THE GLOBAL FINANCIAL CRISIS AND INTERNATIONAL LIQUIDITY: THE IMPACT OF PETROLEUM PRICES

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Introduction

In recent years, the economic repercussion of rising energy prices have been widely debated by national governments, international institutions, multinational business and economic consultants. In this age of industrialization, transportation and mass production of goods and services, energy represents the key behind rapid socio-economic transformation and sustainable growth. Modern living depends on energy to the extent that no home can afford not to make use of electric power and gas-related products. Such high dependency has linked the future development of mankind to the existence of energy sources to ensure the meeting of man basic needs and the enhancement of productivity growth. Until today, the prospect of developing new sources of energy to substitute for fossil fuel has shown very little sign of encouragement. Despite attempts to investment in various projects related to energy worldwide, the potential for finding a substitute for conventional energy sources remains to be achieved.

Most conventional energy resources comprising oil and gas are primarily located in the Middle East where population density and energy consumption are low. The gap between production and consumption of energy comes from the fact that most consumers are highly industrialized countries with heavy dependence on

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imported oil to meet domestic requirements. Oil exporters enjoy low price elasticity of demand which allows them to increase the price without the fear of a sharp decline in quantity demanded. Due to the narrow economic base and small absorptive capacity of these countries, they are able to accumulate large reserves and enjoy current accounts surpluses. Such trends could have spillover effects by creating global imbalances through higher prices, liquidity shortages, inadequate global demand and currency devaluations.

The main objective of this paper is to highlight the impact of the global financial crisis on international liquidity imbalances. Earning foreign exchange is important for supporting the capacity to import, especially in developing countries. Balances of payments equilibrium strengthens global economic and financial stability by facilitating the flow of trade, capital and labor. The financial crisis could have adverse effects on global stability by redistributing income in favor of exporters of energy sources.

The Global Financial Crisis

The global financial crisis currently sweeping across countries has been widely debated by academicians, policy makers, businesses, politicians, economists, groups and individuals worldwide. Due to the magnitude of the crisis and the uncertainty about future implications, countries began to feel the pinch by rushing to take precautionary measures and bail out banks, financial institutions and companies before collapse.

In the United States, where the crisis originally started, the government is spending billions of dollars to rescue the economy from slowing down. Already unemployment in the United States stands at about 7 percent which is the highest since early 1980s.

Similar trends are developing in other Western countries including the Europe Union and Japan which will deepen the global recession.

The International Monetary Fund (IMF) has revised its projection for 2009 by estimating the growth of global GDP to decline to 2.2 percent compared to 3.7 percent in 2008 and 5 percent in 2007.[1] The spillover effect of the financial crisis could weaken the ability of developing countries to induce growth due to shortages of foreign exchange and liquidity problems. Slow growth in global demand, especially for minerals and primary products, could jeopardize developing countries efforts to sustain development and reduce the impact of global trends.

The prices of minerals, including petroleum, have declined in recent months reflecting a devastating impact on the exporting economies of these products. Among others, petroleum prices stand at about US$38 today compared to about $140 a year ago. In the case of countries with high dependency on a limited number of products for export, the decline in global demand reduces the country's capacity to imports especially capital goods and skills which are needed to support development projects. Among oil producing countries Saudi Arabia, Bahrain and Kuwait have already curtailed their spending by reducing allocations for investment in a number of projects.

Getting out of the crisis will not be easy given the loss of confidence in financial markets and uncertainty about future trends. As the IMF points out "the global economy is in a severe recession inflected by a massive financial crisis and an acute loss

1 See International Monetary Fund, (IMF), World Economic and Financial Surveys: World Economic Outlook (Washington: IMF, 2009).

of confidence."[2] The latest conference, which was held in London during the period 2-3 April, 2009 involving the G20, promulgated measures to lesson the impact of the crisis by providing $1 trillion to stimulate economic growth both locally at the level of an individual nation and globally. Furthermore, to support the effort for reducing the impact of the financial global crisis on developing countries, the World Bank allocated $50 billion global liquidity program. Decline in global demand is expected to hit developing countries hard by decreasing demand for their exports made primarily of agricultural products and raw materials.[3]

Globally, the decline in demand is largely due to slow growth in industrialized countries. Rising unemployment in the US and other Western countries caused aggregate demand to decline affecting not only local production but also global demand for goods and services. In particular, exports of developing countries have contracted causing foreign exchange earnings to decline. To a large extent, the pace of economic development in these countries depends on their ability to import capital goods and technology. The financial crisis has not only reduced the flow of capital, but also has caused balance of payments disequilibrium, currency devaluation, slow rates of economic growth and global recession. In addition to the economic and financial consequences, the global financial crisis is expected to generate social, political and environmental repercussions.[4]

Originating in the United States the global financial crisis in 2008 has stemmed from the inability of the capitalist institutions

2 See International Monetary Fund (IMF), World Economic and Financial Surveys: World Economic Outlook, April 2009 (Washington: IMF, 2009), p. 1

3 (www.moneynews.com/financenews/world_bank_trade/2009)

4 See "The Real reason for the Global Financial Crisis ... the Story no one's talking about", www.maretoracle.co.uk/Article6335.htmi

to meet the challenges of the new global economy driven by globalization. Recent economic trends in Asia, mainly China and India, has witnessed the emergence of new global economic players. As a consequence, Western economies lost their trade dominance over global markets by having China and India becoming major producers of capital goods and technology. The new global economy promotes services as an important economic alternative for production and exports of physical products. The emergence of new global centers including Dubai, Singapore, Taiwan and Hong Kong has similarly diverted a substantial amount of financial capital away from the traditional centers into the east.

In Western countries, lack of regulatory measures and inadequate supervision by central banks and government agencies led commercial banks and other financial intermediaries to ease restrictions on lending by providing inadequately collateralized often to unaccredited worthy loans. Such tendency gave incentive for a large number of people to borrow at an easy terms using the money mostly to purchase consumer products or real estate instead of investment in production of real output. Rising unemployment and slowing down of the economy in the wake of the financial crisis led millions of people to default on payments of their debts creating a sharp decline in bank liquidity. To reposition their operations, banks began to introduce new restrictions on lending which in turn impacted investment expenditures, especially by private sector.[5]

Without collective cooperation comprising all countries, the effects of the crisis will be prolonged forcing the global economy deeper into recession. The global financial system currently practiced is a product of Bretton woods agreement which gave the

5 See Umer chapra, The Global Financial Crisis: Can Islamic Finance Help? New Horizon, January-March 2009, www.newhorizon-islamicbanking.com

International Monetary Funds and the World Bank a substantial power over global financial transactions and capital flows. Lending to developing countries in particular, was linked to the IMF structural adjustment programs supported by free market agenda. Governments in these countries are forced to reduce financial assistance and eliminate subsides to farmers and manufacturing producers as a prerequisite to obtaining financial support to remedy balance of payments disequilibrium and support the country's capacity to import.

Commodity Prices

Petroleum prices have been the most affected by the global financial crisis and rapid decline in international demand. After soaring to a level never experienced before, reaching to about $143 per barrel in July 2008, petroleum prices collapsed to about $35 per barrel by the end of the same year. This increase in petroleum prices was largely due to rapid growth in global demand, especially in China and India. High rates of economic growth in these two countries have widened the gap between global demand for energy and capacity of supply. Heavy dependence of industrialized and non-industrialized countries on imported oil to meet demand requirements is expected to impose additional burdens on government budgets, balances of payments, investment expenditures, human development, poverty alleviation programs and economic growth. Low earnings of foreign exchanges, especially in developing countries, are likely to reduce demand for imports which in turn will have a negative impact on global demand for goods and services. International liquidity is essential for stimulating global trade and supporting development. According to the Economist commodity-price index metal prices went down by 51.1 percent compared to a year from now whereas industrial commodity-price index suffered 47.6 declines during the same period.

In most developing countries, earning of foreign exchange depends primarily on exports of a limited number of primary products with high elasticity of demand. Thus, in the case of higher petroleum prices the ability of non-oil producing countries to expand production for exports and promote global competitiveness has been weakened. Similarly, petroleum and petroleum products represent important components of production costs which impacted development programs by imposing constraints on the country's capacity to import, especially capital goods and raw materials. Economic development underscores the importance of access to global knowledge, skills, technology and information for building capacity capable of increasing productivity and sustaining economic growth. Oil is one of the most important commodities traded globally and, therefore, the stability of the oil market is essential for sustaining financial flows and trade transactions.

Despite heavy investment in a variety of energy related projects, until now, no alternative energy sources have been developed to reduce dependence on imported fossil fuel. Almost two thirds of the known-reserve of conventional energy sources is located in non-industrialized countries with low population density and low economic productivity. However, the prospect that a substitute for fossil fuel will be found is not likely to happen in the near future and, therefore, the risk of imbalances between demand and supply is expected to continue keeping the global energy market volatile. It is estimated that the primary demand for oil is to increase by 1.3 percent per year over 2005 – 2030 or the equivalence of 99 million barrels in 2005 and 116 million barrels in 2030. About two thirds of this increase in demand will be originating in developing countries. Meeting such requirement implies that the oil industry needs to invest a total of $4.3 trillion over the period 2005 – 2030 or $164 billion per year.[6]

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6 International Energy Agency (IEA), A Monthly Oil Market Report, June 2008.

Table 1 illustrates the amount of proven reserves of oil distributed by regions. The table shows that at the end of 2005, total world reserves of oil accounted for 1,204 billion barrels with 62 percent of which is located in the Middle East. The importance of the Middle East as a key player in the global energy market is a manifestation of its influence over the main determinants of supply. Now, given the global demand for energy, the question whether the Middle East will continue to supply sufficient amount of oil to meet demand remains to be seen. Members of the Organization of Petroleum Exporting Countries (OPEC) with less than 10 percent of world population are in control of about 80 percent of world known oil reserves. Bridging the gap between demand and supply not only requires collective cooperation among producers and consumers, but also the construction of an effective strategy for crisis management. Such collective action will ensure stability of financial markets and reduce the risk of global recession. International trade is bias in favor of exporters of manufactured goods, technology and services which imposes constraints on non-industrialized countries to get fair share in world trade and foreign direct investment.

Table 1
World Proven Crude Oil Reserves by Region, 2007

Region	Proven crude oil (M/b)	% of total world
North America	25,914	2.2
Latin America	134,691	11.2
Eastern Europe	129,049	10.7
Western Europe	15,110	1.3
Middle East	741,566	61.6

Region	Proven crude oil (M/b)	% of total world
Africa	119,572	9.9
Asia and pacific	38,282	3.2
Total World	1,204,182	-----
OPEC	939,016	78

Source: Organization of the Petroleum Exporting Countries (OPEC), Annual Statistical Bulletin 2007 (Vienna, 2007)

Global Trends

The period following the end of the cold war and the collapse of the communist economic system, has witnessed a substantial increase in conventional energy prices in general and petroleum prices in particular. Such surge in energy prices has become a major concern for policy makers, energy analysts, Organization of Petroleum Exporting Countries (OPEC), international organizations and industry by projecting scenarios of worldwide recessions and rising cost of production. Throughout the 1980s and 1990s, investment in the discovery of new oil supplies was curtailed due to low prices and slow global demand. However, low investment in conventional sources as well as in alternative sources of energy was met with rapid global demand for energy during the last few years, especially in Asia where China and India became a prime consumer of energy. Furthermore, projection about future global economic trends showed that India and China will continue experiencing high rates of growth in the early years of the new millennium.

As a consequence, oil prices increased sharply reaching to about $140 per barrel in June 2008 compared to an average of $28 in 2003, $12.28 in 1998 and $1.5 in 1970. Responding to rising demand, OPEC increased its oil supply by about 4 million barrels a day since 2003. The sharp rise in petroleum prices has brought windfall profits to OPEC member countries most of which in the form of international reserves made of foreign currencies. This in turn has caused the transfer of a large proportion of global liquidity into small but wealth oil producing countries.

Economic and financial stability at the level of both local and global markets underscores the importance of global cooperation as well as the need for efficient management of international liquidity to stimulate aggregate demand and reduce the risk of recessions. As table 2 illustrates, China and India have surpassed all world regions by growing at 9.7% and 7.6% in 2008 compared to 11.9% and 8.6% in 2007 respectively. Sustaining such rapid growth will continue to put pressure on global demand for oil. Unless growth rates become moderate, the prospect of global energy balance will remain unrealized in the immediate future.

Table 2
Economic Growth Rates, 2007-2008, %

Region	2007	2008
World	4.9	3.9
OECD	2.7	1.8
USA	2.2	1.2
Japan	2.0	1.7
Euro-zone	2.6	1.7
China	11.9	9.7
India	8.6	7.6

Source: International Energy Agency, Oil Market Report, June 2008

In recent years, globalization has increased global interdependencies among nations by liberalizing trade and financial transactions, promoting capital flows, and increasing labor mobility. Modern information and communication technologies have enhanced financial services by connecting global markets through electronic networks and satellite broadcasting. Such trends gave rise to new markets dominated by key players, mainly multinational business, industrial countries and global institutions. Similarly, information technologies speeded up international transactions by linking individuals, businesses, markets and organizations worldwide. Globalization, though its meaning is vague, involves worldwide exchanges of goods and services, capital flows, and telecommunication technologies.

As multinational nationals, oil companies are fully integrated in the globalization process for being key players in the global energy markets. Almost two thirds of oil production, distribution and shipping are controlled by these companies, better known the seven sisters. Due to the importance of oil trade and because of the rise in oil prices in recent years, these companies exercise tremendous economic and financial powers over the global markets. For example, in 2007, total revenues of the top five major oil companies (BP, ExxonMobil, Total, Royal Dutch/Shell and Chevron) were about $1.5 trillion. Deregulation and the globalization of financial markets along with rising demand for energy have strengthened the position of these corporations. In this regard, globalization has weakened the power of the state by transferring more power to international corporations and institutions. In other words, increasing interdependencies has caused countries to rely more on imported goods than domestically produced products, on communication system mostly originated in other countries, and on technology not necessarily designed for their environment. Table 3

illustrates the earnings of the top five major oil companies. As the table indicates, net income earned by these companies more than doubled between 2003 and 2007 increasing from $61,429 million to $122,213 million respectively.

Table 3
Net Income of Major Oil Companies, 2003 – 2007 (m$)

Oil company	2003	2005	2007
BP	12,432	19,314	17,287
ExxonMobil	21,510	36,130	40,610
Total	7,944	14,885	18,063
Royal Dutch/Shell	12,313	25,311	27,565
Chevron	5,294	11,098	13,479
Total	61,429	109739	122,213

Source: OPEC, Annual Statistical Bulletin, 2007

Globalization has eased restrictions on global trade and finance by giving greater access to global markets. Export-led growth policies require building capacity capable of facilitating global connection for absorbing knowledge and disseminating information. Balances of payments disequilibrium weaken the ability of the economy to sustain growth by imposing constraints on its international trade transactions. As a consequence, availability of foreign exchange becomes necessary to pay for the country's global obligations. A deficit in the balance of payments could cause devaluation of the national currency which reduces the country ability to meet its external obligations, especially serving the foreign debt and paying for imported goods. Such trends create uncertainty about future growth by discouraging foreign direct investment in

the local economy. In other words, without liquidity, the country suffers from capital flows causing brain drain, disinvestment, skill shortages, knowledge denial and limitation on technology transfer. Oil import price increases is refereed to as OPEC tax because of the transfer of wealth outside oil importers. The money paid to oil producers may not be invested back in the country which represents a loss of resources.[7]

Global Liquidity

Global liquidity constitutes monetary assets used mainly for financing international trade transactions and correcting balances of payments disequilibrium. Liquidity is a stock measured in a given time period showing the distribution of international reserves among various countries. The need for these reserves is vital for facilitating trade transactions and settlement of foreign obligations.

Enhancing the reserves position depends largely on the country's export trade as well as on global demand for its products. In China, for example, rapid economic growth in recent years improved considerably the country's balance of trade position causing reserves to increase from $168.9 billion in 2000 to $1559.5 billion in 2007. Similar phenomena identified among oil producing countries where recent surge in oil prices has resulted in transferring large amount of global liquidity to few countries, mainly those in the Middle East and North Africa. International reserves earned by these countries increasing from $165.5 billion in 2000 to $721.8 billion in 2007. Due to the small size of their economies and because of the limitation of their absorptive capacity, these countries have

7 See International Monetary Fund, World Economic Outlook: Globalization and Inequality (Washington: IMF, 2007)

been enjoying a favorable balance of trade position by accumulating a substantial amount of surplus. This in turn has caused deficits in balances of payments in a number of non-oil producing countries. Among nations, the developing countries are expected to suffer most because of the rise in oil import bills and the inability of exports to meet rising oil prices.

In recent years, the balance of payments situation has been aggravated by rising global food prices which have added additional burden on net export earnings of most non-oil importing countries. The prevailing condition jeopardizes efforts of government policies and programs to alleviate poverty and promote socio-economic development. The challenges facing many of these countries are so great that will take much needed financial and technical assistances to correct imbalances in their economies. The pressure of higher oil prices and shortages of liquidity underscores the urgency for a greater global cooperation and the need for a better management of international financial transactions. In other words, urgency is need for reengineering the international financial system in order to ensure global financial stability and maintain balances of payments equilibrium. Imbalances could create economic disorder and cause political instability. The global financial crisis has worsened the situation further by reducing global demand for primary commodities, especially from developing countries. Without exports, most of these countries will not be able to meet their global financial and economic obligations including serving the national debt.

Nations with high dependency on imported oil are expected to suffer from liquidity shortages which are needed to meet their international obligations. For example, poor countries are in dire need for foreign exchange to support development programs and,

therefore, shortages of liquidity brought by higher imported energy bill could jeopardize their future prospect to alleviate poverty and sustain development. Settlement of international transactions is usually resolved through revenues earned from export of mainly primary products, the prices of which are highly unstable. Furthermore, the global financial crisis has increased economic vulnerability by subjecting the economies of these countries to liquidity problems and balance of payments disequilibria. Higher oil prices are expected to worsen the situation by diverting a large portion of their foreign exchange to pay for imported fuels. Under such circumstances, management of the international financial system becomes necessary for reducing uncertainty about future fluctuations of export earnings. In additions, capital flows into these countries are restricted due to economic and political considerations which in turn cause disequilibrium in balances of payments. Poor countries usually do not have investments abroad to supplement their reserves to compensate for reduced earnings from external sources, i.e. they rely heavily on export earnings to support the demand for imported goods and services.

A liquidity surplus by a small number of countries increases the prospects for a global recession by reducing global aggregate demand. Every time oil prices increase larger amount of international liquidity is transferred to oil producing countries. In recent years, the capacity of the oil exporting countries to spend money has declined reducing in the process the global circulation of international liquidity, i.e. nations with export potential will face decline in demand for their exports due to liquidity shortages in the rest of the world. With the exception of oil, the demand for non-oil imports is expected to fall due to inability of many countries to finance their non-oil imports. Such trends are likely to slow global demand causing global recession. Past liquidity trends have shown

that there is close relationships between higher oil prices and global liquidity. However, excess liquidity earned by oil producing countries usually finds it way into the financial markets seeking investment opportunities. Larger proportion of these surpluses end in Western banks, investment in Western countries and in buying armaments with little left to be invested in developing countries.

In recent years, oil producing countries have begun to realize the importance of economic diversification and start investing a large sum of their oil earnings on projects at home. For example in Saudi Arabia building the King Abdullah City is expected to cost $35 billion most of which is financed from oil money.

Instability of foreign exchange earnings makes it difficult for developing countries to meet their international obligations. In addition, the demonstration effect induces these countries to spend large amount of their foreign exchange earnings on imported luxury products instead of payment for imported capital goods and raw materials needed for development. Such practices reduce economic diversifications by delaying development process to alleviate poverty and promote economic sustainability. High priority must be given to imported technology to meet the immediate needs of the country development requirement.

Global expenditures on imported oil has accounted for 4.2 percent of global GDP in 2007. The recent sharp increase in oil prices is expected to increase the 'oil burden' (oil expenditures relative to GDP) in relation to global GDP to about 6 percent in 2008. For many countries especially the developing ones, such trends could have a substantial impact on their economies. The oil burden is already causing concern among policy makers, academicians and planners in developed and developing countries. Domestically, inadequate

liquidity decreases productivity by increasing production costs which reduces the country global competitiveness.

On the other hand, oil producers will continue to argue in favor of higher prices to maximize the return from non-renewable resources. Low states of economic development in these countries provides incentive for charging higher prices in order to pay for their development projects and improve the quality of life in their countries. In addition, political instability and external interference undermines market stability, especially in the Middle East, where historical trends have proven to be disruptive to oil flows. For many energy consumers, especially the United States, oil is a strategic commodity which falls into the domain of their national security. Such importance gives oil high priority in constructing future energy policies.

In recent years the relationship between consumers of oil, mainly Western countries and oil producing countries has deteriorated because of the events in Iraq, Venezuela, Iran, Algeria, Nigeria. The Western military invasion and the threat of embargos and sanctions against economic interest of oil producing countries could have destabilizing effects on the global economy. The rise of anti-western feelings in many of the developing countries including the Arab world increases uncertainty about the future flow of oil by encouraging people to use force for achieving their national objectives. Oil prices are sensitive to changes in global demand and security problems which in turn undermine efforts to increase market stability.

Energy Imbalances

Because of its significant components of production costs, higher oil prices are expected to have negative impact on growth prospects of both local and global economies. In OECD countries, for example, productivity growth is expected to decline from 2 percent currently to about 1.5 percent per year in 2030 which in turn could slow the demand for energy consumption. However, recent growth trends in Asia, especially China and India, are expected to continue to pressure demand for oil in order to meet productivity requirements and population increase. Meeting global requirements for oil, demand is to rise by 29 million barrels per day from 2006 to reach to 113 million barrels per day in 2030. Most of the increase is expected to come from developing countries with energy consumption is to double reaching 56 million barrels a day by 2030. The Asian countries alone are to see an increase of 17 million barrels a day or two thirds of all developing countries combined. As shown in Table 4, World's demand for oil increased from 85.91 million barrels a day in 2008 to 86.47 million barrels a day in 2010. Most of the increase in demand for oil comes from the Asian countries, where China's demand alone is to increase from 7.90 million barrels a day to 8.38 million barrels a day in 2010.

In the longer run however, the demand for oil is expected to come from rapid economic growth in the Middle East where demand is estimated to reach 9.7 million barrels per day in 2030 compared to 2 million barrels per day in 1980. Latin America requirement for oil demand is to reach to 7.0 million barrels per day whereas in Asia the demand for oil will be reaching to 29.7 million barrels of oil per day in 2030 compared to that of 4.4 million barrels per day in 1980.

In China, the demand is expected to reach 15.3 million barrels of oil in 2030 or at an average yearly increase of 3.4% between 2005 and 2030. It seems that in the longer term most of the demand for oil will originate in developing countries where average yearly increase is estimated at 2.5% between 2005 and 2030. Such trends will widen the gap between demand and supply causing prices to continue soaring.

Table 4
World Oil Demand and Supply 2008-2010 (in million b/d)

OIL DEMAND	2008	2009	2010
China	7.90	8.10	8.38
Other Asia	9.49	9.52	9.69
Total OECD	47.77	46.90	46.90
Total non-OECD	38.14	38.68	39.57
World	85.91	85.58	86.47
OIL SUPPLY			
OPEC	35.71	33.78	35.44
Non-OPEC	49.75	49.76	49.95
World total	85.46	83.53	85.39

Source: United Nations, The Impact of the Global Financial Crisis on the World Oil Market and its Implications for the GCC Countries (New York: United Nations, 2009)

Sources of current supply of oil are shown in Table 5 reflecting the importance of OPEC countries in future energy supply. In 2007, the share of OPEC in total world supply of oil accounted for 42% whereas North America supplied about 17% of world total or less than half of demand requirements.[8]

Table 5
Global Supply of Oil (million barrels/day)

Region/World	2004	2005	2006	2007	2008
North America	14.6	14.1	14.2	14.3	14.1
Europe	6.1	5.6	5.2	5.0	4.6
Pacific	0.6	0.6	0.6	0.6	0.7
China	3.5	3.6	3.7	3.7	3.8
Other Asia	2.7	2.7	2.7	2.7	2.7
Latin America	4.1	4.3	4.4	4.2	4.1
Africa	3.4	3.7	3.9	2.5	2.6
OPEC	33.1	34.2	34.3	35.5	---
World	83.4	84.6	85.4	85.5	---

OPEC: World Oil Outlook 2008

Creating a global energy balance, both in terms of security of supply and security demand for oil are important. OPEC countries are under pressure to guarantee supply by keeping the flow of oil in line with world demand. However, unlike other globally traded commodities, the supply of oil is influenced by political, strategic and national security factors which make future flows highly

8 See OECD, World Energy Outlook 2006 (Paris: OECD, 2006)

uncertain. The 1973 oil embargo and the rise in petroleum prices is still a reminder of the risk that history may be repeated. The Middle East where most of the oil is produced remains one of the most volatile regions in the world. Both external and internal factors could contribute to the instability of the region reflecting global disruptions of oil and sudden hike in prices. In addition, most oil producers are developing countries facing many challenges including high growth rates of population, greater demand for services, economic restructuring, new job opportunities and social development. These programs are likely to reduce the ability of OPEC countries to meet global supply requirements. On its part, OPEC is taking precautionary steps to increase oil supply by planning to invest $150 billion between now and 2012. These investments are to increase OPEC capacity by 4 million barrel of oil per day. Also, OPEC expects that oil consuming countries will closely look at the global supply requirements and take some initiatives to increase supply not only through production of conventional energy sources but also by investing in the development of new energy sources, reducing tensions in oil producing countries, maintaining stability of the dollar and increasing global cooperation.[9]

Global imbalances constitute an important obstacle for the flow of trade among nations. Not only are imbalances influence international trade movements, but also investment expenditures. Weakening the national demand for investment could have negative impact on global trade by reducing the capacity to import, especially manufactured products. The stability of the world economy underscores the importance of capital flows to facilitate international transactions. Recent increase in oil prices has increased imbalances by redistributing global liquidity in favor of small countries. Maintaining global balance will require recycling of excess liquidity earned by oil exporting countries by buying goods

9 See OPEC: Oil Market Report, June 2008

and services in the global markets. Unfortunately, large number of developing countries could suffer badly from the surge in oil prices in the form of balance of payments deficits, higher prices, increasing costs and declining profits. These countries may respond by adopting policy measures to reduce the impact of higher oil prices but such polices may prove to be unsustainable if oil prices continues on the rise. In the longer run, the challenge facing these countries is to invest and develop alternative energy sources.[10]

Formulating policies to predict future trends in the oil market is extremely difficult. Unlike other commodities, neither demand for nor supply of oil is easy to predict due to the nature of factors that govern demand and supply. To reduce uncertainty and ensure market stability, global cooperation is needed for bridging the gap between supply and demand for oil. Such cooperation will increase confidence in international markets by allowing countries to construct policies capable of inducing economic growth as well as investing in new sources of energy. Balance of payments disequilibrium could undermine international trade movements by imposing constraints on oil consuming countries to import goods and serves to meet their development requirements. In addition, many of these countries are in debt the service of which comes mainly from earning of their exports.

The demand for oil is expected to continue to grow due mainly to the Chinese and Indian factors. During the last two decades India and China have been experiencing substantial economic growth brought largely by sharp rises in domestic demand for oil. These two countries account for one third of world population and recently their economies have been growth at about 8-10 percent per annum. In 2005, growth in global trade was estimated at about 7

10 Center for Strategic and International Studies (CSIS), The Changing Risks in Global Oil Supply and Demand: Crisis or Evolving Solutions? Working paper, September 30, 2005 (Washington).

percent compared to 11 percent the year before. With the exception of India and China with their exports growing at 20 percent, the growth rates of several other developing countries are most likely to be much less.

The future demand for oil is influenced by several factors including population growth, economic development in non-industrialized countries and global management. World population is expected to increase by an average of one percent between now until 2030 reaching 8.2 billion or by an increase of 1.7 billion from 2006. Almost 94 percent of this increase is expected in developing countries where low productivity and the prospects of higher economic growth will contribute to increasing demand for energy. Similarly, the age structure of the population and the rising number of those below 50 could have implications to economic growth and consequently putting pressure on energy demand. However, the demand for energy is expected to ease because of global recession and slow growth in international trade transactions. Global economic activities are projected to decline by about 1.5 percent in 2009 causing aggregate demand both globally and locally to decline. For instance, in the United States, the biggest consumer of oil, crude oil demand and production is expected to decline from 21 million barrels a day to 19.9 in 2009 whereas globally the demand is to fall from 86 million barrels a day to 85.7 in 2009.

Global Liquidity and Growth Potentials

Economic growth, especially in developing countries, depends heavily on the country's ability to import capital goods and technology needed for building technological capacity and diversifying the productive structure. Development is a process of structural changes that focus on the supply side of the economy

to strengthen the productive capacity, induce technologic change, diversify production, increase services and improve worker skills. The growth potential of an economy depends on the creation of productive capacity capable of stimulating aggregate demand and increasing investment spending. Without investment capabilities, economic growth remains stagnant due to lack of adequate stimulus and weak linkages. Availability of international reserves is vital for promoting development and stimulating economic growth.

Globalization has increased the speed at which goods, services, knowledge, information, technology, labor and capital are circulated globally. Such new trends could facilitate economic growth by allowing countries to take advantage of the new economy and induce growth at home. Among other things, knowledge has become a key factor in creating wealth and in enhancing global competitiveness. Therefore, advancing the cause of knowledge underscores the importance of building capacity for applying, absorbing and creating knowledge. Inadequate liquidity undermines economic growth by limiting access to global knowledge and information. The developing countries are in need of such knowledge in order to build an energy capacity capable of reducing the future impact of global markets on their economies.[11]

During the last several years, many developing countries have experienced balance of payments deficits and deterioration of terms of trades due to weak economic performance and low export demand. Most developing countries have a narrow export base which imposes constraints on development by reducing the ability to meet the country's liquidity requirements. Almost two thirds of export of developing countries, including OPEC members,

11 United Nations Conference on Trade and Development (UNCTD), Globalization for Development: The International Perspective (New York: United Nations, 2008).

comes from production and exports of a few primary products such as petroleum, cotton, coffee, minerals, banana and tea. Sharp fluctuations in prices and demand for these products increase instability of export earnings reflecting changes in income, prices, unemployment and government revenues and expenditures. For supplementing their liquidity, many developing countries rely on foreign debt and foreign direct investment to finance their international obligations and pay for their immediate imports.

Table 6 provides a summary of balances on current account in different regions between 2001 and 2014. With the exception of the Middle East and developing Asia, the table shows that the rest of the world including the United States and other advanced countries will suffer deficits on current account between 2009 and 2014. Both the Middle East and developing Asia are expected to accumulate about one trillion dollars in reserves by 2014. In developing Asia including India and China current account balance is to increase from $36.6 billion in 2001 to 761.5 billion in 2014.

Table 6
Summary of Balances on Current Account, Selected Regions (Billions of US$)

Region	2001	2005	2007	2008	2009	2010	2014
World	-161.1	53.7	-27.9	-45.8	-46.3	-42.9	-47.0
Advanced countries	-207.7	-394.0	-731.2	-465.0	-371.3	-371.6	-193.2
United States	-384.7	-729.0	-731.2	-673.3	-393.2	-396.8	-476.8
Japan	87.8	165.7	211.0	157.1	76.4	56.0	75.3
Africa	0.9	2.8	10.7	12.2	-72.7	-57.9	-49.8
Middle East	40.4	97.1	254.1	341.6	-10.2	56.2	205.1
	36.6	162.3	406.5	422.4	481.3	469.0	761.5

Source: International Monetary Fund (IMF), World Economic and Financial Surveys: World Economic Outlook, April 2009 (Washington: IMF, 2009)

Increase in oil prices could have negative impact on aggregate demand causing gross domestic product to decline. As a consequence, expenditures on both public and private investment may decline causing job losses and slow productivity growth. In the case of the developing countries, such trends undermine their development projects by disallowing the economy from growing up to its potential. Similarly, higher oil prices increase the cost per unit of output produced pushing up the cost of living. Under globalization, macroeconomic policies become less effective due to external forces which in turn make government policies unable to manage the economy and correct financial imbalances. The weakening of macroeconomic policies could spell trouble for developing countries which are in dire needs for financial stability and external balance.

In relation to the economic consequences of higher oil prices, the International Monetary Fund (IMF) estimates the impact of a $10 increase in crude oil prices on the global economy. The results are listed in Table 7 showing that all regions will suffer decline in real GDP and experience inflation because of this increase. As Table illustrates, in 2005 global GDP declined by -0.5 % whereas GDP in the United States decreased by -0.8 to be followed by -.06 in industrial countries, -0.8 in Euro area and -0.4 in Japan.

Table 7
Impact of A Permenent US$10 Per Barrel In Crease In Crude Oil Prices After One Year (% of 2003 GDP)

Item	Real GDP	Inflation
World	-0.5	n.a.
Industrial countries	-0.6	0.4
United States	-0.8	0.6
Euro area	-0.8	0.6
Japan	-0.4	0.2
Others	-0.4	0.2

Source: IMF (2000) and staff estimates as reported by Hillard Huntington, the economic consequences of Higher Crude Oil Prices, Stanford University, research paper # 9.

A more detailed assessment of the impact of a permanent rise in oil prices on macroeconomic variables is shown in Table 8. Oil importing countries are to experience decline in real income, consumption and unemployment. Such impact should highlight the seriousness of energy supply by sending a warning to policy makers, national governments and international institutions for looking seriously into the energy question.

Inflation is another likely product of higher oil prices both locally and globally. Energy prices represent a major item in production costs which determine the success of enterprises. As a consequence, not only inflation reduces the share of the profit in total income, but also inversely affects aggregate demand by weakening the purchasing power. Domestically, increase in prices usually discourages incentive for growth by destroying the confidence in the local economy. Both foreign and local investors find it difficult to make decisions due to uncertainty about future trends and cost movements. Enterprises may be faced with devaluation of foreign

exchanges which causes the prices of imported goods to rise. At the global level, inflation increase prices of traded goods and services which induce balances of payments deficits. Oil importers, especially developing countries are in a disadvantage position because of high share of oil imports in total imports and due to increasing cost in the domestic economy. These countries usually have larger foreign debt the service of which is paid with earnings from exports. In addition, high degree of concentration in trade making developing countries exports more vulnerable leading to deterioration of the terms of trade and balance of payment disequilibrium. The depreciation of the dollar in recent years has fueled prices and increased speculations about the ability of developing countries sustaining higher price increases.[12]

Table 8
Impacts Of A Permenant $10 Rise In Oil Prices (Oil prices rise from $30 to $40)

Year	1	2	3
Real GDP	-0.3	-0.6	-0.4
Real consumption	-0.4	-0.7	-0.6
GDP price index	0.2	0.5	0.9
CPI	0.7	1	1.3
Core CPI	0.1	0.3	0.6
Employment (000)	-125	-451	-270
Unemployment rate	0.1	0.2	0.1

12 See William Cline, Impact of the Lower Dollar and Higher Oil Prices on the US Current Account Balance, Peterson Institute for International Economics, November 2007.

Short-term interest rate	0	0	-0.1
Current account ($bln)	-30	-29	-47
Inferred GDP impact (Billion $) #			
Real GDP	-36.6	-73.2	-48.8
Oil wealth loss	-38.2	-38.2	-38.2
Real income = Real GDP + oil wealth loss	-74.8	-111.2*-	-87.0

Source: Huntington, Hillard, The Economic Consequences of Higher Oil Prices, Energy Forum Modeling, Stanford University. http:/www.stanford.edu.group/EME/Research/Doc

Because of the importance of energy prices in various sectors of the economy, the immediate impact of the rise in prices of oil will be on the purchasing power. The cost of living is measured in domestic currency which adds to consumer price index. Similarly, produces that face rising costs pass the increase to consumers by charging higher prices for their products and services. This may be associated with productivity declines and loss of jobs due to weakening competitiveness and diminishing global demand. Under such circumstances, it is unlikely that real wages will increase enough to offset the decrease in purchasing power. In the developing countries, such trends could be devastating to the local economy by impacting poverty alleviation programs, investment confidence, government revenues and expenditures, unemployment, income distribution and economic growth. Industrial countries may attempts to shift their production operations, especially production of manufactured goods into the developing countries to gain comparative cost advantages and

remain competitive in the global markets. Globalization has opened the door for countries to compete in global markets which helped in managing rapid increase in energy prices by producing goods and services in those countries which are still enjoy low wage rates such as China and India.

Aggregate Demand and Global Liquidity

International liquidity is a stock of monetary assets, mainly foreign currencies and gold, used for settlement of global trade and maintaining balance of payments equilibrium. In other words, facilitating world trade and promoting global stability will depend on the circulation of international liquidity to meet the demand for exports and imports of various nations as well as to ensure lending for foreign capital used in technology transfer, knowledge acquisition, short term financing and other international obligations. In many countries, economic growth depends on both imports and exports the financial settlement of which is usually done through international currencies, especially the dollar. As a result of increasing global interdependencies, nations are required to gain access to trade and services for sustaining growth both locally and globally. Poor countries with limited exports could suffer from liquidity shortages to meet their obligations due to fluctuations in foreign exchange earnings and the rise in imported bill for oil and other petroleum products. Similarly, economic growth in industrialized countries depends on export of manufactured goods and technology, mainly to developing countries. Under such circumstances, the existing of adequate liquidity becomes necessary for strengthening confidence in global markets and by keeping the flow of trade uninterrupted.

Higher oil prices cause liquidity distribution to the oil exporting countries which have smaller propensity to spend than oil importing countries. Countries with high labor costs and capital intensive production have the tendency to suffer due to inability to compete and because of loss productivity. This makes government task to manage macroeconomic variables and stabilize the economy very difficult, i.e. monetary management over the economy weakens because of trade openness and balance of payments constraints. Countries with heavy dependence on imported oil are expected to experience slow economic growth and deterioration in its external balance.

In recent years, the rise in oil prices has greatly influenced the liquidity positions of many nations by redistributing foreign exchange in favor of small nations, mainly oil exporting countries with a limited absorptive capacity. Revenues from oil have so far exceeded their capacity to spend by generating pools of unused liquidity. For example, Table 9 shows that the four oil exporting countries in the Middle East, Saudi Arabia, Qatar, Kuwait and United Arab Emirates, accumulated close to $200 billion in surplus in 2007 whereas current account balances among OPEC countries accounted for about $350 billion in the same year. In 2007, the Gulf countries spent only one half of their earnings from export on imported goods and services leaving the rest in idle surplus funds. This is mainly due to the limitation of their absorptive capacity constrained by small population and low level of economic diversifications. As long as oil prices continue on the rise, these countries will continue to enjoy surplus in their current accounts. The capacity to utilize revenues from oil is too small to induce wide circulation of liquidity. Economic development programs and investment policies are inadequate to recycle all revenues made from oil exports.

Table 9
Total Exports, Imports and Current Account Balance, Seleted Countries In The Middle East, 2007

Region	Total Exports	Share of oil in total exports	Total Imports	Current account balance
OPEC	1,013,427	730,434	580,048	334,301
S. Arabia,	299,990	206,480	88,036	95,300
Kuwait	61,427	60,019	19,400	52,734
UAE	156,634	74,552	127,010	31,570
Qatar	37,952	27,801	22,042	5,453
Total GCC	556,003	368852	256,520	185,057

Source: Organization of the Petroleum Exporting Countries (OPEC), Annual Statistical Bulletin 2007

International Liquidity Management

In this age of globalization, adequate management of the global economy becomes essential for promoting trade and maintaining flows of finance and investment. Global economic interdependencies makes national economies sensitive to fluctuations in global demand and supply of trade and finance causing in the process slow rates of economic growth, political instability, social tensions, environmental degradation, and weakening national sovereignty. As the International Monetary Fund points out "the crisis was largely caused by weak risk management in large institutions at the core of the global financial system combined with failures in financial regulation and supervision." Without collective action involving national governments, non-governmental organizations, multinational business and international institutions, the likelihood that adequate management over the macroeconomic variables to

ensure global equilibrium will remain unattainable. Globalization has changed business practices by increasing interconnection among nations. Such trends have increased dependency on international markets for trade, finance and technology.

Balance disequilibrium reduces the country's ability to promote development by weakening the country capacity to imports and increasing economic vulnerability. Stability of the global economy will require collective action that minimizes the risk of global recession and providing financial support to countries which experience deficits in their balances of payments. Higher growth in the global economy depends on international demand as well as on the distribution of liquidity among nations. Demand for exports induces global growth by allowing countries to increase production and create employment, particularly in developing countries. For these countries, export earnings are essential for promoting socio-economic development and sustaining growth. In their early stages of development, these countries depend on imported manufactured goods and technology for supporting investment programs and building productive capacity. Thus rising share of energy in total imports could jeopardize growth potential by disallowing these countries from meeting development basic needs. Table 10 shows the impact of a $10 increase in petreloum prices on current account in several regions and countries. Oil exporters, especially those in the Middle East are to gain most from the increase in petroleum prices. Among losers are those experiencing high economic growth such as India, Brazil and developing Asia.

Table 10
Expected Current Account Impact Of A $10 Increase In Petroleum Prices In 2004

Region	Billions of US$	% of 2003 GDP
Other emerging markets and developing countries	101.7	1.3
Total exporters	133.5	4.3
Total importers	-31.8	-0.7
Africa	21.9	3.9
Nigeria	7.4	12.8
Central and Eastern Europe	-2.2	-0.3
Former Soviet Union	24.7	4.3
Russia	20.3	4.7
Developing Asia	-14.9	-0.5
Indonesia	0.3	0.2
China	-7.6	-0.5
India	-5.6	-1
Middle East	65.3	9.3
Libya	4.5	18.4
Kuwait	5.9	13.3
Qatar	3.4	16.8
Saudi Arabia	29.3	13.3
United Arab Emirates	8.5	10.6
Iran	9.2	6.7
Iraq	3.4	13.6
Western Hemisphere	6.9	0.3

Region	Billions of US$	% of 2003 GDP
Venezuela	7.9	9.3
Argentina	1.3	1.1
Brazil	-1.2	-0.2
Mexico	6.3	1

Source: OECD International Energy Agency (IEA).

Managing global liquidity and facilitating global trade require urgent initiatives to reduce the risk of global recession, financial instability, liquidity shortages and balance of payments disequilibrium. Undertaking such action underscores the importance of global cooperation and the construction of collective policies capable of restoring confidence in global financial markets and institutions.

Global interdependencies and interconnection has greatly influenced decision-making and policy construction in all countries. Economic globalization increased trade and investment opportunities among nations by encouraging production for exports. Countries are to take initiatives for opening up their economies by liberalizing trade and privatizing the local economy. The flow of goods and finance are induced by financial globalization which brought financial markets and multinational businesses close to each others to facilitate international transactions and maintain greater flows of trade and investment. Reducing the risk of global interdependence requires countries to manage globalization by increasing economic flexibility and monitoring liquidity position.

Global supply shocks create imbalances within the economic structure by subjecting the economy to higher domestic prices, balance of payments disequilibrium, currency devaluation and productivity declines. Management of global transactions strengthens the control over macroeconomic variables and restores confidence in the economy. OPEC should provide financial assistance to countries facing liquidity shortages due to balance of payments disequilibrium. Such funds help recycling OPEC surplus back into the global economy through expenditures on imported goods and services.

Most developing countries are under financial stress due to high energy prices. Shortages of liquidity restrain the developmental process by reducing productivity and slowing down economic growth. Recycling oil money keeps international flows relatively stable by reducing the impact of balances of payments deficits on trade transactions. Most exporters of technology and manufactured goods are non-developing countries which represent the drive behind the growth of the global economy. Slow export demand undermines the stability of the international financial and economic system and, therefore, assisting developing countries meeting their short term liquidity requirements reduces the risk of global recessions. Benefits from such financing ensure economic and financial stability of oil exporting countries by keeping the flow of oil revenues uninterrupted. These countries rely heavily on export of crude and petroleum products for supporting investment programs and sustaining development.

Petroleum exporters should establish emergency funds for supporting the least developed countries to achieve high rates of economic growth and to alleviate poverty. Accelerating the process of economic development in these countries creates linkages

which stimulate demand and minimize price vulnerability in the global markets for energy. Providing incentive for poor countries encourages foreign direct investment which can be arranged through the recycling of surplus liquidity in oil exporting countries. The potential for returns on investment in developing countries is expected to be higher because of convergence hypothesis which suggests that poor countries have high productivity growth compared to rich countries.

With the increased uncertainty about future demand and supply it becomes necessary to have an emergency sachem for financing countries with high degree of commodity fluctuations. International institutions such as the IMF can make the funds available for maintaining capital account convertibility and bailing out countries with balance of payments difficulties.

In developing countries, the private sector and institutions must be encouraged to take an active role in the management of both the use of energy resources and the utilization of liquidity. Government policy is to develop incentives for encouraging private sector contribution by providing the necessary findings for research and development. Without adequate monitoring, financial liberalization could lower the size of the country reserves by permitting imports for luxury products and non-productive technologies.

Oil producing countries in the Gulf have increased their return form the increase in world energy prices. They have improved the overall balance of payments position by accumulating substantial amount of surpluses. Regional current account surplus increased to 35 percent of regional GDP in 2007 compared to 30 percent in the previous year. It is expected that in the next coming

15 years, the demand for energy will continue to grow at an annual growth rates of 3 percent allowing oil exports to enjoy a substantial liquidity surpluses. The bulk of this growth in energy is to come from the Asian countries, mainly India and China, with combined GDP growth rates of about 20 percent. The combined share of China and India GDP in total global GDP increased from 3.09 in 1990 to 6.35 in 2004. A sustained GDP growth in these two countries is expected to continue at an average of 8 percent for the next coming decade.

International reserves represent the country purchasing power in global markets. Most of theses reserves are made of foreign currencies, mainly dollar used by the country to settle its external transactions. In other words, these reserves are used as a "buffer stock" for maintaining balance of payments equilibrium as well as to support the country's exchange rates. Shortages of reserves could cause substantial demotic macroeconomic instability. Minimizing the risk of such instability requires governments to formulate adequate strategy for managing international reserves.

An important factor that contributed to rise in commodity prices is the depreciation of the value of the dollar. Previous historical trends have shown that commodity prices were negatively correlated with the dollar reflecting the changes in commodity prices in relation to the value of the dollar. Recently, however, the value of the dollar has been declining due largely to slow growth rates, large current account deficits and higher oil prices which brought by rapid growth of global demand for winery. Since 2002, the dollar has depreciated by about 25 percent. It is estimated by the IMF that a 1 percent real depreciation of the dollar would result in an increase of greater than 1 percent in the real prices of gold, oil,

aluminum and copper.[13] The pegging of various currencies to the value of the dollar has caused the exchange rates of these currencies to fluctuate in the same direction as the value of the dollar. Globally, the rise in food prices and increase in consumer price index in many countries are attributed to the depreciation in the value of the dollar.

By 2010 the world demand for oil is expected to reach to 93.1 million barrels a day. The amount of investment needed to supply this amount is expected to exceed a trillion dollar. Supply from conventional areas may cost even more due to the declining reserves and rising cost of technology used in production and discovery. The problem facing global oil requirements is related to the fact that growth in demand is greater than the growth in supply. Even with new discoveries in Africa and Russia the amount of the new reserves fall short of meeting future demand requirements. Unlike several other traded commodities, oil supply is not solely determined by market prices. The supply of oil is influenced by non-economic factors including political, social and environmental forces which increase uncertainty about future growth to meet demand. In addition, oil is a nonrenewable resource which is expected to deplete faster as output is supplied. Most oil production and reserves is located in developing countries with ambitious development plans of their own. Supporting these plans, the developing countries need to make more of their produced supply for domestic consumption instead of exports. Thus higher economic growth in these countries will reduce future global supply creating shortages. Avoidance of future imbalances depends on investment in the development of new sources of energy.

13 International Monetary Fund, World Economic Outlook: Globalization and Inequality (Washington: IMF, 2007)

Conclusion

In 2008, the financial crisis in the United States spilled over to the rest of the world impacting global trade, finance, and output. Non-industrialized countries have been hit hard by the global economic downturn as evidenced by deterioration in their terms of trade, balance of payments equilibrium, capital movements and budget deficits. This coupled with the world-wide credit crunch and falling commodity prices has caused the economies of many countries, both developed and developing to experience severe demand decline and output reduction. Among the most adversely impacted are oil and gas producing countries by having oil prices declining by 63 percent and 50 percent for natural gas. Such price shocks could have undesired consequences both to local economies and globally.

International liquidity provides emergency funding to ensure economic stability through correction of balance of payments disequilibria. Most developing countries often suffer from shortages of reserves to maintain stability of their economies. The rise in petroleum prices during the 1970s and 1980s have brought fear that productivity of both local and global economies will be negatively affected. Under such circumstances, sustaining growth could prove to be difficult. Unstable growth reduces these countries capabilities to achieve their macroeconomic objectives. Overcoming these unpredictable trends requires developing global strategies to minimize price vulnerability and sustain economic growth.

Rapid economic growth in China and India in recent years has caused concern about future demand for energy consumption. These two countries, share among themselves a combined population of about one the third of world's total. Under such circumstances,

high economic growth will require substantial amount of energy consumption. However, most energy has to be imported through global trade. For example, in 2007 China consumed an additional 377,000 barrels of oil per day whereas India's consumption reached 150,000 barrel of oil per day. In other words, the combined demand by these countries accounts for about 500,000 barrels of oil per day.

The future prospects of global oil market stability will depend on the growth in demand for energy, especially from the newly emerging markets in Asia, as well as on the ability of existing supply capacity to satisfy demand. In recent decades, the discovery of new oil reserves to meet rising demand has been slow. Neither has investment in alternative energy sources has been successful so far in the development of a commercially viable substitute for conventional energy sources. The dynamism of macroeconomic variables and growth in population are expected to widen energy imbalances unless adequate energy policies, both locally and globally, are constructed. Under such circumstances, international cooperation is vital to bridge the gap between supply and demand for energy. Petroleum-based products are presently used directly and indirectly in the production of several goods. This renders oil even more valuable commodity than just a source of fuel.

An important implication of the global financial crisis is the slow growth in global GDP. According to the IMF estimate, global economic activities are to decline by 1.3 percent in 2009. In addition, output per capita is expected to decline worldwide affecting about three quarters of world population. The severity of such trends is expected to depend on the ability of the American economy's stability to pull out of its current recession. Confidence in the global markets is tied to the performance of western economies and their capabilities to correct global imbalances brought by about the global financial crisis.

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