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Introduction

In 2007, significant offshore oil discoveries were made off the coast of Ghana, a West African nation of 25 million that had just graduated out of low-income status. Ghana's then-president, John Kufuor, was ebullient, remarking, "Even without oil, we are doing so well, already. Now, with oil as a shot in the arm, we're going to fly."[1] But the dinner table conversation between one of the authors and his Ghanaian wife was less "we're in the money!" than "oh, no."

This doubting response to a development that will surely bring income and wealth to Ghana exemplifies the increasing ambivalence with which citizens regard major commodity discoveries. In the case of Ghana, the question is whether its economic and political institutions are capable of successfully managing the sudden influx of income and wealth that the production of oil is likely to bring—or whether the oil wealth will complicate macroeconomic management to the detriment of traditional industries and encourage a reversal of the country's steady yet still fragile evolution into a mature democracy. It is an open question.

How did we arrive at such pessimism, and is it warranted? How is it that valuable natural resources are not considered an unqualified blessing for the countries that find them? Intuitively, one would assume that more valuable resources would lead to better development outcomes—that finding oil, gold, or other precious minerals would amount to receiving manna from heaven. In fact, for many countries, resource wealth has come to be viewed as a curse. Even one of the principal architects of the Organization of Petroleum Exporting Countries (OPEC), former Venezuelan Minister of Mines and Hydrocarbons

1. "UK's Tullow Uncovers Oil in Ghana," BBC News, June 18, 2007.

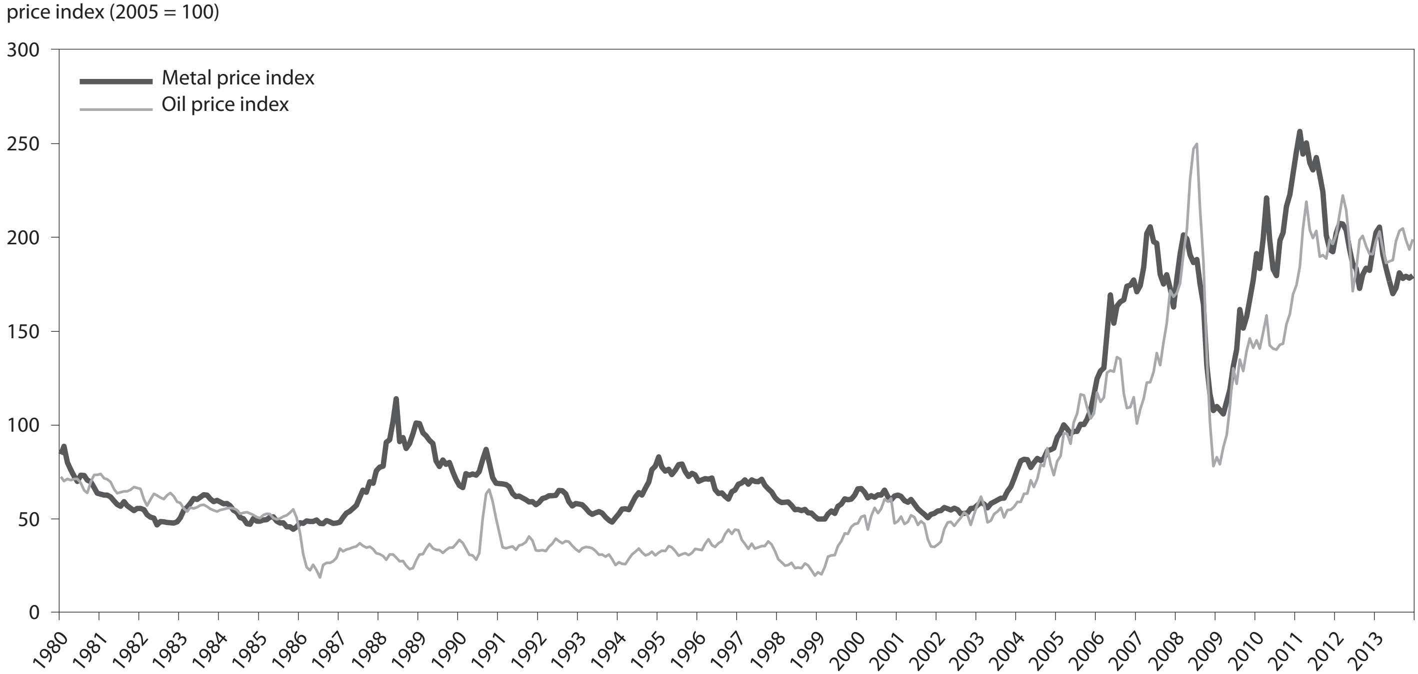
Juan Pablo Pérez Alfonso, referred to his country's oil wealth as "the devil's excrement"—and that was when Venezuela was the most prosperous, democratic country in South America.

This book is about one of the more curious findings/nonfindings in the history of economics: that valuable natural resources, such as oil, natural gas, and other mined commodities are not, in the main, associated with better development outcomes and may even retard long-run rates of economic growth and discourage political development. Economists have long argued over the impact of resource endowments on economic performance. Common sense would seem to suggest that if one finds oneself sitting on a gold mine, then one should mine gold (or drill oil, as in the example above). But countries that have specialized in the production of extractive or "point-source" resources, such as mined commodities like gold, diamonds, and oil, tend to be poor, creating a nagging sense that specialization in extraction is a losing proposition in the global division of labor, condemning countries to be "hewers of wood and drawers of water." This finding is true despite the fact that their primary exports are some of the most valuable commodities on earth and that their value has been growing particularly rapidly of late.

The 21st century commodity boom, during which real prices for most globally traded commodities more than doubled (figure 1.1), catalyzed a gold rush–like frenzy of exploration effort, resulting in radical upward revisions of proven oil and/or natural gas reserves and mineral deposits in many "legacy" (long-time) exporters (Iraq, Saudi Arabia, and Venezuela) as well as discoveries by much smaller and/or nonlegacy exporters. Countries across West Africa (Côte d'Ivoire, Ghana, and Liberia), East and Southern Africa (Kenya, Mozambique, and Uganda), and Southeast Asia (Cambodia, Myanmar, and Vietnam) have seen their proven energy and mineral reserves increase significantly. In recent years, Mongolia has emerged as one of the world's fastest-growing economies, driven by surging output from huge copper, gold, and coal mining projects. Even Afghanistan, a minor trader whose most lucrative export is fruits and nuts, is now estimated to have more than a trillion dollars' worth of mineral deposits. Where these deposits are found, massive inflows of investment capital typically follow. More often than not, however, this investment capital and the vast natural resources it exploits do not catalyze broad-based, inclusive growth.

Over the years, concerns about the role of resources and development have been sharpened in a number of ways. They concern the possibility that despite recent trends, natural resource products have experienced long-term declines in price; that the prices of these commodities are unusually volatile, complicating planning and giving rise to boom-bust cycles; and that by drawing in money and attention, temporary booms may undermine, perhaps irreparably, other segments of the economy. What these propositions, all of which are debatable, suggest is that countries in which resource extraction plays a central role in economic life are effectively running uphill, at a long-term relative disadvan-

Figure 1.1 Oil and metal prices, 1980–2013



Note: Values deflated prior to indexation.

Source: IMF (2013).

tage in terms of economic performance in relation to more diverse, balanced economies.

It is not just that the focus on resource extraction may put these countries on a disadvantageous long-term economic trajectory. As a group, their political histories are disproportionately characterized by instability and conflict. One possible explanation for this phenomenon is that the presence of "contestable" resources heightens competition for control of the state or enables the continuation of less than best practices with respect to governance. Another is that weak political institutions have retarded the development of more complex forms of transactions and forced an implicit reliance on extraction in economic life.

In either case, the potentially deleterious impact of natural resources on development is captured in the phrase "the resource curse." The implications are greatest for the commodity producers themselves, ranging from complications for macroeconomic management to the potential encouragement of political authoritarianism and, in the extreme, the precipitation of violent civil conflict. It was in Libya—where minerals and fuels account for 97 percent of exports and more than half of GDP (Center for International Development 2010)—that the mostly peaceful Arab Spring uprising first turned violent, leading ultimately to intervention by the North Atlantic Treaty Organization. For outsiders, the resource curse presents long-term challenges with respect to coping with violence in exporting states and its facilitation of unwanted transborder phenomena, including terrorism, drug trafficking, and illegal migration and human trafficking.

Major powers may become entangled in these weaker states in an effort to block these undesirable spillovers. Such entanglement was underscored by the trial in the Hague of former Liberian president Charles Taylor for crimes against humanity committed during the diamond-fueled civil wars of Liberia and neighboring Sierra Leone—which, apart from the immediate destruction, were exploited by al Qaeda and other terrorist groups to evade anti–money laundering and terrorist finance efforts and eventually required the intervention of British troops and US-supported multinational forces.

But great power involvement may not always be so defensive or altruistic in nature. From Allende in copper-exporting Chile to Lumumba in copper- and uranium-rich Zaire (now the Democratic Republic of the Congo), the historical record is littered with US and Western involvement in or support of coups against elected leaders whose political platforms threatened Western business interests. The combination of valuable resources and weak institutions, which may encourage violent domestic conflict, may attract the attention of outside powers with less lofty motives. In contemporary times, among the shifting justifications for the US invasion of Iraq (and Iraq's earlier invasion of Kuwait) was the control of oil.

With its rise as an economic, political, and military force, China too is poised to exert critical influence on the fortunes of resource-based economies around the globe—and to create anxiety for the incumbent powers as well. If

China were to become involved in the domestic politics of countries in which it holds large equity stakes in natural resources, it would not be the first major power to have done so.

China's rise occurs against the backdrop of attempts by the West—broadly encompassing Western nongovernmental organizations (NGOs), Western governments, and the multilateral institutions that Western governments dominate, such as the World Bank—to formulate new ways of better managing the resource curse. These initiatives—for example, the Kimberley Process Certification Scheme (KPCS) with regard to "conflict" or "blood" diamonds and the Extractive Industries Transparency Initiative (EITI)—can be regarded as a way to assuage troubled consciences, act as a precommitment mechanism to forestall more damaging forms of intervention, and promote more humane and rational uses of these resources. Whether they can be effective and, crucially, what role China will play with respect to these efforts remain open questions.

The commodity price boom or "supercycle" of recent years has raised the stakes and created an additional set of concerns for Western governments. The problem can be seen most clearly in the oil industry, where high oil prices in recent years, apart from representing a massive transfer of wealth from consumers to producers, have conferred enhanced financial and political power on producing states, which are generally underrepresented in the institutions of global governance where rules and procedures are formulated. The implication is that this enhanced power further weakens adherence to international norms, such as those governing human rights and participation in global environmental governance. Put simply, higher prices empower these regimes to pursue their aims.

Exporting states' aspirations are sometimes revisionist in nature: Believing that they have not received their just rewards under the status quo, they seek to weaken, circumvent, or otherwise undermine the liberal, rules-based international order that has prevailed since the end of World War II, in both its economic and political dimensions. China's emergence as a major importer and investor in extraction, and its willingness to accommodate revisionist exporters (Iran, Sudan, and, until recently, Myanmar), further exacerbates the diplomatic challenge, potentially undercutting international efforts in recent years to encourage greater transparency and improved management of natural resource wealth, as noted above, as well as Western diplomatic initiatives, including economic sanctions, targeted at resource exporters like Sudan. This issue is of particular salience for US policy toward Africa. By some estimates, China has surpassed the United States as the single largest provider of aid to the continent, and Chinese outward foreign direct investment is heavily targeted at the extractive sector. The resource boom may have catalyzed a "new scramble for Africa" (Carmody 2011). The last scramble for Africa ended badly, with European powers shooting it out in World War I. Although the war started in the Balkans, it was preceded by an intense naval arms race, motivated in large part by the desire to secure access to colonies (and commodities) around the world. The potential that this resource boom will occasion a geopolitical confrontation between the United States and China must be considered.

Internally, tightening commodity markets and higher prices facilitate repression, incentivize contestation of political control, and make it easier to finance insurgency. These conditions may also confer increased international political and economic clout on revisionist producers and investors. Many fear that the "Beijing Consensus"—a term applied to China's pursuit of marketization without democratization—is being exported around the globe, with illiberal regimes being propped up by the deep coffers of Chinese investors.

It is possible that these problems will be self-eradicating, as a decline in commodity prices from their current elevated levels would deprive revisionist countries like Russia, Iran, and Venezuela of revenues and thereby some power to influence events. Although real prices for oil and metals were flat or declining between 1980 and 2000, the past 13 years have seen rapid price increases and recurrent price spikes (see figure 1.1). But the general consensus appears that high prices reflect increased demand associated with the acceleration of growth in China, India, and other countries; relatively easy monetary conditions globally since 2001; anticompetitive action by OPEC; and possibly, in the case of oil, long-run constraints on supply (Carter, Rausser, and Smith 2011). Accelerated growth in China, India, and elsewhere may be secular in nature, easy money is a cyclical phenomenon, and the jury is still out on whether the global supply of oil is being exhausted (Simmons 2005, 2007). In short, although it is unlikely that commodity prices will remain at their current levels indefinitely, it would be a mistake to dismiss current prices as entirely the product of a speculative bubble. The *2013 World Energy Outlook* forecasts that global demand will rise by 33 percent by 2035 (IEA 2013).

These concerns have elicited a variety of policy responses to various facets of these issues. The West African civil wars of the 1990s generated two related policy initiatives: KPCS, to eradicate trade in conflict diamonds, and the Diamond Development Initiative (DDI), to address broader development concerns, particularly with respect to small-scale alluvial diamond mining. The role of diamonds in fueling violent political conflict has been attenuated, but this attenuation may be temporary; it is unclear how much of the decline in conflict stems from policy and how much reflects other factors and is subject to reversal. Immediate concern has shifted from civil war to the issue of militarized forced production in Zimbabwe.

EITI aims to strengthen governance, transparency, and accountability by encouraging companies to report payments and governments to report revenues in oil, gas, and mining. Recently, the United States has sought to construct a Kimberley-like certification process for certain minerals believed to have fueled mass violence in the Democratic Republic of the Congo and surrounding areas.

The other issue is the growing clout of revisionist producers. A possible response would be to deny them commodity export–derived revenues.

Unilaterally, consuming countries could reduce oil and gas consumption through conservation and development of alternatives. (One could argue that high prices represent implicitly "green" incentives, but conservation could have the same effect even if it resulted in a price reduction.) Although the United States has fruitlessly pursued "energy independence" since the Nixon administration, it now seems possible. An even more profound effect may be generated by the reemergence, through new discoveries and new technologies, of North America as a major source of hydrocarbon production.

North American energy independence would not signal an end to significant US involvement in and engagement with energy-exporting countries, however: Major trading partners in Europe and Asia will continue to be import dependent, and political instability in producing countries can propagate ever more quickly through the international system via global markets. Whatever its export position with respect to energy, the United States can scarcely afford to entirely retrench from an energy-focused foreign policy.

A number of multiauthor and edited volumes address aspects of the resource curse in considerable detail (for example, Humphreys, Sachs, and Stiglitz 2007; Lederman and Maloney 2007; Arezki, Gylfason, and Sy 2012; Arezki et al. 2012; Barma et al. 2012; Dobbs et al. 2013). This book differs from those works in two principal ways. It does not go into detail on the economics of contract and tax regimes for extractive industries; these issues are addressed adequately elsewhere. It does take seriously the critical and inadequately examined political economy of resource extraction in both its intra- and interstate dimensions.

The book is organized as follows. Chapter 2 briefly reviews the basic economics of the resource curse. It concludes that on purely economic grounds, there is reason to be concerned that the impacts are worse in poor countries than rich countries. Although a variety of policies and approaches can be implemented to mitigate harm, none is perfect; and for most countries, successful implementation depends critically on the capacity of the political system, which is weak in many poor resource-centric countries.

If there is a resource curse, it probably lies in the deeper political economy of institutions, rather than in economic management per se. These domestic political challenges are taken up in chapter 3, which makes the case that the resource curse operates primarily through political and institutional channels, with deleterious effects on democracy, bureaucratic and state capacity, and domestic political stability. In particular, it finds that the effects of natural resource wealth are conditional on preexisting institutions and price levels: When preexisting institutions are bad and prices high, the resource curse is more likely to emerge.

Chapters 4 and 5 move to the realm of interstate politics, examining first the ways that resource wealth shapes the foreign relations of resource exporters and then the rise of China as a major commodities importer. Oil exports in particular emerge as a driver of both more bellicose behaviors toward other countries and less participation in global governance institutions, which has implications for the adoption and observance of international norms. These effects are price sensitive: Higher oil prices embolden oil exporters to adopt more aggressive foreign policies.

China's rise as a commodity importer has drawn increased scrutiny of its foreign affairs, resulting in an emerging two-pronged conventional wisdom: (1) China's foreign policy stance is driven in large part by resource-seeking behavior and (2) China's resource-seeking behavior is "rogue," undermining democracy, human rights, and attempts to promote good governance in the developing world. This conventional wisdom has been great fodder for pundits but heretofore subjected to comparatively little rigorous scrutiny. Chapter 5 finds strong evidence that China's outward foreign direct investment is highly concentrated in extractives. It finds less evidence that China's official development assistance and arms transfers are as rogue as conventional wisdom suggests.

Chapter 6 examines multilateral good governance schemes. What is striking is that all of the initiatives reviewed are less the product of textbook economics than campaigns by Western NGOs. As a consequence, their success depends heavily on the efficacy of naming and shaming campaigns directed at producers and the willingness of Western governments to back these efforts up with legislation. The growing importance of non-Western consumers, who at least for the moment seem less sensitive to these concerns; non-Western producers, which may be less susceptible to shaming; and non-Western governments, which may be less supportive of these efforts may pose a profound long-term challenge to this approach.

Chapter 7 summarizes the core arguments and findings of the book and sketches out some policy responses, some aimed at alleviating the resource curse in new and emerging exporters via domestic policy decisions, others aimed at broader, multilateral accords for promoting good resource governance. Given the diversity of economies and commodities covered, no single policy choice, or even bundle of choices, provides a panacea. However, chapter 7 discusses how governments in countries grappling with newfound resource wealth can structure ownership in ways that are more likely to harness that wealth for improved developmental outcomes. In particular, it highlights the potential for partnerships between Western and non-Western entities to combine the flush capital reserves of non-Western investors with the good governance awareness of Western firms and the NGOs that follow them.

For the United States and other Western countries, it is important that this process produce a race to the top rather than the bottom: Just as the resource curse is contingent on institutional quality, so is its avoidance. Well-functioning institutions enormously improve the odds of successful implementation of the technocratic solutions sketched out in the chapter. Poor governance in resource-centric states is associated with state failure and attendant transborder spillovers, as well as a heightened likelihood of interstate conflict. The emphasis on enhanced transparency in the resource sector, going beyond the norms applied in other sectors or business activities, is no simple matter of wide-eyed altruism. Ultimately, good governance in the resource sector can help avoid the resource curse and the "public bads" that often follow it.