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Guyana's First Oil-Dependent Budget—Exxon Drills Oil and Guyana Digs a Fiscal Hole

Bad Budget Precedents Set as Country Spends Its First Chunk of Oil Dollars

The Guyanese government enters a new epoch with the passage of this year's budget—oil revenues now constitute 29 percent of its spending plan. This is the first year that the government has drawn down its oil revenues for budgetary purposes. The new revenues contribute to a substantial increase in the size of the budget. The budget increases have been heralded by the country's leadership as evidence of the wisdom of oil and gas extraction for Guyana.

A careful examination, however, reveals several red flag warnings. The amount of revenue from the new oil venture demonstrates that Guyana is being short-changed. The use of the revenue shows that Guyana has mismanaged its initial share of the profits.

In short, this year's budget shows that the amount of oil revenues collected to date:

- Failed to cover annual budget deficits;
- Supported additional spending but in a manner that is unsustainable;
- Failed to reduce debt; and
- Contributed nothing to the Sovereign Wealth Fund (SWF).

By spending all of the money that was received from oil in the fiscal year 2022 budget, this first year has set bad precedents.

Budget Background

Revenues for the new budget are valued at G$432 billion (USD$2.1 billion). Total revenues include a transfer of oil revenue from the Natural Resources Fund (NRF) of G$127 billion (USD$ 606 million), or 29 percent of total government revenues.[1] The NRF receives and holds oil revenues from Guyana's share of the profits.

Guyana's total government expenses equal G$529 billion (USD$2.5 billion), including capital expenditures of G$217 billion (USD$1.0 billion). The expenses more than double last year's capital budget of G$104.4 billion (USD$ 501 million).

[1] Ministry of Finance, Guyana. Budget Estimates 2022 Vols. 1-3.

The budget is also supported by G$87.7 billion (USD$420 million) in borrowed funds.[2]

The budget deficit, which is measured as revenue after expenses (and before grants and financing), is G$97.7 billion (USD$469 million).[3]

The non-oil budget deficit, which equals the amount of non-oil revenues minus total expenses, totalled G$224 billion (USD$1.08 billion).[4] The non-oil budget is an important measure of how dependent Guyana is on oil revenues each year. When the non-oil deficit exceeds the amount of oil revenues, it may be evidence of overspending—a red flag warning.

In one forward-looking statement contained with the annual budget speech, Guyana anticipates revenues to be deposited into the NRF from oil production in future years. The projections identify G$243 billion (USD$1.1 billion) in 2023, G$279 billion (USD$1.33 billion) in 2024 and G$372 billion (USD$1.78 billion) in 2025.[5]

Observations

This is the largest budget in recent memory. The transfer this year from the NRF to the 2022 budget is the entire amount that Guyana has received from start-up oil production at the Liza Destiny site from December 2019 through the end of 2021.

Table 1: Guyana's Use of First Tranche of Oil Revenue Compared to Its Principal Goals

Fiscal Goals	Status
Close annual deficit	Partial, not enough revenue to close deficit
Increase spending	Yes, but borrowed $G87.7 billion (USD$420)
Reduce debt	Debt increased
Contribute to sovereign wealth fund	No contribution was made

In a prior report, IEEFA outlined the goals that Guyana planned to achieve with the new revenues: 1) close deficits; 2) increase funding for annual budget needs; 3) reduce debt; and 4) contribute cash to a new sovereign wealth fund (SWF) patterned on other SWF funds like the world's largest such fund in Norway.[6]

1. In 2022, the oil revenues were not enough to cover the non-oil budget deficit of G$225 billion (USD$1.08 billion). The new revenue from oil production of G$127 billion (USD$ 606 million) fell short of the non-oil budget deficit. The non-oil budget deficit is calculated by subtracting the total amount of non-oil revenue from total government expenditures. (Total revenues equal G$432

[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*
[5] Ministry of Finance. Guyana. Budget Speech 2022.
[6] IEEFA. Guyana's Oil Deal: Promise of quick cash will leave country shortchanged. October 2020.

billion minus G$127 billion, or G$305 billion. Total expenses are G$529 billion.)

2. The 2022 budget does fund new needs, but it does so in an unsustainable manner. The new revenues partially supported the government's 37 percent increase in spending over last year's budget. The higher spending level was made possible through a combination of new oil revenues and new borrowing. New spending should not exceed the amount contributed into the NRF. It did. Initially, the government had agreed that in any year, the amount of increased spending would not exceed the amount of the oil revenue received.

3. The 2022 budget and the new oil revenues did not reduce debt. The government borrowed an additional G$87.7 billion (USD$420 million) in 2022. Guyana's total indebtedness between December 2021 and December 2022 is expected to increase by 14 percent. IEEFA pointed out in its earlier report that Guyana would have to go deeper into debt as a consequence of the oil and gas extraction. So far, IEEFA's estimate has proven to be accurate.

4. There were no contributions made to Guyana's SWF. According to the IMF, Guyanese officials agreed initially to constrain annual spending to avoid exceeding the amount transferred to the NRF.[7] Spending would be further constrained by a fiscal mechanism that would transfer 50 percent of the proceeds from the NRF to the sovereign wealth fund. In this year's budget, no money was transferred to the SWF, and overall spending exceeded the amount transferred to the NRF.

The Guyana government has disclosed that it is looking forward to increased revenues from oil production over the next three years. This could allow the country to close its annual deficit if spending is constrained. Additional fiscal discipline will be essential if debt is to be reduced and a meaningful contribution is made to the SWF.

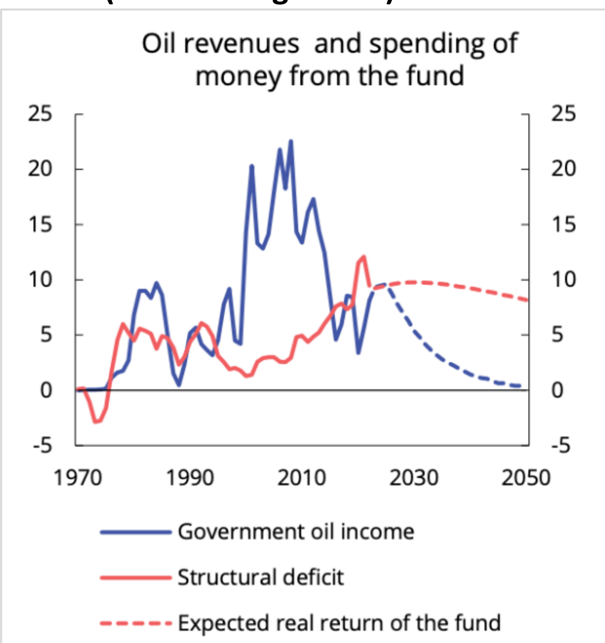
Guyana has published the amount of revenue that is expected to be available next year and for two subsequent fiscal years. The approach to public disclosure of the projected oil revenues is worrisome, since it lacks proper budget context. Without disclosing the level of anticipated expenditures, Guyana's revenue disclosure is misleading.

The Norwegian example provides a strong note of caution to Guyana. Norway's recent budget shows the country is going through a transition from a period of very high annual oil revenues that allowed it to cover budget deficits and build a $1 trillion reserve, to the current period where revenues marginally cover deficits and the reserve ceases to grow. The outlook through 2050 will not cover deficits (See Figure 1) and cannot be relied upon to build its SWF any further.

[7] International Monetary Fund. Guyana: 2019 Article IV Consultation-Press Release; Staff Report; and Statement by the Executive Director for Guyana. September 17, 2019

Norway has successfully attached its fortunes to that of the oil and gas industry since the late 1990s. The country has a transparent annual budget process that contains a robust discussion of the economy, specifically the oil and gas outlook. It also acknowledges that the amount in Norway's SWF is not expected to continue to grow due to a decline in future oil revenues. Further, the country has made it clear that it will need to rely on a more diversified set of businesses beyond oil and gas as it looks forward to the future.

Figure 1: Norwegian Government Oil Revenues, Spending and Structural Deficit (1970 through 2050)[8]



Right now, Guyana has not publicly put in place any of the fiscal infrastructure required to achieve its goals (see below). Its planning seems hyper-focused on future oil and gas revenues. The following questions should be publicly addressed to further the public dialogue on oil production in Guyana, and to properly assess the benefits and costs that come with it.

Questions

1. Since 2019, Guyana amassed G$126.7 million (USD$606 million) for its share of oil revenues. The money was contributed to the 2022 budget. IEEFA estimates that the oil companies received approximately G$718 billion (USD$3.6 billion) for the same period. From the Guyana government's forward-looking projections, it appears that this same oil revenue split will be in play until at least through 2025. The same ratio that currently short-

[8] Ministry of Finance and Statistics, Norway. National Budget 2022, Section 3.1.

changes Guyana will only be changed to a 50/50 split when Guyana pays off the total development costs and any other hidden liabilities, like the costs identified in the still-to-be-released pre-contract cost audit.[9] These liabilities have not been made public. Without knowing how much Guyana owes the oil companies, it is impossible to tell how much the country is actually going to receive and when. This is a hidden debt owed by Guyana. And it is impossible to know when Guyana will start receiving a fairer take until this is properly disclosed.

Right now, it appears that the total development cost increases every time ExxonMobil announces a new oil find.[10] This means Guyana must immediately pay for the development and operational costs for the Liza Destiny project and all costs associated with the development of Liza Unity and some 17 other sites. In addition, the failure to settle on the legacy costs owed to the oil companies means it is not publicly known when Guyana will receive annual revenues that enable it to cover its deficits, responsibly support new spending, reduce debt and contribute to a sovereign wealth fund.

Under a 50/50 split, for example, Guyana would not have received G$126.7 billion (USD $606 million), but instead G$418 billion (USD$2 billion). The broader implication is that the world is moving away from fossil fuels, and it is not known how long Guyana's oil and gas reserves will be a resource that produces significant cash. The critical financial questions:

- As of April 2022, what is the total development cost that Guyana owes the three companies?
- What are the legacy costs that were the subject of the pre-contract cost audit that has not been released?

2. The government of Guyana has disclosed its projected oil revenue for the next three years. What is the basis for the assumptions? How many barrels will Guyana receive, and how much is estimated per barrel?

   What are the other revenues and expenses that will make up Guyana's budget over these four years? How much is expected as an annual non-oil deficit?

   While Guyana has taken steps to improve transparency related to its annual debt practices,[11] why isn't it also developing new multi-year full budget projections? It is poor budget practice to release oil revenue projections without any information regarding how it is derived or the role it plays in a complete revenue and expense analysis. It is misleading to offer a projection that Guyana will receive oil revenues as if there were no claims against it. If

[9] Stabroek News. Audit of Exxon pre-contract costs stalled by mix-up. February 11, 2021.
[10] For example, see: ExxonMobil. ExxonMobil makes three new discoveries offshore Guyana, increases Stabroek estimate to nearly 11 billion oil-equivalent barrels. April 26, 20222.
[11] Ministry of Finance. Guyana. Guyana Annual Borrowing Plan Fiscal Year 2022.

the country is looking to leverage outside investment, poorly designed fiscal tools will result in the opposite occurring.

3. Oil prices have recently increased. This should improve revenues for Guyana in 2022. lEEFA's first report estimated that oil prices would remain low. The increase in oil prices is related to Russia's intervention into Ukraine, a factor that has disrupted oil and gas markets. It is unknown how long the war will last. When it concludes, prices are likely to decline again.

Overall, it is completely understandable why the government increased spending this year— the promises made about new oil revenues and the needs of Guyana's citizenry due to the pandemic all but required it. The new oil revenues, however, are not large enough to meet the expectations created by the oil companies and government leadership. That is why borrowing took place this year and why no money was contributed to the sovereign wealth fund.

Guyana has not told the public—and may not even know—how much it actually owes ExxonMobil in total development costs. This outstanding obligation is a form of debt since it is a multibillion-dollar liability that will be paid off over several years. The liability has an effective priority lien on Guyana's revenues., Exxon Mobil has failed to either inform its shareholders of a substantial receivable or to take action to secure its claim to recoup expenses it incurred as long as 20 years ago.

The one-sided contract short-changes Guyana. It also detracts from the efforts to improve Guyana's competitive position in the world. It will be clear to any outside investor that the country is spending beyond its means and that the oil project lacks transparency.

About IEEFA

The Institute for Energy Economics and Financial Analysis (IEEFA) examines issues related to energy markets, trends and policies. The Institute's mission is to accelerate the transition to a diverse, sustainable and profitable energy economy. www.ieefa.org

About the Author

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Tom Sanzillo, director of financial analysis for IEEFA, is the author of numerous studies on the oil, gas, petrochemical and coal sectors in the U.S. and internationally, including company and credit analyses, facility development, oil and gas reserves, stock and commodity market analysis and public and private financial structures. Sanzillo has experience in public policy and has testified as an expert witness, taught energy industry finance and is quoted frequently in the media. He has 17 years of experience with the City and the State of New York in senior financial and policy management positions. As the first deputy comptroller for the State of New York Sanzillo oversaw the finances of 1,300 units of local government, the annual management of 44,000 government contracts, and over $200 billion in state and local municipal bond programs as well as a $156 billion global pension fund.