Oil funds

Business

Most oil producing countries in the world of capitalism always want more.

They want more profit, and more market share, and more revenues from oil among others. The realizations of these objectives have been attained through the successful initiation, development and management of oil revenues in most instances. Indeed, the effective development and management of oil revenues has become a major priority for all oil producing nations. The reasons for this are certainly clear; better revenue management are positively correlated with improved quality and profits. However, the efficient management of oil revenues can present challenges, especially in the case where producing nations are unable to accurately evaluate and assess their priorities in regard to their strengths and weaknesses objectively. One major limitation that has been presented in both academic and empirical literature is on how to deal with the multifaceted issue of better management of resources.

Types of Oil fundsThere are three main types of oil funds. These include savings funds, stabilization funds and financing funds funds. Because the finite nature of oil revenues and un-diversified base, oil producing countries have set up funds for future generations. According to Davis, Ossowski, Daniel, and Barnett, (2001) “ A volatile and uncertain fiscal revenue source renders fiscal management, budgetary planning, and the efficient use of public resources difficult particularly in the case when it makes up a large share of total revenue”. This fact is also highlighted by Medas and Daria (2009) in stating that “ oil revenue volatility poses particular challenges for macroeconomic management in OPCs.

” This has called for the need to develop or establish a financial investment. The savings fund involves “ Transfers to the funds are made independently of oil market and/or overall fiscal developments (a given percentage of government revenue goes to the fund” (Medas and Daria, 2009). The uncertainty and turbulent nature of the global oil market has necessitated the need by governments to develop fiscal financial policies aimed at enhancing the public spending of oil revenues for better management. The overall objective of savings funds is for posterity. According to Medas and Daria (2009), “ government accumulates large resources -ranging from 10 percent to 70 percent of GDP for future generations.” Medas and Daria (2009) stabilization funds on the other hand are fund set up by governments to smooth up the operations of revenue in cases of oil vitality.

The main objectives of this fund are for operational objectives and policy objectives. In the realization that frequent and massive adjustments in expenditure have a resounding effect on investments and plans, there is need to create a benchmark. This is the role played by stabilization fund. According to Davis et al (2001), “ a stabilization fund is a mechanism designed to reduce the impact of volatile revenue on the government and the economy. Its objectives may also include supporting fiscal discipline and providing greater transparency in the spending of revenue.

“ Stabilization funds in two aspects. These include the contingent stabilization funds and stabilization funds and the fungibility resources. The former, as the name suggests is aimed to smooth the fluctuations in the recurrent resources in the budget. This is achieved the reductions or total elimination of resource related revenues that are precipitated by uncertainty

and volatility of the resource. Various oil producing countries have flexible legislations that govern the operations of contingent stabilization funds.

This is because, according to Davis, Ossowski, Daniel, and Barnett, (2001) Contingent funds with fixed rules may prove difficult to design and operate it may not be possible to specify long-run averages for prices or revenues with any degree of confidence, nor to determine whether a particular shock is likely to be permanent or not. Last, the financing fund are designed to effectively finance the overall budget balance. According to Davis, Ossowski, Daniel, and Barnett, (2001) " a financing fund provides an explicit and transparent link between fiscal policy and asset accumulation, and addresses fungibility issues." this means that changes in the assets held by the fund correspond to those in the overall net financial asset position of the government, which is driven by the overall fiscal balance" (Ossowski, Villafuerte, Medas, and Thomas, 2008). This type of fund is more related to the political economy of the state. This is because it supports temporary adjustments on expenditure without impacting greatly on expenditure fragmentation.

Challenges in effectively developing working policies that have the capacity to ensure the above discussed oil funds achieve their objectives exist in large numbers. This is not particularly hard to discern given the levels of inefficiency and corruption that has characterized the management of resources in some countries. This is because of lack of transparency and accountability in the operations that directly involve the expenditures of oil funds. This problem is further compounded by the lack of comprehensive policy on how to manage the funds. According to Ossowski, Villafuerte,

Medas, and Thomas (2008), the problem of accountability and transparency is exhibited by vast oil producers because “ Only a few of the oil funds examined have a clear, comprehensive, and transparent investment strategy” Furthermore, accountability, integration of oil funds into the budgets and asset management vary and depends largely on the political economy of the particular country. This fact is buttressed by Ossowski, Villafuerte, Medas, and Thomas (2008) in stating that “ Transparency and accountability practices for oil funds differ substantially across oil-producing countries.

” The fiscal stance of oil producing countries, their conventional fiscal indicators non – fiscal balances are not properly balanced by non-oil indicators. In addition to the above, most oil producing nations have failed to effectively integrate oil funds within their budgets and properly manage assets financed by oil funds. The pivotal reasons for setting up oil funds vary from one nation to the other and depend on number of factors that are in most instances unique to a particular nation. Funds may be set to as demonstrated by Sturm, Francois and Gonzalez (2009), “ ensure intergenerational equity, maintain competitiveness in the market, strengthen demand management or make expenditure less driven by short-term revenue availability.” The most important thing is that there should be a laid down policy framework on how the funds set aside will meet their aims of objectives. This will call for accountability and transparency, rid off corruption and underline right priorities.

Given the above perspectives, it would be prudent to state here that countries engaged in oil production need to bear in mind that fluctuations

and volatility of the resources affect not only the immediate plans in regard to service provision but also long term projects. This opinion has been supported by several other researchers and writers in natural resource amangemnet. The underlying philosophy is that in order that specific market objectives and envisaged competitiveness in the industry are attained, oil producing nations need to increasingly adopt transparent and accountable policies in regard to the management and allocation of oil revenues. Essentially, this will translate into increased efficiencies, market development, market competitiveness and improved performance. Good management of portfolios of in management is best initiated where common measures of performance have been delineated.

Researcher have however pointed out that it might take a long time before oil funds become fully exploited for the benefits of the entire populations. The rules of operations must be open and transparent to the public. Last, there is need to invest the resources abroad to prevent the dilution of competitiveness from non-oil sectors.