

Export Growth - Fuel Price nexus in Developing Countries: Real or False Concern?

Kangni Kpodar,^a Stefania Fabrizio,^b and Kodjovi Eklou^c

In many developing countries, despite the current favorable environment of relatively low international oil prices and the debate on climate change, tight control on domestic fuel prices is still prevalent, often giving rise to large subsidies. A major bottleneck to fuel subsidy reform is that policymakers are concerned about the consequences on export-oriented sectors, which typically drive economic growth, bring in foreign exchanges and are potential large employers.

Against this backdrop, this paper investigates how a rise in domestic fuel prices affects export growth in a sample of 77 developing countries over the period 2000-2014, taking advantage of an original fuel price database compiled by Kpodar and Abdallah (2017). Our analysis focuses on three main questions: (i) does an increase in domestic fuel prices hamper a country's export performance? (ii) is there any heterogeneity related to energy dependency and access to alternative source of energy? and (iii) does this effect vary with the temporal horizon?

We find that domestic gasoline or diesel price increases have a negative effect on real non-fuel export growth. But, while this negative impact is mild or non-significant for countries with a low energy dependency ratio, it becomes significant and sizeable for countries with high energy dependency ratios, arguably where energy inefficiencies are more pronounced. Further, the adverse effect of fuel price increases on exports declines with better access to electricity. Furthermore, investigating large fuel price shocks suggest that they do not necessarily have disproportionately large effects on export growth. Finally, in disentangling the short-run and medium to long-run impact, the findings suggest that the adverse effect of fuel price shocks on export growth is short-lived. It is mostly concentrated within the first two years after the shock and becomes weak and non-significant thereafter. Nevertheless, this could translate into a permanently lower level of exports unless the medium-term efficient gains from better allocation of resources materialize.

This paper tackles important gaps in the existing literature such as the scarce evidence on the energy prices-competitiveness link in developing countries, the lack of cross-country studies allowing to draw broad policy conclusions relevant for a large group of countries, and the limitations in existing studies which do not control for macroeconomic factors that matter for export dynamics, or do not explore how the energy prices-competitiveness link may change with the temporal horizon.

As for the policy implications, countries seeking to increase domestic fuel prices (whether it is in the context of a subsidy removal plan or it is driven by higher international oil prices) should consider, when appropriate, mitigating measures and structural reforms that focus on reducing energy inefficiencies and enhancing access to other sources of energy, which should help a long way in minimizing potential adverse consequences of higher fuel prices on exports. Access to credit is critical to enable firms to undertake the investments needed to switch to a more energy efficient technology. Fiscal space permitting, boosting infrastructure spending, including to support adequate and reliable access to electricity, would be beneficial to the productive sectors.

a Corresponding author: International Monetary Fund and FERDI, 1900 Pennsylvania Ave NW, Washington, DC, 20431, USA. Email:kkpodar@imf.org

b International Monetary Fund, 1900 Pennsylvania Ave NW, Washington, DC, 20431, USA. Email: sfabrizio@imf.org

c International Monetary Fund, 1900 Pennsylvania Ave NW, Washington, DC, 20431, USA. Email: keklou@imf.org