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The findings of this brief reflect the opinions of the authors and not those of the African Development Bank, its Board of Directors or the countries they represent.

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Key Points

- Weekly theme: «Energy subsidy reform in Africa: challenges, successes and lessons»
- Global equity financial markets stabilized after marked losses in the previous week.

Energy Subsidy reform in Africa: challenges, successes and lessons

From 2011 to date, many African countries took steps to drawdown on unsustainable fuel energy programs. The case for energy subsidy reforms was based on the fundamental argument that poorly targeted energy consumption subsidies deprive countries of scarce resources critical to other priority sectors. In Africa it is estimated that the top quintile of the income distribution captures about 45 percent of energy subsidy; the bottom quintile only receives 8 percent. In 2011 alone, fuel consumption subsidies in Nigeria, Cameroon and Ghana cost USD 7.5 billion, USD 600 million and USD 276 million, respectively. These spending accounted for 30%, 12% and 3% of federal government spending in those countries. These shares sharply contrasted the proportion of public spending on health in these countries which stood at 7.5%, 8% and 4% of total federal government spending, respectively.

Several factors contributed to the pervasiveness of energy subsidies on the continent and most of these factors were shared across countries. First, the administrative ease with which subsidies can be implemented as fiscal tools to provide visible benefits to all was desirable. This was especially true of countries with limited capabilities of providing targeted social welfare benefits to the poor. Second, the desire to prevent the transmission of spikes in global petroleum prices to the domestic economy was deemed important. This was true of cases where spikes in global petroleum prices were anticipated to be temporary. However, the persistence of shocks to energy prices meant the sustained use of central government resources to finance energy subsidies. Third, well-intentioned desires to expand the population’s access to energy products added to states’ burden of energy subsidy. These factors had solidified the political feasibility of energy subsidies making them difficult to remove without political consequences.

Source: IMF (2013)

Figure 1: Energy subsidies versus public spending on education and health (2011)
Despite these challenges, several African countries have taken steps to eliminate barriers towards successful and sustainable energy policy reforms and to ensure that the fiscal space resulting from the reduction in energy subsidies can be used for productive and efficient government spending. As a prelude to sustainable energy subsidy reform, countries took steps to reform public energy companies, and devise short-run measures to mitigate the impact of energy price increases on the poor. For instance, since 2011, by substantially reducing energy subsidies, fuel prices in Namibia and Niger were made to track international prices, while cross-subsidies in public and freight transport were equalized fuel prices between urban and rural areas. In Ghana, cross subsidies in favor of kerosene and liquefied natural gas, and price ceilings on public transport fares were used to mitigate the impact of energy price adjustments. Similarly, since 2012, the Nigerian government has made adjustment, albeit minimal, for national petrol and diesel prices to adjust to global levels while maintaining the price of Kerosene unchanged. However, these changes continue to be disputed. The 2013 budget shows that allocation for fuel subsidy has gone down to 20% of government spending. ‘Life-line’ tariffs in Kenya and Uganda provide cross-subsidized electricity rates for households consuming less than 50kWh and 15kWh, respectively.

Over 2008-2012, Gabon and Mozambique deregulated gasoline and diesel prices by 26% and 38%. Both countries took steps to expand budgetary allocations for social protection services including social benefits through work, income generation, community development, and expansion in public transport networks. Over the same period, Ghana took steps to ensure fuel-price adjustment formulae were made public. The National Petroleum Agency (NPA) was delegated with regulatory powers that were sheltered from political intervention. Energy reform in Niger had two components. The first component allowed international price variations to be passed down to domestic prices starting June 2011, while the second component drew down existing subsidies in the following 18 months.

Contrastingly, Namibia that boasts a fairly developed fiscal system has consistently used a formula to set fuel pump prices. The fuel price formula consisted of three components: basic fuel price based on the international spot price; domestic fuel levies and charges; and an account used to smooth volatility and local pump prices. Even though fuel prices are generally allowed to move in line with international prices, government accommodated volatility and pass-through of prices. However, fuel subsidies in Namibia are integrated into well-developed publicly funded social welfare programs. Social security, welfare and public housing spending averaged 5% of GDP in 2005-12.

There are unifying themes in these recent energy reforms that would serve instructive to other nations considering energy reform. First, the durability of the reforms will be enhanced by development of efficient social safety net frameworks and political commitment to announced goals of the subsidy reform. Second, dialogues with different stakeholders regarding the cost of subsidies and extensive public information campaigns have proved instrumental in minimizing social unrest. Third, research and analysis focusing on the costs of subsidies and price-controls and the benefits of reform are essential to measure economic gains.

1. Energy subsidy reform in sub-Saharan Africa (2013), International Monetary Fund, IMF Africa Department.
2. AEFB Vol.03, Issue 02, Jan 09-13, 2012.

Stock Markets

Global Markets

The week was characterized by positive market news, resulting in modest gains in equities in both US and European markets. US Industrial production rose in August by the most in six months, indicating U.S. manufacturing contribute more to expansion in jobs. Reports from the Federal Reserve showed that output at factories, mines and utilities climbed 0.4 percent after performing dismally. Manufacturing (EMPRGBCI), which makes up 75 percent of total production, advanced by the most this year. The strongest vehicle sales in almost six years are propelling factory activity, encouraging companies such as Ford Motor Co. (F) to boost plant capacity. A pickup in global markets and stronger consumer demand would help spark further progress in the sector that struggled earlier this year. These factors contributed towards a relatively more favorable economic outlook in the U.S. The DJIA gained 0.76% while the FTSE, CAC40 and Nikkei 225 Index rose 5.5%, 2.9% and 3.5%, respectively.

African Markets

Taking a cue from global markets, the South African All Share Index rose by 1.4% as global investors continue their holdings of emerging markets assets. Cyclical stocks such as mining and bank stocks gained the most. The Egyptian main index continues to be affected by sluggish domestic investor confidence amid continued political instability. Accordingly, the Egyptian composite index (EGX30) shed off 1.9%. In Kenya, the release of better than expected earnings in the banking sector for the first quarter of 2013 led to 0.24% gains in the NSE 20.
Commodity Markets

**Crude (Brent)**: The price of crude oil rose by 1.9%, on accounts of stronger performance in US Industrial production boosting the demand for oil. Reports from the EIA indicated monthly average crude oil prices increased for the fourth consecutive month in August 2013, as supply disruptions in Libya increased and concerns over the conflict in Syria intensified.

**Gold & Silver**: The price of gold price fell marginally by 0.2% as easing tensions with Syria and expectations that the US Federal Reserve will unwind its monetary stimulus led to the metal’s largest weekly loss since late June. However, silver price ended the week marginally higher at 0.3% as a result of favorable outlook for industrial demand for the metal. Unlike gold, silver is used in wide range of industrial applications and its price therefore is driven by the level of global economic activity.

**Cotton**: Cotton slipped by 0.6%, reaching $81 cents/pound. The latest price reduction come as a result of a slump in purchases by top cotton consumer China. China holds about 60 percent of world cotton stocks in state reserves. A radical plan to ditch its stockpiling programme in favour of subsidies to farmers that could lead to a long-term cut in China’s imports has also hurt market sentiment. During the week, Indian traders declared that Chinese imports from India slowed, reducing gains for Indian farmers ahead of the next sowing season.

**Coffee**: Arabica price ended the week unchanged at $106.75 cents/pound while robusta fell 0.7%. Robusta coffee fell by 0.7%–its lowest in more than six weeks on speculation that rain in Vietnam, the world’s largest producer of the variety, will benefit the crop starting Oct. 1.

**Cocoa**: The price of cocoa rose by 3.8%, recording its largest weekly gain since September 2012. Speculative buying, over concerns of dry weather in top grower Ivory Coast, has driven recent gains.
Currency Markets

The dollar edged higher against the Euro (0.9%) and Yen (1.9%) during the week after data showed a sharp fall in U.S. weekly jobless claims and a contraction in euro zone industrial output. Markets have tempered their expectations for any aggressive stimulus withdrawal by the Fed. That has led investors to lower long dollar positions built on expectations the Fed will unwind stimulus in recent months.

In Africa, currency markets showed mixed signs. The South African rand rallied against the dollar (0.7%) buoyed by the end of strikes at some gold mines. The Nigerian naira extended losses against the dollar (0.7%) due to strong demand for forex.

Sovereign Debt Issues in Africa

African yield spreads showed modest changes during the week, in response to global economic developments. Despite civil unrest in Egypt, yields on the Egyptian USD 2020 bond were lower on the month, shrinking to 9.1% compared to 9.2% at the end of the previous week. The rise in inflation reduced the attractiveness of Nigerian bonds for both local and international investors. In Ghana, the spread shrunk by 0.2% on weak market liquidity as expectations rose of potential excess demand at the next bond auction.

Relief Efforts on the continent

South Sudan: As of September 1st 2013, humanitarian agencies assessed that 27,000 people in five states need assistance following flash flooding. Over 17,000 of them are in Warrap State. In Unity State logistical constraints have prevented partners from accessing flooded areas and assessing needs, meaning that the total number of people in need could be significantly higher. Funding imbalances persist between emergency activities, such as food assistance, and longer-term activities addressing the basic drivers of needs, including livelihoods support.

Developments Partnerships

Guinea: The AfDB Group approved support for Guinea’s Conakry Electricity Network Rehabilitation and Extension Project (PRERECC) with loan and grant totaling US $16.66 million. The project will help to improve governance and commercial management of Guinea Electricity company (EDG), to support the government in reforming the sub-sector and to extend the electricity distribution network to 12 neighbourhoods in the Ratoma and Matoto municipalities in Conakry.
Countries in Focus

Liberia: The Liberian Senate concurred with the lower House on the passage of the Decent Work Bill setting the minimum wage at US$6 per day. Despite the passage of the bill, the issue of setting up of a Minimum Wage Board across every sector in the country remains an important task. Liberia's current minimum wage is set at US$0.25 per hour (or equivalent to US $2 per day).

Namibia: National Petroleum Corporation of Namibia (Namcor) is offering its Kudu Gas Project stake worth N$340 million. The Namcor board of directors disclosed its intentions to offload 70% of its 54% stake in the Kudu Gas Project, which is Namibia's planned N$10 billion power station that will generate electricity from a project called Kudu Gas Fields in the coast of the southern town of Oranjemund. The current shareholders of the gas project are Japan-based Itochu Corporation with 15%, while UK oil exploration company Tullow Oil has 31%.

Updates on African Economic Indicators

South Africa: Exports of goods and services from South Africa into Ghana have grown from about US$138 million in 2010 to US$516 million in 2012. Products such as vehicles, machinery, mechanical appliances; electrical equipment, base metals, aircraft, vessels and associated products contributed to the increased exports to Ghana. This made Ghana the second largest export market for South African goods in West Africa after Nigeria.

Zambia: Zambia's headline consumer inflation braked to 7.1 percent year-on-year in August, from 7.3 percent in July, mainly because of lower prices for food and non-alcoholic beverages.

Mauritius: The number of tourist arrivals from Europe declined by 5.1% to 50,050 in April from 52,550 one month earlier. Tourist arrival from France accounted for half of total tourists at 24,700, which was 3.4% lower than in March. The decrease in tourist flows was mainly due to the European debt crisis. Europe is Mauritius’ main source of tourists.

Nigeria: Nigeria’s naira fell to its weakest in more than 20-months on the interbank market on Thursday, as central bank tightening measures failed to stem the local currency's decline in the face of strong dollar demand.

Kenya: Kenyan shares fell to a seven-week low on Thursday as investors booked more profits and turned to higher returns in the debt market, while the shilling remained stable against the dollar. The weighted average yield on Kenya’s 91-day Treasury bills fell to 9.9 percent at auction from 10.5 percent last week.

Mozambique: A Mozambican state agency issued a government-guaranteed, seven-year bond valued at $500 million at a yield of 8.5%. This is the country’s first dollar bond issue. Its size makes it eligible for JP Morgan’s influential emerging markets EMBI index and gives it a level of liquidity that the government’s local-currency bond offerings lack. Rated B+ by Standard and Poor’s and Fitch, Mozambique issued just one local-currency bond a year between 2008 and 2012 and secondary market trading is virtually non-existent.
Global Economic Leading Indicators

Chinese Purchasing Managers' Index (PMI)

India Purchasing Managers' Index (PMI)

Japan Purchasing Managers' Index (PMI)

USA Purchasing Managers' Index (PMI)

Eurozone Purchasing Managers' Index (PMI)

US ISM Manufacturing Production Index

Source: US, Institute of Supply Management, 2013
## Appendix Table 1: Stock Market Movements – Week ending 06 September 2013

<table>
<thead>
<tr>
<th>Region/Country</th>
<th>Index Name</th>
<th>Index Code</th>
<th>Benchmark (31/07/2013)</th>
<th>31/12/2012</th>
<th>Value at end of last 2 Weeks (08/23/2013)</th>
<th>Value at end of last Week (08/20/2013)</th>
<th>Value at end of current Week (09/06/2013)</th>
<th>Market Capitalization (US$, million)</th>
<th>Weekly % change (09/06/2013)</th>
<th>Year to date % change</th>
<th>Week under review</th>
<th>Previous week</th>
<th>Dec 31 2012 - September 06</th>
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<td>USA</td>
<td>Dow Jones Industrial</td>
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Source: Bloomberg. ▲ value at end of 07/09/2013

## Appendix Table 2 : Exchange Rate Movements – Week ending 06 September 2013

<table>
<thead>
<tr>
<th>Region/Country</th>
<th>Currency Code</th>
<th>Value at end of last 2 Weeks (08/23/2013)</th>
<th>Value at end of last Week (08/30/2013)</th>
<th>Value at end of current Week (09/06/2013)</th>
<th>Weekly %change (09.06.2013)</th>
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Others
Europe
EUR 0.75 0.75 0.76 ▼ -0.83 ▼ -0.53
Japan
JPY 98.34 98.04 99.90 ▼ -1.86 ▲ 0.31

Source : ADB Statistics Department September 2013.
▲ in the interbank currency market.