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Impact of Oil Price Drop on Lebanon's Economy & Petroleum Sector

Lebanese gains and losses from lower oil prices

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The fall of crude oil prices by 50 percent since June is seen to largely benefit oil-importing economies and to challenge oil exporters. In the case of Lebanon, an energy importer and aspiring energy exporter, there are mixed effects on its broader economy, and vital lessons as it works to launch its oil and gas industry.

On the economic front, the World Bank highlighted in a recent report the primary benefit of the oil price drop to come from a lower fuel bill for the national electricity company, Electricité du Liban. This is significant given that in the past four years exceptionally high oil prices have cost the Lebanese government, on average, an astounding 4.7 percent of GDP to maintain electricity prices constant, by covering any price difference above $23 per barrel.

Another positive impact is the fall of 20 liters of gasoline from LL39,000 to LL22,000, benefiting consumers. If low prices are sustained, the effects can eventually create an economic boost by increasing the spending power of cash-strapped consumers. However, some economists are advocating slightly raising gasoline taxes to help reduce the budget deficit and finance higher wages for civil servants.

On the negative side, the flow of remittances from Lebanese emigrants could be at risk. In 2014, Lebanese expatriates sent a significant $7.7 billion to support families back home – which constitutes more than 16 percent of Lebanon's GDP. As 60 percent of these financial flows come from Gulf countries, they could be at risk due to lower oil price leading to project delays, budget cuts and may ultimately impact the employment and income of Lebanese working in the Gulf Cooperation Council states.

This has caused Central Bank Governor Riad Salameh to find falling oil prices the biggest economic challenge facing the country in 2015.

Other sectors are also likely to be impacted, including energy-intensive industries such as Lebanese manufacturers. Lower fuel bills can decrease their production costs, enhancing their competitiveness.

On the political front, the flow of political funding from neighboring countries could possibly decline and influence domestic politics as well as regional conflicts in Syria and Iraq.

When it comes to Lebanon's embryonic oil and gas sector, the sharp energy price drop offers a significant cautionary tale as the country prepares to launch its first licensing round.

As Lebanese witness the extreme volatility of energy markets, this serves as a reminder of the painful repercussions on the economies and citizens of countries highly reliant on commodity exports. This is why proper planning will be crucial early on. For example, a stabilization fund must be set up to cushion the economy. Countries with poor planning such as Venezuela and Yemen, for example, are expected to face deficits of 17 and 9.5 percent of GDP respectively and will have to borrow internationally to maintain their current spending.

This can also be an opportunity to persuade the Lebanese to diversify the economy away from the oil sector. Future oil revenues will have to be invested to develop other industries, and saved for future generations.

The new reality of cheaper oil also has unclear effects on investments in new oil exploration and development. Several dynamics could pose serious risks for Lebanon as it works to launch its first licensing round. It can however be turned into an opportunity if decision-makers devise a thoughtful strategy to attract investors.

Energy companies are widely reported to be tightening their budgets and have a reduced appetite to explore new basins. A striking Goldman Sachs analysis found that almost $1 trillion in future oil project investments across the world will no longer be economically viable with Brent crude at $70. Countries, such as Lebanon, seeking to attract new investments must now compete more seriously with other countries that could slash royalties and taxes to maintain the interest of companies.

On the flip side, the situation today might be an opportunity to start new exploration projects. Some analysts anticipate that energy prices will rebound in the long run and believe that now is the right time to advance offshore exploration – which would start production in five to eight years, making the most out of future oil price booms. Such projects could be economically viable given the decline in drilling equipment costs which make up to 40 percent of the total cost of offshore projects.

These are timely insights as the Cabinet reviews decrees outlining how best to attract international oil companies while maximizing Lebanon's share of profits, and the best timing to launch the licensing round.

The strategic importance of these decisions deserves to be widely and transparently debated. It is the right of Lebanese citizens to be informed and involved in shaping strategic choices that will impact their future.

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