A Pandemic and a Price Plunge
Oil-Rich Kleptocracies in Uncertain Times

By Alexandra Gillies

Oil and other natural resources fuel most of the world's kleptocratic networks. When the new coronavirus pandemic first hit in early 2020, the global drop in oil demand sent the commodity's already-low prices plummeting further. For the oil-rich kleptocratic regimes of the world, this shock further constrained the patronage and corruption possibilities available to them. The ways in which these networks have responded to the dual crises of collapsing revenue and a worldwide pandemic may offer potential opportunities to support democracy, curtail illicit financial flows, and even combat climate change.

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Market crash and an uncertain future

In June 2020, U.S. authorities seized a penthouse condo in Miami allegedly purchased with oil revenues stolen by a member of Congo-Brazzaville's first family. According to the court filings, the president's son allegedly diverted funds from the national oil company's accounts to acquire the condo, as well as expensive cars, private flights, a $650,000 Los Angeles hotel bill, and other luxury properties.[1] Though discouraging, the charges in this case are hardly shocking. In Congo-Brazzaville and many other countries, ample evidence shows how authoritarian regimes have used oil industry spoils to enrich their inner circles and strengthen their grip on power. The 2008–2014 oil boom was a prime moment for sev-eral dictators to nurture their national oil industries by partnering with foreign oil companies that had little issue with their repressive and corrupt tendencies and expanding the corro-sive reach of their national oil companies (NOCs).[2] They then steered the oil windfalls toward their allies through bloated oil sector deals, as well as other forms of public spending, preferential access to credit, and monopoly control over various areas of the economy. Bits of the oil largesse benefited larger groups of citizens as well, whether through public sector jobs, subsidies, or public goods. As long as the oil revenues continued to flow, the regimes mostly were able to quell potential unrest. And, with oil prices regularly topping $100 per barrel, there was plenty left over for political elites in systems permitting unchecked power to spend extravagantly on mega-yachts, fleets of supercars, $450 million paintings, and other trappings of a globetrotting luxury lifestyle.[3]

This model is less affordable now. In 2014, oil prices plummeted and took revenues with them. The oil revenues collected by Middle Eastern governments in 2019 were half of what they were in 2012.[4] Then, in 2020, the new coronavirus arrived on the scene, global demand for oil dried up, and prices dropped even lower. Since hitting rock-bottom in April 2020, prices have recently settled above $40 a barrel—an amount that nonetheless is lower than the level many oil-dependent countries need to balance their budgets.[5]

Oil's future looks uncertain. Although many industry experts are predicting that oil will rebound in the near term, they also expect the market will exhibit longer-term decline as the world transitions to cleaner fuels.[6] In response to today's low prices and this bearish prediction, many oil companies are cutting their budgets, narrowing their portfolios, and (in selected cases) deemphasizing oil in their future plans. In Africa, for instance, companies have hit pause on major projects in Angola, Chad, Gabon, Nigeria, Uganda, and elsewhere.[7] Some investors are backing away from the industry entirely, with major hedge funds divesting from fossil fuels and oil stocks falling from weak demand. Oil-dependent kleptocracies will be much slower to adjust.

Variable impacts across producers

The current downturn and future instability of the oil market will hit some producer countries harder than others, including those exhibiting kleptocratic tendencies. The more dependent a country is on oil, the more the decline will hurt. The producers of higher-cost, "dirtier" oil will also face a tougher road ahead. Where production costs are low, such as in the Persian Gulf, operations should remain viable at lower prices. Where production costs are higher, as in Algeria, Kazakhstan, Venezuela, and offshore in the Gulf of Guinea, it will be more difficult to attract investment and collect a healthy return. Producing countries also arrived at the COVID-19 crisis in different fiscal positions. Qatar, Saudi Arabia, Azerbaijan, Russia, and Kazakhstan had some savings and the fiscal space to borrow to get through the immediate turmoil; others, such as Angola, Chad, Congo-Brazzaville, and Venezuela, were already facing debt crises.[8]

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Political contexts also vary. A number of regimes used the previous commodities boom to entrench themselves in power. In Azerbaijan, high oil prices enabled the ruling elites to assert control over the entire economy, and this control will not be easily undone even as oil revenues fall.[9] In Equatorial Guinea and Congo-Brazzaville, the political opposition has suffered from years of disenfranchisement, and long-standing dictators retain their firm grip on power.[10] That said, where politics are shifting, the decline in oil may help speed potential transitions. Angola's long-time ruler handed over power to his successor in 2017, and the new government has had to embrace significant reforms in order to weather the economic crisis and secure major financing from the International Monetary Fund.[11] Low oil prices have reduced room to maneuver for incumbents seeking to hold onto power, whether in the face of popular uprisings as in Sudan and Algeria or elections as in Malaysia and Nigeria. When oil revenue can no longer prop up a faltering regime, leaders with significant corruption challenges run a greater risk of being shown the door.

Possible governance trends

Despite this variation, a few governance trends are likely. Corruption will undoubtedly absorb fewer dollars than it did during the boom years. At $40 per barrel prices, there simply is not enough money available to regularly inflate oilfield service contracts by millions of dollars, award favorable pricing terms to politically-connected oil traders, or collect bribes from oil-thirsty investors. Instead, governments and companies alike will seek to minimize production costs and avoid the excess expenses associated with corruption schemes.

Any corruption that does continue will carry heavy opportunity costs. If a kleptocrat relies on certain oligarchs or a high-spending NOC to run their patronage system, these actors may

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still receive an outsized share of the country's oil money. Every dollar captured by private interests further gouges the scarce public funds available for managing the pandemic or providing other public goods during a period of economic recession. NOCs are an area to watch, given the central role they play in many kleptocratic political economies. Research conducted by the Natural Resource Governance Institute shows that, on average, when oil prices drop, the money that NOCs transfer to the state drops even more dramatically.[12] In other words, NOCs tend to hold onto a disproportionately large share of scarce public funds. In Angola, for instance, oil prices fell by 50 percent between 2012 and 2016, but NOC transfers to the public budget fell from $25 billion to $6 billion.[13] This trend suggests that some kleptocratic leaders may be tempted, despite the wider fiscal crisis, to continue to use NOC spending to reward loyal insiders and manage other political pressures, not least because NOC revenue typically comes under relatively less scrutiny from outside actors such as the International Monetary Fund.

Because oil industry investment dollars are in scarcer supply, current events also shift leverage away from oil-producing governments and toward companies and investors. Companies likely will be more selective about their chosen investment areas, so they could choose to avoid states or regions with high corruption and political risks. Such preferences could further dampen oil sector corruption—a positive dynamic. Conversely, a "race to the bottom" could ensue. Governments, desperate to keep oil companies from exiting or narrowing their investment plans, could offer deals that contain weak fiscal, environmental, or operational requirements. Observing the deals made during this time of crisis could help reveal which governments are choosing to trade their country's longer-term needs for their own short-term political security.

What is at stake

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On the kleptocracy front, the oil industry supports some of the world's least democratic governments. It also represents a major source of the illicit financial flows that spread offshore into accounts, companies, and assets worldwide, with destabilizing impacts. The recent FinCEN files are just the latest illustration of the scale of stolen money circling the globe.[14] Less oil money available to kleptocratic regimes could lead to political openings and help reduce the amount of illicit money flowing through these global channels. Assertive anticorruption activity targeting these states can help to bolster these positive trends.

Kleptocratic oil producers also are considering how to respond to the longer-term shift toward cleaner energy. Some observers have characterized recent oil market decline, prompted by the COVID-19 pandemic, as a "dress rehearsal" for the upcoming decline in demand for fossil fuels.[15] Some producers will double down on oil, especially since prices may well rebound in the near term. Such regimes, whose economic survival and political futures depend on high oil demand, may pose obstacles to global responses to the climate crisis. They would represent powerful vested interests willing to fight for the oil-fueled status quo. Their NOCs could continue producing at levels incompatible with the Paris climate agreement, and their politicians could thwart the collective action needed for the world to advance to a future that is less dependent on petroleum products. However, energy transition realities could finally push other producer countries toward diversifying their economies, which could have democratizing political impacts as well.

During the recent boom years, oil-rich kleptocratic regimes enjoyed a range of options. They could pay off their rivals, enrich their allies, direct some largesse toward their citizens, and still fund their luxurious lifestyles. These regimes now face a much harsher set of tradeoffs. In a post-COVID environment, the choices kleptocratic regimes are obliged to make may offer new opportunities, including for cutting off illicit financial flows at their source, fighting climate change, and identifying pathways for democratic reform.

Endnotes

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