

# *The Political Economy of Natural Resource-Led Development*

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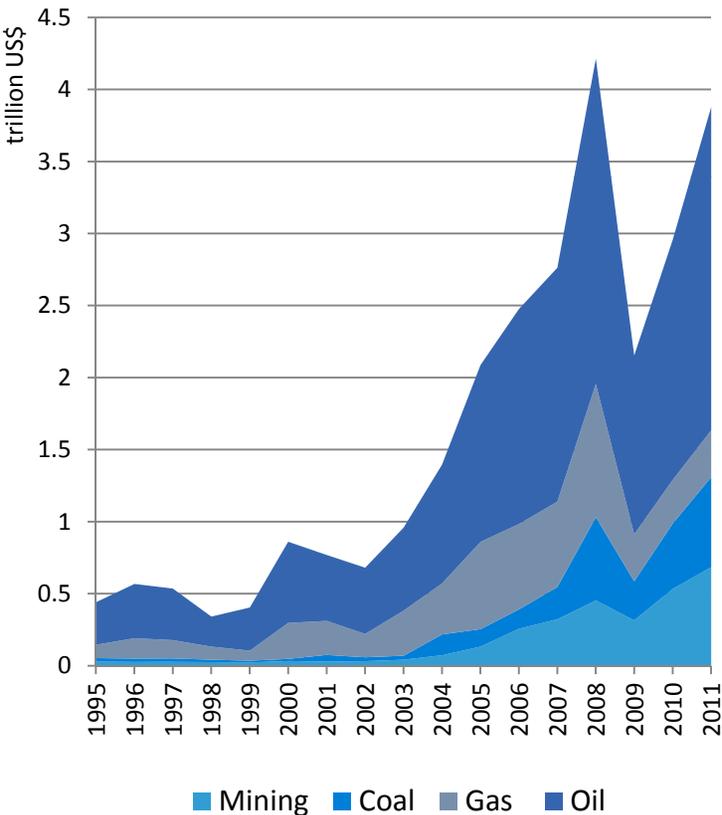


THE WORLD BANK

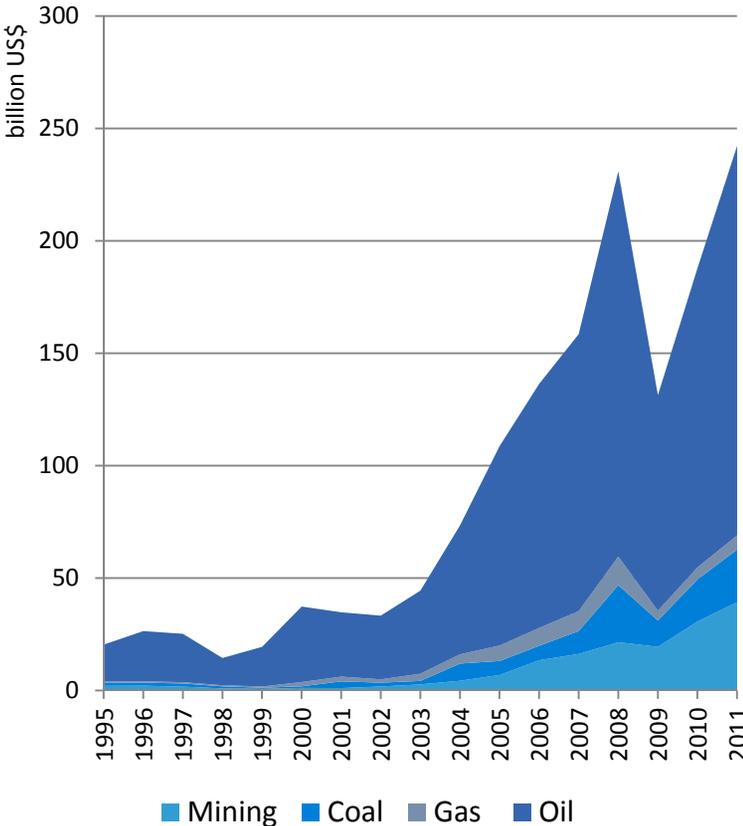


Rents from Mining, Oil, and Gas are growing rapidly-  
and Africa is very much part of the new frontier

**World**



**Africa**



Source: World Bank *Wealth of Nations* Database 2012  
IMF WB Fiscal Policy Conference

Anand Rajaram, World Bank, 2013

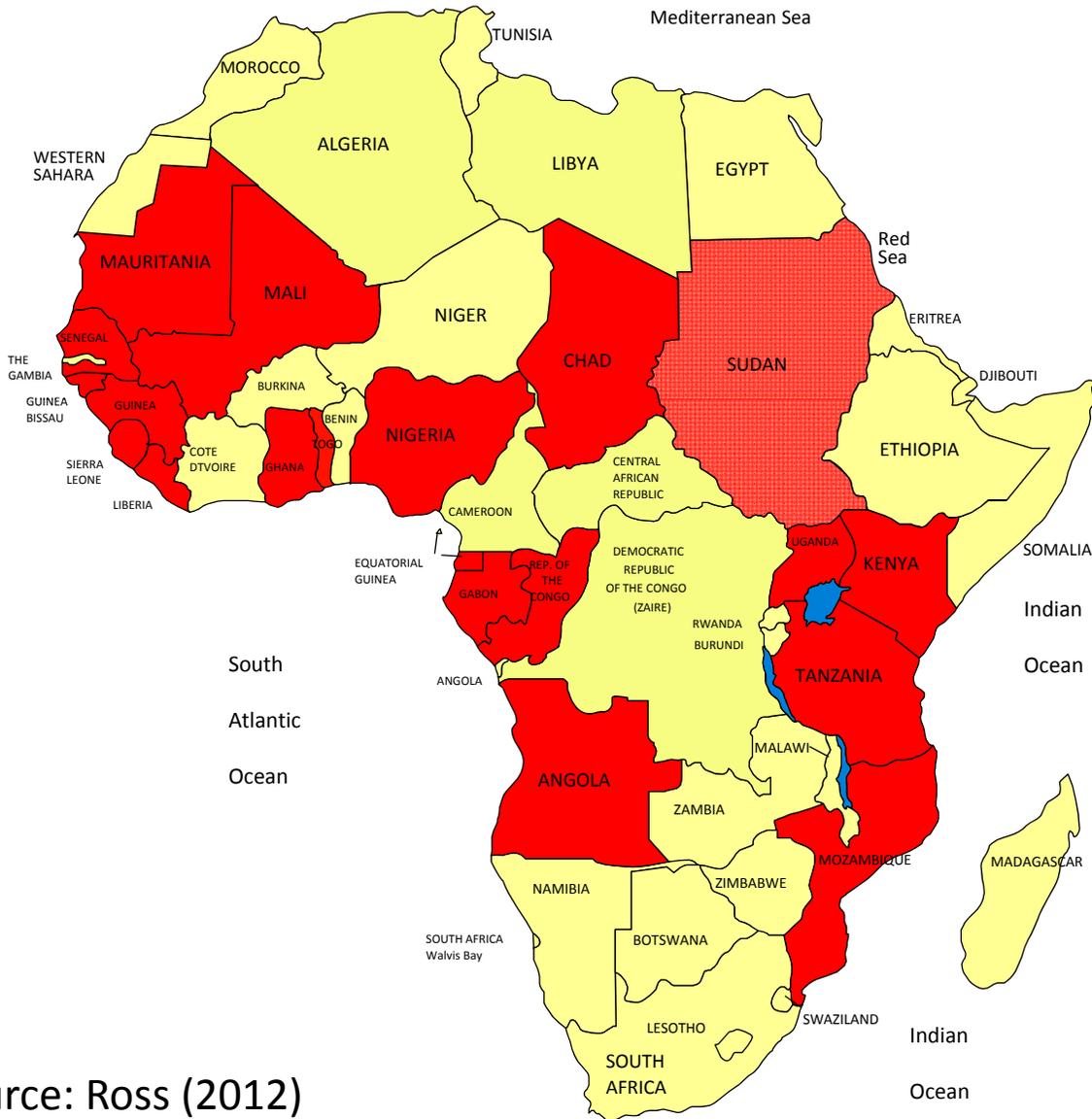
# SSA Oil Producers circa 1995



The number of fuel producers is growing rapidly, including in Sub-Saharan Africa

Source: Ross (2012)

# Likely SSA Oil Producers circa 2015

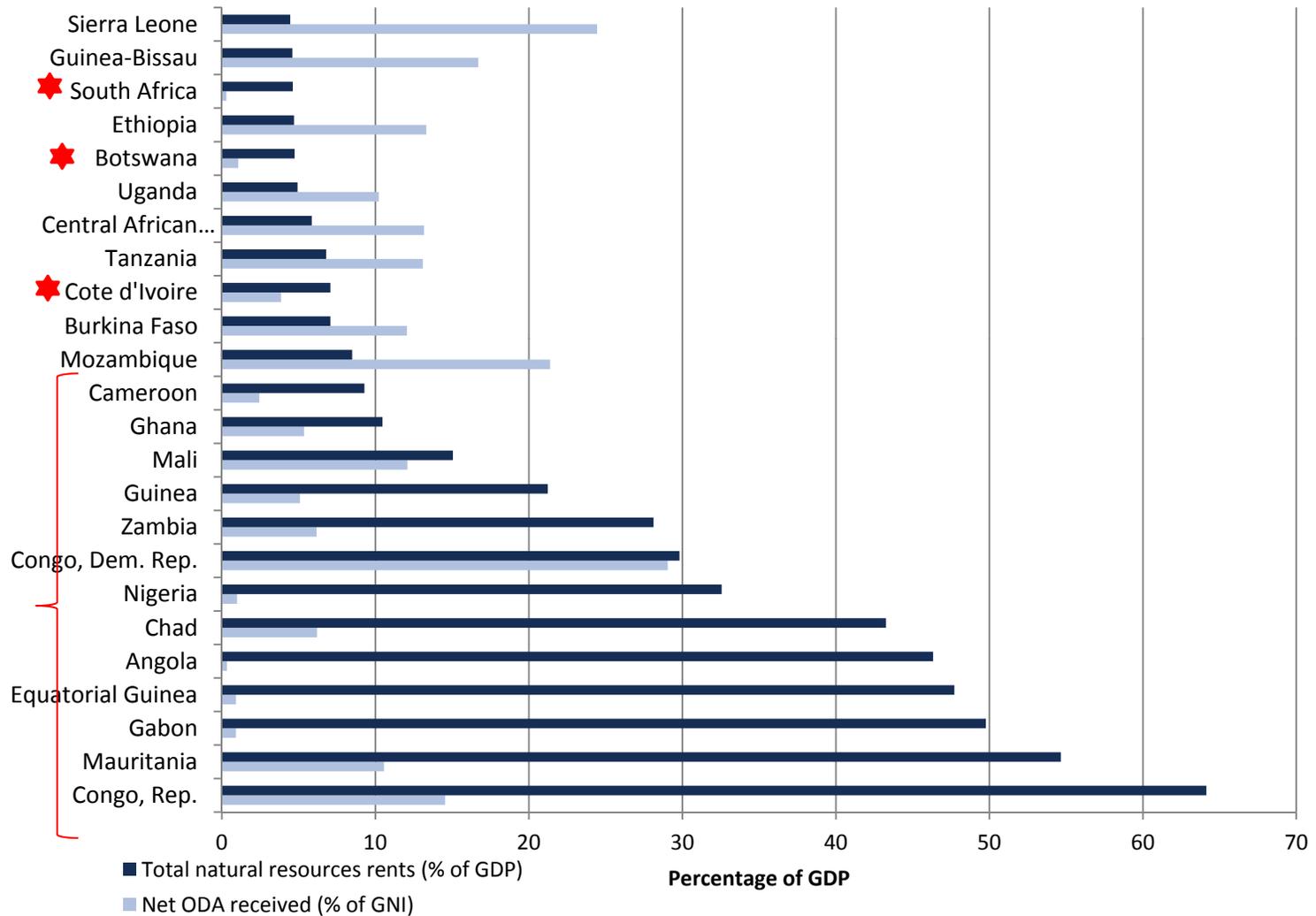


Many of these countries have limited capacity or technical knowledge : they cannot easily integrate extractive industry into their economies.

Role of oil rents will escalate in all these countries creating new political dynamics.

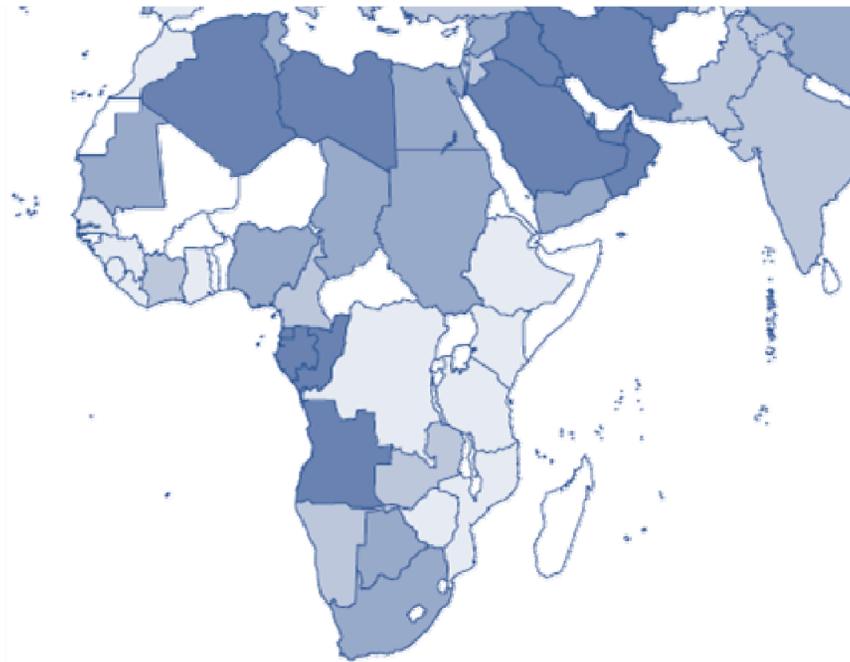
Source: Ross (2012)

# Extractives are Changing the Political Dynamic in Sub Saharan Africa - rent from EI will exceed aid in 16 of 24 countries

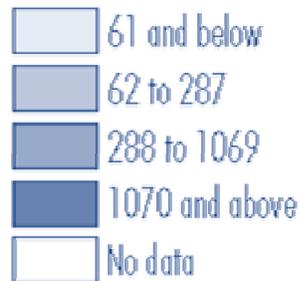


Source: Wealth of Nation Database 2012; World Development Indicators. (Data for year 2010)

# Sub-Saharan Africa Is Still Under-Explored – so this shift towards extractive revenues is likely to continue

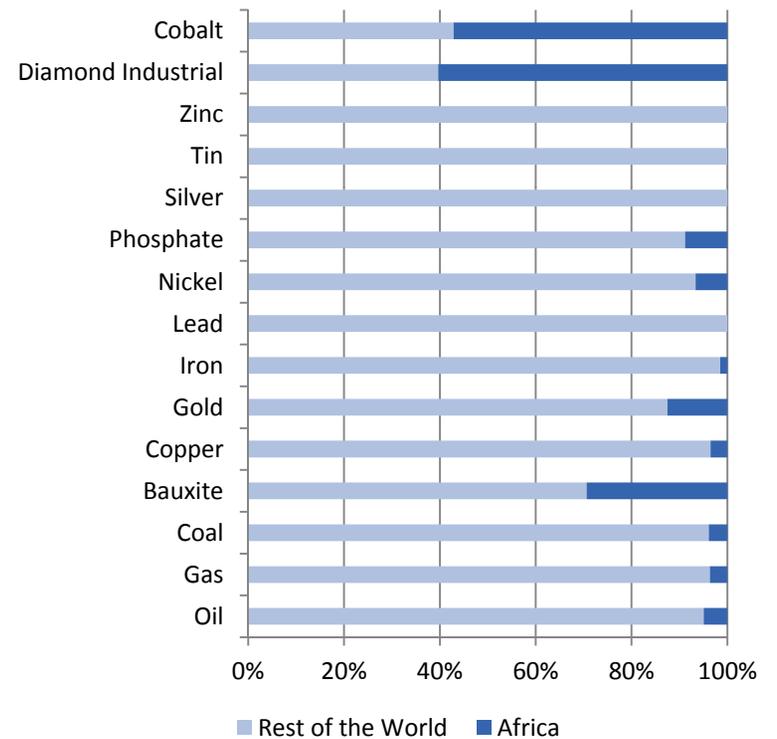


**Rents per Capita**



IMF WB Fiscal Policy Conference

**Proven reserves in selected minerals, 2010**



Source: USGS 2011, Gelb, Kaiser, and Viñuela 2012.

Anand Rajaram, World Bank, 2013

# Some Countries Have Not Made Good use of Resource Wealth

- » Nigeria is a middle income country (PCI \$1280) that has had significant resource revenues since the discovery of oil in 1955
- » But ... **68%** of its population remains below the poverty line in 2010 (only 36% in 1970)
- » It is ranked **156<sup>th</sup>/187** on the Human Dev. Index
- » Risk of maternal death is **3.4** (LIC ave. 1.8)
- » Its **infrastructure** is not much better than a low income country
- » **Only 58%** of the population has access to safe water (LIC ave. 63%)
- » **Only 50%** has access to electricity
- » Very limited economic diversification, high rates of unemployment

Similar statistics for many other RRCs – Angola, Cameroon, Chad, DRC, Equatorial Guinea, Gabon, Ghana, Guinea, Liberia, Niger, Sierra Leone

But there are many examples of resource rich countries that have done very well - **Canada, the USA, Norway, Australia, Chile, Indonesia, Malaysia, Botswana, Trinidad and Tobago – even the Netherlands (famous for the Dutch Disease)**

**How can SSA countries achieve good development dividends from natural resources?**

# Quality of Institutions – critical factor for success -1

## » The quality of institutions matters for growth

- » Mehlum, Moene and Torvik (2006) - if you control for institutional quality the negative correlation between resource dependence and growth performance disappears. Institutions that encourage “grabbing” lead to the resource curse, those that encourage “production” lead to growth – (composite index of: rule of law, bureaucratic quality, corruption in government, expropriation risk, and contract repudiation indices).

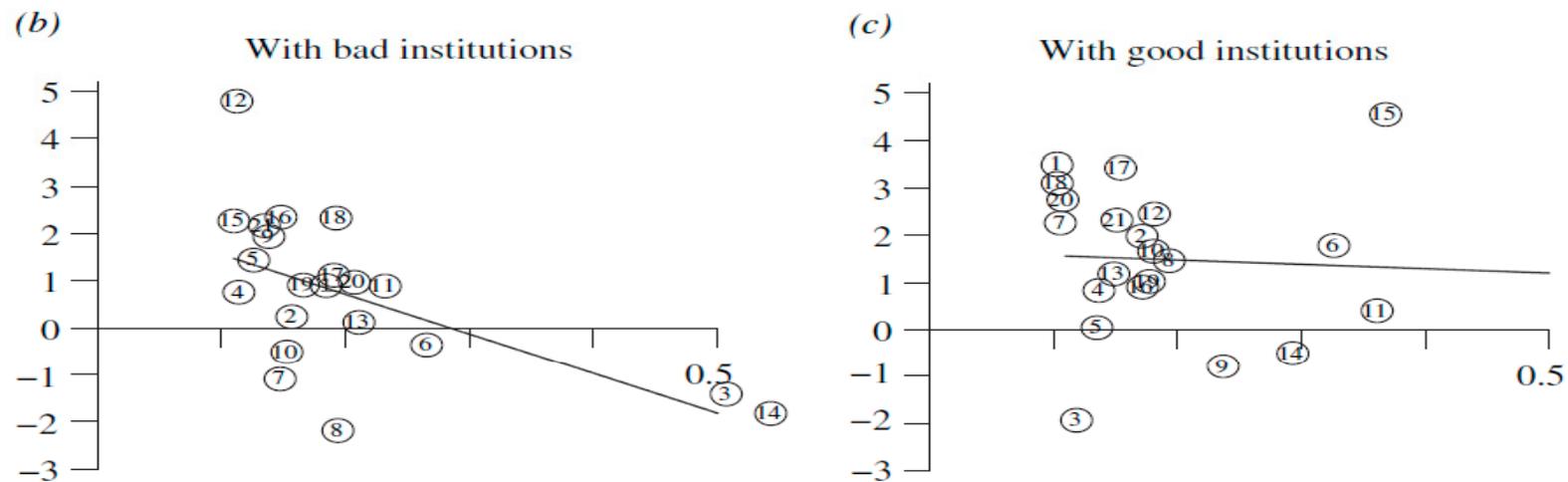


Fig. 1. *Resources and Institutions (a) all resource rich countries (b) with bad institutions (c) with good institutions*

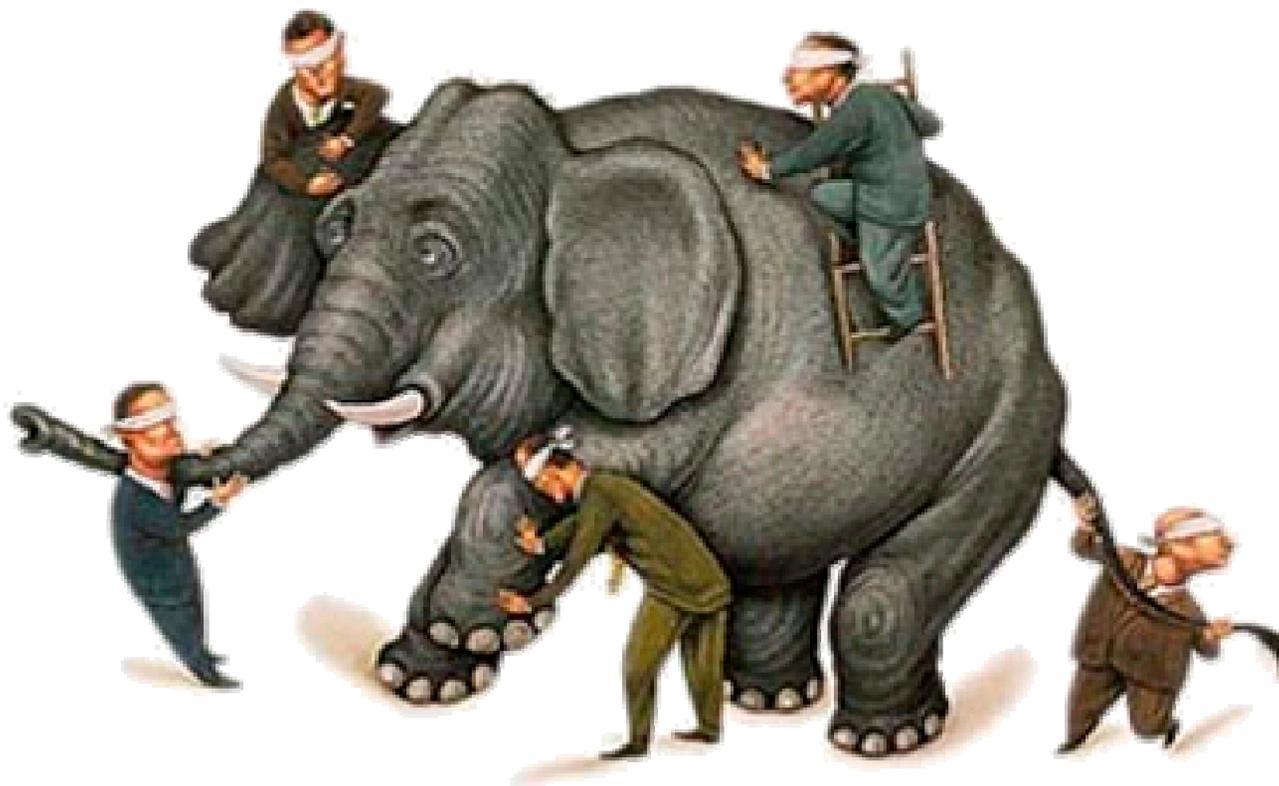
## Quality of Institutions – critical factor for success

- » Haber and Menaldo (2012) argue that states with poor quality institutions at the time of resource discovery may rely on extractive sectors for revenue and deepen dependence
- » Much of the literature concludes that states that have “good” institutions are able to translate natural resource wealth into long term inclusive development, those with “bad” institutions suffer the problems of failed development, inequality and conflict
- » Is this tautological? What kinds of institutions matter?
- » Are institutions deeply endogenous or can countries create effective institutions?



## If the quality of institutions differentiates countries that make effective use of resource wealth from those that do not ...

- What determines the quality of institutions? ... History and ... Politics
- **Politics is the elephant in the room ...often not recognized or understood**



# How does politics influence institutional quality?

- » *“Politics is the process by which a society chooses the rules that will govern it. .... Political institutions determine who has power in society and to what ends that power can be used. ... political institutions that are **sufficiently centralized** and **pluralistic** as **inclusive** political institutions. When either of these conditions fails, we refer to .... **extractive** political institutions. .... Extractive economic institutions naturally accompany extractive political institutions. ... Extractive ..institutions ..are structured to extract resources from the many by the few and .. fail to protect property rights or provide incentives for economic activity.” - Acemoglu and Robinson (Why Nations Fail)*
- » Fukuyama (The Origins of Political Order) identifies three important political institutions:
  - > a strong state / rule of law /accountable government
- » And notes: *“effective political institutions, ... are simultaneously powerful, rule bound and accountable. ... A successful modern liberal democracy combines all three sets of institutions in a stable balance. “*
- » Ross (Does Oil Hinder Democracy, 2001) – because of rentier effect/ repression effect/ modernization effect – oil rich states are less democratic/less accountable
- » Eifert, Gelb and Tallroth (2003) – suggest that different types of political regimes –differ in their institutional features including political stability, govt. time horizons, transparency, legitimacy – with consequences for development outcomes
- » Haber and Menaldo (2012) – time series analysis suggests that, over the long run, oil/mineral rents do not promote dictatorship

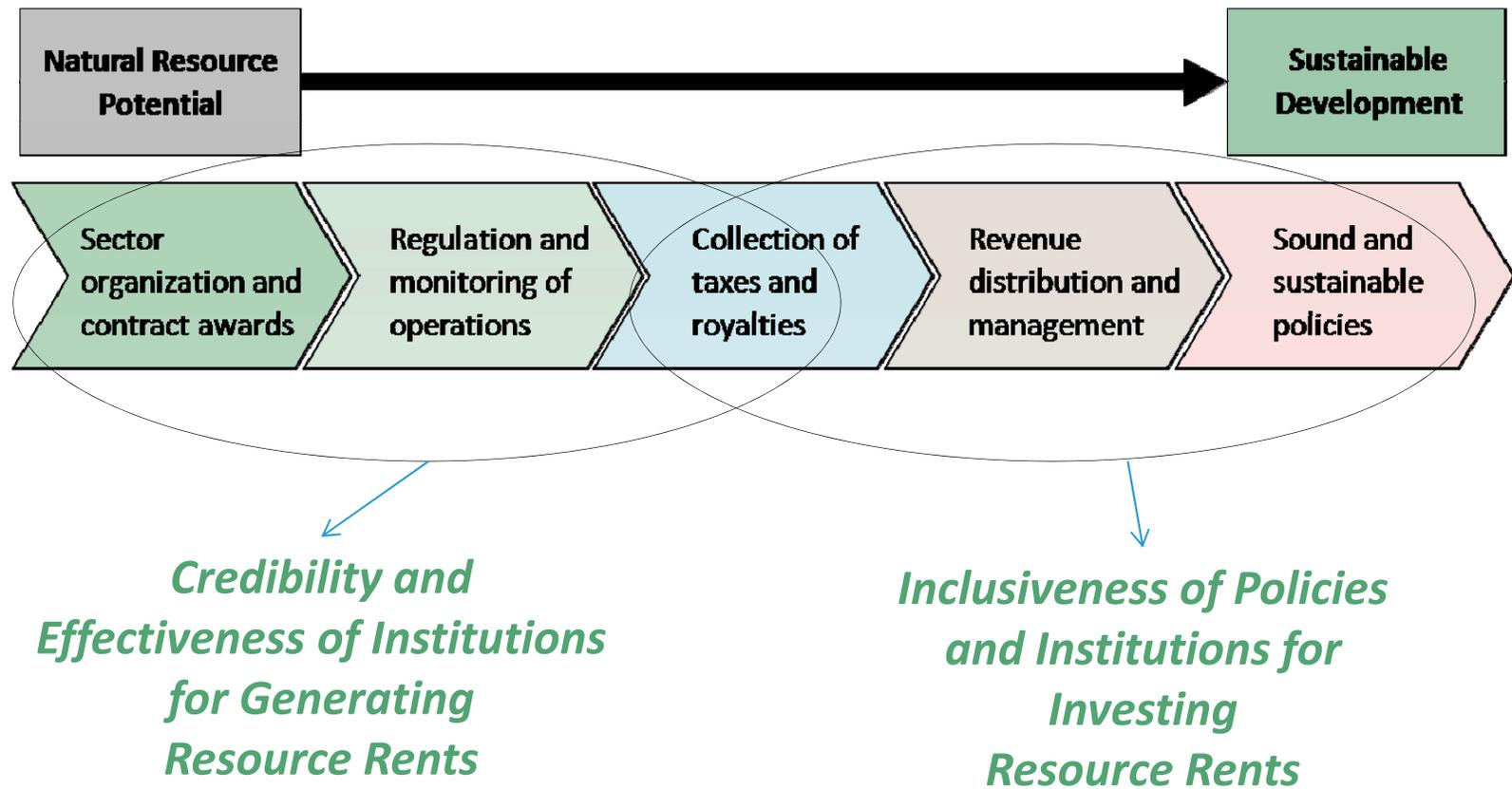
## Our approach – focus on how the politics of extractives influences institutions/relationships between key actors

» Key EI actors – the state, society and EI developers

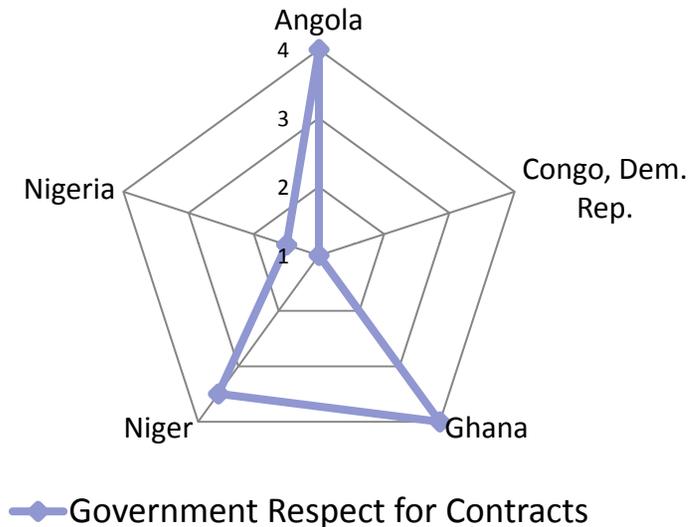


- > State may represent a narrow elite group and also be less trusted by citizens
- > A politically insecure government may be more likely to strike a non-transparent, corrupt deal with non-reputable developers
- > Civil servants may also seek to extract rents if politicians are seen to be self-interested
- > The extractive company may then face a hostile public that believes resources are being extracted at their expense
- > Vicious cycle of conflict and unstable government may follow
- > We could also identify a positive relationship where a virtuous cycle occurs – critical role of institutions in providing credibility/accountability

The EI Value Chain provides institutional specificity to link natural resources to development outcomes



# Institutions for Generating and Investing Rents

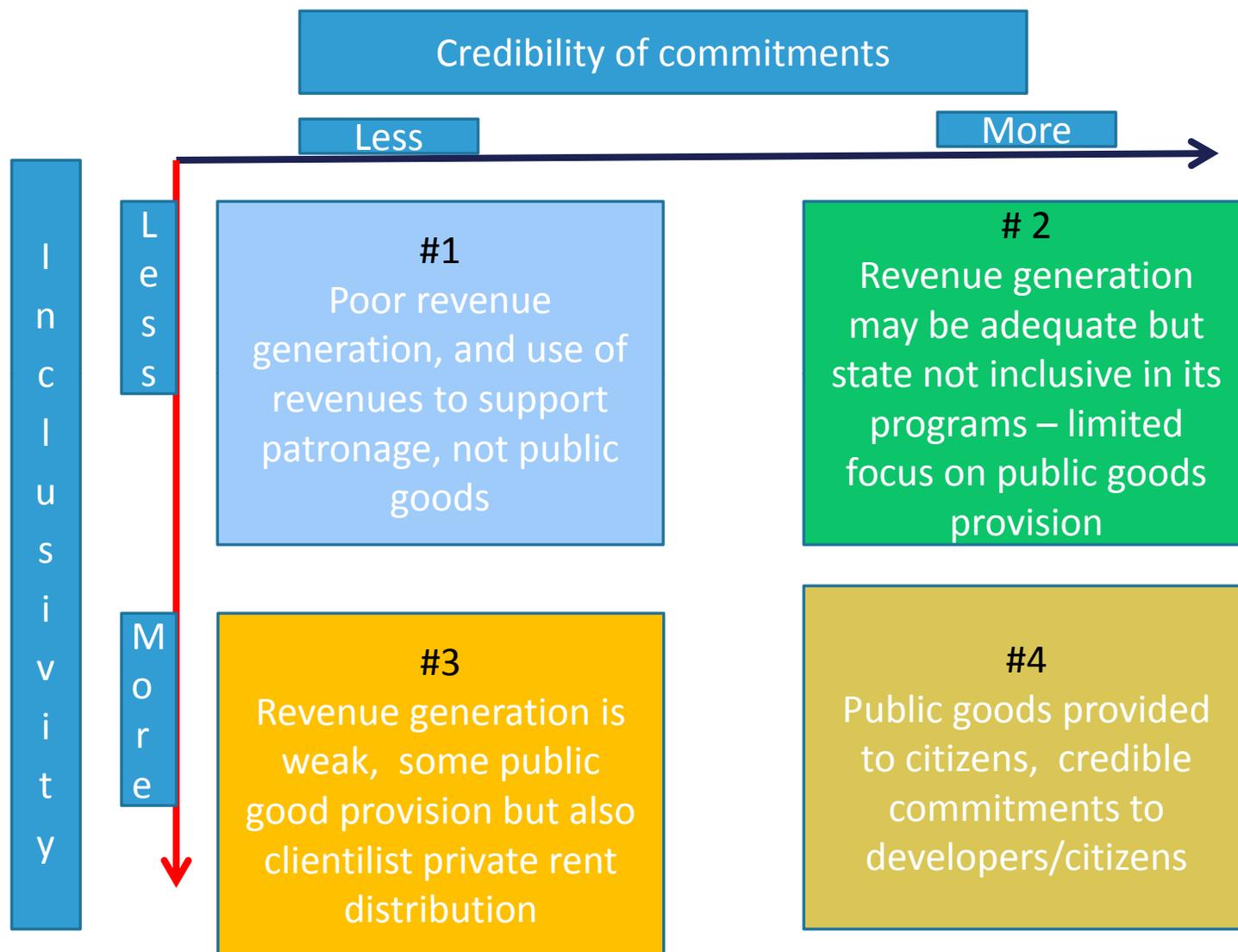


Governments vary in their capacity to maximize natural resource revenues – Angola, Ghana and Niger do better than the DRC or Nigeria on contract credibility

Source: Institutional Priorities Database (AFD)

- » **Institutions for RR Countries**
- » Transparency of resource contracts, sector regulation & revenue mgt. is critical to restrain corruption.
- » Policy making should be inclusive and reflect social aspirations.
- » Inclusive policies/institutions for investment in human capital are critical for long term sustained development.
- » A capable civil service is necessary.
- » Budgetary institutions need to be focused on public goods and services.
- » Institutions for investing the rents productively is key - Public investment management is a critical institution to strengthen in RR countries.
- » Parliamentary oversight and civil society engagement requires strengthening.
- » A strong and independent judiciary is a critical institution to check abuse of executive power and strengthen accountability.
- » **So, how do we get from here to there?**

# A typology of political economy of RRCs



In political science terms, patrimonial regimes do worse than regimes that practice programmatic pluralism



Political inclusiveness	Credibility of intertemporal commitment	
	Less credible / weaker enforcement	More credible / stronger enforcement
<b>Less inclusive</b>	<p><b>Patrimonial Rule</b></p> <p>Political instability with high contestation; emphasis on private (elite) goods; exploitation of public resources for private gain</p> <p><i>DRC</i></p> <ul style="list-style-type: none"> <li>• High discount rate</li> <li>• Risk avoidance</li> <li>• Narrow distribution of rents</li> </ul>	<p><b>Hegemonic Government</b></p> <p>Uncontested autocracy or one-party regime; either predatory or benevolent; emphasis on private (elite) goods with some particularistic and public goods</p> <p><i>Angola</i></p> <ul style="list-style-type: none"> <li>• Low discount rate</li> <li>• Risk taking</li> <li>• Narrow distribution of rents</li> </ul>
<b>More inclusive</b>	<p><b>Clientelist Pluralism</b></p> <p>Political competition based on extensive use of clientelism; provision of particularistic goods; low horizontal accountability</p> <p><i>Nigeria</i></p> <ul style="list-style-type: none"> <li>• High discount rate</li> <li>• Risk avoidance</li> <li>• Broader distribution of rents</li> </ul>	<p><b>Programmatic Pluralism</b></p> <p>Electoral competition based on programs geared toward collective welfare enhancement; provision of public goods; horizontal and vertical democratic accountability</p> <p><i>Ghana</i></p> <p><i>Botswana</i></p> <ul style="list-style-type: none"> <li>• Low discount rate</li> <li>• Risk taking</li> <li>• Broader distribution of rents</li> </ul>

# Some Concluding Thoughts

- » Citizens (current & future generations) are the true owners of the natural resources and must benefit from their extraction
- » Recognizing the political context can strengthen incentive-compatible efforts to improve development outcomes
- » Transparency, accountability and citizen participation are good institutional principles for resource use
- » **Investment in institutions is critical for resource-rich countries**
  - > Invest in Institutions of Transparent Management – Contracting, Regulatory, Sector, Revenue, Budgetary, Investment
  - > Invest also in Institutions of Restraint /Checks and Balances/Accountability - Judiciary, External Audit, Legislature, Media
  - > Invest in Citizens – in inclusive policies for education and health





# Thank you

