Natural Resources: Curse or Blessing?

Are Natural Resources a Curse or Blessing for Developing Countries in Africa?

Patrick Weimert

Patrick Weimert currently studies International Affairs at the Hertie School with a specialization in international security. He is particularly interested in security issues in the nexus between international security and development policy. He has also worked as an intern at the NATO CIMIC Centre of Excellence, as a Professional Year Student at the Stabilisation Platform of the German Federal Foreign Office / GIZ and as an intern at the German Federal Foreign Office. He is particularly interested in the topic of civil-military cooperation.

A recurring theme when it comes to natural resources is their perception as curse or blessing for the countries that posses them. While some scholars argue that the discovery of natural resources is one of the key drivers of corruption and the weakening of democratic institutions, others even claim them as prerequisite for economic development.

Representatives of the *dependency theories* argue for the nationalisation of natural resources as a mandatory policy to achieve development. *Modernisation theories* are less deterministic and differentiate between wealth and development generated by resource extraction. However, with some representatives of the latter even mentioning the extraction of natural resources as a prerequisite for his economic development (Rostow, 1960). Today, the idea of mineral resources as precondition for development is highly challenged by the economic take-off of resource poor Asian countries and the lack of economic development in resource-rich African countries. With many of the poorest African countries paradoxically also being some of the resource-richest, the narrative of the resource curse was born in the field of international development theory.

The following essay will look at the most recognized theories, fundamental economic assumptions, and some cases of the 'curse' on the African continent. Comparing theory with real-life cases, this paper aims at answering whether resource-rich countries in Africa are destined to lack development or if there is a lift to the curse.

The Resource Curse

Among international development scholars, Sachs and Warner (1995) were the first ones to find empirical evidence for a negative statistical relationship between natural wealth and economic growth between 1971 and 1989, meaning that resource-rich countries were, oddly enough, less likely to experience successful development. Contradictory to previous predictions, resource-poor countries around East-Asia experienced economic growth that quickly surpassed the ones of resource-rich Africa or Latin America.

Building up on this revolutionary discovery, other scholars have discovered that only a fraction of the world's resource-rich countries have managed to keep their GDP per capita growth rates higher than the 2.2% average of low-income countries (Gylfason, 2001). With the empirical evidence growing, the narrative of a resource curse spread among international development scholars. Reversing the initial theories, resource abundance was even considered the cause of poor economic development.

Nowadays, the relationship between natural resources and economic development is considered far more complex. While it is true that resource-rich countries, especially in Africa, have experienced lower development rates than their resource-poor neighbours, correlation does not automatically constitute causation. Furthermore, the African continent also witnessed examples of countries that transformed its resource wealth into successful development, or were initially trapped in the resource curse, but managed to escape it (Amundsen, 2017).

In 1994, among the top 15 countries with the highest pre capita income, 5 were considered resource-rich (World Bank). In the case of Africa, prominent examples have also managed to transform their resource wealth into wealth and development of its people. Botswana's transformation from one of the

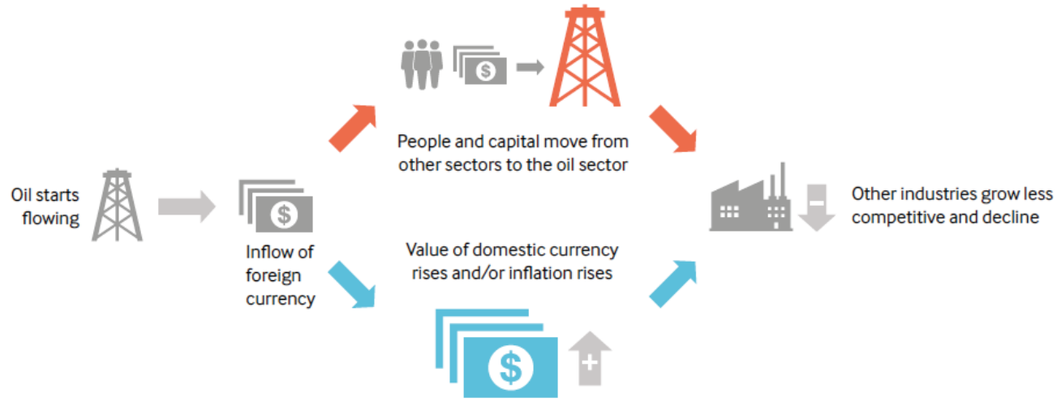
poorest countries in the world into an upper-middle income country is directly related to country's discovery of diamonds (Hillbom, 2008).

In order to understand whether natural resources constitute a curse or blessing for developing countries, the following part will investigate the theories that constitute the foundation of the resource curse narrative.

The Dutch Disease

Among the theories surrounding the resource curse, the most known one is perhaps the Dutch Disease. Having its origins in the Dutch experience in the 1960s - 70s when natural gas discoveries led to economic challenges, like the decline of the manufacturing sector (The Economist, 1977). It was later picked up by Sachs and Warner as explanatory factor for their discovered negative relationship between natural resources and economic growth (1995). Other scholars have conceptualized the idea and developed its implications further.

Essentially, a sudden discovery of natural resources will have a negative effect on other sectors of the economy, especially the ones reliant on exports. Explaining the Dutch Disease requires separating a country's economy in three sectors: Services and other non-tangible goods, agricultural and manufactured tangible goods, and resource-based tangible goods. Representatives of the Dutch Disease claim that a boom in the resource-based good production will ultimately lead to decline in the other sectors (Corden and Nearly, 1982).



This is based on the assumption that increase revenues in the natural resource sector will lead to exchange rate appreciation and inflation, due to the increase of inflow of foreign currency. While these changes in currency and commodity prices also have an immediate effect on the economy, its long-term impact includes deep changes of a country's economy, including a shift of labour and capital from the other sectors into the resource sector (NRGI, 2015). The increase of revenue is parallel to an increased demand for services connected to the resource sector, be it the demand for mechanics, chemical engineers or logistical experts, the high revenues from the resource sector outcompete service prices in the manufacturing sector.

Ultimately, contributing to an increase in the real exchange rate as most services are captured in the resource sector, the scarcity of services in other sectors causes prices to rise.

While the prices in the world market remain the same, rising manufacturing prices in one country will lead to higher relative prices compared to international competitors. Hence, manufacturing exports become more expensive, imports cheaper, and the manufacturing sector becomes internationally uncompetitive. Therefore, some scholars go as far as describing the Dutch Disease even having a de-industrializing effect on countries (Corden and Nearly, 1982).

The Dutch Disease:
refers to an economic phenomenon where a sudden influx of revenue from natural resource exports, such as oil or gas, leads to the appreciation of the national currency. This currency appreciation makes other sectors, particularly manufacturing and agriculture, less competitive in the global market, causing their decline. The term originated from the Netherlands' experience in the1960s

With Africa being one of the most resource-rich continents, the consequences of natural resource discovery have been the cause of a declining manufacturing sector in many countries, like Nigeria, Angola, or Ghana (Mien and Goujon, 2022). In the literature surrounding the Dutch Disease in Africa, Nigeria is a recurring theme because it experienced many of the theory's problems after the discovery of significant oil resources.

The Dutch Disease phenomenon in Nigeria is a complex economic challenge stemming from the country's heavy dependence on oil exports. This reliance has had profound consequences for various aspects of the Nigerian economy, contributing to a set of interconnected issues commonly associated with Dutch Disease. The discovery and exploitation of oil resources have led to a substantial boom in the oil sector, making it a dominant player in the country's GDP composition. Therefore, Nigeria's economy has been heavily reliant on the revenue generated from oil exports. There have been many consequences of this heavy reliance on oil, with one of the primary manifestations of the Dutch Disease in Nigeria being the appreciation of the national currency. As predicted by the theory, the influx of revenue from oil exports drove up the value of the currency, a phenomenon that, like in the theory, had a negative effect on other sectors of the economy (Otaha, 2012).

The appreciation of the Nigerian naira made non-oil sectors, such as manufacturing and agriculture, less competitive in the global market. As the cost of Nigerian goods increases on the world market, these sectors experienced a decline in competitiveness. Ultimately, leading to some degree of de-industrialization in the country. The rapid growth of the oil sector has led to the flow of resources, services, and capital away from other industries. Thus, manufacturing, and agricultural activities have suffered as a result, contributing to a broader economic imbalance. Nigeria's vulnerability to fluctuations in global oil prices is another characteristic of the Dutch Disease. While high oil prices bring increased revenue into the country, low oil prices can result in economic challenges, like unstable government income (Otaha, 2012).

The country's economic power became closely tied to global oil prices, lacking the resilience of a more diversified economy. Inadequate investment in areas such as trans-

portation, education, and healthcare has further exacerbated the impact of Dutch Disease. Neglect in developing infrastructure in sectors other than the oil industry has created problems for the overall economic development of the country. Following the idea of the resource curse, its over-dependence on the oil industry has slowed the development of other sectors that could contribute to sustainable economic growth (Otaha, 2012).

However, the literature surrounding the Dutch Disease is far from a homogenous, with many authors pointing at the short comings of the theory and empirical cases that contradict it. When arguing for labour movements between a rising and a declining sector, one has to assume full employment. This is not the case in most developing nations. Additionally, resource extraction industries only require a small number of employees, making the possible movement of labour minimal (Corden, 1984).

Cases like Botswana show that the Dutch Disease is not an inevitable phenomenon in Africa. The country in Southern Africa is known for effectively managing its diamond resources, and its experience contrasting with the negative consequences often associated with Dutch Disease. Botswana's prudent management of its diamond wealth involved policies aimed at minimizing the adverse effects that typically accompany a heavy reliance on natural resource exports. Unlike Nigeria that faced issues such as currency appreciation, de-industrialization, and economic volatility, Botswana has implemented strategies to mitigate these challenges (Barczikay, Biedermann and Szalai, 2020).

One key factor contributing to Botswana's relative success is its establishment of the Pula Fund (Government Investment Account), which acts as a sovereign wealth fund. The fund helps to manage the inflow of revenue from diamond exports, avoiding rapid currency appreciation and allowing for more sustainable economic development. While Botswana has not entirely avoided the challenges associated with resource dependence, it has demonstrated a proactive approach to managing its natural resource wealth, foster economic stability, and secure development. However, conditions can change, and scholars disagree over the country's ability to adapt once they have reached the predicted exhaustion of its mineral resources in 2052 (Barczikay, Biedermann and Szalai, 2020).

Like all economic theories, the Dutch Disease is attempting to simplify a much more complex world, which leads to shortcomings and empirical cases that contradict the theory. However, this does not mean that it is not valid to analyse the world and has even been highly successful in understanding Nigeria's economic problems. There are no social laws, similar to the physical law of gravity, that guarantee certainty over a specific social outcome. Therefore, theories can only deliver a framework on how to understand the world. Its shortcomings should not be considered a reason for rejection, but an incentive for further research.

The Resource Curse and its Effect on Democracy

When it comes to explanations why some countries are affected by the resource curse and some are not, there are three schools of thought: The cognitive explanation, the societal explanation, and the statist explanation.

First, representatives of the cognitive school of thought argue that policy makers in resource rich countries experience a sort of myopia or strategic shortsightedness (Ross, 1999). With a steady inflow of governance revenue secured through resource-related taxes, policy makers have a lower incentive to develop strong economic policies (Wallich, 1960). Some scholars go as far and argue that poor economic management even leads to policy makers significantly overestimating the longevity of natural resource wealth, leading to an increase of their government spending to an unsustainable amount (Manzano and Rigobon, 2001). Essentially, it perceives policy makers as lottery millionaires that instead of investing their money in a sustainable asset, assume the winnings will last forever. Countries that have experienced the resource curse are victim to bad policy making rather than the occurrence of resources. However, the theory is criticized for portraying policy makers as irrational actors, which contradicts most economic assumptions. Furthermore, it does not explain why private sector actors are not behaving in a similar, irrational way, upon the discovery of natural resources (Townsend, 1995).

Second, the societal school of thought rejects the individual failures of policy makers and takes a deterministic approach towards the influence of private corporations. With the majority of tax revenue collection coming from one sector, the relevant sector can have significant influence on policy making, pressuring policy makers into economically bad decisions. While most societal theory scholars draw from examples from Latin America, Nigeria's experience with Import Substitution Industrialization (ISI) policies and its failure to transition away from ISI, has exacerbated the country's dependency on oil (Auty, 1994). ISI is an economic strategy where a country aims to develop its national industries and reduce import dependence. However, once the country discovered significant oil resources, the domestic supply already outcompeted international oil companies. Subsidizing an already overly competitive supplier led to an exacerbation of the national industry's dependence on domestic oil. This rose the oil companies influence to such a degree that they could influence decision makers to not lift ISI policies, even though they were slowing down economic development in other sectors (Egwaikhide, 1997). Nevertheless, criticism regarding societal explanations of the resource curse point out that they tend to generalize countries' individual experiences as universal theory. While Nigeria experienced a dependency on domestic suppliers, ISI policy in Sub-Sahara Africa paradoxically led to a dependency on foreign suppliers (Lawrence, 2005). Furthermore, the increased political influence of private corporations only applies in the specific cases, where they managed to successfully claim resource rents, like in Nigeria. It also fails to explain the resource curse in countries with a nationalized natural resource sector, a common theme among developing nations.

Figure 2: The Resource Curse on Democracy (Source: NRGI, 2015)

Finally, the statist school of thought is the most recognized explanation of the resource curse today since it combines explanations from the cognitive and societal schools of thought. Most recognized, the idea of the *rentier-state*, arguing that with a high percentage of the government budget deriving from resource rents in resource-rich countries, the government is less reliant on the collection of taxes from its citizens. In some cases, the discovery of natural resources has had a significant effect on the erosion democratic institutions, the manifestation of authoritarian structures, or democratic backsliding. Generally, there seems to be a positive, statistical relationship between government's responsiveness its citizens and government reliance on citizen taxation, making democratic transition more likely in countries dependent on citizen taxation (NRGI, 2015).

> What some refer to as a curse is a phenomenon that is known and feared farbeyond the realm of natural resources: Bad policymaking.

Also, decision makers are also less involved in the needs and requests of its citizens if the government functions independent of them. Additionally, higher government control over natural resources tends to create a system of secrecy, which prevents accountability of financial mismanagement.

One African country that experienced almost a textbook example of the rentier-state is Equatorial Guinea, a small nation located in Central Africa. In the country's pivotal moment in the 1990s, a discovery of substantial oil reserves promised transformative economic changes, but paradoxically ended up damaging the country more than it benefited. Today, the country struggles with an economy heavily dependent on oil, making up a significant part of its GDP. While oil exports have fuelled an overall increase of GDP, the downside of overreliance on these natural resources has been the erosion of democratic institutions and an increase of authoritarianism (Sá and Rodrigues Sanches, 2021). Politically, Equatorial Guinea shares similarities with the theory, characterized by prolonged rule under President Teodoro Obiang Nguema Mbasogo. With the majority of the oil resources laying in the hands of the president or his family, authoritarian governance and restricted political opposition have resulted in a lack of transparency and accountability, mirroring developments described by the rentier-state theory. Since the 1990s, the government was less reliant on taxation of its citizens and could function based on resource taxation, making it also less necessary to listen to political opposition. Thus, despite its oil wealth, the benefits have not been equitably distributed, leaving a significant portion of the population without tangible improvements in living standards or access to basic services (Sá and Rodrigues Sanches, 2021). Even though the overall GDP increased, so did inequality and economic dependency. Setting the country up for economic collapse once it runs out of natural resource revenue.

Everything was paired with an increase in corruption, particularly in the management of oil revenues, contributing to economic disparities. In essence, Equatorial Guinea's experience very much reflects the complex dynamics of resource abundance and governance challenges witnessed in resource-rich African countries. While oil wealth has offered economic opportunities for some, the accompanying corruption, economic inequality, and rising authoritarianism underscore the necessity for mitigating policies and comprehensive strategies for sustainable development.

Similar to the Dutch Disease, these developments are in no means inevitable. Democratic backsliding can be prevented by effective governance, including increase citizen participation, transparency of government spending, and equitable distribution of wealth.

The Distinguishing Factor – Good Governance

It is important to consider that a recurring feature of the resource course, be it the Dutch Disease or the rentier-state, is that it is avoidable. All countries might experience some degrees of negative consequences to resource wealth, but some seem to address them better than others. The differentiating factor between countries strongly affected by the 'curse' with countries that turned natural resource revenue into wealth and development is governance, particularly good governance (World Bank, 1992).

Good governance stands as a crucial factor in safeguarding nations against the problems posed by the resource curse. The effective management of these resources requires a comprehensive framework grounded in principles of transparency, inclusivity, economic diversification, adherence to the rule of law, and responsible social and environmental practices.

Central to good resource management is the imperative of transparency and accountability. Governments must establish transparent mechanisms governing the exploration, extraction, and sale of natural resources, demonstrating a commitment to publicly disclosing contracts, revenues, and financial transactions associated with resource extraction. This transparency not only fosters public trust but also serves as a deterrent against corruption. Consequently, robust accountability mechanisms are essential to handle the actions of public officials and institutions engaged in resource management, with independent audits and oversight bodies playing a pivotal role in ensuring the responsible use of revenues (UNODC, 2018).

Inclusivity is a foundational element of effective governance in the context of resource management. Involving stakeholders such as civil society, local communities, and non-governmental organizations in the decision-making process is essential. This inclusive approach addresses the diverse needs and concerns of various segments of society, fostering a sense of shared ownership and collective responsibility. Additionally, it avoids the loss of connection between the government and its citizens, when citizen taxation is no longer the main source of income in of a state (UNODC, 2018).

Economic diversification emerges as fundamental to mitigate the resource curse. Policymakers should prioritize diversifying the economy beyond immediate gains from

natural resources. Investments in education, infrastructure, and non-resource sectors contribute to the development of a sustainable and resilient economy. Additionally, countries should find domestic use of the suddenly cheap domestic resources, instead of selling all to foreign investors. Simultaneously, the establishment and responsible management of independent resource-wealth funds serve as a safeguard, enabling nations to save and invest resource revenues for long-term stability, providing a buffer against economic volatility and the eventual exhaustion of resources (Gelb, 2010).

A robust legal framework, underpinned by the rule of law, is essential for sustainable resource management. Governments should enact and enforce clear laws regulating the extraction, taxation, and overall management of natural resources. An independent judiciary is equally crucial, ensuring fair adjudication of disputes, upholding contractual obligations, and fortifying the broader legal infrastructure. Furthermore, social and environmental regulation safeguards counterbalance against potential negative impacts of resource extraction. Considering the effect of mineral extraction on the environment, implementation and enforcement of stringent environmental regulations are essential to mitigate ecological harm. Simultaneously, redistribution of resource revenues to community development programs develops local infrastructure, education, healthcare, and other essential services (UNODC, 2018).

Lastly, control of corruption is an integral component of the good governance framework. Governments should adopt and enforce policies to combat corruption in the management of resource revenues. This involves strengthening institutions responsible for preventing and prosecuting corruption, alongside fostering a culture of accountability. Whistleblower protections further incentivize the reporting of malpractice, acting as a crucial deterrent against corrupt practices (UNODC, 2018).

Good governance serves as a guiding principle in navigating the complexities of natural resource management. Furthermore, it is important to mention that good governance is not an uncommon phenomenon among resource-rich, African countries. Even though many countries struggled to capitalize their natural resources sustainably, there is multiple examples of successful resource management. Next to the already mentioned Botswana, Namibia stands out as a notable example of avoiding the resource curse through effective governance practices. Blessed with substantial diamond and uranium resources, the country has implemented effective policies to capture these assets, while maintaining sustainable development. Key to this success has been a commitment to inclusivity, through a community-based resource governance. The government actively involves local communities in decision-making processes related to resource extraction, mitigating social tensions, and ensuring that the benefits of these resources reach a broader segment of the population (Schnegg and Kiaka, 2018). By prioritizing transparency, inclusivity, economic diversification, adherence to the rule of law, and responsible social and environmental practices, countries can unlock the transformative potential of their natural resources, fostering sustainable development and prosperity while mitigating the risks associated with the resource curse. Negative consequences of natural resource discoveries, like the rentier-state, are a real threat to resource-rich countries, but there is empirical evidence suggesting that there is no unavoidable law that puts countries into their demise. What some refer to as a curse is a phenomenon that is known and feared far beyond the realm of natural resources: Bad policymaking.

Conclusion

In conclusion, the answer on whether natural resources are a curse or blessing for developing countries in Africa is complex. The resource curse narrative, as outlined by the Dutch Disease and the rentier-state, highlights the potential risks associated with the discovery of natural resources. Empirical evidence, particularly from resource-rich African countries like Nigeria and Equatorial Guinea, underscores the challenges of over-dependence on resource exports, which led to economic imbalances, de-industrialization, or democratic erosion. However, amidst these challenges, good governance emerges as the distinguishing factor. The experiences of countries like Botswana and Namibia demonstrate that effective resource management, grounded in principles of transparency, inclusivity, economic diversification, adherence to the rule of law, and responsible social practices, can mitigate the negative impacts of the resource curse. These countries have successfully avoided the Dutch Disease and maintained democratic resilience through effective policymaking. The resource curse is not an inevitable fate but rather a consequence of bad policy choices. However, this makes policy making ever more complex, since one policy could be successful in avoiding the resource curse in one country, while leading to its economic demise in another one. With the ongoing energy transition, natural minerals that had limited relevance until now are suddenly becoming the object of desire for many powerful bidders. Protecting one's own industry with regulation might help the economy to take-off in one country but could lead to even more dependency in others. For the better or the worse, there is no general law.

References

Amundsen, I. (2017). Nigeria: defying the resource curse. Corruption, natural resources and development: From resource curse to political ecology, 17-27.

Auty, R. (1994). Industrial policy reform in six large newly industrialising countries: The resource curse thesis. World Development, Vol.22, No.1, pp.11-26.

Barczikay, T., Biedermann, Z., & Szalai, L. (2020). An investigation of a partial Dutch disease in Botswana. Resources Policy, 67.

Corden, W. and Neary, J. (1982). Booming Sector and De-Industrialisation in a Small Open Economy. The Economic Journal, Vol.92, No.368, pp.825-848.

Corden, W. (1984). Booming Sector and Dutch Disease Economics: Survey and Consolidation. Oxford Economic Papers (pre-1986), Vol.36, No.3, pp.359-380.

Egwaikhide, F. O. (1997). Import substitution industrialization in Nigeria: A selective review. The Nigerian Journal of Economic and Social Studies, 39(2), 183-203.

Gelb, A. H. (2010). Economic diversification in resource-rich countries. In Beyond the Curse. International Monetary Fund.

Gylfason, T. (2001). Natural Resources, Education and Economic Development. European Economic Review, Vol.45, pp.847-859.

Hillbom, E. (2008). Diamonds or development? A structural assessment of Botswana's forty years of success. The Journal of Modern African Studies, 46(2), 191-214.

Lawrence, P. (2005). Explaining Sub-Saharan Africa's Manufacturing Performance. Development and Change, 36(6), 1121-1141.

Manzano Mazzali, O., & Rigobon, R. (2001). Resource Curse or Debt Overhang? (No. 8390). National Bureau of Economic Research, Inc.

Mien, E., & Goujon, M. (2022). 40 years of Dutch Disease literature: lessons for developing countries. Comparative Economic Studies, 64(3), 351-383.

NRGI: Natural Resource Governance Institute. (2015). The Resource Curse: The Political and Economic Challenges of Natural Resource Wealth

Otaha, J. I. (2012). Dutch disease and Nigeria oil economy. African Research Review, 6(1), 82-90.

Ross, M. (1999). The Political Economy of the Resource Curse. World Politics, Vol.51, No.2, 297-322.

Rostow, W. (1960) The Stages of Economic Growth: A Non-Communist Manifesto. Cambridge: Cambridge University Press. Chapter 2, "The Five Stages of Growth–A Summary," pp. 4-16.

Sá, A. L., & Rodrigues Sanches, E. (2021). The politics of autocratic survival in Equatorial Guinea: Co-optation, restrictive institutional rules, repression, and international projection. African Affairs, 120(478), 78-102.

Sachs, J. and Warner, A. (1995). Natural Resource Abundance and Economic Growth. National Bureau of Economic Research: NBER Working Paper Series, No.5398.

Schnegg, M., & Kiaka, R. D. (2018). Subsidized elephants: Community-based resource governance and environmental (in) justice in Namibia. Geoforum, 93, 105-115.

The Economist. (1977). The Dutch Disease. The Economist.

The World Bank. (1992). Governance and Development.

The World Bank. (1994). Expanding the measure of wealth: Indicators of Environmentally sustainable development. Environmentally sustainable development studies and monographs series No.7.

Townsend, R. (1995). Consumption Insurance: An Evaluation of Risk-Bearing Systems in Low-Income Economies. The Journal of Economic Perspectives, Vol.9, No.3, pp. 83-102.

UNODC: United Nations Office on Drugs and Crime. (2018). What is Good Governance? Module Series on Anti-Corruption: Module 2 Corruption and Good Governance.

Wallich, H. (1960). Monetary Problems of an Export Economy: The Cuban Experience, 1914–1947. Harvard: Harvard University Press.

Greetings from our contributors