In this work the IMF has changed the debate on energy subsidies. They have argued correctly and persuasively that we must go beyond explicit subsidies and recognize that letting pollution go uncharged is to give a zero price to something that is very costly, in other words, to subsidize. Failing to correct market failure is to undermine the effectiveness of markets. Further, they take the concept forward in serious and important calculations which show just how pervasive energy subsidies are in rich countries and in poor. It is a splendid contribution.

Nicholas Stern
IG Patel Professor of Economics and Government
Chair, Grantham Research Institute on Climate Change and the Environment
London School of Economics
President of the British Academy

This book builds on an extensive cross-country analysis to make recommendations on how to best implement reforms aimed at reducing state subsidies on energy. The first part of the book identifies the costs of not implementing such reforms: (i) an increased burden on public budgets, which reduces the scope for investing more in energy-saving or clean innovations; (ii) an accelerated depletion of natural resources; (iii) an increase in inequality between high- and low-income households; and (iv) more CO_2 emissions, which aggravates the process of global warming. The book also identifies a number of political economy factors to explain governments' reluctance to engage in energy subsidy reforms, in particular, the lack of confidence in governments, and it makes suggestions on how such factors could be (or were) mitigated. The cross-country analysis shows a wide diversity in the way various countries approached the problem. Overall, the book is a gold mine for researchers and policymakers working on energy and sustainable growth and development.

Philippe Aghion
Robert C. Waggoner Professor of Economics, Harvard University

Although our planet has to grapple with the twin problem of scarce energy resources and the adverse environmental consequences of burning fossil fuels, many countries are still subsidizing petroleum products, electricity, natural gas, and coal. This wonderful study offers the best and most comprehensive estimates of such subsidies for a sample of 176 countries. A convincing case is made that these subsidies not only aggravate scarcity and pollution, but also crowd out health and education spending and depress private investment. Furthermore, they are highly distorting and a very inefficient way of redistributing incomes. The 22 country case studies offer warnings, but also suggestions for sustainable reform. This timely book is a must for policymakers in developed and developing countries.

Rick van der Ploeg
Research Director, Centre for the Analysis of Resource Rich Economies
and Professor of Economics, University of Oxford

The best policy-related economics is empirical work that is new, brave, and important. *Energy Subsidy Reform: Lessons and Implications* hits all three targets: new, because the research uncovers the extent and damage of energy subsidies globally, with a scope never before seen; brave, because it challenges both the poorer countries to reconsider what has been a subsidy to the rich cloaked as welfare, and the richer countries to recognize the scale of their own wasteful distortions; important, because it gives practical steps and examples of how this call to action against fiscal and environmental crime can be met. This is the kind of study we need addressing one of the key underappreciated policy disasters of the world today.

Adam Posen
President, Peterson Institute for International Economics

Energy Subsidy Reform

Lessons and Implications

EDITORS
Benedict Clements, David Coady, Stefania Fabrizio,
Sanjeev Gupta, Trevor Alleyne, and Carlo Sdralevich

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Sanjeev Gupta
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Preface

This volume provides the most comprehensive estimates of worldwide energy subsidies currently available, drawing on data from 176 countries in the areas of petroleum products, natural gas, coal, and electricity. It lays out an analysis of "how to do" energy subsidy reform, drawing on insights from 22 country case studies and analyses carried out by other institutions, and it offers summary narratives and analyses of the reform efforts undertaken in each of those countries. Among the findings that emerged from the analysis are the following.

Energy subsidies have wide-ranging economic consequences. Although aimed at protecting consumers, subsidies aggravate fiscal imbalances, crowd out priority public spending, and depress private investment, including in the energy sector. Subsidies also distort resource allocation by encouraging excessive energy consumption, artificially promoting capital-intensive industries, reducing incentives for investment in renewable energy, and accelerating the depletion of natural resources. Most subsidy benefits are captured by higher-income households, reinforcing inequality. Even future generations are affected through the damaging effects of increased energy consumption on global warming.

Energy subsidies are pervasive and impose substantial fiscal and economic costs in most regions. On a "pretax" basis, subsidies for petroleum products, electricity, natural gas, and coal reached US$492 billion in 2011 (0.7 percent of global GDP or 2 percent of total government revenues). The cost of subsidies is especially acute in oil exporters, accounting for about two-thirds of the total. On a "posttax" basis—which also factors in the negative externalities from energy consumption—subsidies are much higher, at US$2.0 trillion (2.9 percent of global GDP or 8.5 percent of total government revenues). Advanced economies account for about 40 percent of the global posttax total, whereas oil exporters account for about one-third. Removing posttax subsidies could lead to a 15 percent decline in CO_2 emissions and generate positive spillover effects by reducing global energy demand.

Country experiences suggest that there are six key elements for effective subsidy reform. These are (1) a comprehensive energy sector reform plan entailing clear long-term objectives, analysis of the impact of reforms, and consultation with stakeholders; (2) an extensive communications strategy, supported by improvements in transparency, such as the dissemination of information on the magnitude of subsidies and the recording of subsidies in the budget; (3) appropriately phased price increases, which can be sequenced differently across energy products; (4) improvement in the efficiency of state-owned enterprises to reduce producer subsidies; (5) targeted measures to protect the poor; and (6) institutional reforms that depoliticize energy pricing, such as the introduction of automatic pricing mechanisms.