

# The Resource Curse: Governing Extractive Industries in the Global South

Written by Jewellord Nem Singh

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Any academic or policy literature examining how to transform resource wealth into genuine social and economic development is bound to encounter the buzz word: *resource curse*. This holds true for states with long histories of resource extraction, such as Chile, Bolivia, Peru, South Africa, and Zambia, as well as to those set to commence intensive extraction, for example in Brazil's rich offshore reserves, Tanzania's gold mining, or Sao Tome & Principe's oil. But the resource curse is also political. Natural resources exacerbate corruption, rent-seeking, and violent conflicts – stuff that convinced leading academics and global governance institutions to adopt a technocratic, depoliticised ideas of good governance. Most exemplary of this is the World Bank-led Extractive Industries Transparency Initiative (EITI). This donor agency-led initiative calls for local accountability and transparency of state agencies. And following Chile and Norway, excess profits ought to be saved and invested in financial markets as sovereign wealth funds. The controversy surrounding the resource curse thesis is whether its key claims of political and economic effects are genuine concerns or over the question of are these arguments – which are based on the experience of Middle East autocracies in the 1970s – perceived and reified, and thereafter turned into self-fulfilling prophecy. Thus, my brief article aims to give a bird's eye view of resource extraction and a political deconstruction of the meanings and effects of the resource curse thesis.

### The Resource Curse and its Challenge to Development

The idea of resource curse did not exist until the 1990s. The apparent paradox was that countries endowed with natural resources have performed worse than those with scarce or no resources at all (Auty 1993; Humphreys et al 2007; Ross 2001). In a simplistic comparison, the proponents compared East Asia's success vis-à-vis Latin America and Africa's resource-rich states. As economists focussed on the relationship between resource wealth and economic growth, what became evident was that "resources have led to worse economic performance" (Sachs & Warner 1997, 2001). As a way of affecting growth, a sudden increase in exports of minerals and hydrocarbons can shoot up exchange rates and negatively affect the competitiveness of the productive sectors – this is known as the *Dutch disease* effect. Political scientists, on the other hand, have been preoccupied with the ways resources – specifically oil – have influenced conflicts, patterns of decision making and democratic performance (Karl 1997; Ross 2001). At best, these arguments reflect *rentier* politics in the Middle East, which have been used to generalise the failures of achieving effective and inclusive governance in the midst of an oil boom.

However, what is evident is the shortcoming of development studies in understanding the opportunities and challenges brought about by the contemporary commodity boom. With the rise of neoliberal ideology, state led development – including state-managed extraction – has been discredited as a model of governing natural resources. Mining opening reforms have swept the developing world in the last three decades, in which the new geography of the bonanza has concentrated in resource-rich regions of Africa, Latin America, Middle East, and Central, South and Southeast Asia. Economic restructuring enabled foreign firms (sometimes also domestic ones) to engage directly with state agencies in crafting laws to recognise private property rights in previously nationalised markets. In the context of low prices between 1980s and 1990s, states were relegated in the margins as regulators rather than direct participants in the global economy. As foreign loans pumping ambitious megaprojects dried up, foreign investment was the only source of fresh capital to resuscitate the minerals and hydrocarbons industries. Apart from the difficulty

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of securing support from international investors, the costs of building domestic capacity for extraction has made nationalist programme of extracting resources infeasible. In fact, many developing countries privatised their state enterprises and the only remaining publicly financed extraction is in host countries with state-owned enterprises (SOEs).

Evidently, a new global context of development is shaping the politics of natural resources in the Global South. Since 2002, commodity prices took a steep rise, which has thus far changed very little despite the economic crisis hitting the core economies since 2008. The demand for oil, agriculture, and metal minerals are driven not by financial markets per se but by the insatiable need to secure access to resources by emerging powers, mainly Brazil, China and India. Equally, a fundamental shift in political economies has taken place across the developing world. This involves the simultaneous eclipse of state activism and the rise of private actors in governing resources at the global level – a trend that has not been reversed despite the opportunities for reforms offered by the commodity boom. The high prices have driven production upwards and a return to an age of resource dependency for these countries. While the salience of the resource curse hypothesis is incontestable, we still need more rigorous studies to understand the ways resources can offer opportunities for development in the Global South.

The challenge of the resource curse is two-folds. Firstly, economists are wary of possible positive means of achieving sustainable growth through sound resource management. One way of gaining more from resource rents is through a conscious state strategy of economic diversification, industrial upgrading and prudent fiscal management. To date, only countries with large internal markets have successfully diversified economic production, namely Argentina, Brazil, Indonesia, Malaysia, and Mexico. Even Chile and South Africa – despite centuries of resource extraction – continue to be dependent on metal minerals for their income. Other countries with weaker institutional capacities, notably in Africa and Latin America, are far more susceptible to the resource curse. A downturn in prices may have far reaching consequences especially if extractive resources dominate the export earnings. Therefore, social spending to reverse the poverty legacies of the past is contingent on the economic fate of commodity production.

Secondly, the political aspect of resource management seeks to find ways of institutionalising political reforms to strengthen administrative capacities of governments in adequately responding to external shocks, rent-seeking, and from predatory behaviour of state agents. What we have learned from the past, in Terry Karl's analysis of Venezuela, is that politicians fall short in making difficult political choices to reform bureaucracies in an attempt to insulate the state from organised interest groups and deploy economic policies more effectively. Equally, in contexts where governance is influenced by external actors, states must exalt political autonomy from the forces of globalisation; they also need independent powers (without being wholly authoritarian) to build economic and social programmes that would not depend on commodity production. These are clearly long-term challenges that are never easy to address.

## **Governing Extractive Industries**

I wish to focus on the political effects of the resource curse. In this debate, the key aspect of resource governance is the extent to which states can exalt autonomy in deciding the management of scarce resources. By political autonomy, I do not simply mean the capacity of elites to obstruct organised rent-seeking groups to capture extractive rents for personal interests. A larger aspect of governance involves finding the appropriate balance between state-led and market-led mechanisms in facilitating the internationalisation of extractive sectors. Put simply, how can state elites maximise foreign investment in natural resource sector without alienating foreign and domestic capital? Since the 1980s, the precursor of economic reforms in mining was low commodity prices and failing state enterprises – both of which led to a decline in commodity production and near collapse of resource-based economies. With high commodity prices, economic development in the new decade is marked by an opportunity to rebuild the state by expanding its scope in economic management as well as achieve greater democratic legitimacy by using rents from export earnings towards poverty reduction and social inequality.

Evidently, the return of the state in managing resources is far from a linear process. While in Latin America there is an argument to make about the activist role of states, the African cases paint a completely opposite picture. For example, Brazil and Chile never relinquished state control over the management of natural resources, evidently shown by the presence of state enterprises in petroleum and mining sectors respectively despite pressures for

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privatisation and liberalisation of the economy (Massi & Nem Singh 2011; Nem Singh 2010). In Argentina, Bolivia, and Ecuador, the governments emerging after a crisis of citizenship have sought to re-negotiate state-society bargains to use natural resources through export taxes as a way of addressing the poverty legacies of the past. With a proffered commitment to social equality, all of these governments argued to move beyond a privatised model of economic management. One way of dealing with the crisis of neoliberalism is to adopt a heterodox economic strategy consisting of prudent macroeconomic policies, expansive social spending, and attempts at revitalising industrialisation and limited renationalisation (Grugel & Riggirozzi forthcoming, 2009). This, evidently, varies across the region depending on national circumstances, historical context, and coalitional dynamics. Argentina and Brazil have succeeded in re-introducing industrial policy in its economic planning while Bolivia, Ecuador and Venezuela seems to have been 'locked in' to a situation of resource dependency.

In contrast, there are only incipient moves towards this direction in some African countries. In Zambia, copper has served as a source of patronage. Reforms to privatize copper were responses to economic restructuring with IFIs binding aid disbursement to economic performance. Between 1998 and 2000, due to low prices, the government changed the tax and mining regulations towards a more liberal orientation, to which the copper sector then had the lowest tax burden in the economy. Whilst the copper sector is experiencing rapid expansion in investments and production, the government has yet to dismantle the low tax regime to attract investment undertaken in the 1990s (Fraser & Larmer 2010; Haglund 2008). Taking a different case, Tanzania is a relative newcomer in the mining industry but its gold exports now rank third in Africa. The industry has attracted more than US\$2 billion out of the total US\$ 3 billion FDI coming into the country since 2000. The scale of dependency is extraordinary: gold mining currently contributes over 3% of government revenues in taxes in 2008 and roughly US\$ 750 million in export earnings (ICMM 2009). Despite endeavours to re-negotiate taxes and royalties through changes in mining laws in 2010, transnational companies are taking the lead in developing the extractive industries with the government chiefly reacting to demands of private capital and donor agencies.

## Concluding Remarks

While my discussion here has focussed on what states can do within the context of neoliberal hegemony in managing extractive industries, the international community clearly has a significant role to play in making resource wealth work for the poor. However, so far, we still need more critical studies on global governance institutions and the construction of normative standards of good governance in managing resources. For one, the debate has been narrowly confined around revenue management where even autocratic governments like Azerbaijan passes the evaluation of the EITI Board yet it continually ranks poorly in the transparency index. More crucially, sound revenue management does not in any way address issues of dependency and a return to primary commodities production. The driving force behind such uncritical debate of growth models is that the whole good governance agenda masks the ideological underpinning of the reforms. Notwithstanding a few cases, like Brazil and Malaysia, economic restructuring in extractive industries are plainly reflexive of the neoliberal ideology. The forces of globalisation are deemed as inexorably pushing states to open their markets to serve the needs of the global economy.

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