

The Role of a Hydrocarbon Fund in Trinidad and Tobago?

Mr. Dennis Pantin and Mr. Dale James
Sustainable Economic Development Unit (SEDU)
Department of Economics, UWI,
St. Augustine. Trinidad
CCMS Senior Policy Seminar. May 2-3, 2005

CONTENT OF PRESENTATION

- 1. Economic Principles in Nat Resource based Economies.
- Key Challenges facing T&T?
- 2. Role of A Hydrocarbon Fund in meeting these challenges?
- 3. Ideal type of Fund(s) for T&T?
- 4. Why a Fund is a necessary but not sufficient condition for rising to the key challenge
- 5. What is the Sufficient Condition?

Key Principles for Natural Resource based Economies

- EMCI Principles:
 - (E)quity: Intra and Inter-Generational
 - (M)easurement of Economic Rents
 - Capture of Economic Rents
 - (I)vestment of Economic Rents
-
- Where Economic Rents are defined as unearned income from nature.

Role of Investment

- Assuming Capture and given Equity Principle, Investment involves:
- Maximising Value Added from Natural Resources together with:
- Diversifying Production to minimise risk exposure from natural resource dependence.

1. Key Challenge Facing T&T?

- To avoid the economic errors made in the two prior hydrocarbon booms of the late 1950s and 1974-1981
- And to exploit the opportunities of the present oil and gas windfalls to create a fully employed, globally competitive economy with equity.

2. Role of a Hydrocarbon Fund in rising to the challenge

- A. Types of possible Funds;
- B. The history of such Funds since the 1950s
- C. Financing Sources for Funds;
- D. Investment Policies
- E. Withdrawal rules

A. Types of possible Funds

- Stabilization Funds to smooth path of fluctuations in price/income from natural resources;
- Heritage or Permanent Funds are Savings and Investment Funds to address inter-generational equity.
- Mixed Stabilization/Heritage Funds

A. History of Funds since 1950s

- 1950s: Kiribati (Stabiliz& Savings)
- 1960s: Kuwait(Stabiliz& Savings)
- 1970s: Alaska, Alberta and Kuwait: (Savings);
- 1980s: Chile(Stabiliz); Oman(Svings)
- 1990s: Oman(Stabilisation: abolished 93)
- ;Azerjaiian, Norway and Venezuela:Savings;
- 2000-2005:Algeria, Iran, Mexico,T&T(Stabiliz)
- Kazathan and T&T(Savings?)

C. Financing Sources for Funds

- Sources include - in the main- income in excess of some set price from hydrocarbons;
- However, Alaska, Alberta include other natural resources including forests;
- Kuwait sets 10% allocation to Savings Fund whatever is price trend.

D. Investment Policies

- Control of Funds vested in most instances in Ministries of Finance and Central Bank which, in some instances, create distinct institutions to manage portfolio: e.g. Norway's 'Chinese wall' between Central Bank and Fund Manager;
- In some instances Parliament also has oversight of investment policies.

E. Withdrawal Rules

- Withdrawal rules vary in terms of extent of transparency, accountability and participation of Parliament and public in process;
- In many instances, withdrawal is at discretion of Government alone;
- Most robust is Alaska's Permanent Fund which requires a referendum for access to the Principal in the Fund.

3. Ideal type of Fund(s) for T&T?

- Distinct Stabilization and Permanent Funds with also differing rules for access;
- Stabilization Fund should be accessible with Parliamentary approval;
- Permanent Fund ought to require referendum

4. Why a Fund is a necessary but not sufficient condition for rising to the key challenge

- As Davis et al have argued Natural Resource Funds may be considered 'Problems posing as Solutions' with their Econometric analysis of 12 oil exporting countries (5 with Funds) showing that in most instances Govt expenditure rose and fell with oil income flow

4. contd

- It is only in a few of these 12 countries that expenditure did not follow oil income flows and for those with Funds this occurred BEFORE and after the establishment of Funds.
- E.g. T&T had a Savings/Stab Fund in all but name in the last oil boom which grew to US\$2.3 billion in 1981;
- By 1987 this disappeared together with US\$1 billion in additional foreign borrowing being incurred.

4. contd

- Even well designed and protected Stabilization and Permanent Funds cannot, in themselves resolve the distortions caused by booming hydrocarbon earnings including the crowding out of other globally competitive production of goods and services.

4. Oil Rentier Economies

- Need to face reality of Oil Rentier Economy defined inter alia, as one in which “ a minority of the pop is engaged in the generation of the rent while the majority is involved in the distribution and utilization of it.”
- E.g. current T&T Real Estate market price trends

4. Transforming Rentier Econ

- Three requirements:
- 1. Technical (easiest of all);
- 2. Transforming the Rentier State to provide for real transparency, accountability and participation;
- 3. Transforming the Rentier psychology of the society.

Technical Solutions

- Modify Nat Income Acts to measure genuine savings;
- Sterilize windfall incomes;
- Establish Modified Currency Board;
- Industrial/HResource/Techn Policy;
- Provide incentives for non-hydrocarbon investment.

Transforming Rentier State and Society

- Civil responsibility for the future beyond personal self-interest involving:
- Public education;
- Advocacy (e.g on Best Uses of Natural Gas and ownership, tax, HRD/technology policy).