

# Transport & Fossil Fuel Subsidy Reforms

Experiences & Lessons Learned

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WB – ESMAP KNOWLEDGE EXCHANGE FORUM

# Why is the transport sector important when designing fossil fuel subsidies reforms?

## 1. **Transport is one of the economic sectors with the highest consumption of fossil fuels worldwide:**

Globally, it is responsible for ca. 25% of energy consumption (2015); >70% are fossil fuels. The sector is directly responsible for close to 15% of global GHG emissions.

## 2. **Transport usually represents a large share of value-added & employment.**

It accounts for ~5% of GDP (directly) in countries like India, Brazil and the EU.

## 3. **It represents a large share of households monthly expenditure.**

On average according to the WB it can represent between 5 to 17% of HH annual consumption (2010) depending on the region.

## 4. **The transport sector wields political power, usually pushes back and can end up derailing the reforms**

Brazil, Haiti...

# Why is the transport sector important when designing fossil fuel subsidies reforms?

## 2 channels of economic impacts from liberalizing fuel prices :

**1. *Direct impact*** in passenger and freight transport by increasing their operational costs; and thus cost of using transport services (incl. public transport, private vehicles, etc.).

**2. *Indirect impact*** to consumers by increasing the price of goods where transport is an important input (such as food).

↪ Incidence of these impacts depends mostly on the structure and regulation of the transport sector

## Failed Reforms.

Brazil's trucking sector strikes paralyze the country.

### Context:

- Brazil attempted to liberalize the energy sector in 1990s, incl. removing fossil fuel subsidies.
- Between 2002-2007 many reforms were achieved and subsidies removed in 2001/02.
- In 2008, oil price increases + oil discoveries led to a reintroduction of ff subsidies. Between 2013-2017 = ~1% GDP/yr.

### Reform attempt:

- In May 2018, the GoB attempted to increase diesel prices by 10% in the context of BRL depreciation and higher oil prices
- For 10 days, truck drivers blocked national highways across Brazil in protest, severely paralyzing economic activity across the country.



## Failed Reforms.

Brazil's trucking sector strikes paralyze the country.

### Consequences of the strikes:

- On May 21st +100,000 truck drivers started a strike, halting deliveries of food and fuel, grounding flights and costing as much as US\$13.5bn, or 0.8% of GDP, during the 10 days strike.
- Cities of Sao Paulo, Rio de Janeiro, Porto Alegre and Pernambuco declared a state of emergency due to fuel shortages.
- To stop the strike the GoB had to revert its reform, and:
  - Reduce fuel prices by 0.46 BRL/Liter,
  - Freeze them for 60 days (extended until December 2018)
  - Eliminate several taxes on trucks for goods (fiscal cost of 9.5bn BRL).
  - Toll exemption on empty trucks and introduction of min. freight fare for truckers.

### Lessons Learned:

- Important to time reforms (phasing + political moment). In Brazil elections in 2018 reduced the GoB's negotiating margin.
- Negotiate beforehand with difficult sectors such as transport and agree on mitigating measures.

## Failed Reforms.

### Roadblocks and riots in Haiti lead to reversal

#### Context (previous attempts):

- **In 2011** government stopped pegging domestic prices to global oil markets leading to large fuel subsidies. Reached 2.2% GDP by 2014.
- **In 2014**, 7% fuel price increase eliminated consumer subsidies on fuels. Backtracked in early 2015

#### Reform attempt:

- **July 2018:** Government introduced a 40% hike in fuel prices overnight, along with mitigation measures:
  - Labor-intensive works (10,000 people had already been recruited);
  - Scaled-up CCT, introduced health insurance for transporters; transport vouchers.
  - To assuage transport unions, agreed to increase transport fares by three times more than what fuel price increases justified.

## Failed Reforms.

Roadblocks and riots in Haiti lead to reversal

### Consequences of the strikes

Large protests in Port-au-Prince and roadblocks across Haiti cost ~2% GDP. 3 people died. Prime Minister resigned. Reform was reversed.

### Lessons learned

- It is not enough to introduce consumer mitigation measures, if these are not properly communicated to the public.
- If other transport subsidies need to be reformed (currency depreciation pushing up costs of parts, wage inflation, etc.), this needs to be managed in parallel of the fuel subsidy reform to control the impact on fares.
- Informality of public transport sector can become an additional difficulty.



## Positive Reforms.

### Ghana fuel liberalization experience.

#### **Context (previous attempts):**

- Several attempts to liberalize prices in the 1990s.
- In 2003, new attempt at liberalization. Stopped due to widespread opposition and reversed the price increase (+90% pump prices); Elections were planned in 2004.

#### **Different Phases: The bases were laid in 2005.**

- In 2005 new attempt of fuel price deregulation which was accompanied by complementary strategic measures:
  1. WB/IMF research revealed that the program was regressive (Coady & Newhouse 2006) + Communication strategy (showcasing above results).
  2. Programs to mitigate the impact on the poorest consumers (elimination of fees for state-run primary and secondary schools; + funding for healthcare in poor areas; an increase in the minimum wage).
  3. Transport Specific Measures: An increase in public-transport buses; a price ceiling on public-transport fares negotiated with bus operators.
  4. Public release of automatic price-adjustment mechanism, transferred to the National Petroleum Authority (NPA).



## Positive Reforms.

### Ghana fuel liberalization experience.

#### Removal & New Reform (2015):

- During the 2007–08 global fuel and food crisis and in the run-up to the 2008 elections, *automatic* adjustment was temporarily suspended. A period of controlled adjustments followed, by which the pass-through was negotiated.
- **Between 2013-2015**, the full removal of fuel subsidies was carried out (with gradual rises until prices reached market levels in mid-September).

#### Lessons Learned:

- A constant dialogue with the transport sector unions and civil society about the cost of subsidies is necessary to maintain commitment to the reform.
- Mitigating measures should come hand in hand with the reform (transport sector measures were negotiated with operators as early as 2005).
- Political will and commitment were key.

## Positive Reforms.

### Philippines Public Transport Assistance Program.

#### **Context: Failed stabilization fund to full liberalization**

- **1990s:** Oil Price Stabilization Fund resulted in large subsidies and government bailouts – USD 0.6 bn in direct subsidy in 1996.
- **1997-98:** phased transition to liberalization of downstream oil sector in midst of Asian financial crisis and currency depreciation. Deregulation law passed in 1998, achieved in two phases.
  1. Transition phase: oil import liberalized and the automatic pricing mechanism implemented with monthly price adjustments
  2. Full deregulation 5 months later with abolition of oil price setting

#### **Challenges:**

- Political opposition to deregulation and independent inquiries in 2005, 2008, and 2012.
- Impact on transport sector, esp. *jeepneys* whose fares are regulated



## Positive Reforms.

### Philippines Public Transport Assistance Program.

#### **Transport mitigating measures:**

- Weekly meetings with the Public Transport group leaders
- Public Transport Assistance Program (PTAP): short-term cash transfers to operators through debit and smart cards.
- Alternative Fuels Program, including investment in domestically produced electric tricycles.
- Social protection program: Since 2007, development of major 4Ps program, including a food assistance, work, rice subsidy and a conditional cash transfer (CCT) programs.
  - **July 2018:** reintroduced PTAP to compensate for incremental costs due to an excise tax hike.

#### **Lessons Learned:**

- Transport support mechanisms matter even when they are very small amounts
- Once set up, these targeted transfers can be reused in periods of price hikes
- Active communication campaign and independent inquiries help inform the public and ultimately gain acceptance for reforms

## Way forward?

### Plan the reform

1. Consider fuel price subsidies with other transport subsidies and design a combined subsidy reform strategy. Also communicate rationale for reforming these jointly.
2. Targeted transport consumer subsidies to the poor to ensure affordability while setting fares at cost-recovery;
3. Supply side measures can help in parallel to reduce costs: eg. support to renew bus fleets, rationalization of bus routes.
4. Transport operators support mechanisms matter even when they are very small amounts. Once set up, they can be reused in periods of price hikes.
5. Maintaining a constant dialogue with the transport sector operators and civil society about the cost of subsidies is necessary to maintain commitment to the reform.

Thank you!

## Way forward? Plan the Reform.

### Ecuador's reform?

In 2018 the GoE discussed the intention of reforming fossil fuel subsidies.

According to a WB study, between 2007-2016 fuel subsidies = between 2 & 8% of GDP per year (opportunity cost). In 2014, Ecuador spent US\$367 per person on fuel price subsidies, whereas per capita education spending was US\$299, and health spending was US\$137.

Discussion around subsidy reform began in the mid-1990s, with limited results. In 2018 – the new Government decided to start a fuel subsidy reform.

1. They started by liberalizing the price of gasoline and are defining a strategy for diesel.
2. The WB is supporting the reform with analytical studies of how different sectors will be impacted by the removal and what could be the mitigating measures. In the transport sector the focus is on both policies that can mitigate price increases in urban transport and freight sectors.