

A dark blue silhouette of a world map is centered on a lighter blue background with diagonal lines. The map shows the continents of North America, South America, Africa, Europe, Asia, and Australia.

Managing Natural Resource Wealth in Resource-Rich Low and Lower Middle-Income Countries



Catherine Pattillo

Strategy, Policy and Review Department
March 21, 2012

Outline

Translating resource wealth to assets

Savings and investment: frameworks, experience, and new tools

Priority area for IMF

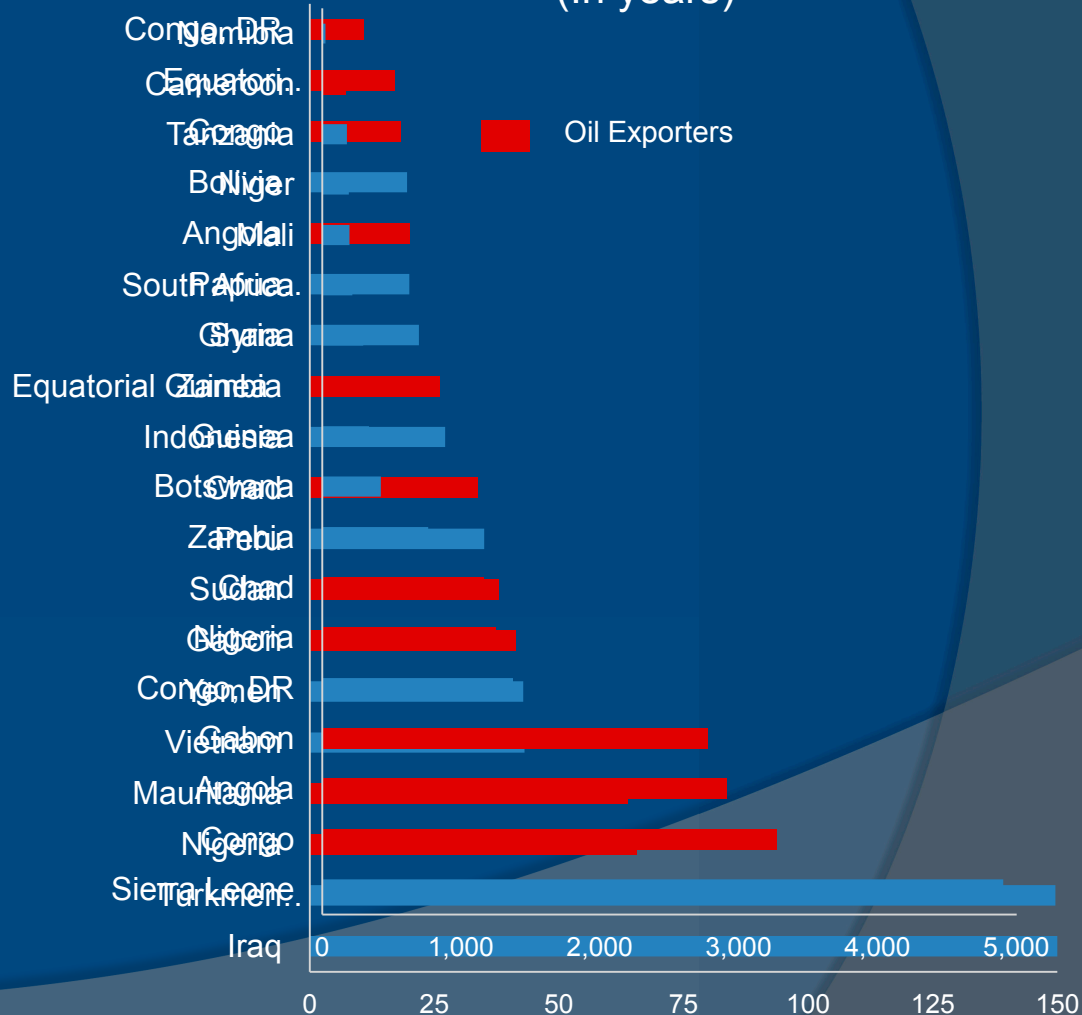
External stability assessments, monetary policy

Substantial Resource Wealth

Short-horizon for some

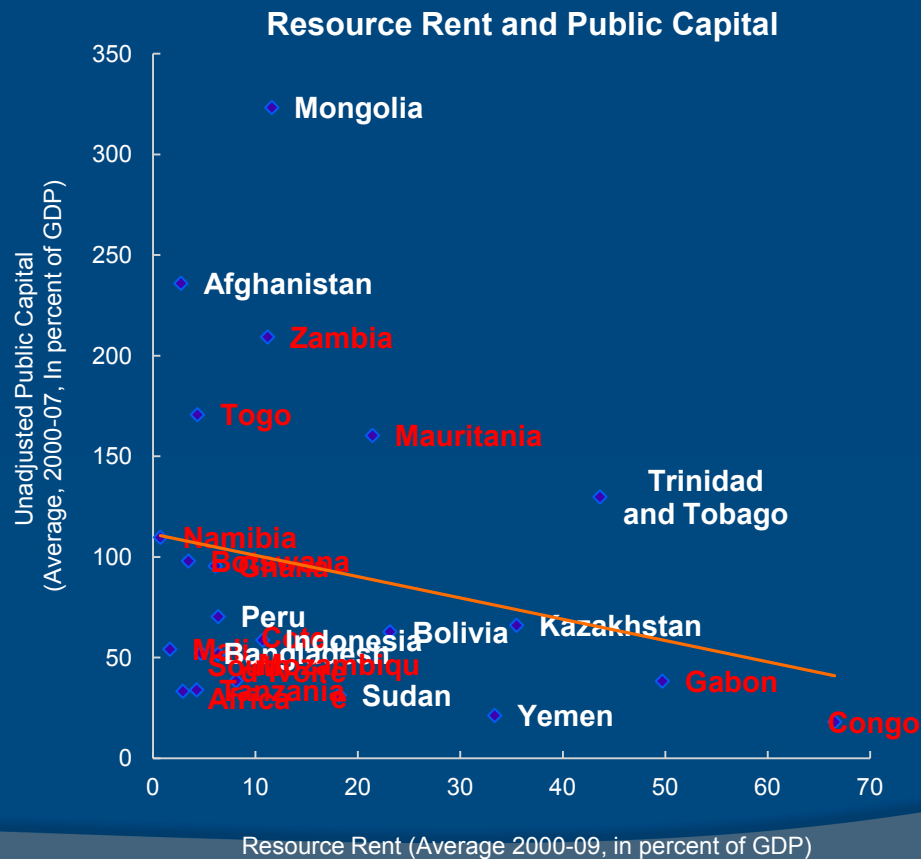
Limited window of opportunity to transform into other assets for sustainable development gains

Reserves over Annual Production of Natural Resources, 2011
 (In Percent of Non-Resource GDP)
 (In years)



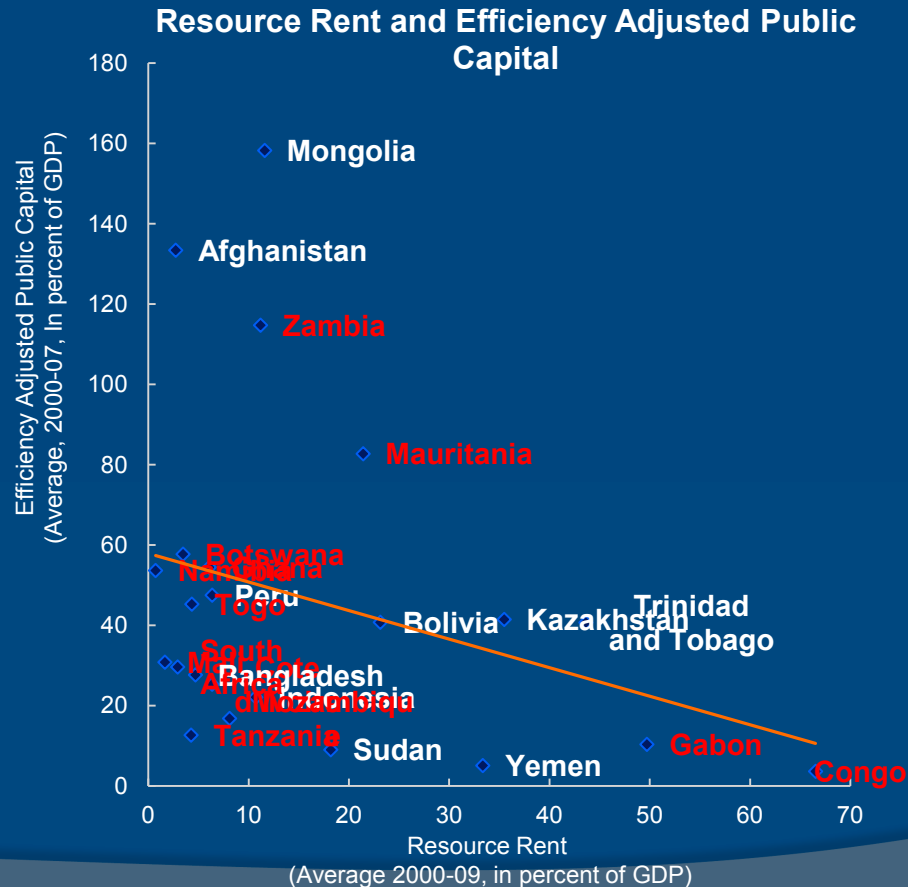
Poor Record on Transforming to Assets

Resource rents lower capital stocks...



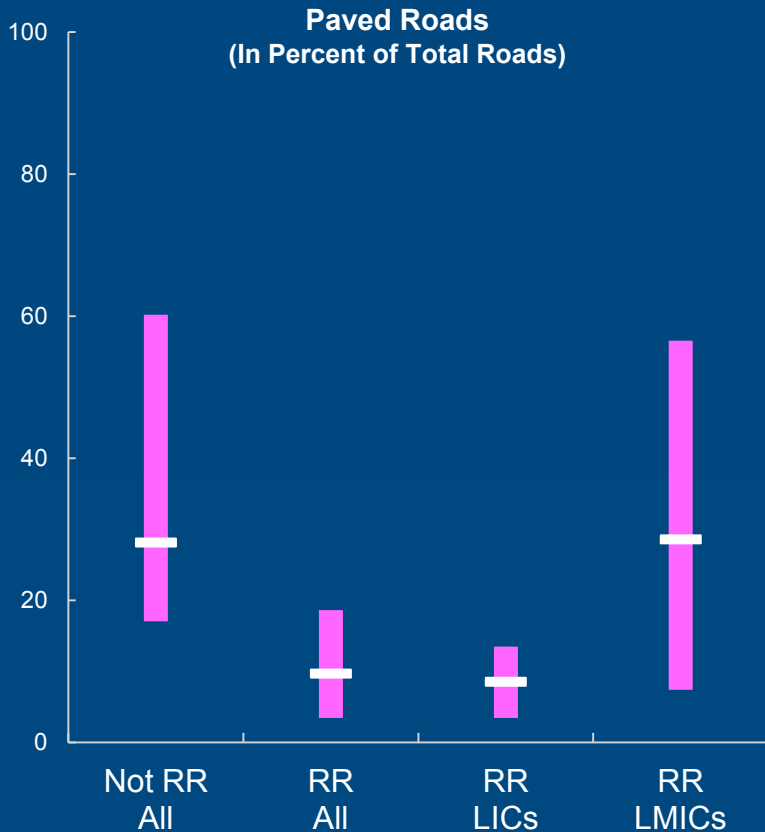
Poor Record on Transforming to Assets

Even more so for likely
“actual” capital

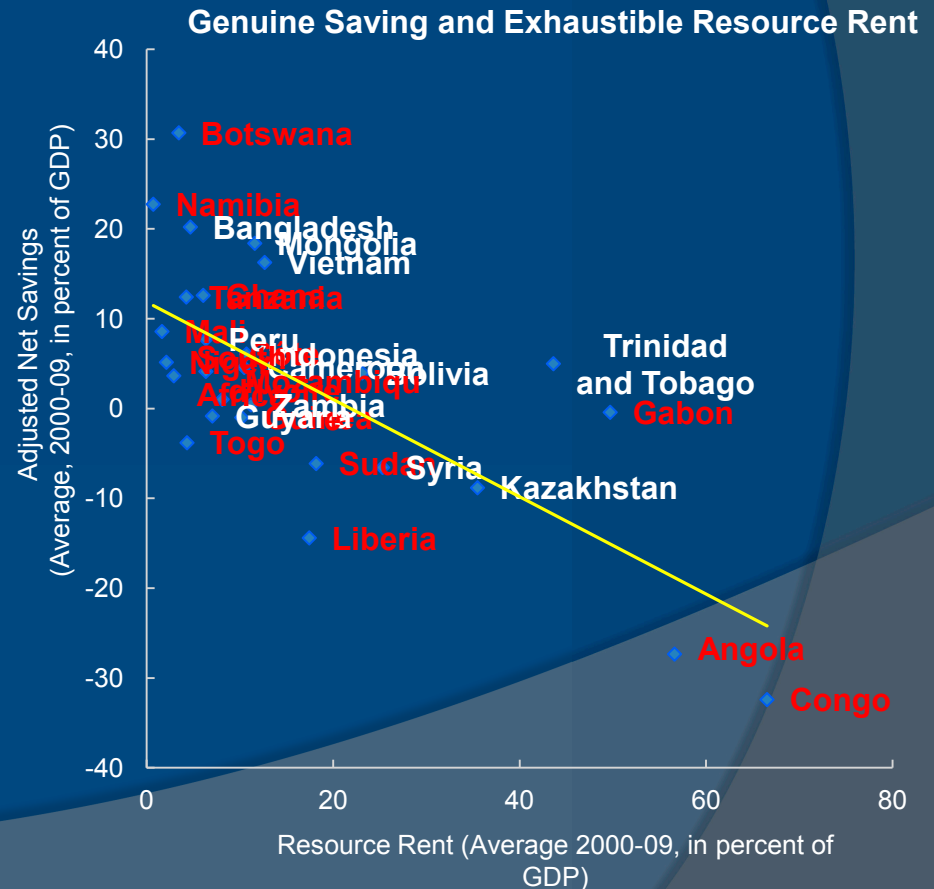


Poor Record on Transforming to Assets

Less infrastructure in resource-rich



Resource rent lower genuine savings



Big Questions

How much resource wealth should be saved?

Should investment be in domestic economy or foreign assets?

How to deal with volatility?

Permanent Income Hypothesis (PIH):

Save most of windfall in SWF

Sustain constant flow of consumption

Silent

Preserve resource wealth, ensure intergenerational equity, maintain stability

PIH Drawbacks

Overlooks long-term development needs in capital scarce, credit-constrained economies

➤ Current generations relatively poorer than future ones

➤ Empirical support that return to capital investment above world interest rate in LICs

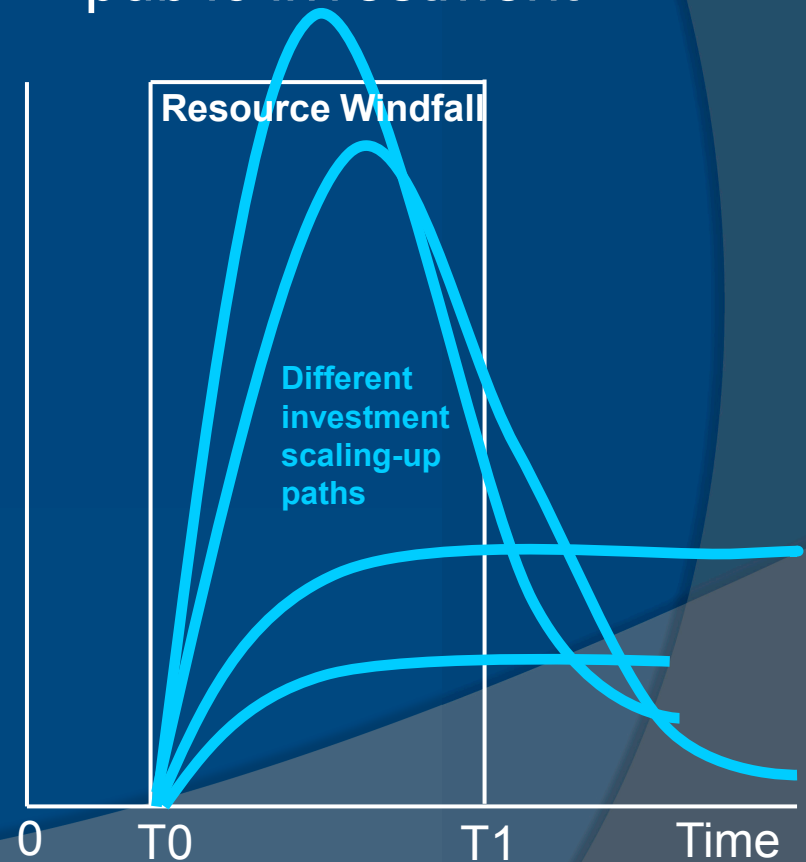
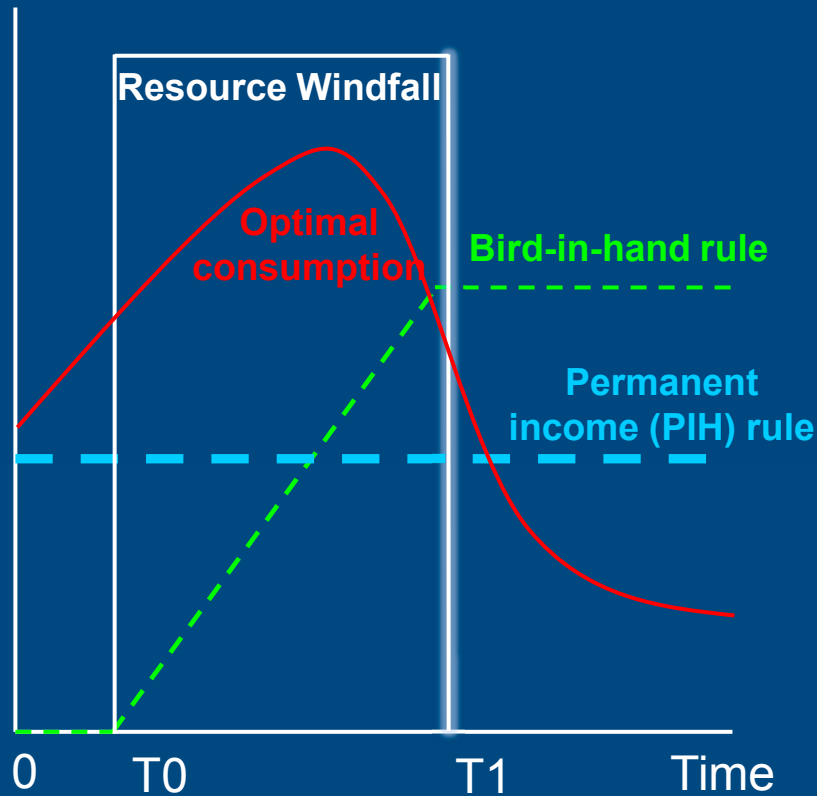
➤ Limited world capital market access, weak domestic tax systems → couldn't exploit these opportunities before resource boom

Fiscal: PIH translated to benchmark for non-resource balance, assumes govt. current spending is no different from capital spending

Use to Bring Development Forward But High Savings Rate Needed

Bring consumption forward

Front-load productive public investment



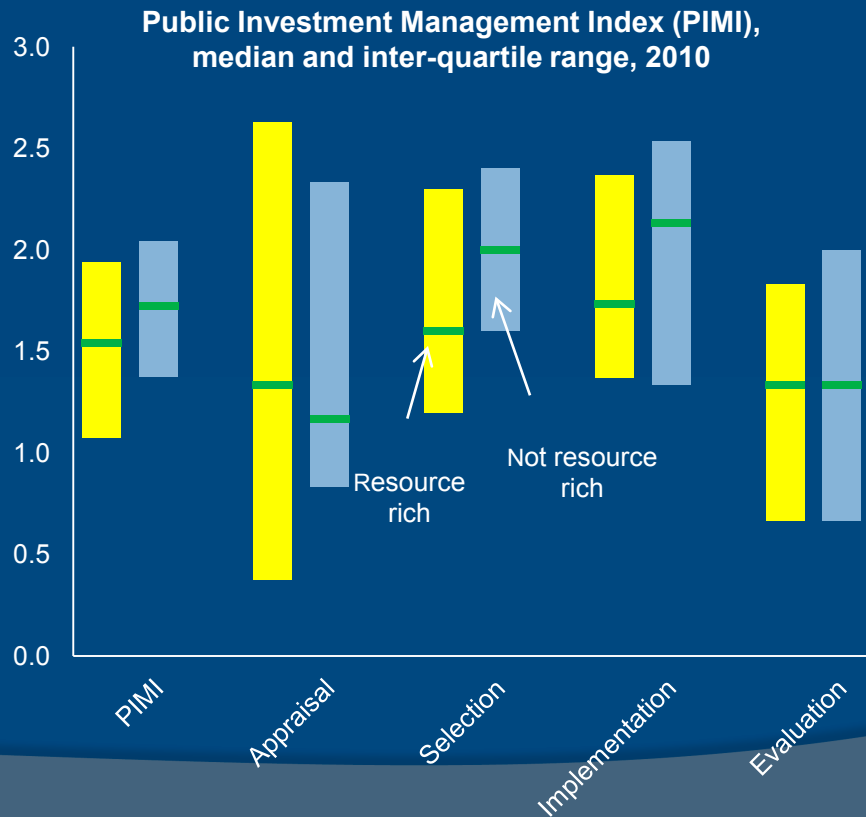
Too much, too fast = challenges

Spending resource income (including on investment) as it accrues:

- Highly volatile government spending path, aggravating macroeconomic instability
- Poor quality investment
- RER appreciation, hurts traded sector
- No funds for recurrent costs (O&M) of higher stock, growth benefits do not last

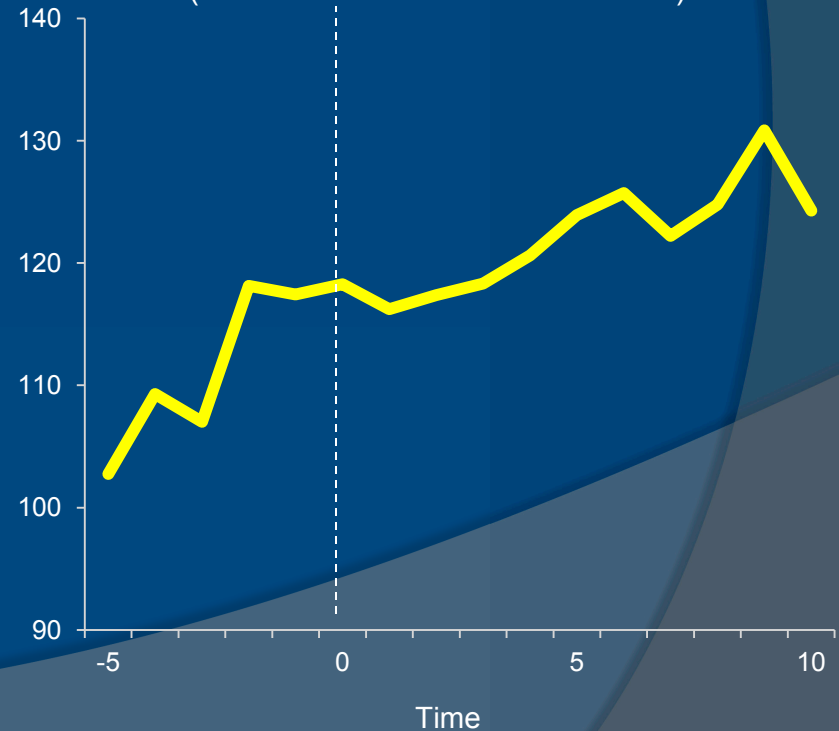
Ramping up Quickly: Low efficiency, Large Costs

Lower public investment management capacity in resource-rich



Investment costs escalate during investment booms

Relative price of investment
(Investment Deflator/GDP Deflator)



Experience with Resource Booms: Stylized Facts

Public consumption 

Public investment (less so private I) 

Relative price of I 

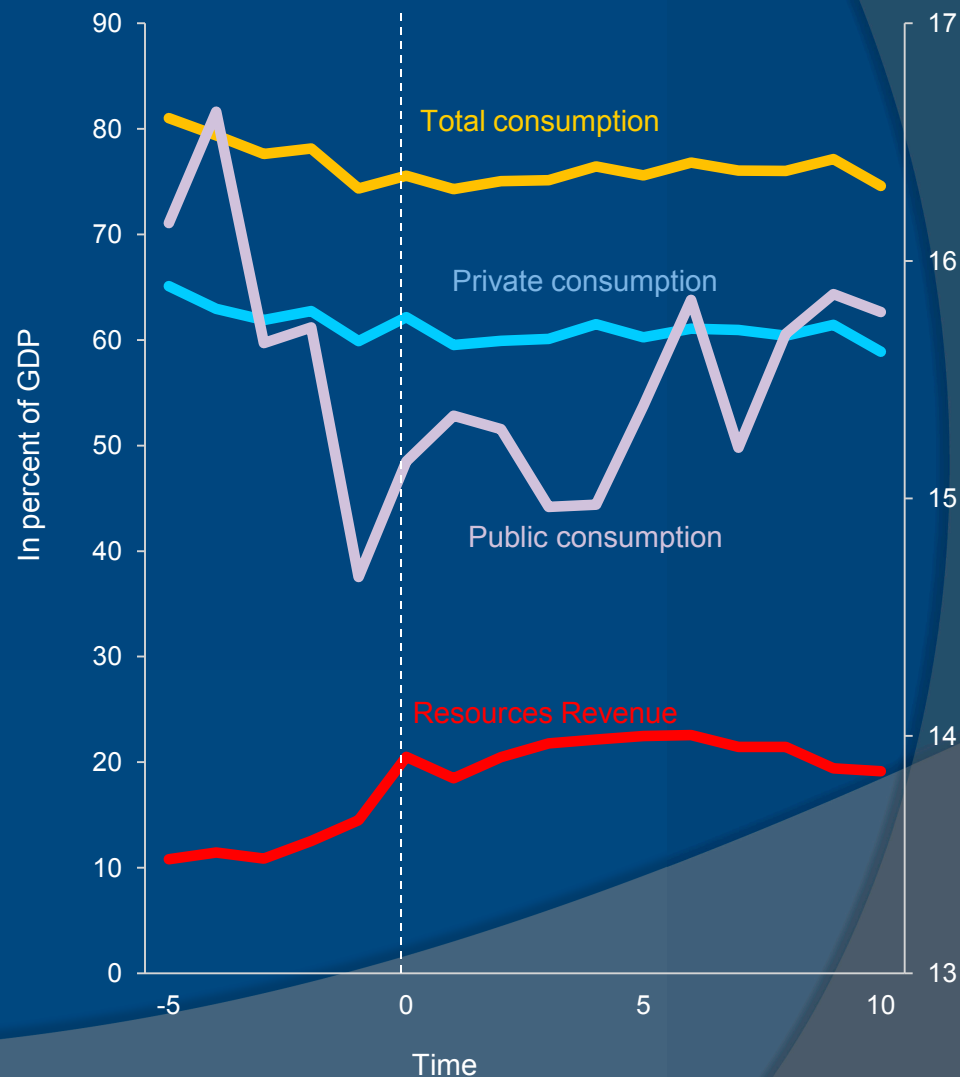
Net exports 

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Experience with Resource Booms: Stylized Facts

Public consumption 

Public investment (less so private I) 

Relative price of I 

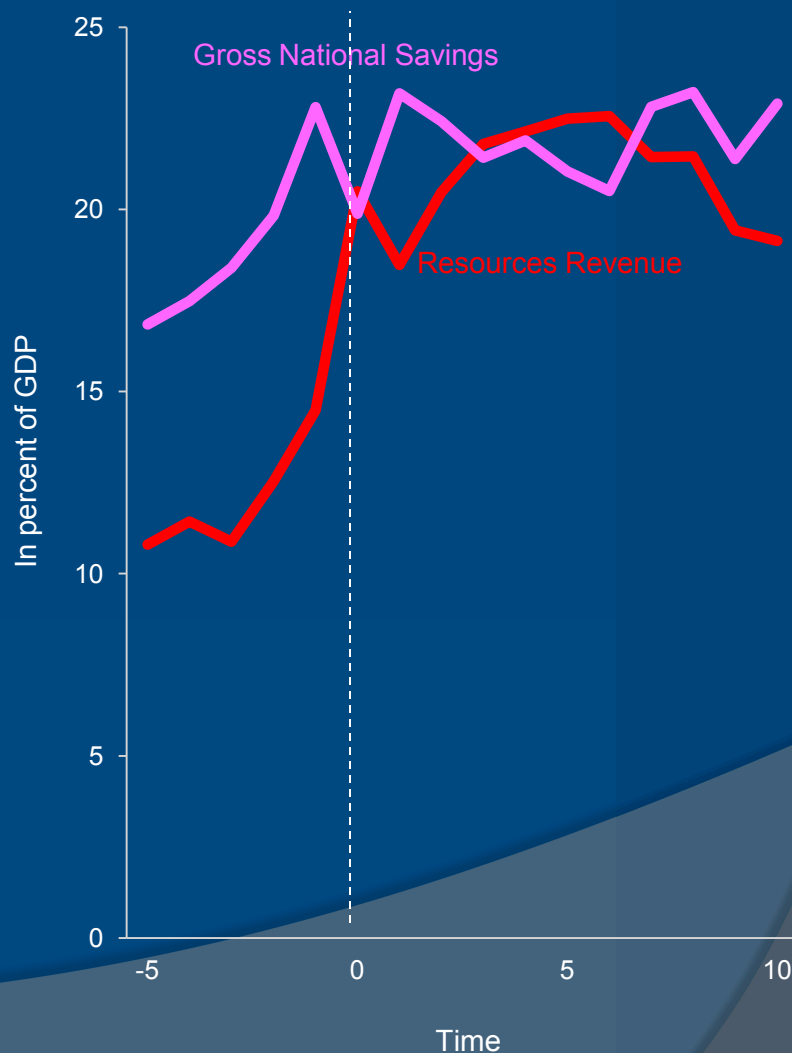
Net exports 

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Experience with Resource Booms: Stylized Facts

Public consumption 

Public investment (less so private I) 

Relative price of I 

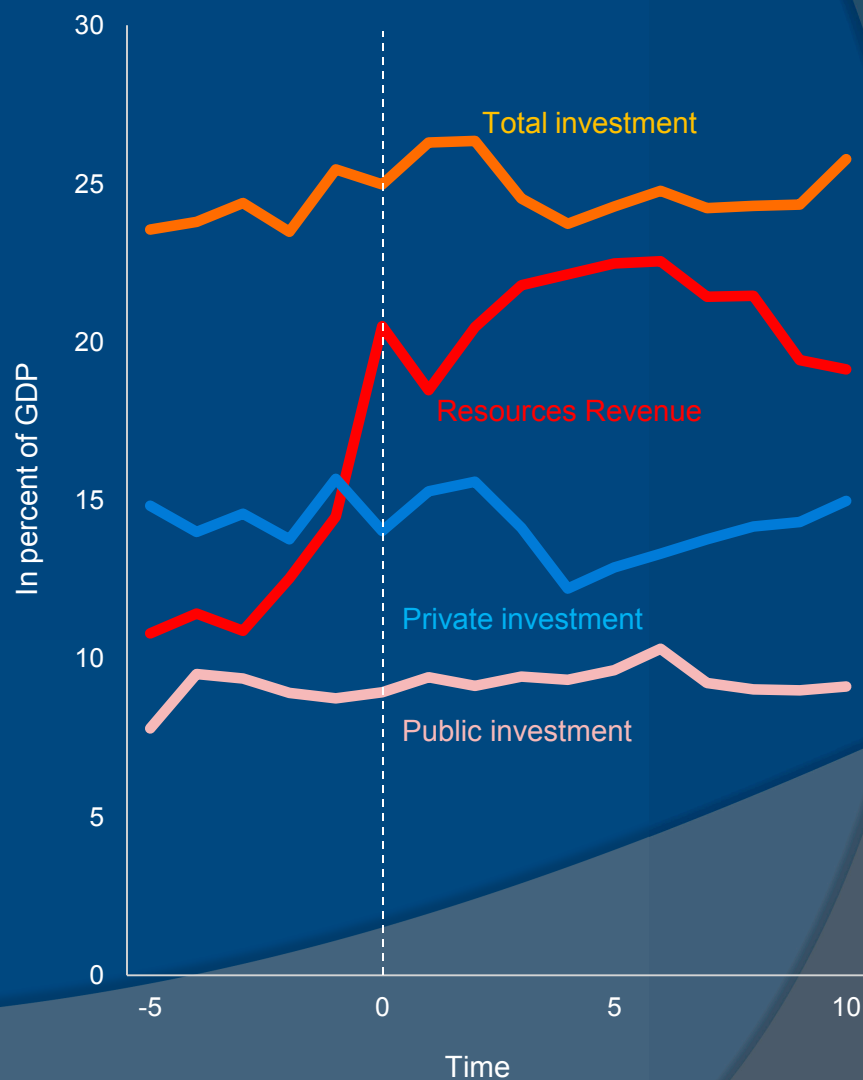
Net exports 

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Experience with Resource Booms: Stylized Facts

Public consumption ↑

Public investment (less so private I) ↑

Relative price of I ↑

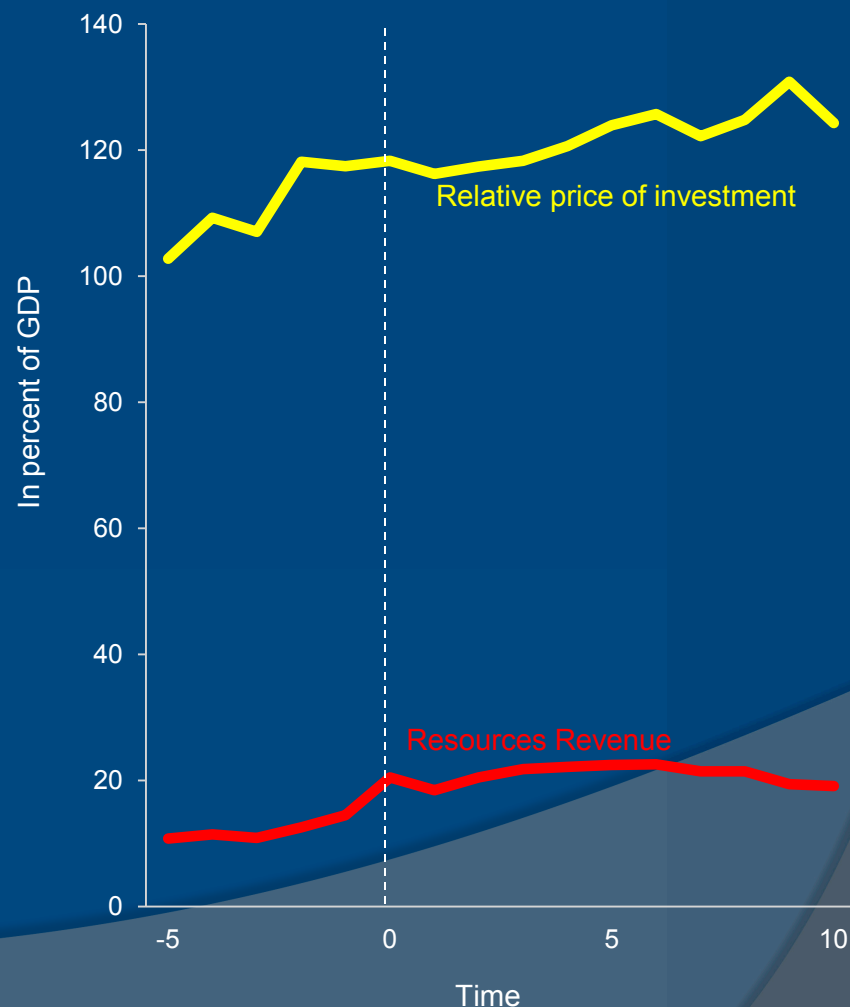
Net exports ↑

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Experience with Resource Booms: Stylized Facts

Public consumption 

Public investment (less so private I) 

Relative price of I 

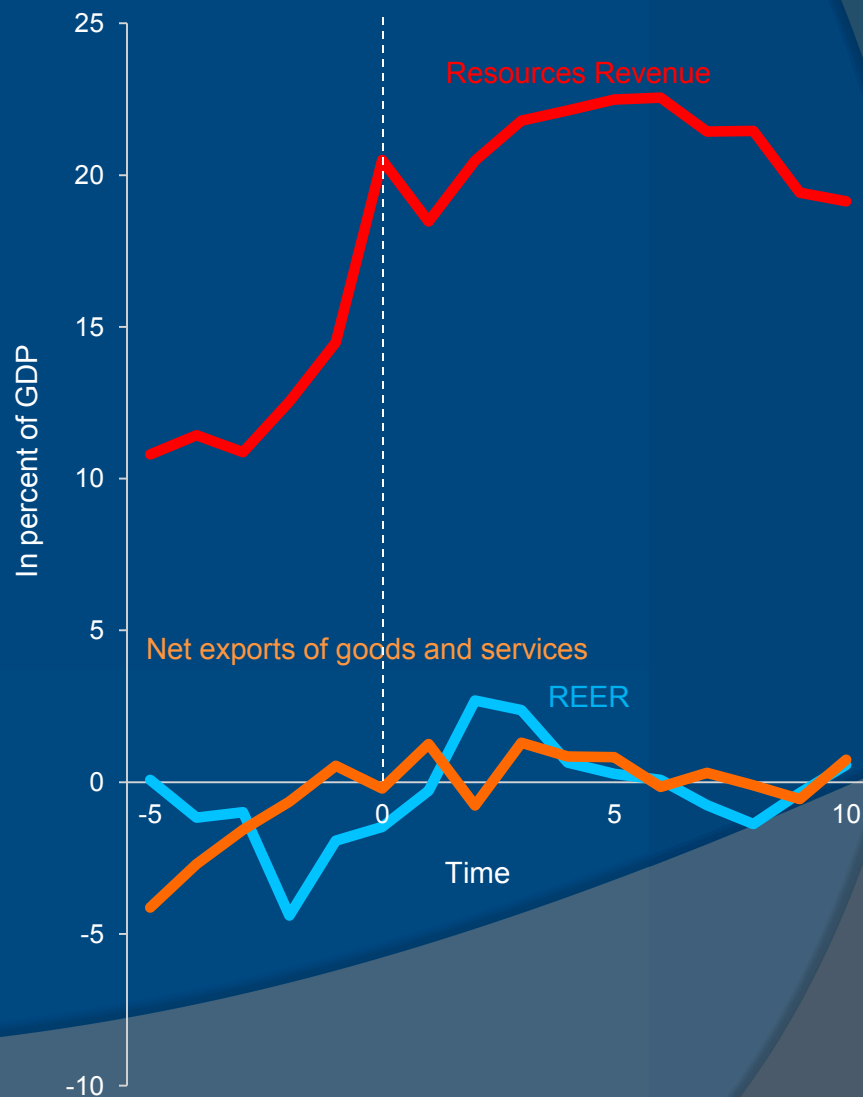
Net exports 

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Experience with Resource Booms: Stylized Facts

Public consumption ↑

Public investment (less so private I) ↑

Relative price of I ↑

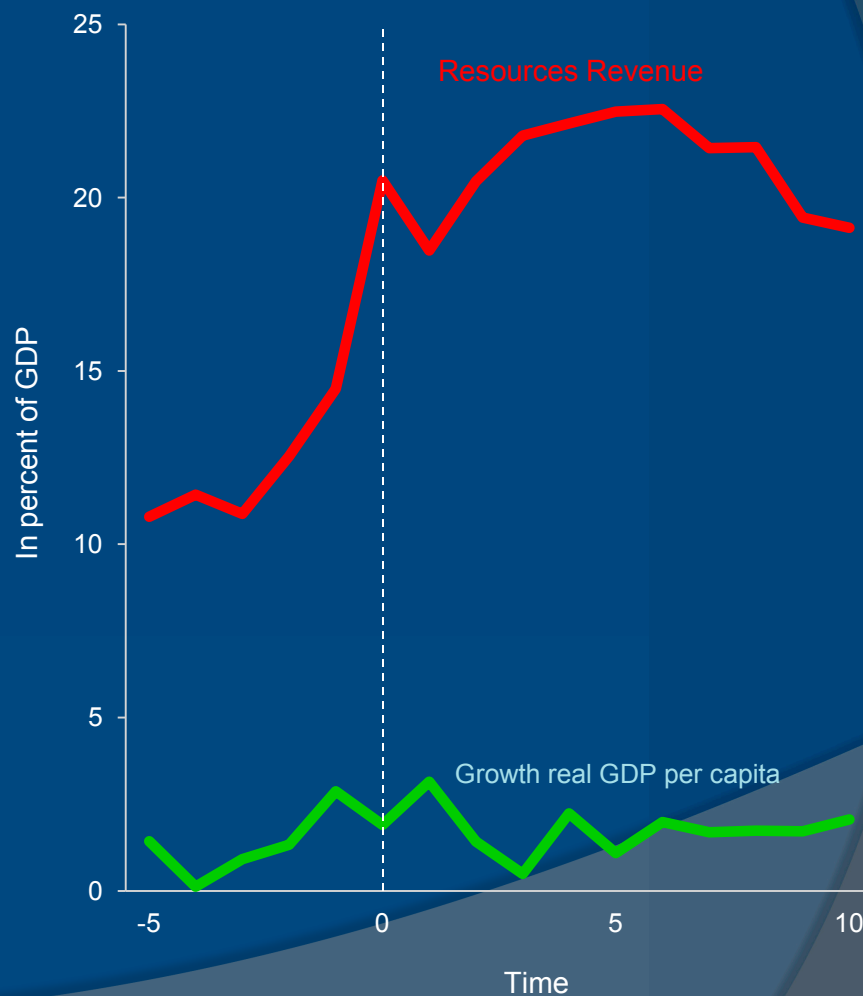
Net exports ↑

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Experience with Resource Booms: Stylized Facts

Public consumption 

Public investment (less so private I) 

Relative price of I 

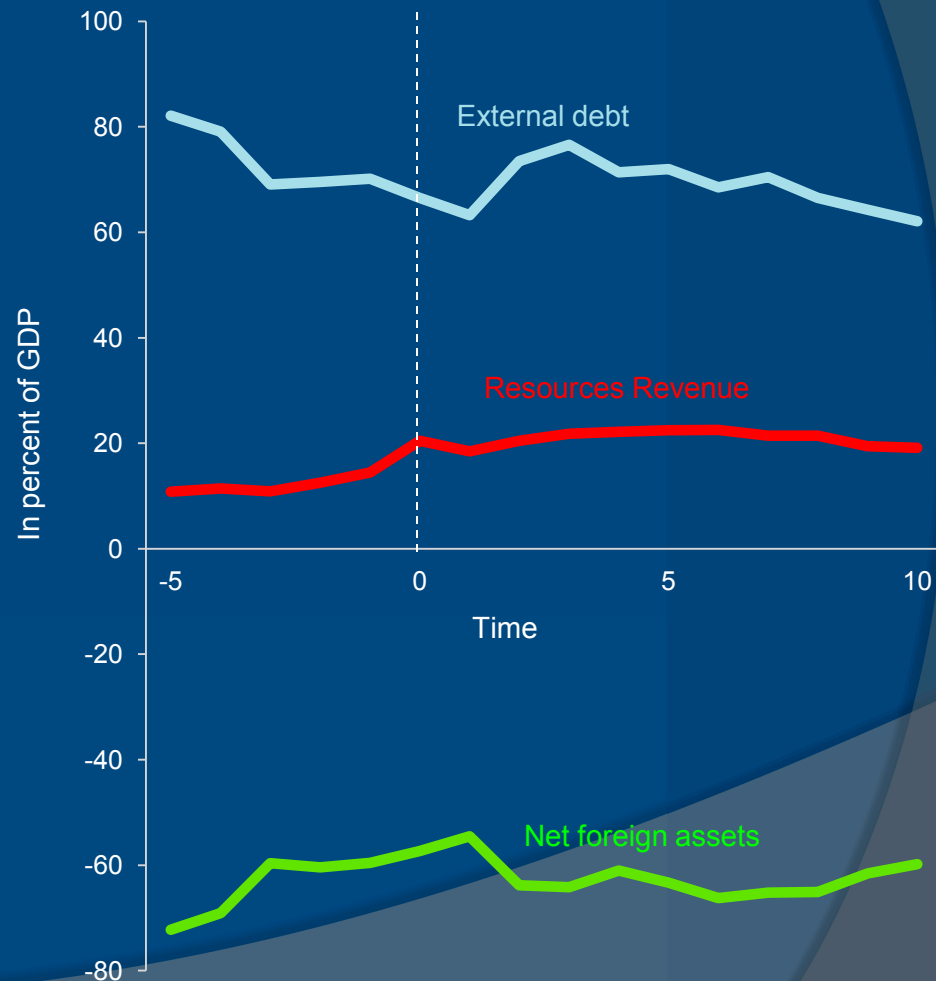
Net exports 

RER appreciation

Higher Debt

Limited growth impact

Better outcomes in 2000s boom



Sustainable Investing Approach (Berg et al, 2011)

Gradual increase in investment → non-invested resource revenue plus other increase in tax revenues goes to **“investment fund”**

Interest revenue from the fund finances recurrent costs

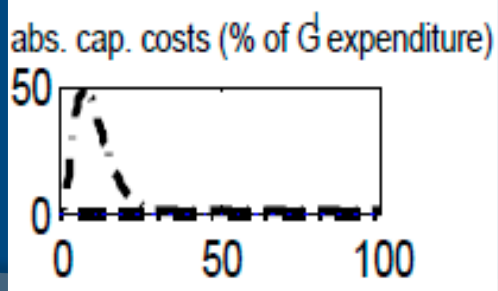
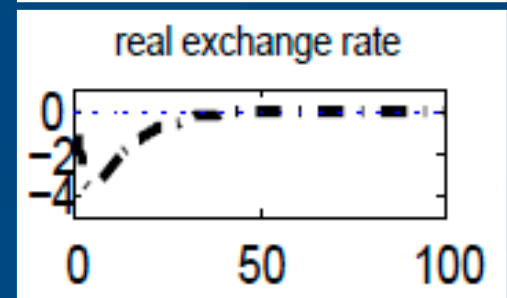
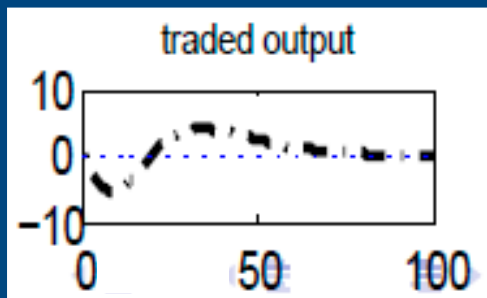
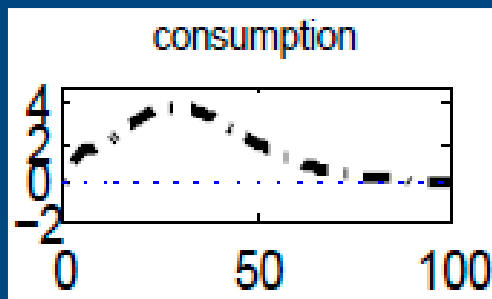
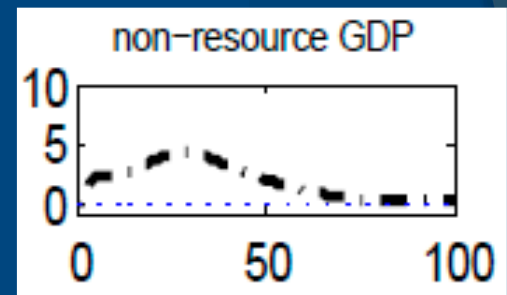
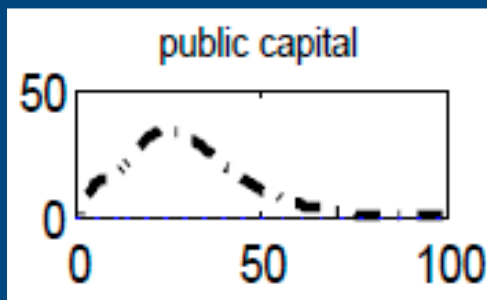
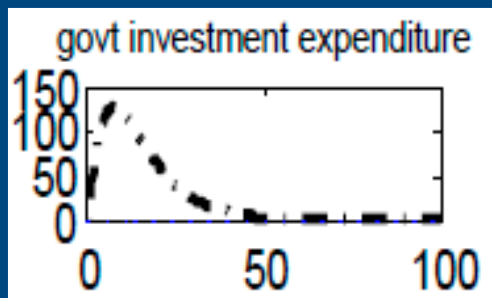
Minimizes instability, reduces absorptive capacity constraints, mitigates Dutch Disease

Preserves resource wealth in form of higher public capital and growth gains

- Tool to help analyze macro effects of different speeds of investment scaling-up with resource wealth

Sustainable Investing Approach

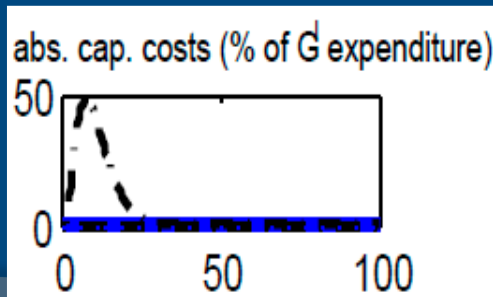
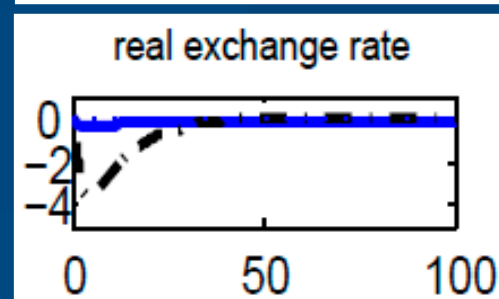
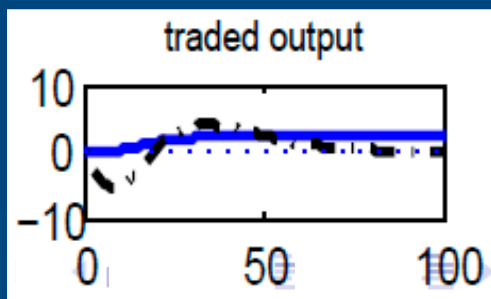
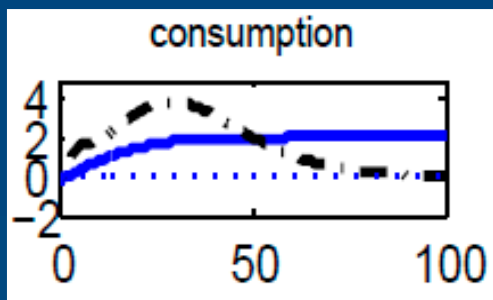
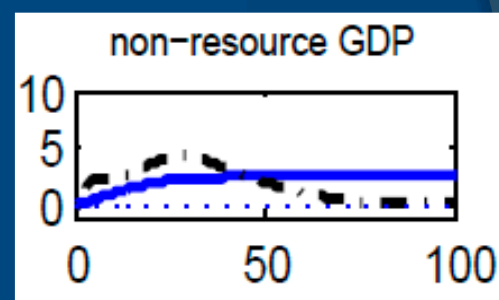
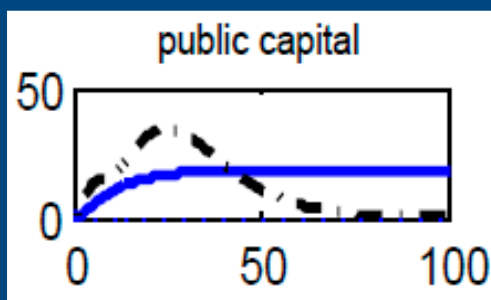
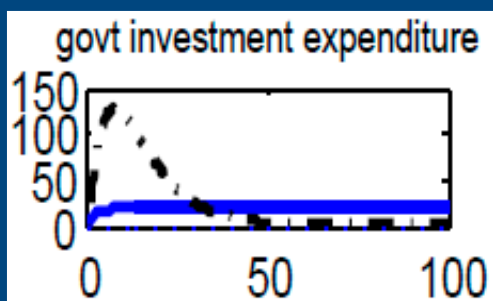
Stylized Investment



Sustainable Investing Approach

Stylized Investment

Sustainable Investment



IMF Policy Paper Underway

Savings and investment frameworks for resource-rich LIC/LMICs

Implications for Fund policy advice on fiscal frameworks, resource funds, PFM, and external stability assessments

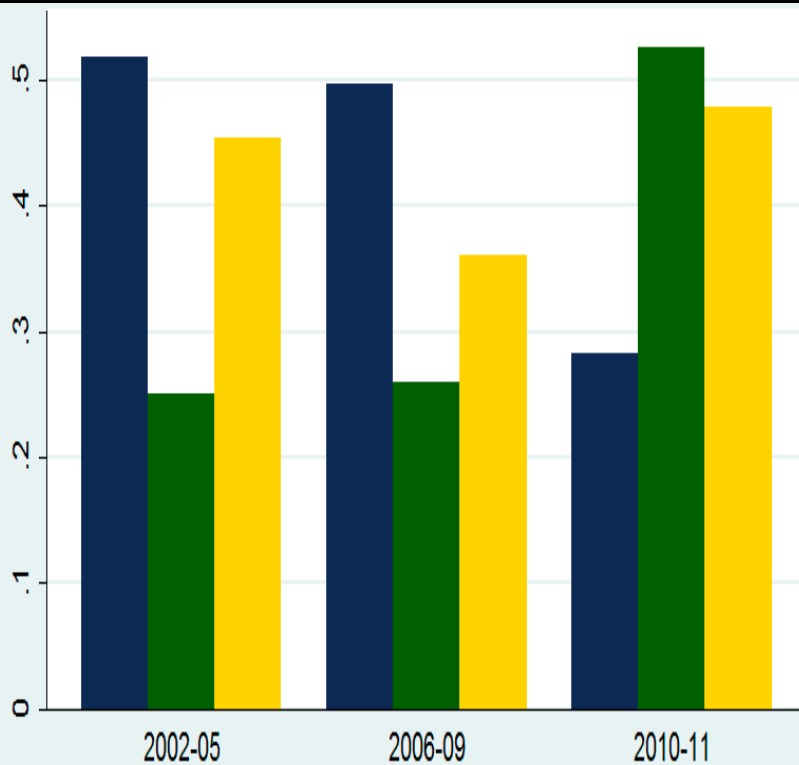
Lessons for enhancing Fund engagement (surveillance, programs)

➤ Objective: practical guidance for countries

Program conditionality

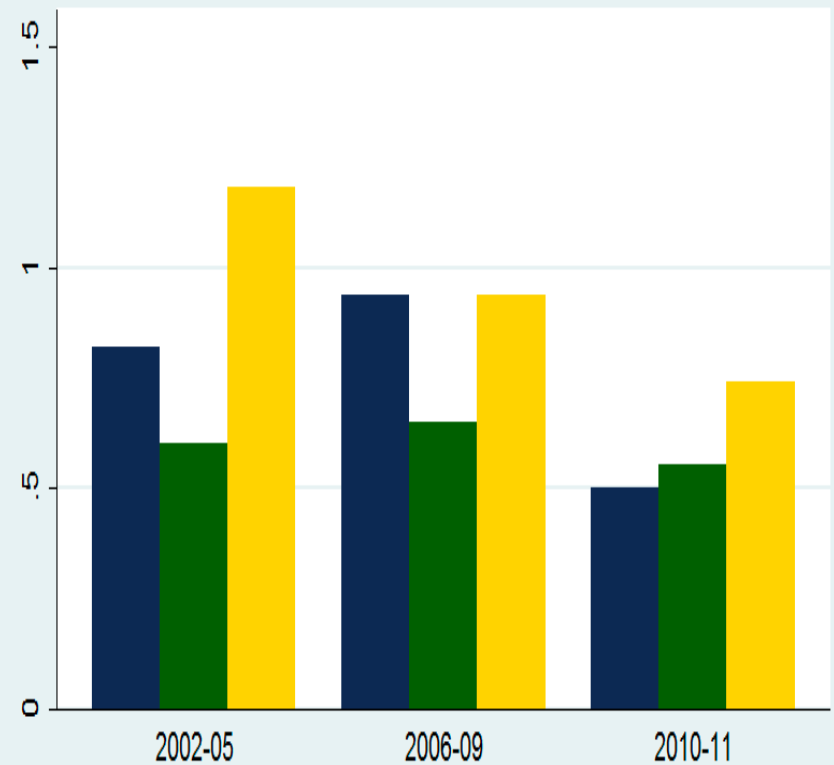
Average Number of Structural Conditions Per Review

Revenue Measures



■ Non-Resource Programs ■ Resource-rich LICs
■ Prospective LICs

Revenue Administration



■ Non-Resource Programs ■ Resource-rich LICs
■ Prospective LICs

External Sustainability Assessments

Macroeconomic balance approach: is medium-term current account (CA) in line with projected fundamentals? (CA “norm”).

New methodologies for resource countries: predict large CA surplus (to finance accumulation of NFA needed for future consumption), more appreciated RER

But neglect LIC characteristics

- Scaled-up investment → potential to expand growth and non-resource exports → current account sustainability

Simple, optimal models with investment can provide normative implications (Araujo et al, 2012). Help inform judgement

Monetary Policy

Monetary policy “in the shadow” of fiscal management of resource revenues, if latter not predictable

Hard for monetary policy to carry stabilization burden if no fiscal smoothing

Reserve accumulation, if combined with full public spending of the “oil dollars” is problematic.

➤ Amounts to trying to use the revenue twice—once as external savings, once as government spending

Fiscal and monetary policies need to be well coordinated

Conclusions

Seize limited opportunity to transform wealth to assets for development

High savings, but modify PIH.

Domestic investment—how much, how fast?

- Improve efficiency, solve bottlenecks, generate funds for O &M

IMF stepping up engagement—distinctive policy advice.



Preface: Resource Dependence

High revenue and export shares from resources in oil exporters

Other less fiscally dependent

Share of exports and fiscal revenue from natural resources, average 2006–10
(In percent)

