
Energy Subsidy Reform: Lessons and Implications

March 27, 2013



Consequences of energy subsidies go well beyond fiscal costs



☐ Depress growth

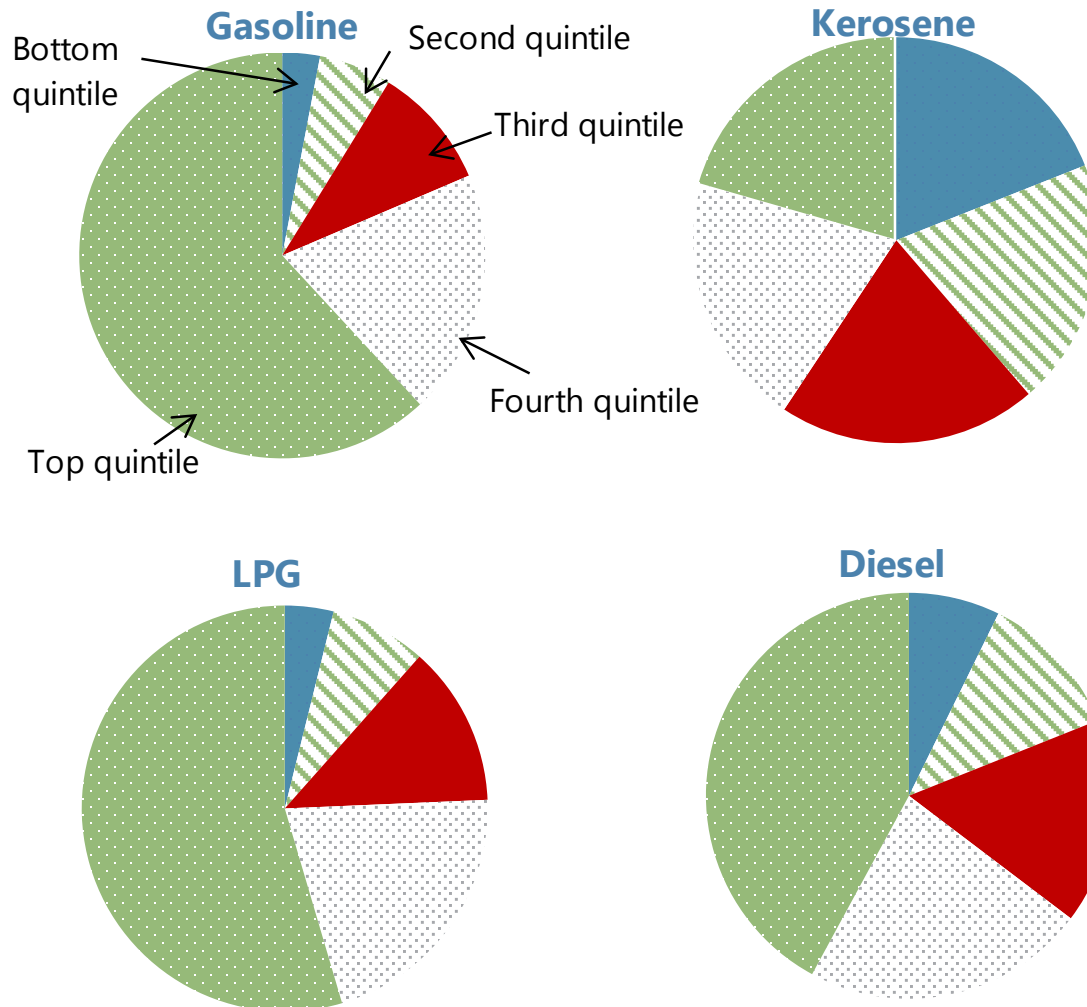
- ☐ reduce investment in the energy sector**
- ☐ crowd-out critical public spending**
- ☐ over-allocate resources to energy intensive sectors**

☐ Exert pressure on balance of payments of energy importers

☐ Create negative externalities (for example, global warming)

☐ Reinforce inequality

Distribution of petroleum product subsidies by income groups





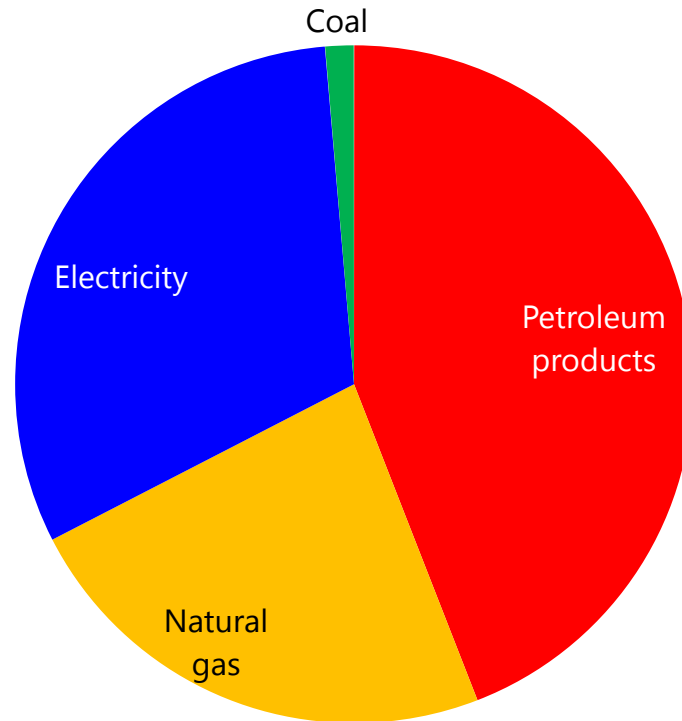
Measuring consumer subsidies

- ❑ **Pre-tax subsidies** exist when energy consumers pay a price below the supply cost of energy, including transportation and distribution costs
- ❑ **Tax subsidies** arise if energy taxes are too low: energy should be taxed the same way as any other consumer product, plus additional taxes to account for the adverse effects of energy consumption
- ❑ **Post-tax subsidies** equal pre-tax + tax subsidies

Petroleum and electricity dominate pre-tax subsidies, while coal subsidies are negligible



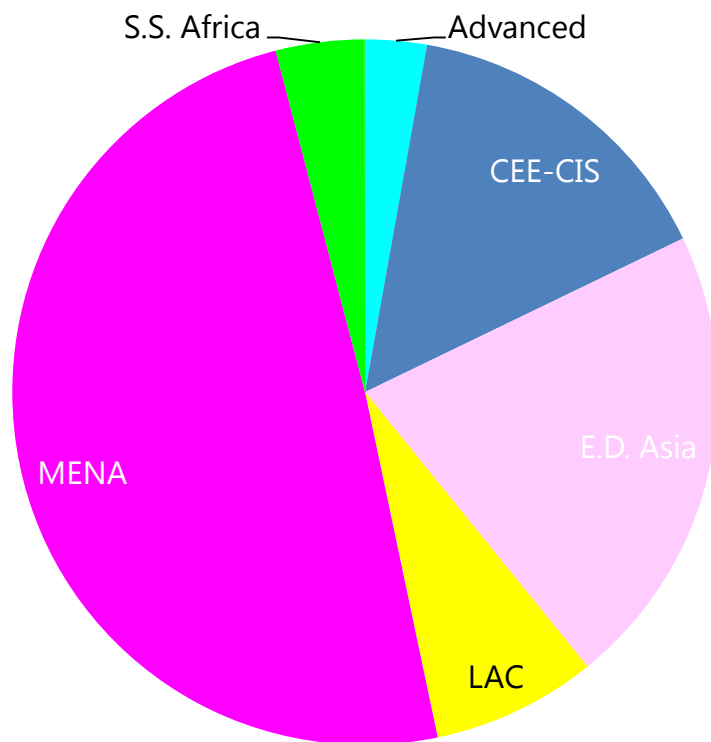
- Pre-tax
\$480 billion



Nearly half of pre-tax subsidies are from MENA region

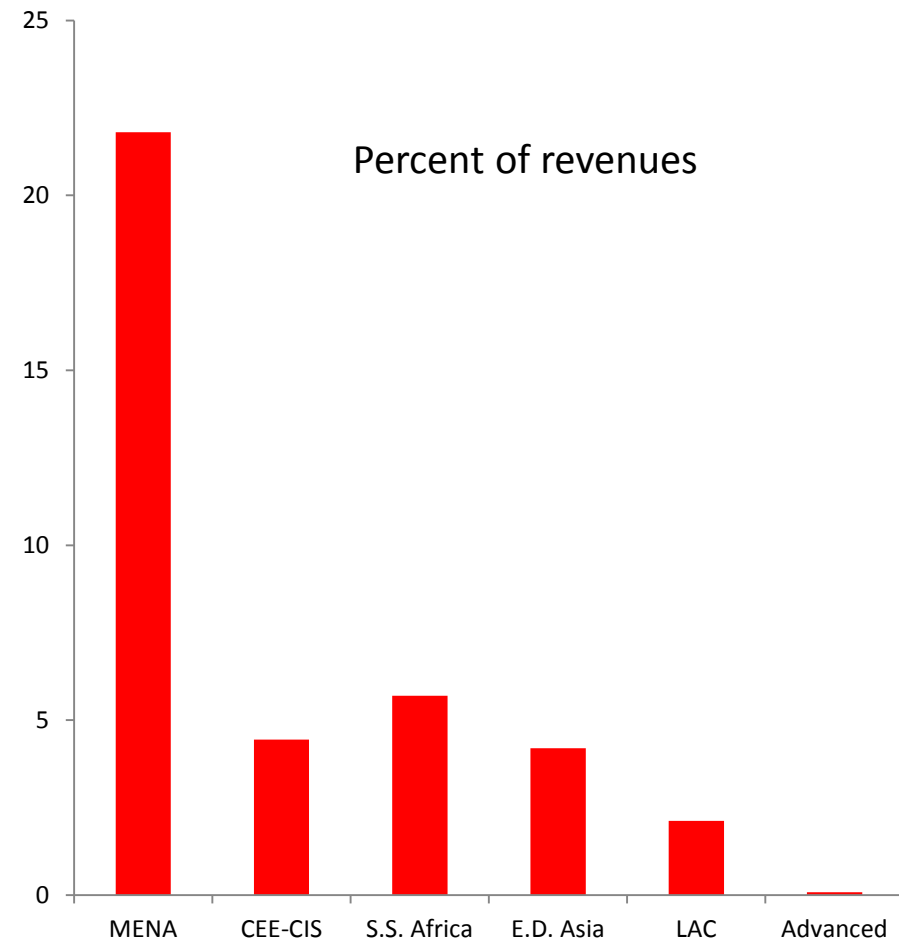
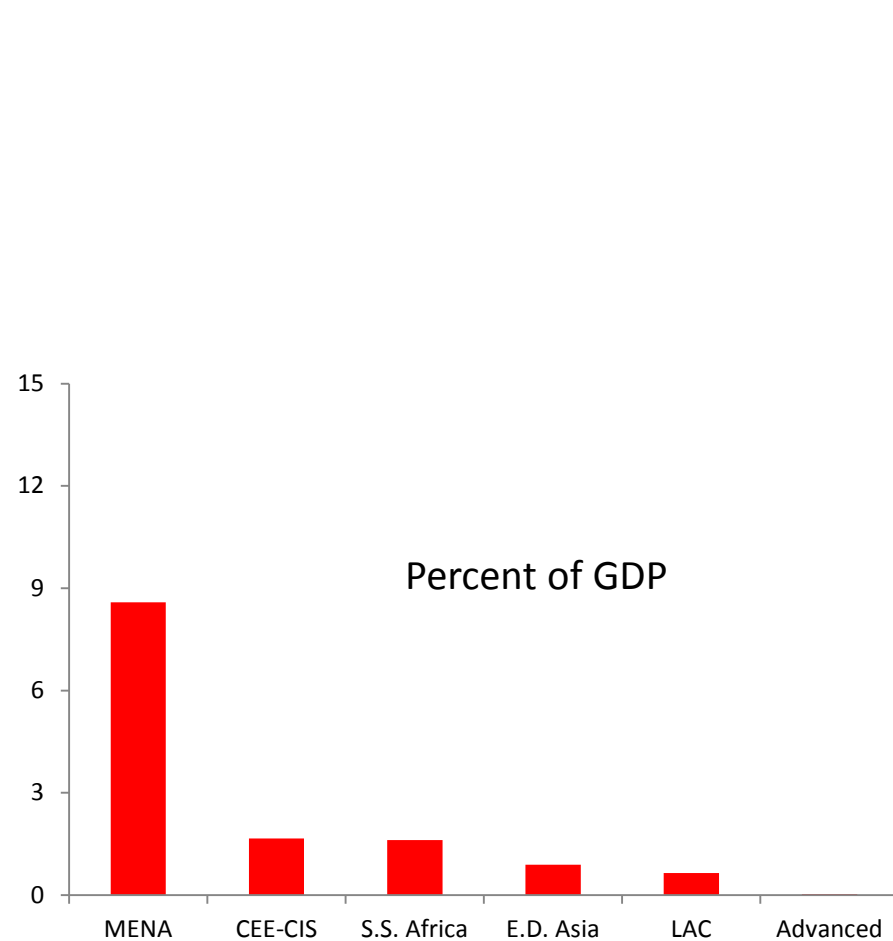


• Pre-tax
\$480 billion (0.7% GDP, 2.1% revenues)



CEE-CIS = Central and Eastern Europe and Commonwealth of Independent States; E.D. Asia = Emerging and Developing Asia;
LAC = Latin American countries; MENA = Middle East and North Africa; S.S. Africa = Sub-Saharan Africa

Pre-tax subsidies as a share of GDP and government revenues are highest in MENA



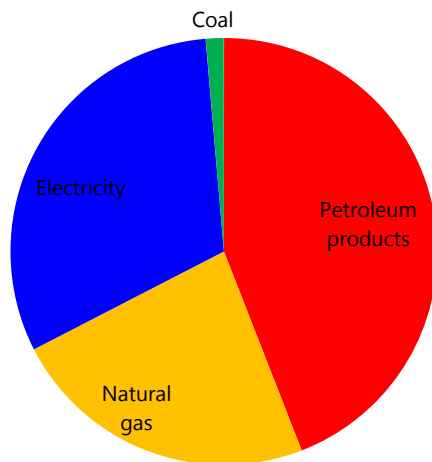
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Post-tax subsidies are four times larger than pre-tax subsidies, with more than a quarter from coal



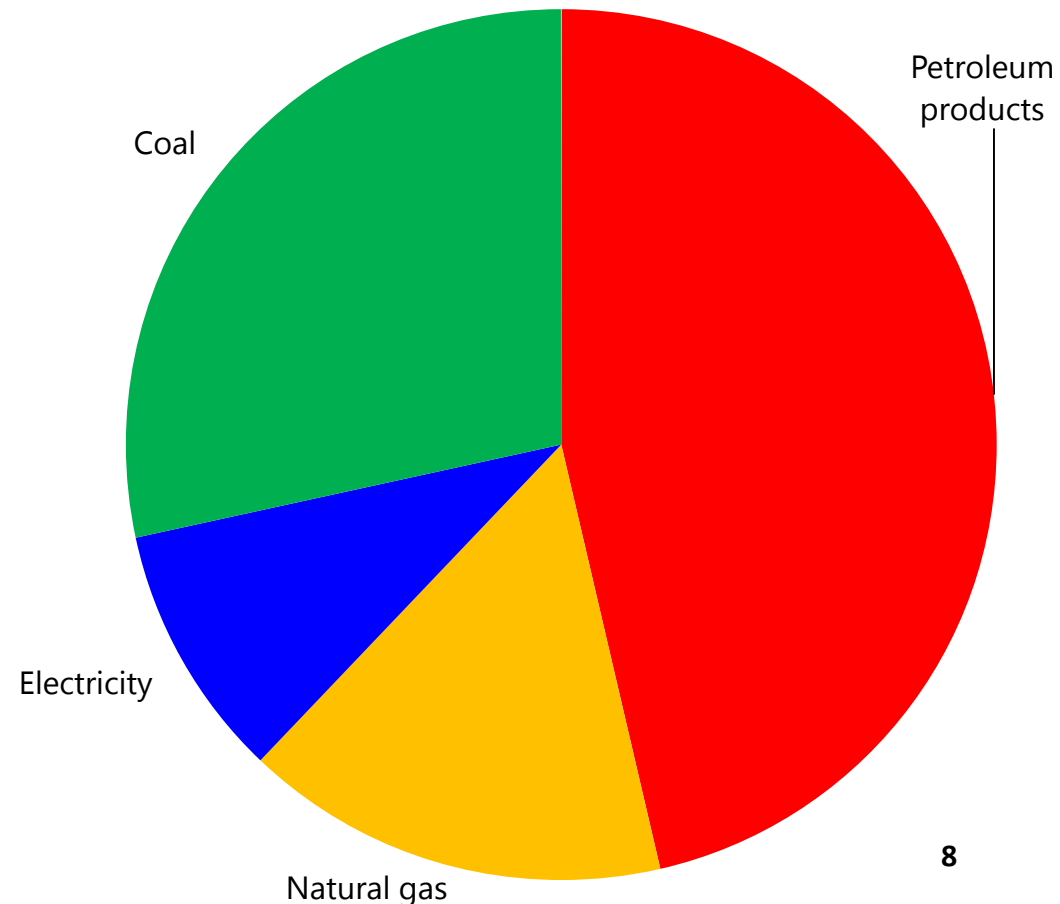
- Pre-tax

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- Post-tax

\$1.90 trillion (2.7% GDP, 8.1% revenues)

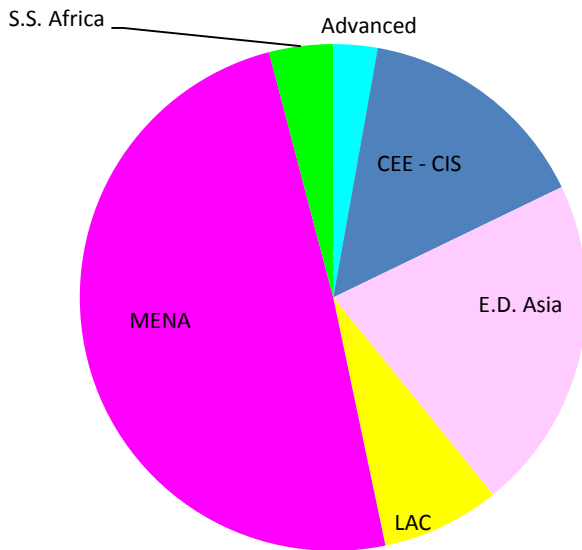


Advanced economies account for 40 percent of post-tax subsidies



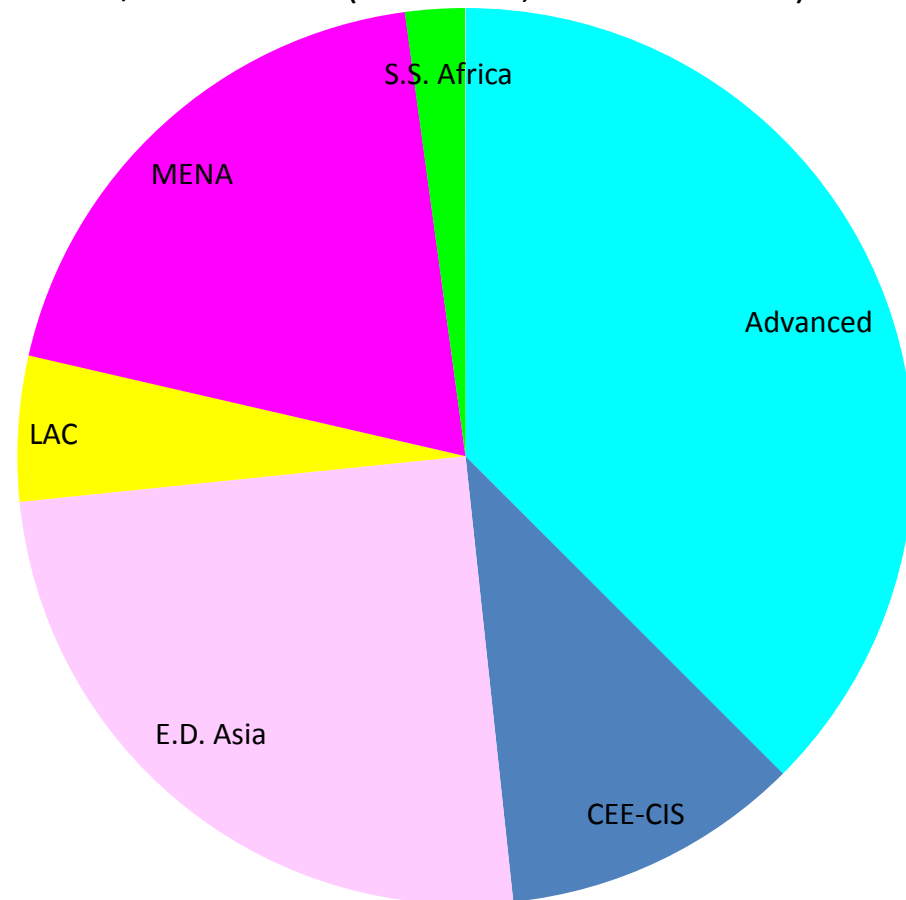
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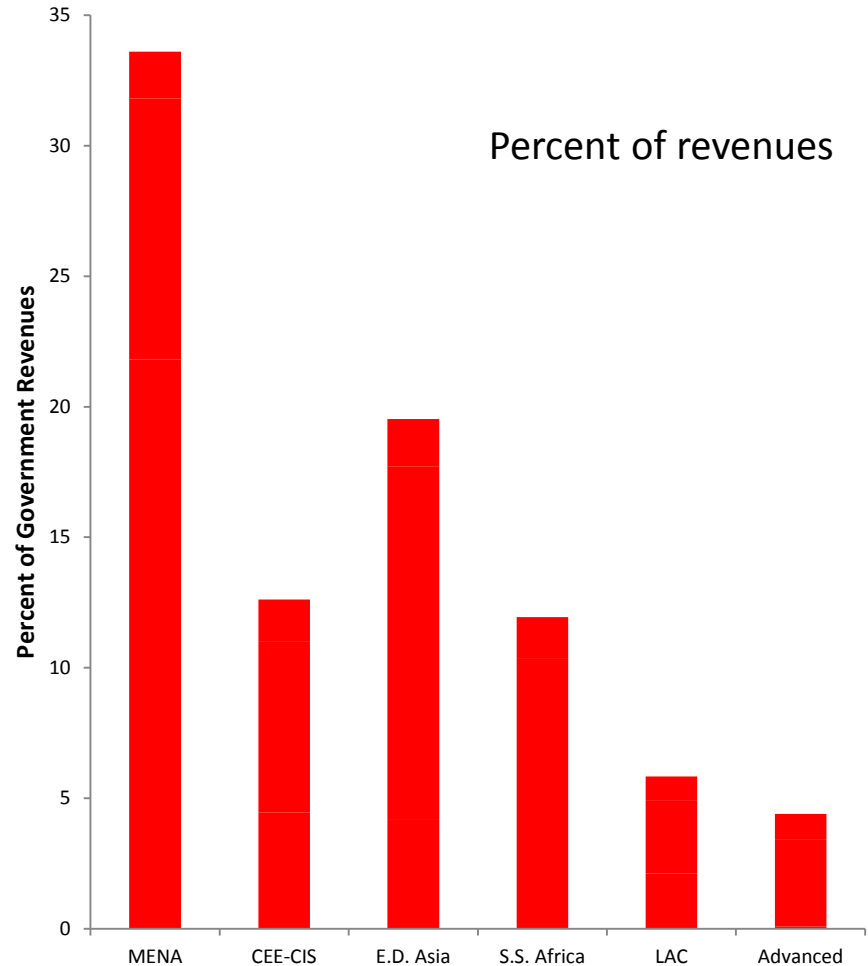
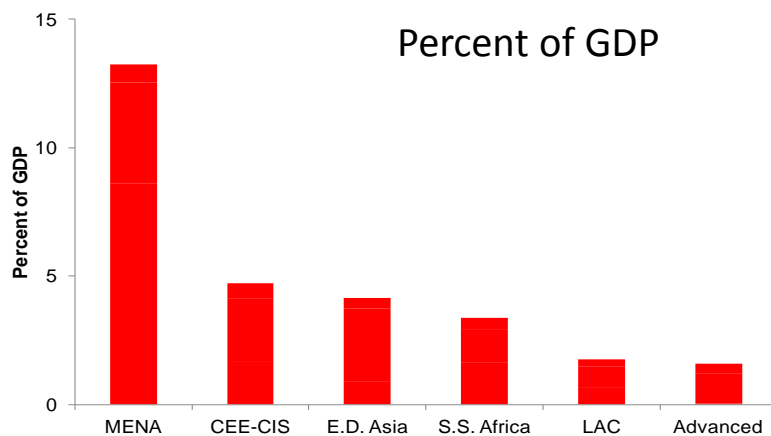


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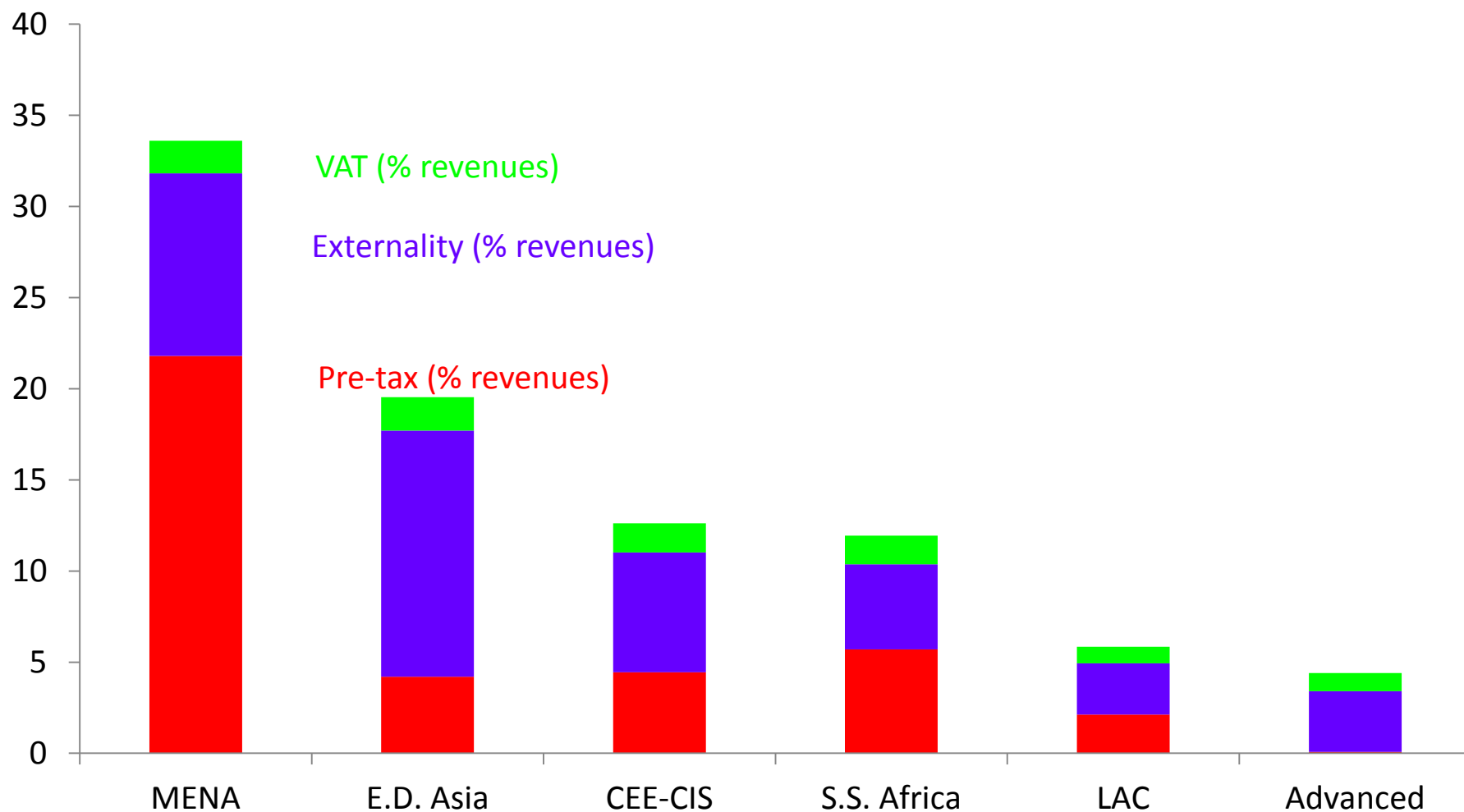


Post-tax subsidies as a share of GDP and government revenues are much higher in MENA



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Under-pricing for externalities accounts for a large share of post-tax subsidies across all regions



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“How to do” subsidy reform

Identify ingredients for successful subsidy reform from 22 country case studies

- ❑ 14 on fuel, 7 on electricity, and 1 on coal
- ❑ broad regional coverage (7 from SSA, 2 from E.D. Asia, 3 from MENA, 4 from LAC, and 3 from CEE-CIS)
- ❑ 28 reform episodes (12 successful, 11 partially successful, and 5 unsuccessful)
- ❑ Supplemented by lessons from FAD technical assistance (19 reports in the past 5 years) on energy subsidies and work by other institutions



Six key reform ingredients

(i) A comprehensive reform plan

- clear long-term objectives
- assessment of the impact of reforms
- consultation with stakeholders

(ii) A far-reaching communications strategy

- inform the public of the size of subsidies and benefits of reform
- strengthen transparency in reporting subsidies



Six key reform ingredients

(iii) Appropriately phased and sequenced price increases

- permit households and enterprises time to adjust and governments to build social safety nets
- sequence increases differently across products

(iv) Improvements in the efficiency of state-owned enterprises (SOEs) to reduce their fiscal burden

- improve information on their costs, set performance targets and incentives, and introduce competition where appropriate
- improve collection of energy bills



Six key reform ingredients

(v) Targeted mitigating measures to protect the poor

- targeted cash transfers are preferred
- when cash transfers are not feasible, other programs can be expanded as administrative capacity is developed
- SOE restructuring may also require targeted measures (e.g., job training)

(vi) Depoliticize price setting

- implement automatic price mechanism (with price smoothing)
- establish an autonomous body to oversee price setting



Thanks!