



Subsidy Reform and Social Assistance

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Seventh African Fiscal Forum

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Outline



I. Fiscal costs of subsidies in SSA

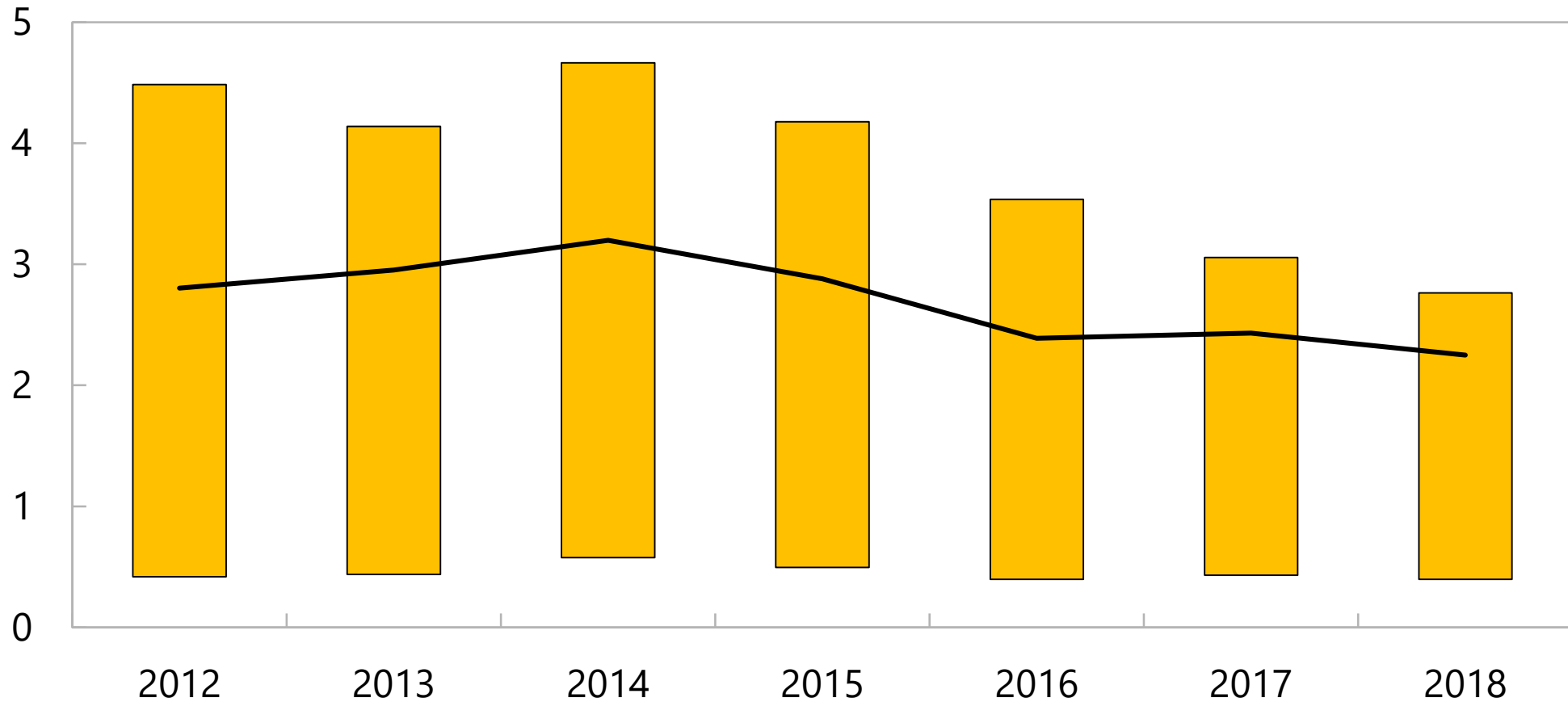
II. Subsidies and economic efficiency

III. Distributional considerations of subsidy reform

IV. Lessons for successful reform

Reported subsidies are frequently large

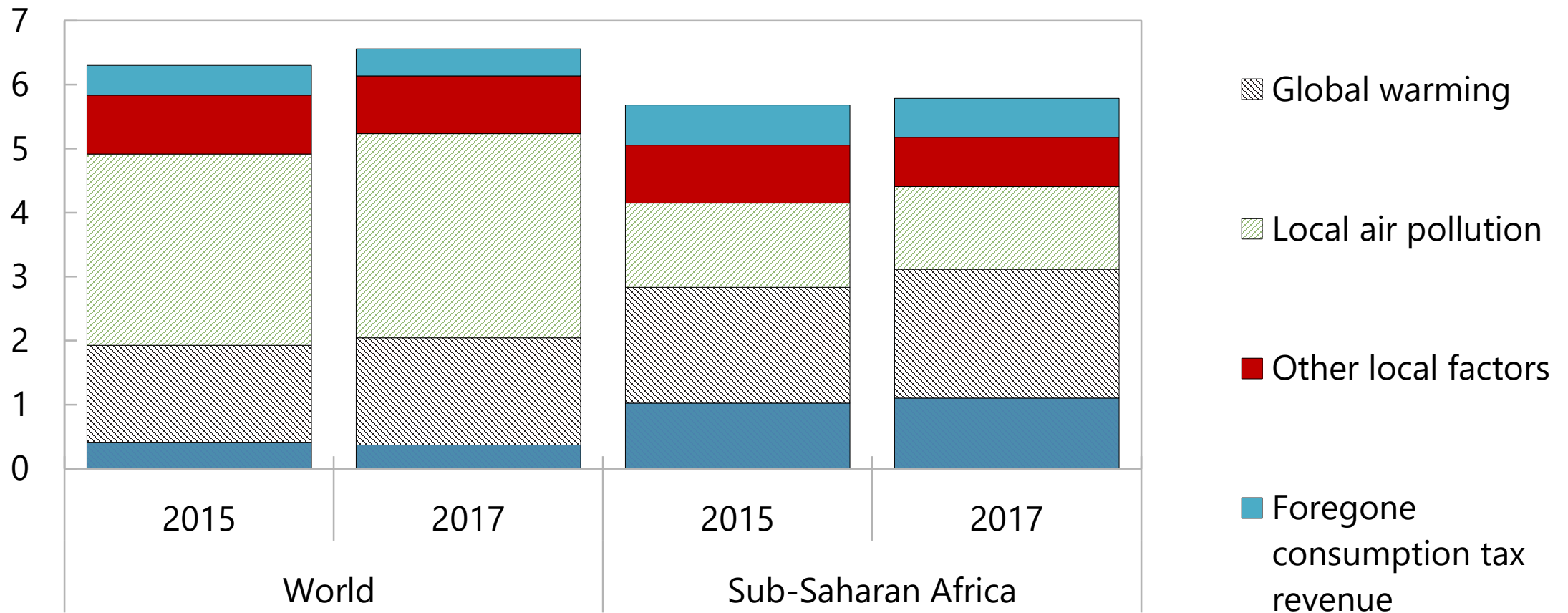
Fiscal Subsidies in Sub-Saharan Africa
(Percent of GDP, average and 25-75 percentile range)



With externalities, subsidies much larger than reported

Energy Subsidies by Subsidy Component

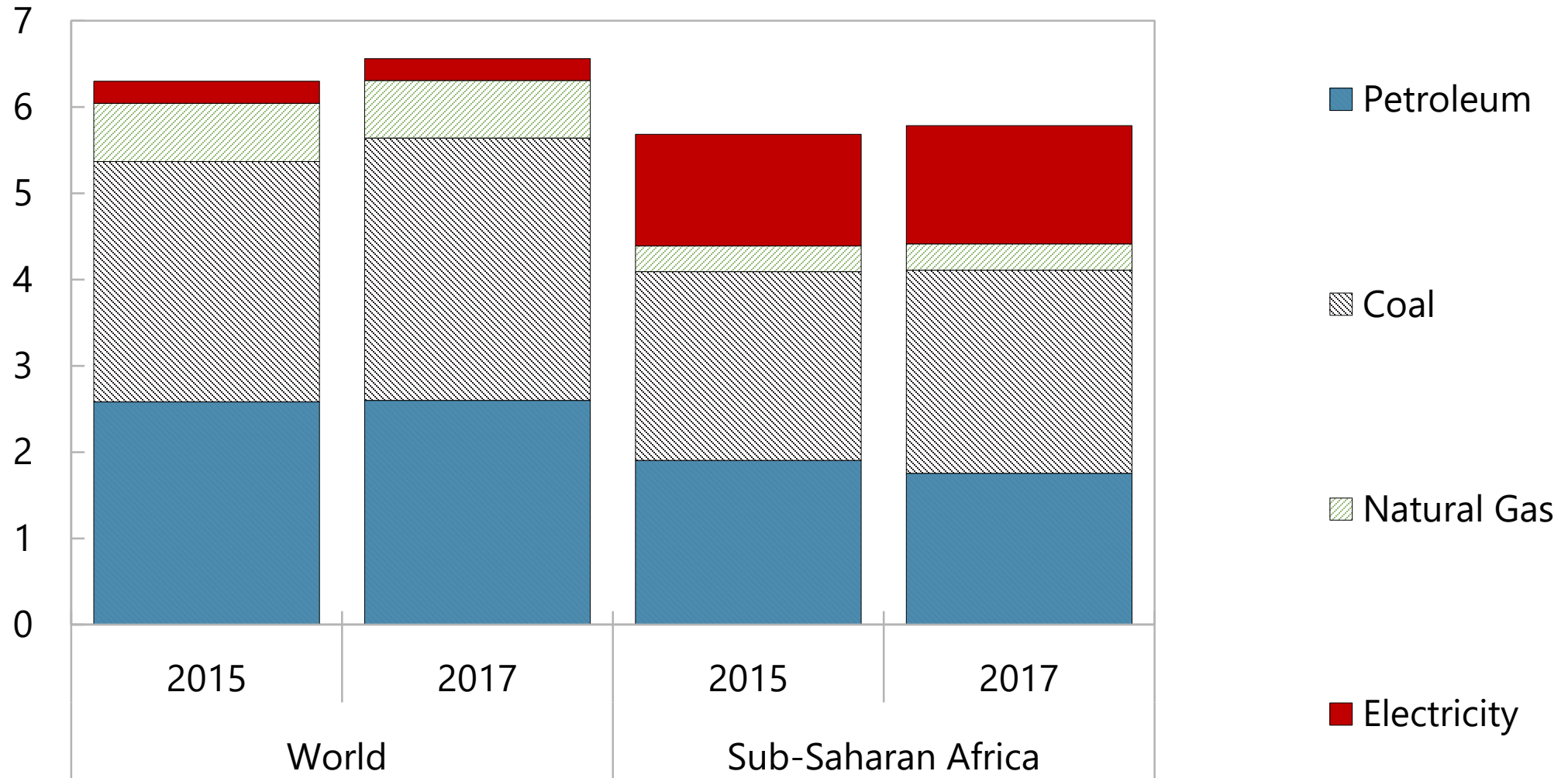
(Percent of GDP)



Source: Coady and others (forthcoming 2019).

Energy Subsidies by Product

(Percent of GDP)



Source: Coady and others (forthcoming 2019).



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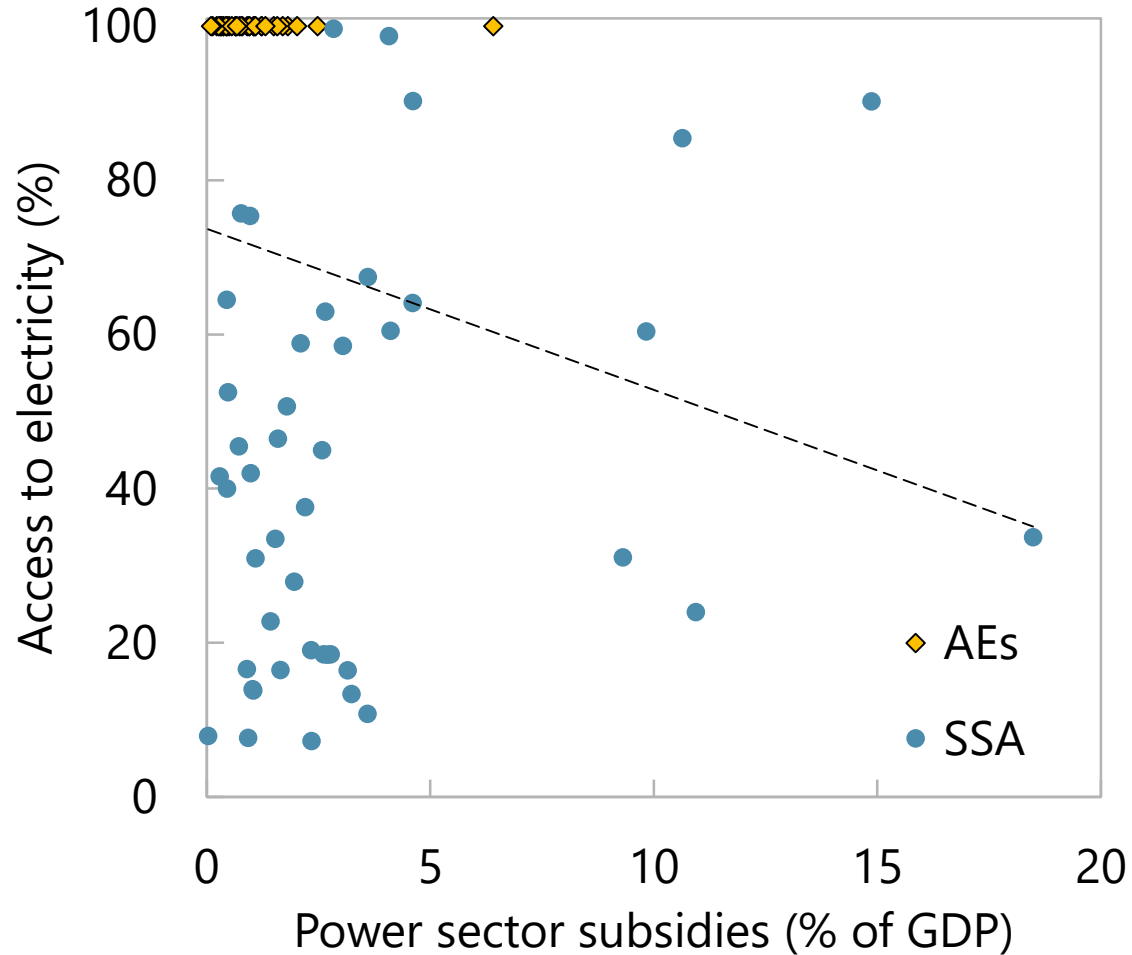
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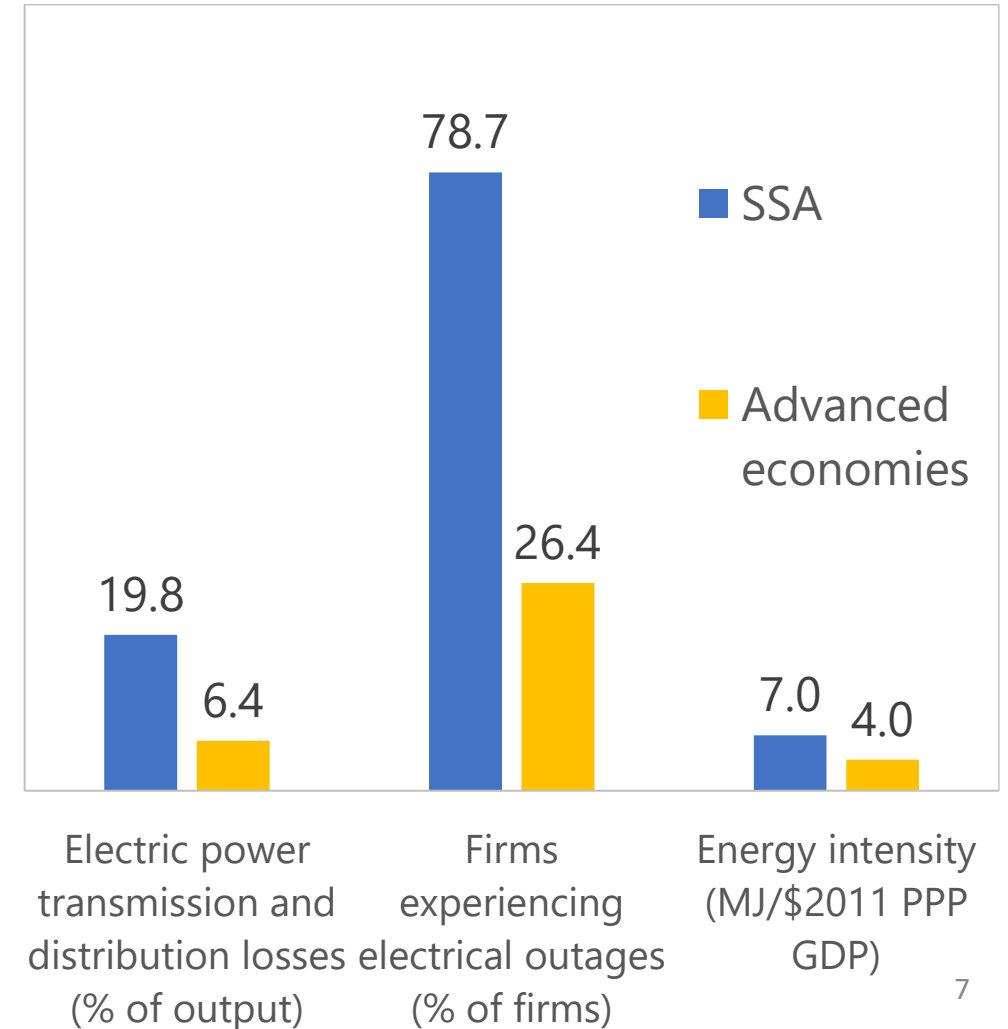
IV. Lessons for successful reform

Energy subsidies often ineffective in SSA

Low access to electricity



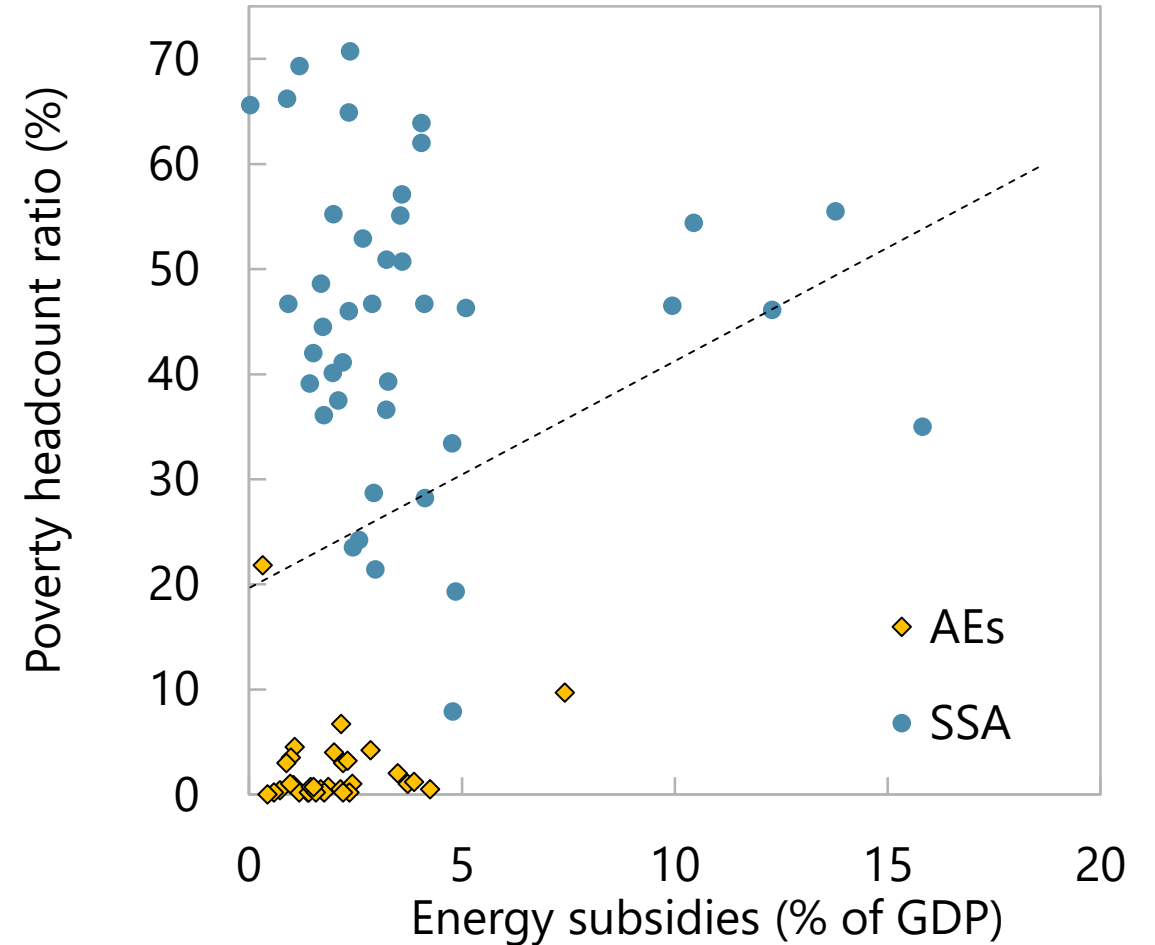
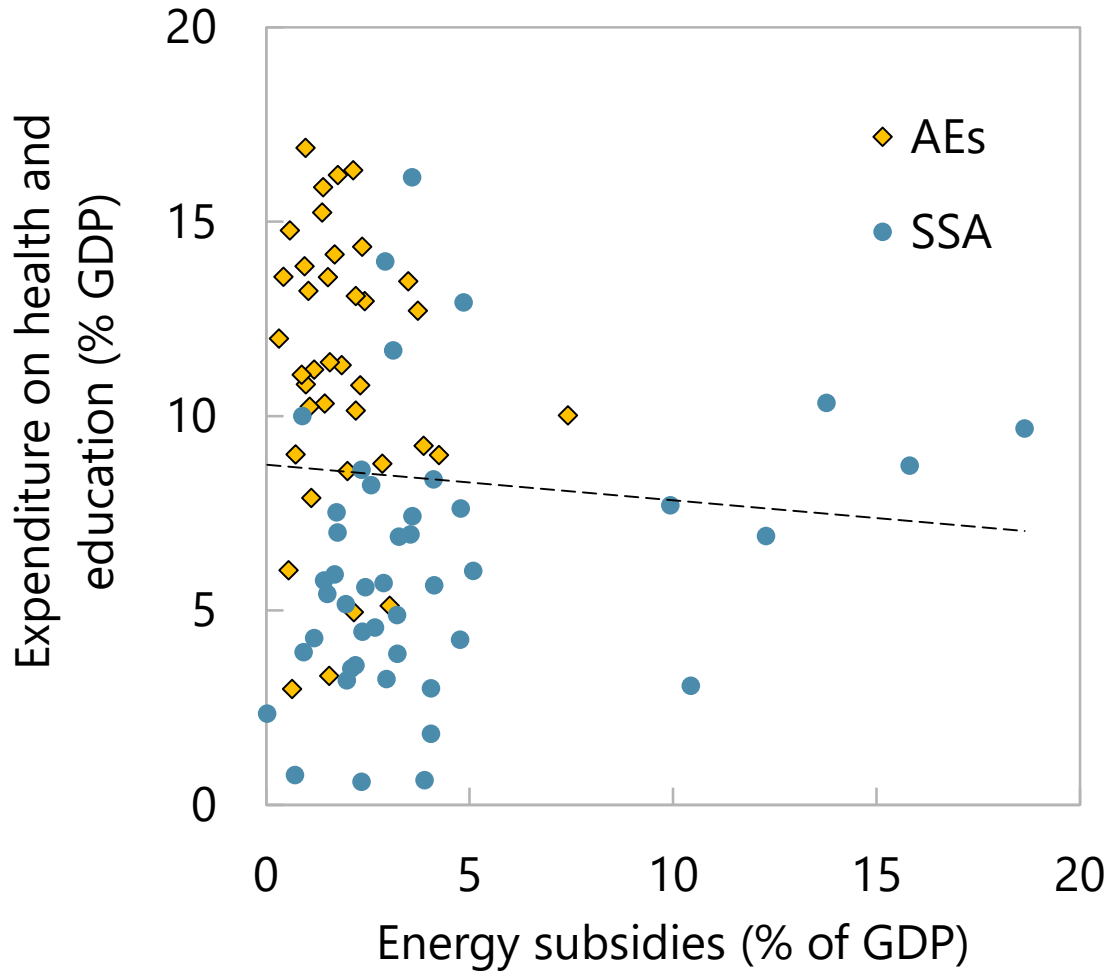
Low energy efficiency



Sources: WDI and IMF database on energy subsidies.

... and subsidies crowd out other spending

Subsidies coincide with low social spending and high poverty rates



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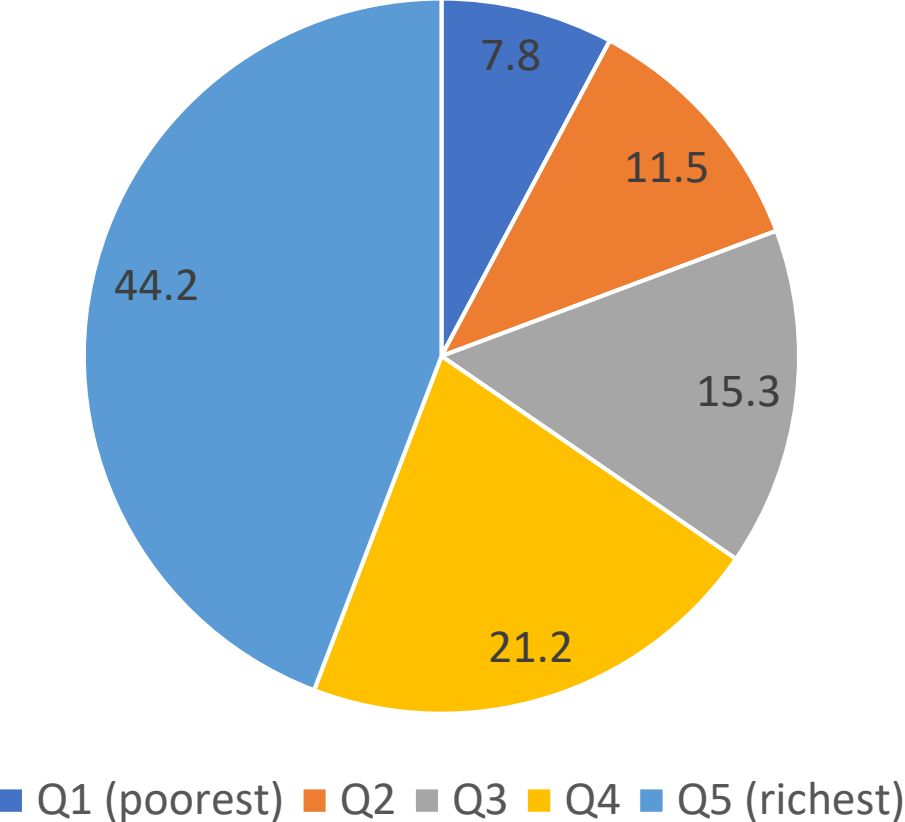
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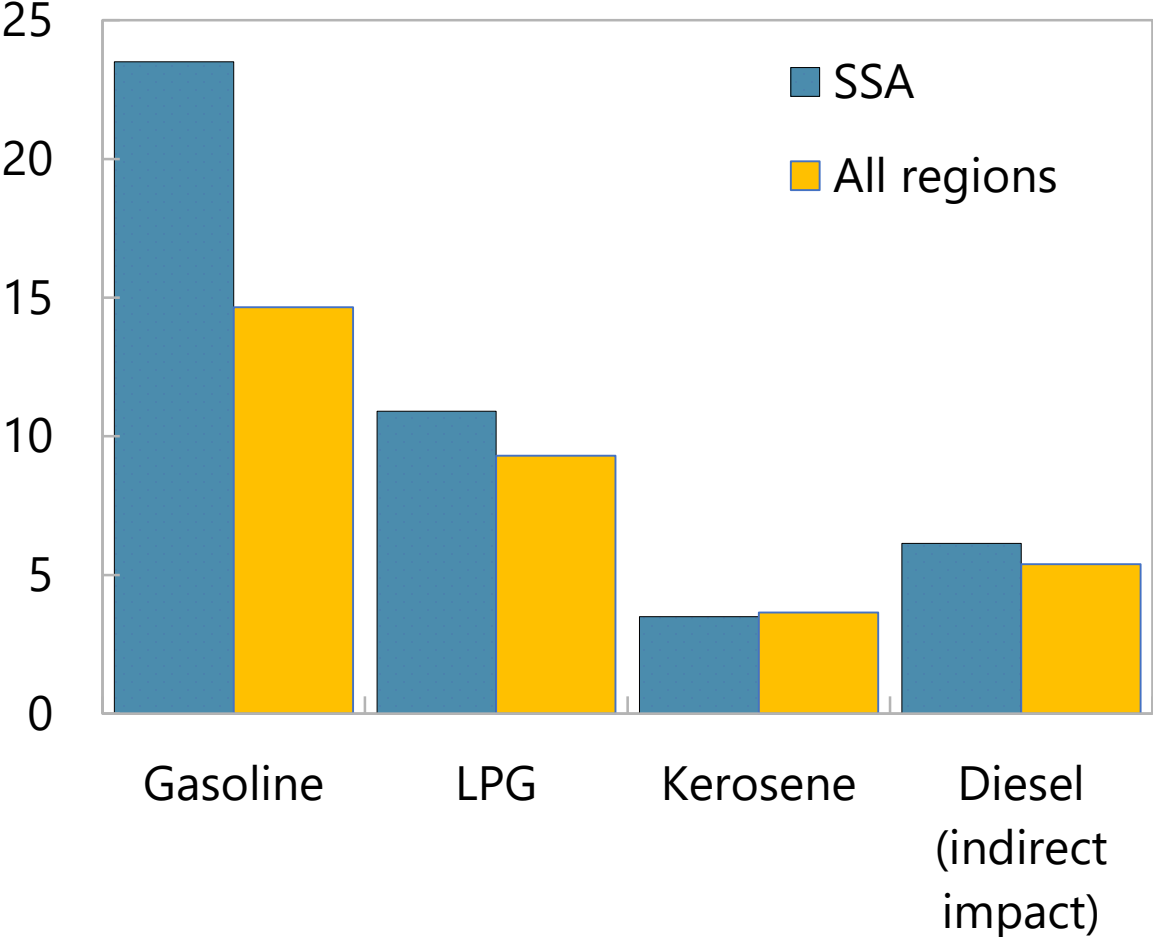
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Fuel subsidies mostly go to wealthier households

SSA: Distribution of Benefits
(% of total fuel subsidy)



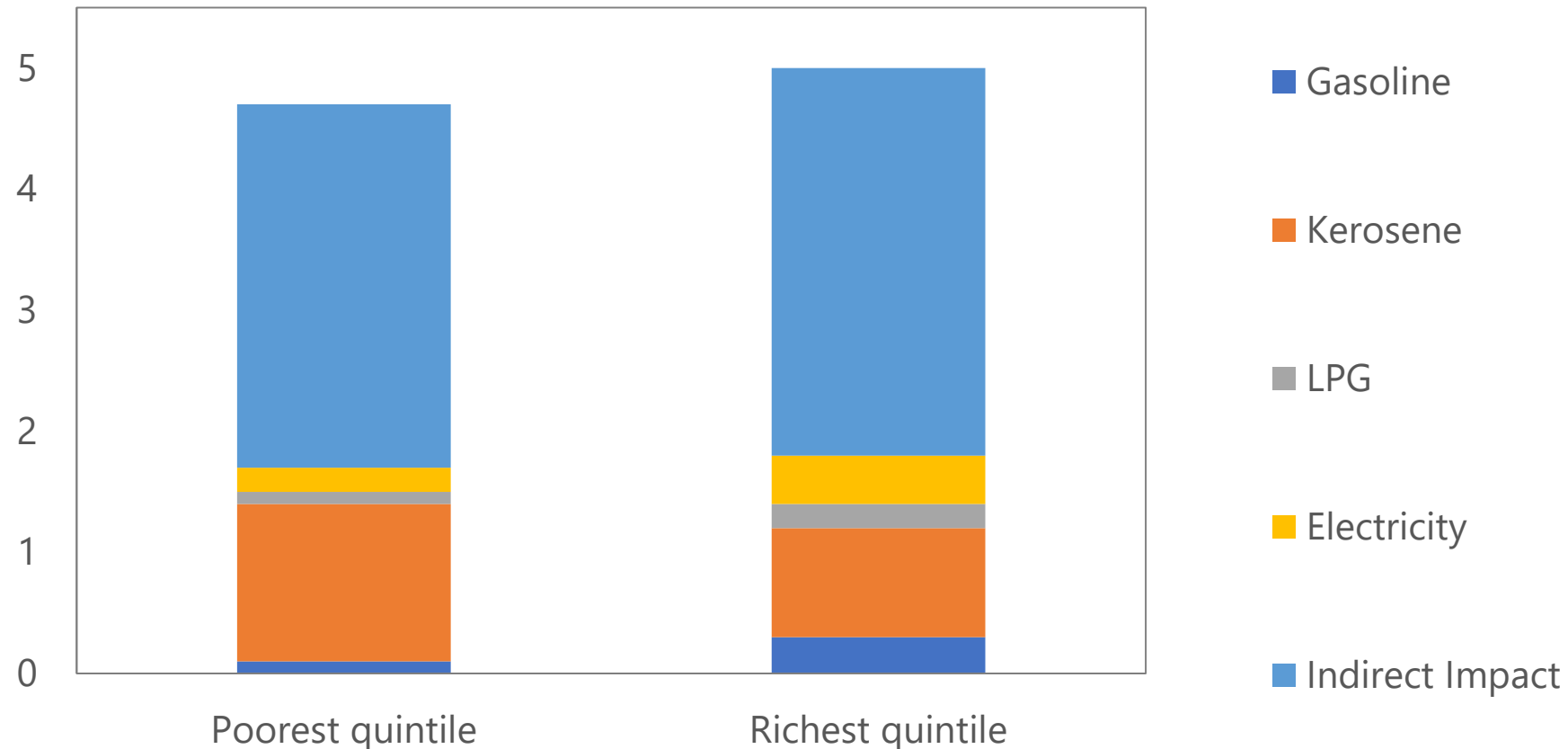
Cost of providing \$1 to the poorest
40% via fuel subsidy (\$)



Sources: Coady and others, 2015, IMF working paper 15/250.

In relative terms, the impact is more equal

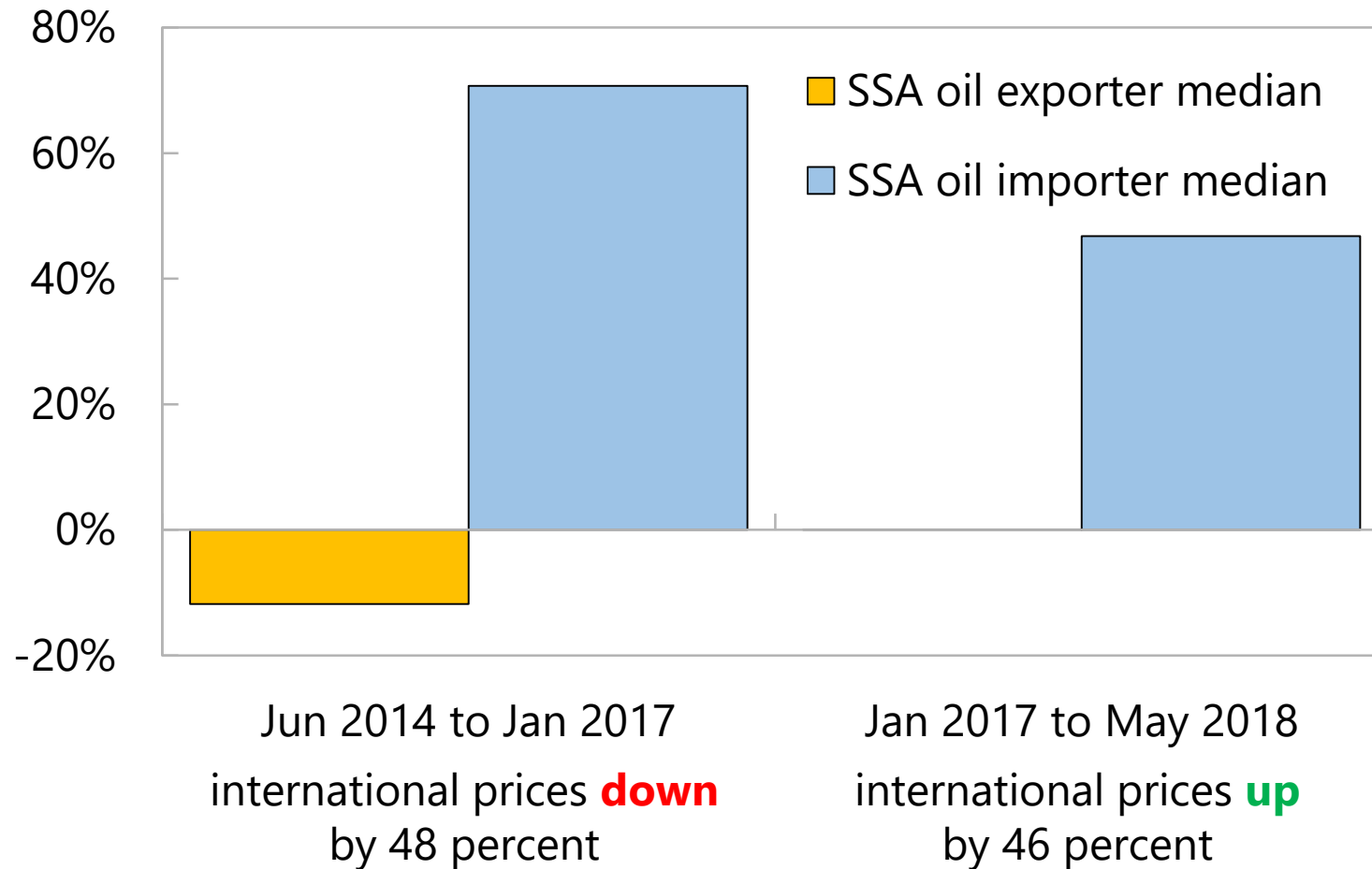
Welfare Impact of Fuel Price Increases
(Percent of household total consumption)



In practice, SSA countries have struggled to adjust fuel prices

Pass-through of International Petroleum Prices

(ratio of change in domestic prices to change in international prices)



Since peaking in October 2018, international fuel prices have fallen by about 30 percent

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Lessons for successful reform

1. Understand the political economy context
2. Devise communication and stakeholder consultation strategy
3. Compensate losers from reform
4. Take accompanying measures to improve service delivery

Political economy context

- Political leaders mindful of pressure from special interest groups may resist reform
- Business and consumer groups with vested interests speak loudest
- Weak governments have little to credibly offer in alternative



Understand the political economy context

Communicate and Compensate

- Communication on subsidy program to mobilize political and public support
 - Indonesia: poor and vulnerable households to benefit as a percent of their incomes
 - Jordan: wealthiest quintile received three times more in fuel subsidies than the poorest quintile
 - Transparency is important for credibility of reform strategy
- Targeted social spending can help mitigate the impact
 - Dominican Republic:
 - Replacement of LPG subsidy with a targeted transfer accompanied by program benefiting drivers of LPG-fueled taxis
 - Presidential decree awarded monthly quantities of diesel to the major (and most powerful politically) public and cargo transport unions

Improve government capacity and implement better-targeted social assistance

- Apply technological innovations (i.e. smart cards and data collection)
- If administrative capacity is adequate, targeted cash transfers can protect poor
 - Armenia's targeted cash transfer program maintained consumption after electricity price hikes
 - Indonesia's nonconditional cash transfer program, which covered 35 percent of the population, helped overcome social and political opposition to fuel subsidy reforms
- If not, other programs can be used in interim
 - Gabon, Ghana, Niger, Nigeria, and Mozambique expanded existing social spending programs targeting the poor
 - Morocco expanded existing support to school-age children, helped the poor with medical expenses, and introduced new support for low-income widows, physically disabled individuals, and users of public transport
 - Philippines maintained electricity subsidies for indigent families, provided college scholarships for low-income students, and subsidized loans to convert engines used in public transportation to less costly LPG

Thank You