustment needed.



# BoP trends

- ❑ Sizeable current account deficit projected in 2015.
- ❑ Longer-term BoP squeeze: Oil sector already trending down relative to non-oil GDP with current account deficit already in medium term.
- ❑ Oil shock accentuates over-valuation of FX rate.



# Fiscal adjustment

**Increase in 2015 OGE fiscal deficit due to both lower oil price and higher spending.**

- Total spending +19%
- Nominal non-oil GDP +16%
- CPI inflation +7%

## Options

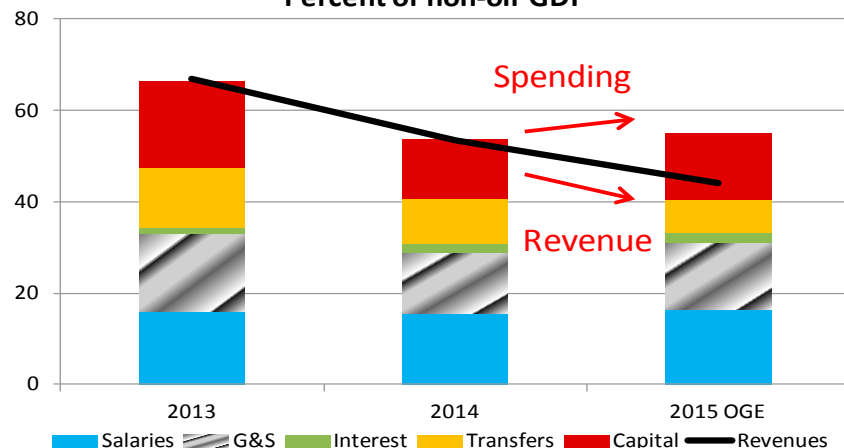
- Stronger revenue effort. Non-oil revenues 14% NOGDP, compared to 20+% for SSA.
- Lower spending on salaries and G&S: 56% 2015 OGE.
- Eliminate fuel subsidies: costly, regressive, and inefficient. Introduce social income support?
- Slower capital spending: need higher efficiency.

**Adjustment constrained by availability of financing for fiscal deficit.**

- Foreign borrowing difficult in current global environment, concerns about future fiscal deficits and debt sustainability, and prospects for sub-salt.
- Domestic borrowing can crowd out private sector despite excess bank liquidity.
- Delayed payments already evident.

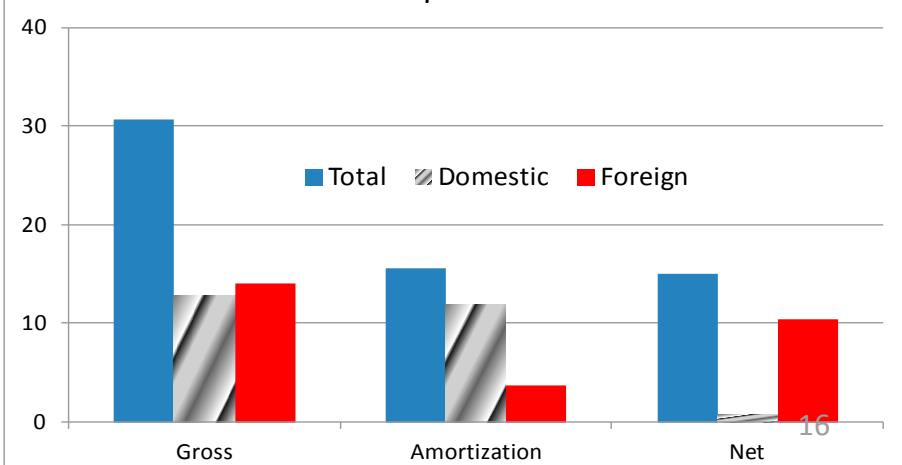
## Budget expenditure commitments

Percent of non-oil GDP



## Loan financing of 2015 OGE

US\$ billion





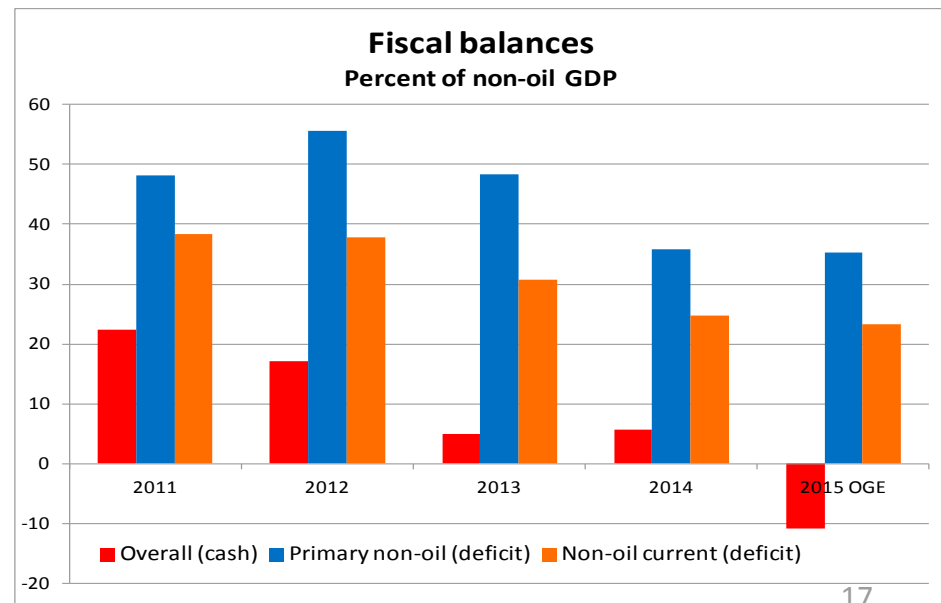
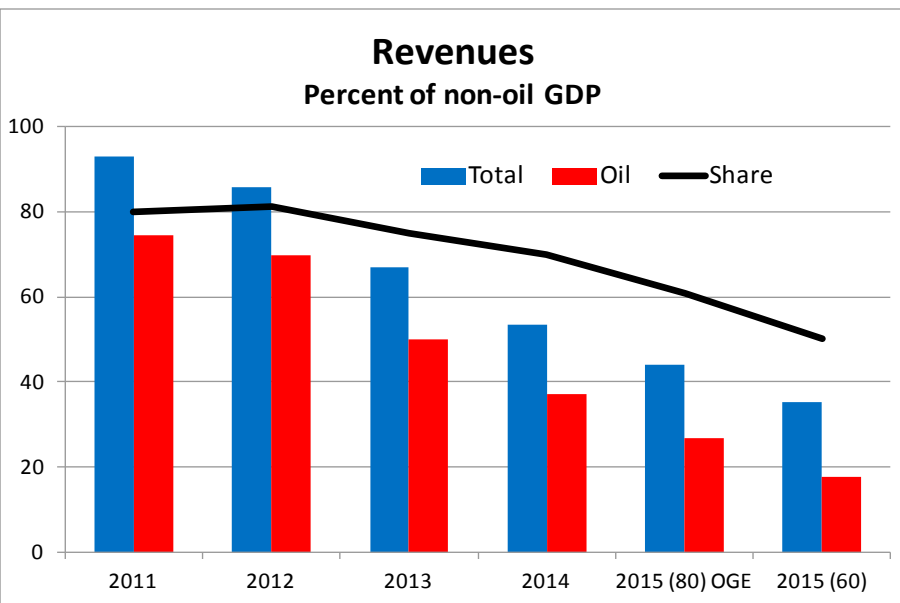
# Fiscal trends

**Angola already faces a longer term fiscal squeeze accentuated by the oil price shock**

❑ Trend deterioration in fiscal balance due to falling oil revenues/NOGDP: 2015 OGE – deficit 7.5% of GDP, 10.8% of NOGDP.

❑ Oil revenue share of total revenues declining, now nearing 50%. Reinforcing longer-term trend of declining revenues share of NOGDP.

❑ Despite tightening fiscal policy stance: declining non-oil primary deficit (discretionary fiscal stance) and non-oil current deficit (discretionary budget savings).



# Medium-term policy objectives

**Angola is not rich**

**It is a post-conflict country that is rapidly extracting its limited oil reserves  
It faces the challenges of both**

**Save and invest for the future**



**Higher capex and restore fiscal surplus**

**Reduce volatility from oil sector**



**Smooth spending (stabilization fund)  
around the new 'normal' oil price**

**Diversified and inclusive growth**



**Shift from consumption to capex.  
Social income transfers**



**Thank you**