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The Political Economy of Natural Resource Richness: Managing the Development Window Opportunity

INTERNATIONAL MONETARY FUND ECONOMIST RABAH AREZKI DISCUSSES CHALLENGES DEVELOPING COUNTRIES FACE IN BUILDING NATURAL RESOURCE INDUSTRIES
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International Monetary Fund economist Rabah Arezki explains the challenge-opportunity matrix associated with natural resource development. And it sounds like a game of [global] Chicken. What comes first: the resources or the managers?

By Jessica Fisher, Columbia MBA ’13

New York, Sept. 28, 2012—In the process of managing natural resource development, “it is perhaps not the natural resources themselves, but the human capital and human resources that are key,” International Monetary Fund (IMF) economist Rabah Arezki said to a group of business and law students at Columbia Law School during a Sept. 20 appearance.

Arezki’s discussion, entitled “The Political Economy of Natural Resources,” was co-hosted by the Vale Columbia Center on Sustainable International Investment (VCC) and Columbia Business School’s Commodity Club.

Arezki introduced the talk with a presentation examining the aftermath of the 2000’s commodity price boom and subsequently high global commodity prices. The resulting increased revenues in resource-rich, middle- and low-income countries – compounded by waves of resource discoveries – presents a now-open window of opportunity for development, and a slew of challenges, he explained.

Specifically, Arezki highlighted Africa’s relatively recent trajectory of natural resource development and economic change. He explained that in large part, as a result of changing phenomena such as evolving exploration and production technology and the trend of investing away from the Middle East, Africa has become a popular hub for E&P discovery and new project development.

Referring to the various challenges associated with resource development efforts worldwide, Arezki noted that there exists “no positive association between an abundance of natural resources and [economic] growth,” despite the notion that natural resources should effectively serve to relax budget constraints on development strategies.

Asking “why the countries that are ‘blessed’ with resources are not developing faster,” Arezki cited the following challenges associated with effective development:

- Loss in price competitiveness (“Dutch Disease”)
- “Debt overhang,” or excessive spending that leads to unsustainable fiscal positions and heavy indebtedness
- Macroeconomic volatility, which requires difficult decision-making by various agents (government, private sector and households)
- Deterioration of institutions (i.e. by corruption, autocracies), the base of the “political resource curse”
- Internal and external conflicts

Arezki addressed the issue of preventing natural resource mismanagement – and natural resources, themselves – from becoming barriers to, rather than facilitators of, sustainable growth and development.

"Let us not repeat the mistakes of the '70's, [when we faced] such high commodity prices," said Arezki, referring to the commodity booms of the 1970's-1980's. "Back then, those countries that invested in large public investment programs ended up with wasted resources [and indebtedness]. The challenge for us today is to not allow countries to spend in a way that will lead to increased maintenance costs and could [ultimately] cause commodity prices to decline."

In seeking to prevent negative fallout from resource development efforts, Arezki listed the following suggestions:

- Diversification of resources, production, and revenue-streams away from the natural resource sector, so that natural resources essentially become a smaller piece of a nation's total "pie;" in this sense, non-resource sector revenue may be used as a hedge against macroeconomic volatility;
- Transfer of / movement away from natural resource wealth/capital to human and physical capital; and
- Employment of frameworks to guide optimal spending on resource development as well as resource use; such frameworks should seek to anchor public spending and smooth consumption.

Arezki explained that any framework for effective resource development would require not only consideration of the mechanisms employed by individual countries (in managing their respective development efforts at various times throughout history), but also consideration of the context and circumstances surrounding each respective nation and development.

He concluded by acknowledging that the challenges related to natural resource development around the world "are multifaceted," and "interlinked."

"Thus, we should apply an integrative approach to solving them," he said.

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NOTE: The Vale Columbia Center on Sustainable International Investment believes that the challenges of poverty alleviation, environmental sustainability and governance should be addressed in an effective sustainability framework for foreign investment. The shared goal for companies, host-country governments and civil society is an investment framework that promotes sustainable development and the mutual trust needed for long-term investments.

The Commodity Club at Columbia Business School is a student-run organization dedicated to the development, investment, finance and trade of natural resources. As the first of its kind among top business schools, the organization seeks to promote effective communication and education about Natural Resources, providing a forum for the world's leading industry executives, investors, traders and economists to engage with the next generation of business leaders.

Jessica Fisher, MBA '13 is a member of Columbia Business School's Class of 2013, and leads developmental efforts for the Commodity Club.