Libya: crude implosion

by Florence Gaub and José Luengo-Cabrera

While Libya may have already collapsed in political and security terms, yet another disaster looms on the horizon: an economic crash which could soon unleash a humanitarian crisis if no solution is found. The main cause is the country's economic structure: it is hugely dependent on oil to generate revenue, the majority of Libya's population is employed by the public sector, and most of its food is imported. Consequently, if the Libyan state goes bankrupt, it will take large parts of the population down with it.

A slippery oil slope

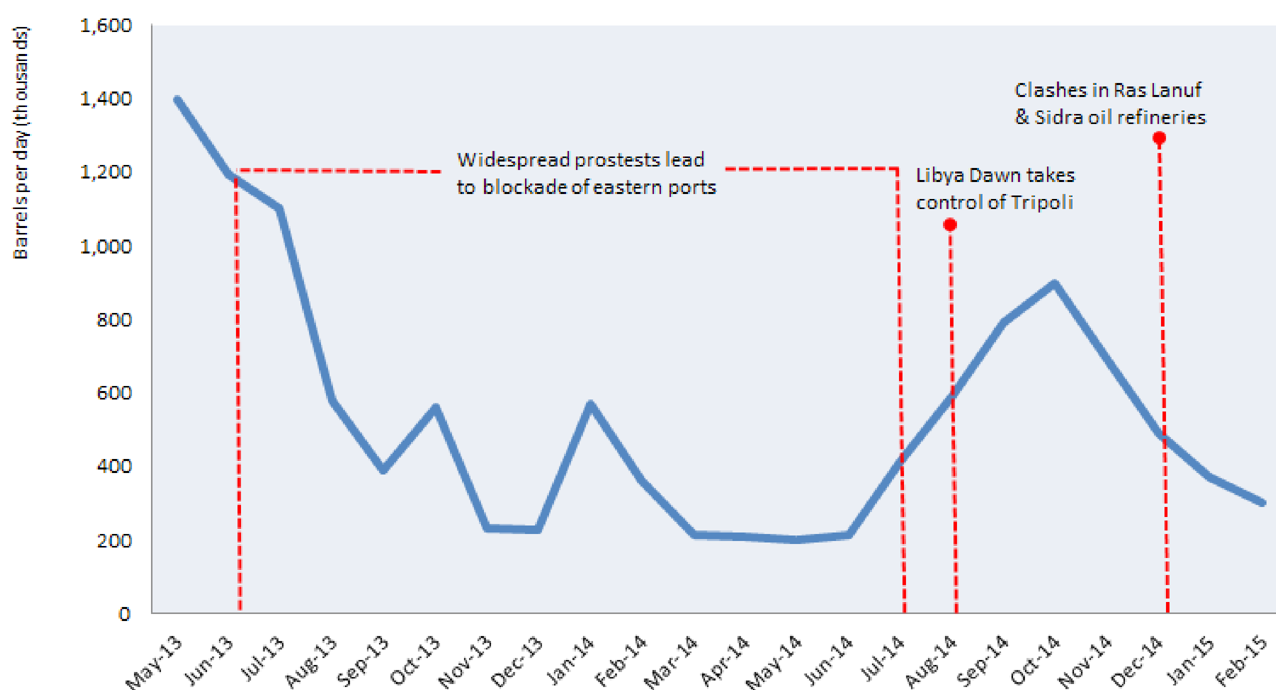
Libya's oil reserves are simultaneously the source of its wealth and its economic weak point. As 90% of its revenues stem from the production and export of oil, the country is highly vulnerable to anything which may obstruct this process. This is exactly what has happened, to varying degrees, since 2011: widespread political disagreement and violence have reduced crude output to below 300,000 barrels per day – a drastic fall compared to the 1.6 million reached in late 2010. To make matters worse, the dip in global oil prices has accelerated the downward spiral of an already ailing economy.

Libya's economy and population have also been hijacked by the country's dysfunctional political process, with the battles between warring factions crippling Libya's hydrocarbon industry. Although oil production levels had begun to recover around October 2014, the fighting at the Ras Lanuf and Sidra oil refineries last December once again caused oil output to plummet. Following an attack on a major oil facility in Mabruk in February, foreign energy companies temporarily halted or scaled-down their operations and upended their long-term investments. Meanwhile, the National Oil Corporation of Libya (NOC) has reported that 80% of its output capacity has been lost and warned of a possible outright suspension of oil production if the fighting continues.

Impending implosion

Given the slump in production and the 60% drop in world prices, the NOC has projected that oil revenues for 2015 will be a mere 10% of what they were in 2012. This is not only due to the ongoing violence, but also because budgets had been based on an overly optimistic estimation of the price of oil.

Without alternative sources of fiscal revenue, the elected government will have to rely heavily on its foreign reserves to meet essential expenditure needs. With 80% of the population employed by the state, some 42% of the annual budget will be spent on paying civil servants, while around $30 billion will be needed to cover the import bill. Militia fighters have also been added to the



Data sources: EIA and OPEC

payroll, worsening a budget deficit which has already ballooned to around $15 billion.

Although foreign reserves have in the past provided a buffer to see off the worst effects of revenue shortfalls, the current rate at which they are being depleted bodes ill for the economy. If the state coffers are emptied, the delivery of basic public services and payments will grind to a halt. And if this occurs, it will probably prompt even more public sector strikes, which have been a consistent feature since 2011.

Perhaps most alarmingly, Libya will soon barely be able to feed its population: the country imports 80% of its food staples, and wheat reserves are set to be exhausted within a month or two. Imports are already down by 60% due to the perilous security situation, and whatever goods do make it to Libya are rising in cost. Demand not only now exceeds supply, but insurance companies have also raised their fees for traders operating in Libya's hostile environment. In recognition of the severe difficulties faced by the Libyan people in procuring basic foodstuffs, the United Arab Emirates already began to send food aid to Libya at the beginning of February.

The spiral of oil dependency

Even if Libyans manage to settle their political differences, the immense infrastructural damage already inflicted will be difficult to reverse in the short term. Libya's future leaders are also now confronted with an estimated reconstruction cost of around $200-$480 billion over ten years. If the 2012 approved annual budget of $68.5 billion is used as a benchmark, considering the large share of funds which will have to be devoted to paying public salaries, imports and energy supplies, very little will be left over for reconstruction efforts – unless international financial aid flows in.

Finally, without restoring oil production to pre-crisis levels, the Libyan authorities will lack the required financial resources to invest in the much-needed development of the non-oil sector. But even if the funds are available, as long as Libya continues to be trapped in a vicious cycle of insecurity, the urgent diversification of its economy will be difficult to achieve.

What is certainly the case for now, is that the country's current over-reliance on the hydrocarbon industry is increasing its economic vulnerability. In this regard, its oil reserves are tragically becoming more of a curse than a blessing.

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