PRESS POINTS FOR CHAPTER 3:

OIL SCARCITY, GROWTH, AND GLOBAL IMBALANCES

World Economic Outlook, April 2011

Prepared by Thomas Helbling (team leader), Joong Shik Kang, Michael Kumhof, Dirk Muir, Andrea Pescatori, and Shaun Roache

Key Points

- **Global oil markets are in a period of increased scarcity, reflecting rapid growth in oil demand in emerging economies and a downshift in oil supply growth.**

- **Gradual and moderate increases in oil scarcity—which seems to be the most likely scenario—would have a small impact on medium-term global economic growth. However, risks remain that scarcity or its growth impact could be more significant.**

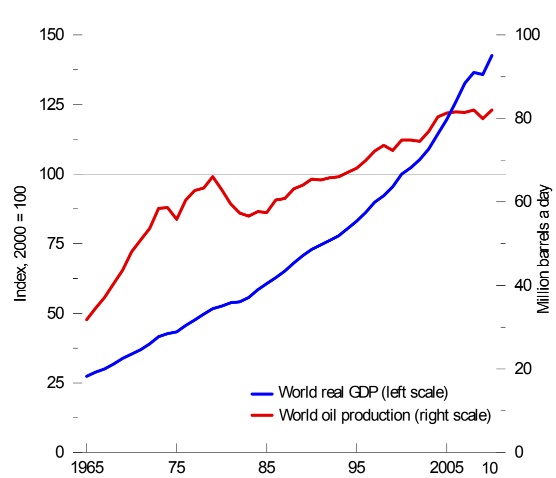
- **A persistent adverse oil supply shock would imply a surge in global capital flows and a widening of current account imbalances.**

- **Policies should aim at facilitating adjustment to unexpected changes in oil scarcity and at lowering risks from larger-than-expected medium-term oil scarcity.**

This chapter focuses on the risks from oil scarcity for the global economic outlook. We analyze the current status of oil scarcity and assess the impact of oil scarcity on global economic growth and global imbalances in the medium to long term.

The recent trend increase in oil prices suggests that the global oil market has entered a period of increased scarcity. The origins of this scarcity can be traced to the tension between the upward shift in global oil consumption growth due to fast-growing emerging market economies and supply constraints, which have led to a downshift in oil supply growth. The latter partly reflects the drag from a growing share of maturing oil fields, which have raised both the production and the opportunity cost of bringing an additional barrel to the market.

Global Oil Production and Real GDP



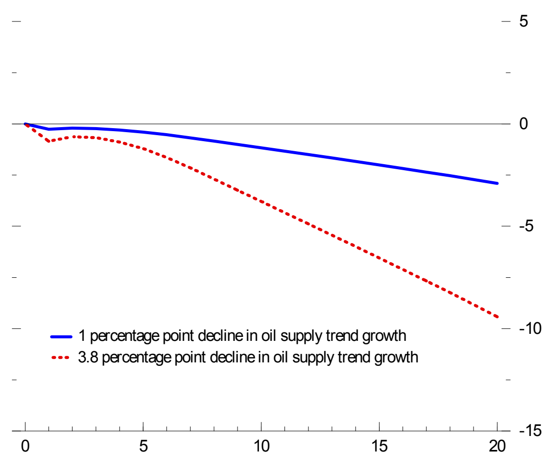
Sources: BP, *Statistical Review of World Energy;* and IMF staff calculations.

Scarcity is reinforced by the low responsiveness of both oil demand and oil supply to price changes, especially in the short-to-medium term. Nevertheless, the longer-term income elasticity of global demand for oil is below that of the demand for primary energy. This difference indicates that oil-saving efforts, technological change, and the move to more service-based economies have appreciable effects on the demand for oil.

It would be premature to conclude that oil scarcity will inevitably be a strong constraint on global growth. Our simulation analysis shows that gradual and moderate increases in oil scarcity, consistent with supply projections by others, may only be a minor constraint on global growth in the medium to long term. In particular, an unexpected sizable downshift in oil supply trend growth of 1 percentage point—from 1.8 percent to 0.8 percent— slows annual global growth by less than ¼ percent in the medium and long term.

Oil Scarcity and Global GDP Growth[1]
(Percent difference; years on x-axis)

A sizable downshift in oil supply trend growth of 1 percentage point slows annual global growth by less than 0.25 percent in the medium and long term. However, there are risks that scarcity or its growth impact could be more significant.



Source: IMF staff calculations.
[1]World: Total of all countries accounts for 78.78 percent of world GDP.

However, such benign effects on global growth should not be taken for granted since scarcity or its growth effects could be more significant. There are downside risks to supply, including from geopolitical risks, that imply that oil scarcity could be more severe and may materialize in large and abrupt changes. The growth effects would be correspondingly larger. In addition, it is uncertain whether the world economy can adjust as smoothly to increased scarcity as we assume, given redistribution and sectoral shifts. The growth effects could be larger, depending on the impact on productivity.

A persistent adverse oil supply shock would imply a surge in global capital flows from oil exporters to importers and a widening of current account imbalances. This underscores the need to reduce the risk associated with growing current account imbalances and large capital flows. Continued progress in financial sector reform is also critical, as the efficient intermediation of these flows is a prerequisite for financial stability.

There are two broad areas for policy action to mitigate the impact of oil scarcity. First, given the potential for unexpected large increases in the scarcity of oil, policymakers should review whether current policy frameworks facilitate the adjustment to such events: macroeconomic policies to ease adjustment in relative prices and resources and structural policies to strengthen the role of price signals would be desirable. Second, consideration should be given to policies aimed at lowering the risk of oil scarcity, including through the development of sustainable alternative sources of energy.