

The Political Economy of Extractive Resources

Discussion Paper

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Abstract

German development cooperation seeks to help partner countries turn extractive resource wealth into sustainable economic development. For this, the Sector Project “Sustainable Economic Development” has devised the technical cooperation (TC) Guidelines “Sustainable Economic Development in Resource-Rich Countries” (GIZ 2015). This study supplements the TC Guidelines with a political economy framework that can help practitioners avoid pitfalls when implementing the Guidelines’ suggested approaches. The study takes political economy theories to explain (1) the dynamics within the circle of a country’s top political elites; (2) the dynamics between these political elites, domestic firms, and the state’s technocrats tasked with nudging firms toward global competitiveness; and (3) the dynamics between the top-level political elites (in the capital city) and provincial politicians in the extraction area. Several case studies are used to illustrate *how natural resource rents* influence each of these three political economy relations. Three remedies are

addressed: transparency & accountability, advocated by the West; resources-for-infrastructure barter trades, preferred by China; and distributing resource revenues to citizens equally via direct cash transfers, tried by Mongolia. Lastly, the study draws closer to the TC Guidelines. Applying the political economy lens developed throughout the study, the final section discusses the dynamics likely to be encountered when implementing the Guidelines’ approaches, i.e. assisting partner countries in long-term strategy development; consensus finding among stakeholders; improving technical education; organising business and worker interests; and giving local communities the means to claim their rights. The study’s aim is to explain why donor-driven reforms (be they for better governance or SME linkage promotion) sometimes fail to meet their intended goals: reformed policies – while outwardly appearing like OECD-institutions – can have an inwardly different function, one that caters to the logic of co-opting elites in order to stabilise the political settlement.

List of Figures

Figure 1: The Limited Access Order	20
Figure 2: The Politics of Industrial Policy triangle	22
Figure 3: Political Settlements with lower-level elites	24
Figure 4: Equatorial Guinea's narrow power base	28
Figure 5: South Sudan's rupture that lead to civil war	30
Figure 6: Chad's attempt to flatten the power structure	31
Figure 7: Natural resource rents minimise the space for industrial policy	34
Figure 8: Mozambique and Angola - The state blocks adding value collaborations	36
Figure 9: Nigeria's fractured Delta, and linkages to the oil sector	39
Figure 10: Peru and Ghana - Local effects of decentralised mining rents	44
Figure 11: Kenya's oil and gas extraction may amplify existing tensions	46
Figure 12: Transparency and accountability to fight corruption	52
Figure 13: Resources for infrastructure - Barter trades with China	54
Figure 14: Direct cash transfers to all citizens	55

Abbreviations

CNPC	China National Petroleum Corporation
EITI	Extractive Industries Transparency Initiative
EXIM Bank	China Export-Import Bank
FRELIMO	Mozambique Liberation Front
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH
TC	Technical Cooperation
ICT	Information and Communications Technology
IMF	International Monetary Fund
KANU	Kenya National Union Party
MDP	Mongolian Democratic Party
MMCP	Making the Most of Commodities Programme
MNC	Multinational Company
MP	Member of Parliament
MPLA	People's Movement for the Liberation of Angola
MPRP	Mongolian People's Revolutionary Party
OECD	Organisation for Economic Cooperation and Development
RENAMO	Mozambique National Resistance
SED	Sustainable Economic Development
SME	Small and medium-sized enterprises
SPLA	Sudan People's Liberation Army
UNITA	National Union for the Total Independence of Angola

Table of contents

1. INTRODUCTION	12
2. THE RESOURCE CURSE	14
2.1 The Economic Resource Curse	14
2.2 The Political Resource Curse	14
2.3 The Social & Ecological Resource Curse	16
3. POLITICAL ECONOMY THEORY – ADDING VALUE AND AVOIDING VIOLENCE	18
3.1 The Limited Access Order	21
3.2 The Politics of Industrial Policy	21
3.3 Political Settlements Theory and Regional Elites	23
4. THE LIMITED ACCESS ORDER AND NATURAL RESOURCES	26
4.1 Repression in Equatorial Guinea	27
4.2 Co-optation and War in South Sudan	28
4.3 Institutional Reform in Chad	30
5. THE POLITICS OF INDUSTRIAL POLICY AND NATURAL RESOURCES	32
5.1 Collusion in Mozambique	33
5.2 Abused State Efficiency in Angola	35
5.3 From Blackmail Linkages to Real Linkages in Nigeria	37
6. REGIONAL POLITICS AND NATURAL RESOURCES	42
6.1 Decentralised Violence in Peru	43
6.2 Local Chiefs in Ghana	43
6.3 Threats of Local Violence and Secession in Kenya	45
7. INTERNATIONAL REMEDIES AGAINST THE RESOURCE CURSE	48
7.1 Transparency and Accountability Initiatives by Europe and the USA	49
7.2 Resources for Infrastructure Deals by China	50
7.3 Direct Cash Transfers in Mongolia	51
7.4 Discussing the Remedies	52
8. IMPLEMENTING THE GERMAN TC GUIDELINES: POLITICAL ECONOMY RECOMMENDATIONS	56
8.1 SED, Linkages, and Structural Transformation	57
8.2 Planning Visions and Implementing Strategies Coherently (GIZ 2015, pp. 24-28)	58
8.3 Activating & Expanding Employment Potential (GIZ 2015, pp. 28-36)	59
8.4 Developing Sites and their Surroundings (GIZ 2015, pp. 37-48)	61
8.5 Extractive Sector Companies as Levers for Development Cooperation (GIZ 2015, pp. 50-53)	62
8.6 Conclusions	63
NOTES	66
REFERENCES	71

Summary

Introduction

High energy and mineral prices have led many countries onto the difficult development path of exploring for and extracting sub-soil natural resources, exporting these resources, and using the ensuing revenues to drive sustainable economic development. Historically, some countries, like the USA or Australia, have managed this path well. But since circa 1980, so many countries have failed at this, that the terms ‘Dutch disease’ (Economist 1977) and ‘natural resource curse’ (Auty 1993) have become common parlance. German technical cooperation (TC) seeks to help partner countries overcome this ‘curse.’ The TC Guidelines “Sustainable Economic Development in Resource-Rich Countries” (GIZ 2015) address the technical levers available to TC practitioners active in this field, and categorise these levers along three thematic fields: (i) national strategic planning, (ii) employment creation, and (iii) local economic development.

This study serves as a supplement to the Guidelines. It illuminates the political economy mechanisms of the ‘resource curse,’ introduces and evaluates general solutions, and points to concrete political pitfalls that implementers of the TC Guidelines may encounter in the field.

The Resource Curse

How the resource curse works (or, according to some, if it even exists) has become a prominent and hotly debated topic in economic and political development circles. The identified resource-curse symptoms (virtually all are disputed, but the tentative consensus in the literature is that for resource-dependent developing countries, reoccurring forms of these symptoms do indeed exist) are the following:

- *Economically*, extractive sectors often exist in isolation from the rest of the economy, which makes skill and technology spillovers difficult. In raising the currency, resource extrac-

tion runs the risk of crowding out other sectors that are better suited for pro-poor growth, notably manufacturing. This can keep resource rich countries overly dependent on one single commodity, and the erratic swings in resource prices make them overly unreliable revenue sources for government planning.

- *Politically*, resource-dependent countries have been found to be more prone to dictatorial forms of government; run higher risks of falling victim to outbreaks of civil war; and are perceived to have, all else equal, higher levels of corruption and weaker governance institutions.
- *Societally*, these phenomena are mirrored in figures showing that countries reliant on resource extraction tend to provide few opportunities for women to work and live independent lives; tend to have unusual chasms between the incomes of the rich and the poor; tend to have low scores on the Human Development Index such as child survival or education levels; and tend to be overly plagued by polluted air, ground, or water bodies near extraction sites.

Political Economy Framework

To understand the dynamics behind these resource curse phenomena, three approaches within a strand of political economy theory are introduced.

- (1) *The dynamics within the circle of a country’s top political elites*: Visionary leaders who want to utilise resource rents for transforming the economy face a problem: the status quo. When law-making and law-enforcing bodies are weak – as they often are in low-income countries – leaders lack a monopoly on violence. Powerful elites, be they religious patrons, heads of ethnic factions, union bosses, army generals, or quasi-mafia lords, often have the means to hold out long enough in the event of a conflict, to destroy not only the

visionary leader's development plan but the entire regime's hold on power. The visionary leader has to accommodate them. The state's security organs are often too weak or too fragmented to enforce laws, which makes it irrelevant how progressive these laws are. Anyone with sufficient violence potential, i.e. anyone who has followers strong enough and ready to confront the state, is, per definition, a member of the elite. They have to be included in the country's rent-sharing machine. These elites, in turn, have to accommodate their respective underlings, for, if they neglect to share, their power quickly subsides as their underlings abandon them to desert to another patron. In short: the pressure to allocate rents informally, along patron-client networks, from the leader to the elites, from the elites to their respective underlings, and further down the pyramid, is great. Economically, this system is much less efficient than would be a merit-based society, checked by the rule of law. But where the state is too weak to enforce property rights impartially, this informal distribution is the default system for providing the most basic ingredient for progress: peace. As the elites stay peaceful, over time, their factions begin to concentrate more on adding economic value, and less on their constant readiness for violent confrontation. This grows the economy; firms specialise and become more productive. Yet, if a common pool of natural resource rents – i.e. free money – enters the scene, the equation is reversed: elites are suddenly less dependent on the revenues from productive firms, but more dependent on 'violence specialists' who guarantee their continued share of the resource rents.

(2) *The dynamics among these political elites, domestic firms, and the state technocrats tasked with nudging firms toward global competitiveness:* in developing countries, the difference between successful and unsuccessful industrial policy can be explained by zooming in on the peak of this patron-client pyramid. Here, three sets of actors determine the dynamics: political elites, state bureaucrats, and domestic entrepreneurs. For industrial policy to work as intended, (i) political leaders must have a genuine interest in productivity-enhancing economic activity; (ii) bureaucrats must have a modicum of capacity to support it (i.e. pockets of technocratic efficiency must exist); and (iii) entrepreneurs must have a genuine interest in becoming globally competitive. In developing countries, each of these three groups has strong (and rational) motivations for averting the development path of steadfastly adding value to the economy. The political *leadership* must be careful when investing in future-oriented industrial policy. Every cent spent on development is a cent lost on lubricating the clientelist network that keeps the regime in power. Leaders often try to combine their two objectives and interfere

with the procurement process, channelling contracts to firms that are politically important, if not always economically deserving. This undermines state bureaucrats, who are, ideally, tasked with supporting productive firms, pushing them toward global competitiveness. Bureaucrats quickly recognise the dynamic and change their behaviour accordingly. In patron-client systems, many *bureaucrats* lose their jobs when power changes hands. Even the technically best-qualified bureaucrats have to look out for themselves, and pockets of efficiency soon again blend in with the mantle of state exploitation. In this environment, *firms* have to assess if their efforts are best invested in improving a product or service, or if it is instead wiser to invest in alliances with powerful elites. This incentive-triangle helps explain why in developing countries it is difficult to focus on adding value, and why, historically, so few countries have managed to become technologically advanced. When natural resource rents become available, elites' incentives to invest in industrial development policies are yet more reduced vis-à-vis their incentives to invest in security and stability. State bureaucrats and firms quickly understand the elites' new priorities, and seek out opportunities to profit according to the new 'rules of the game'. Rent seeking and lobbying become more worthwhile strategies than pushing toward increased economic competitiveness.

(3) *The dynamics between the top-level political elites (in the capital city) and provincial politicians in the extraction area:* since resource deposits tend to be located in particular geographic areas, central governments, in deriving most of their revenues from such 'point-source' resources, tend to have special relationships with the provincial politicians of these extraction areas. Recall that top-level elites base their power in great part on the allegiance of the underlings within their respective factions. These underlings are their clients (viewed from above), but they are also regionally based mid-level patrons (when viewed from below). They will demand from their top-level patrons a share of the rents that is in accordance with their holding power (the region's patron's disruptive capacity). If natural resource deposits are found in a region, the potential power of that region's patron greatly increases, since secession would leave the region with all of the resource rents. For regional politicians, displaying modesty toward the central government is seldom an option: facing competition for their leadership position, regional politicians could be replaced by an adversary. This makes the relationship complex, and for top-level elites, co-optation alone, when dealing with lower-level elites from resource rich regions; is not enough.

Case Studies – The Political Economy of Natural Resources

The first set of case studies examines the dynamics within the circle of a country's top political elites to show that:

(i) Equatorial Guinea's harsh dictatorship cannot solely be attributed to the leader's unfortunate character traits. Having to worry excessively about personal safety leaves him few meaningful avenues to invest in the country's development. Having come to power in a coup, and having averted several attempted coups himself, the president would, were he to invest larger portions of the oil rents into empowering fellow citizens, risk empowering some of his many potential adversaries.

(ii) South Sudan's rampant corruption that permeated the government and army before its 2013-14 civil war did not lead to the outbreak of the war, but most likely delayed it, as the informal distribution of oil rents was used as a strategy to avoid the war. The war only broke out after the president took a more confrontational approach against the most anti-progressive elements in his government (those factions seeking to confront Sudan and blocking Kiir's efforts to reconcile and cooperate with Khartoum).

(iii) Chad's progressive pipeline project failed because its redistributive policies were too ambitious, not accounting for those who benefitted from the status quo and had the power to destroy the plan.

The second set of case studies examines the dynamics among the political elites, domestic firms, and state technocrats to suggest that:

(iv) In Mozambique the developmental triangle of elites-bureaucrats-entrepreneurs faltered from collusion and rent-seeking at each of its three corners: the political elite's efforts to link local SMEs to the operations of multinational companies were hampered by the fact that these efforts were based more on informal connections than on the domestic firms' capabilities. And donor initiatives to strengthen state agencies by establishing pockets of efficiency had little effect on creating linkages because the political elite was not behind these projects. The state technocrats, in turn, soon began to use their newly gained capacity for rent-seeking, setting up firms for themselves and placing these at the newly opened rent-gates: the coming gas and coal industries.

(v) In Angola, by contrast, the state organ responsible for

oil, Sonangol, is highly professional and thus a true pocket of efficiency. But its efficiency at extracting rents from the oil sector is solely at the mercy of the elites. Consumption spending trumps development spending, and virtually none of Sonangol's efficiency benefits Angola's poor.

(vi) In Nigeria, the state is weaker and more fragmented. In its oil-producing region, oil is stolen, and ransoms are elicited from foreign extraction companies, thinly veiled as 'security contracts.' Historically, Nigeria's attempts to provide local linkages have led to little more than elites setting up silent partner firms to help foreign extraction companies meet the local content stipulations. Yet, recent developments indicate more success in genuine local content. Together with a peaceful handover of power in the 2015 elections, these developments give reason for tentative optimism in Nigeria.

The last set of case studies examines the dynamics between top-level (national) political elites and provincial politicians in the extraction area to explain why:

(vii) In Peru, sending large sums of resource rents down to the extraction-area localities did not have the hoped-for democratising effect, but instead led to local violence. The differences between devolved revenues earmarked for the few resource extraction regions and those earmarked for other regions were so large (nearly an order of magnitude) that local leaders instigated several forms of disputes (most intensely, community violence over sub-national borderlines near extraction areas). Akin to the dynamic at South Sudan's national level, Peru's local rents are so large that the difference between having them and not having them becomes an all or nothing game – with the stakes high enough to draw violence between the contenders.

(viii) In Ghana – where decentralised mining revenues are much smaller than in Peru – rents lead to profligacy among the local officials. But contrary to the dynamics in Peru, this provides Ghana's national polity with stability. Other western observers have lamented Ghana's decentralised corruption as a foul spot on the vest of Ghana's otherwise exemplary democracy. This study, instead, points out how these mechanisms at the local level, resemble a particular pattern, recognizable from other country's national politics: from a systemic perspective, tolerating this lower-level-elite enrichment may provide Ghana's polity with the stability needed to function as well as it does at the national level.

(ix) In Kenya, recent oil and gas discoveries on opposite sides of the country could lead to increases of already existent

inter-communal violence (near the oil extraction sites), and to increases of already existent hostilities by locals toward the central government (near the suspected gas fields). This could break Kenya's political settlement with regional elites and lead to insurgencies and even secession attempts.

Resource Curse Remedies

The study introduces three remedies for these resource curse ailments:

(I) Transparency and accountability initiatives: in the 1990s European NGOs began to focus on transparency in the extractive sector as a mechanism for fighting corruption. This agenda was formalised by the British government in the early 2000s. By 2010 the US government pushed toward making transparency legally binding for listed extraction companies. The trend continues, and more such laws are following throughout the world.

Transparency & accountability initiatives in dealings between host governments and multinational companies can help (a) reduce information asymmetries and hence leave a greater revenue portion with host countries, and, more importantly, it would (b) reduce the suspicions and mistrust among host country elites. Domestically, when introduced carefully, transparency can help developing-country elites bring more of their bargaining into the light of day, and collectively agree to earmark certain funds for development spending. Yet, if introduced with a big push, as 'rectifying' a developing country's political settlement to make it resemble that of an OECD-country, this can drastically backfire. Chad's failed pipeline project shows why: progressive laws fail, if they grant powerful elites significantly fewer rents than their peace-disruption potential would apportion them, were they to demonstrate it.

(II) Resources-for-infrastructure trade deals: since the 2000s, China's barter trades, mostly with African countries, have spread even faster than western transparency initiatives, and may present the latter's direct antithesis. Branded as 'eye-to-eye,' with 'mutual respect,' and 'win-win' outcomes, they have become a quick and easy - 'no-questions-asked' - alternative to western loans laden with governance conditionality.

Resources-for-infrastructure deals can be immensely useful for quickly providing e.g. roads that are direly needed for a country's generic economic activity. They can also serve as tools for developmentally visionary reformers, by sign-

ing resources away before they can be turned into rents that become politically difficult to manage. Yet dangers abound. The 'mutual respect' involved in such government-to-government deals, sometimes autocracy-to-autocracy deals, can turn 'win-win' for a small cadre of elites alone - building prestige projects that the people do not need. Another fear regards sustainability: if projects are built by outsiders, without knowledge spillovers, the chance to build a domestic industry is foregone, and the local capacity even to maintain the imported rails and roads is hard to come by. Yet, as developing countries' governments become ever-more accountable to their citizens, the opportunity arises to build on the good (inherent in averting resources from ever turning into sticky rents), and leave behind the ugly (barter deals' opacity): Western alliances of extraction and construction firms, with donor organisations or development banks could offer versions of resources-for-infrastructure deals with transparent terms and pro-poor projects.

(III) Direct cash transfer schemes: think tanks are increasingly buzzing with this idea as the cure for most of the resource curses' problems: paying resource revenues out directly to all citizens equally, as dividends on the wealth beneath their feet, is a simple technical remedy that brings with it a host of promises. Since 2005, Mongolia has been a pioneer in experimenting with several variants of this tool.

The idea of direct cash transfers is exciting for three reasons: (first) there are few policies better suited for helping the poor move out of the dollar-per-day bracket than giving them a second dollar (Banerjee/Duflo 2011); (second) affordable and scaled biometric identification systems make this policy's implementation possible; (third) once begun, this policy could initiate an irreversible social contract. But this remedy too, has to be viewed with caution, less for its negative side effects once in place (there hardly are any), than for its difficulty to implement if tried too ambitiously.

Each of these remedies promises to rectify an aspect of the resource curse. As partial cures for the curse, they have obvious powers, but if relied upon as panaceas, their weaknesses come to bear and can make them counterproductive.

Guiding the TC Guidelines

Lastly, the study focuses more narrowly on the advice given in the TC Guidelines, supplementing it with political economy insights generated in the theory and case-study sections. Concretely, what can this study offer TC practitioners who

are about to implement the Guidelines? The core insight that practitioners may take away is that hitherto bewildering behaviour on behalf of partners can be explained with reference to the underlying political economy mechanisms and the incentive-forces these mechanisms exert on individual actors throughout the system (be it at the top political leadership level with regard to *strategic planning*; be it at the state bureaucratic, the educational, or the business association level with regard to *employment creation*; or be it at the local community or municipal government level with regard to *local economic development*).

Planning long-term visions: the study diverges from the widely held notion that vision planning is essentially a technical economic undertaking that can be copied from other parts of the world. Fragile political settlements cannot sustain overly progressive reform-plans if these go against the interests of powerful groups. The basic groundwork for drafting successful vision documents is the political give-and-take among powerful groups. As reform-minded leaders have to co-opt some of these groups in order to be able to confront others, it can be difficult to decipher from the outside, which of their actions reflect predatory behaviour and which reflect developmental leadership.

Employment creation: the study examines two examples: (i) technical and vocational education and training (TVET), and (ii) coordination among unions and business associations.

TVET initiatives can function differently in developing countries than one would expect from OECD-country experiences. If, for getting a job, personal connections are more important than merit, this dynamic is mirrored in the behaviour of TVET recipients. While those who have the needed connections may see TVET as a nuisance they would rather avoid (because they have the security that anything they need to know can be learned on the job), those who lack the needed connections may see TVET as a waste of time if they are not paid for it directly (because they sense that being technically better than a connected competitor will not be the decisive factor for getting in). This dynamic can be particularly refined in the natural resource sector, where much is still organised informally. The resultant behaviour by TVET recipients may be misunderstood by TVET facilitators who are unfamiliar with the political economy logic introduced in this study.

When helping *unions and business associations*, TC practitioners have to expect such formal organisations to be infil-

trated by or altogether inferior to informal alliances based on various patron-client networks that are not merit-based but often chauvinistically exclusive to insiders of certain groups. In the absence of the rule-of-law, such informal alliances serve a developmental purpose in providing stability and security to between-group trades. But the straightforward agendas, championed by formal associations that are modelled after OECD-world associations (e.g. seeking to provide of open information exchange), are quickly robbed of their innocence, warped to serve one informal team at the expense of another. This dynamic can leave unprepared external advisors at a loss, since the informal teams do not openly wear identifying jerseys.

Developing sites and their surroundings: the study addresses three aspects of the TC Guidelines' focus on local economic development: (i) providing information, (ii) supporting political decentralisation, and (iii) creating social capital.

Information asymmetries are often a tool used by some, in their quest for exercising power over others. Helping local communities in extraction localities means to enter a highly politicised space. Outsiders' influence can sometimes alter the existing power equilibrium, and thus, unknowingly, become a cog in the game of jockeying for local power. The study shows that, going into such endeavours, it is indispensable for TC practitioners to have a firm grounding in the various mechanisms that wait below the surface of seemingly straightforward disputes.

With *political decentralisation*, new challenges arise at the local level. Enhancing the capacity of local level state agencies, be it merely administrative or political, brings the political economy dynamics from the national to the local level. This is a difficult process, and does not automatically benefit the impoverished local community.

When attempting to create *social capital by supporting local change agents*, it must be kept in mind that some who pose as 'local change agents' do so for the opportunity thus granted by outside supporters who, in transferring their own OECD-world experiences, can easily misunderstand the local political settlement, and can be deceived by targeted rhetoric.

Extractive sector companies as lever for development cooperation: for *western* extraction companies, once active in difficult political environments, it can become next to impossible to satisfy all three of their principals: company shareholders, democratic home governments, and domestic

leaders. Quantified project objectives may help TC practitioners as rudimentary benchmarks for working with such extraction companies. Yet, these can easily be circumvented or undermined. The *real* cooperation benefit will come from more qualitative targets that are case specific, and that only materialise to the extent that the different actors' incentives for cooperation can be made to overlap.

Engaging with *resources-for-infrastructure deals* must be based on the knowledge that 'big-push' good-governance reforms are difficult to implement in low-income countries. German TC must find ways to combine (i) rigorously demanding pro-poor spending and transparency stipulations; with (ii) carefully engineering these stipulations as piece-meal conditions that all the powerful domestic players can live with.

Concluding remarks

Take serious the informal system that accommodates powerful elites: the dynamics among elites in developing countries may be comparable to a cold war, where several powerful actors possess the capacity to disrupt the system. Powerful groups have to be included in any development strategy. Technical Cooperation succeeds when it goes beyond seeking to help

reformers devise laws that resemble those of the OECD-world. Practitioners may once find themselves in a situation where the claims of an individual at a negotiating table seem too backward to even be considered. Yet the political leader, for some reason entertains this individual, seeks to find a 'consensus' that moves toward these absurd claims.

As wrong as this may seem, before advising the leader to push through, effectively excluding that 'backward' person from the negotiation table, it helps to recall the political economy logic. Leaders have to weigh all the informal channels, all the unspoken possible consequences. The field of developing country politics is anything but backward; it is delicate and highly complex. Developing-country leaders are usually in the position they are, because they are experts at navigating this field.

Start modest, combine reforms, and implement them via trial-and-error: delivering new reform policies should come in carefully dosed and well-timed combinations of several of the above tools. More important than choosing *the right* reform tool, is to flexibly implement whichever tools are chosen, adjusting them to the country's political settlement. Single big solutions hardly ever lead to the desired outcomes, especially when taken as blueprint copies from other parts of the world.

1

Introduction



To ‘strike gold’ – contrary to the metaphor – does not necessarily entail a fortunate course of events. The commodity price booms and busts of the 1970s and 80s and their devastating effects have been well documented in the following decades of research. Countries that extract sub-soil resources (e.g. oil, gas, or minerals) have often experienced slower than expected economic growth, dictatorial rule, civil wars, and high inequality (be it measured in income disparities between the richest and the poorest, or in the opportunities afforded to men but not to women). Part of the problem is technical and straightforward: a volatile revenue stream that blocks development planning; an exchange rate appreciation that blocks export industrialisation; and a natural geographic and economic isolation of the extractive sector that blocks technology spill-overs. Yet, another part of the problem is political and more complex: many observers of resource politics in developing countries have lamented poor leadership, short-sighted planning, excessive corruption, and political infighting that has often led to clashes of violence, and sometimes to outright civil war. This study aims to explain these latter phenomena, by tracing a thread of incentives that guides elites in resource-driven countries to make economically unsavoury decisions.

Can resource-rich but otherwise poor countries become advanced industrialised countries? In spite of their poor collective record, several resource-rich countries have indeed developed successfully. How they managed to do this is a timely question. Since the early 2000s, another commodity price boom is underway. Driven by the energy and raw material needs of fast growing emerging markets, new explorations have turned many of the world’s hitherto resource-scarce countries into mineral exporters. If the demand keeps increasing, this commodity price ‘super-cycle’ might stretch on through the 2020s (Erten/Ocampo 2013). Yet, if the supply of shale oil lowers long-term prices (they recently dropped by half), and if the maturity of China’s economy lowers its long-term growth rate (it recently dropped by a third) the boom might already be over (Morse 2014; Economist 6th Dec. 2014). Either way, development partners are shifting their focus, as ever more countries graduate from their past dependence on foreign aid. German development cooperation sets out to assist partner countries in their quest for turning mineral resources into drivers for structural transformation and sustainable job creation. For this, the Sector Project “Sustainable Economic Development” has devised German Technical Cooperation (TC) Guidelines, called “Sustainable Economic Development in Resource-Rich Countries” (GIZ 2015). The TC Guidelines focus on the three thematic fields of (i) *Strategic Planning*; (ii) *Employment Creation*; and (iii) *Local Economic Development*.

But can any sort of development cooperation succeed in countries where the political undertow pulls in the opposite direction? Partners in resource-driven developing countries often seem eager for progress and, initially, enthusiastic about commencing progressive reforms. Yet, as time passes, they often seem to slow down in taking the necessary steps, or worse, begin to actively undermine reforms. This study’s aim is to give those tasked with implementing the TC Guidelines a tool for understanding the informal mechanisms at work. It introduces three variants of a new strand of political economy theory: the Limited Access Order (North et al. 2009); the Politics of Industrial Policy (Whitfield et al. 2015); and Political Settlements Theory (Khan 2010). Each of these is particularly suitable for examining a political economy phenomenon that is related to one of the Guidelines’ three focus areas.¹

The guiding thread throughout this study is that in most low-income countries leaders lack a monopoly on violence, which hampers their ability to implement ambitious reforms. They instead have to engage in arduous bargaining rounds with several elites, each powerful enough to cripple not merely the leader’s reform agenda, but the regime’s hold on power.

The study is structured as follows: Section 2 outlines the findings of the ‘resource curse’ literature; and Section 3 introduces the political economy theories with which the study intends to explain the ‘resource curse.’ Sections 4, 5, and 6 use this political economy lens to look at real-world examples. Three case studies accompany each of these sections. The Limited Access Order framework is used to show the effects resource rents have in three politically fragile countries – Equatorial Guinea, South Sudan, and Chad (Section 4). The Politics of Industrial Policy framework is used to show the prevalence of informal networks when governments attempt to stimulate domestic industrialisation via linkages to the resource sector – in Mozambique, Angola, and Nigeria (Section 5). Lastly, Political Settlements Theory is used to show the difficulties involved with decentralisation efforts meant to bring development to extraction regions – in Peru, Ghana, and Kenya (Section 6). Section 7 then discusses three remedies for overcoming the resource curse – Western calls for more transparent governance; Chinese deals, known as resources-for-infrastructure; and Mongolia’s policy of transferring resource rents to all citizens equally. Section 8, by way of a conclusion, supplements the TC Guidelines more directly. By drawing on the political economy mechanisms illuminated throughout the study, this section explains the incentives that cause some of the difficulties likely to be encountered when implementing the Guidelines.

2

The Resource Curse



Australia, Canada, and the United States have successfully developed their economies on the basis of natural resource extraction, and Chile, Malaysia, Indonesia, and Botswana are still doing so today. Yet, since around 1980 many more resource rich developing countries have failed miserably at turning their sub-soil wealth into economic development.²

Economically, extractive sectors mostly exist in *isolation* from the rest of an economy; the sectors can *crowd out* other sectors better suited to foster pro-poor growth; and the swings in resource prices make them overly *unreliable* revenue sources for governments.

Politically, resource dependent countries have been found to be more prone to *undemocratic* forms of government; run higher risks of falling victim to outbreaks of *civil war*; and are perceived to have higher levels of *corruption and weaker governance institutions*.

Societally, these phenomena are mirrored in figures showing that countries reliant on resource extraction provide fewer opportunities for *women* to work and live independent lives; tend to have greater *income gaps* between the richest and poorest parts of society; and, in some areas, have strikingly low indicators of *human development*, such as child survival or education rates. Other studies have found health and environmental hazards near or related to resource extraction sites.

Outlining the ‘resource curse’ findings in such broad terms necessarily conceals many nuances, caveats, and some outright contradictions in this literature. Before moving on to the explanatory political economy theories, the following three sub-sections give more detailed overviews of the debates by referring to renowned studies and some of their respective critics.

2.1 The economic resource curse

Enclaves: resource extraction is capital intensive, meaning that extraction machines need few workers to operate them. The machines are so specialised and sophisticated that supply, maintenance, and repair work is mostly done by overseas firms, not local companies. Extraction sites can also be located in areas so difficult to reach from a country’s productive hubs (its cities) that even the most rudimentary supplies, such as food & beverage or laundry services are brought in from abroad. This often makes resource extraction unsuitable for creating meaningful jobs for sizable parts of the population in low-income countries (as opposed e.g. to a light manufacturing sector). For a country that is at the beginning

of structurally transforming the economy from lower value added agriculture and petty services to higher value added activities such as manufacturing, it is difficult to link resource extraction to other sectors (Hirschman 1958; Singer 1975). For thorough critiques of the enclave curse argument, see Wright/Czelusta (2004), and Morris et al. (2012).

Volatility: for undiversified economies, erratic and unpredictable swings in world commodity prices make for erratic and unpredictable swings in revenue streams, and long-term fiscal expansions for development projects become next to impossible to execute. Dependence on a single sector with great windfalls from price spikes, followed by revenue shocks has proven extremely difficult for developing country governments to handle (Gelb 1988). Macartan Humphreys and Martin Sandbu (2007) describe the problems that resource dependent countries have when attempting to introduce institutions for countercyclical spending (i.e. saving funds), and trace the political economy mechanisms that undergird such systematic failures. Other recent contributions have come to see price volatility as *the* core problem for resource rich countries (van der Ploeg/Polhekke 2009; Ross 2012).

Dutch disease: some sectors, particularly manufacturing, have been found to enhance productivity more than other sectors (Rodrik 2011). By putting larger groups together to produce a good competitively, manufacturing creates environments for learning tacit organisational tasks (e.g. how to collectively make a textile factory more efficient). This emits productive (and hence scalable) activities more often than other sectors do. When natural resource extraction begins, the sums involved are often so large that they can choke the productive sectors out of existence. This can happen directly, if the surge in revenue flows increases the local currency, making producers for local markets less competitive with imports, and making exporters less competitive on the world market. It also happens indirectly, by creating alternative (non-tradable) sectors, such as construction or real estate dealings, which have fewer positive developmental effects than manufacturing, but become nonetheless attractive alternatives for the country’s entrepreneurs who could otherwise have spent their energies on growing the manufacturing sector.³

2.2 The political resource curse

By the same dynamic that resource rents lead entrepreneurially minded individuals away from manufacturing and toward less productive sectors, such as real estate, resources can also lead entrepreneurially minded individuals to turn their

attention to siphoning off money from the extractive sector directly (Karl 1997; Tornell/Lane 1999; Robinson et al. 2006). This can happen in many ways: a country's president or oil minister can negotiate a deal that is overly favourable for a foreign extraction company in return for an illicit side deal (oftentimes cloaked in a proscription to set up a joint venture with a dormant domestic firm); a bureaucrat in the oil ministry, treasury, customs department, or central bank can find ways of enriching herself without fear of repercussions – to the contrary, such 'gate-keeper' jobs are often competitively sought after, not for their modest pay, but for the opportunities they provide for embezzlement (Collier 2007, 161); a local community can steal – 'bunker' – raw materials directly from an extraction site or from the pipes (Shaxson 2009). A study on Philippine, Malaysian, and Indonesian timber showed how political elites, in their rent-seeking efforts, purposefully dismantled regulatory institutions in order to misappropriate the windfall gains (Ross 2004a). In the course of the 2000s, the resource curse literature has thus shifted from hypothesising the core of the curse to be of an economic nature (primarily in the Dutch disease), to one of a political nature, i.e. that resource wealth weakens a country's governance institutions (Sala-i-Martin/Subramanian 2003; Mehlum et al. 2006).

The notion that the curse's 'root cause' is weakened political institutions was arguably as close to a consensus as this literature ever got. But this has recently been contested and revised: Ross (2012) finds, in general, no evidence for the claim that resource wealth causes weaker governance institutions; rather, he contends that resource wealth (a) lifts countries into a higher GDP bracket (into 'neighbourhoods' of comparator countries which have evolved better governance institutions due to their otherwise derived higher incomes), and (b) resource wealth is more difficult to govern than other, non-resource-derived incomes. This leads him to conclude that resources do not weaken institutions, but merely demand stronger ones. Part of the focus in the literature thus swings back toward a variety of other causes for the curse, such as the Dutch disease. For Ross himself, the causes are primarily gender inequality (see below) and price volatility (see above). Nonetheless, countries with strong institutions for enforcing rules impartially (e.g. Norway) seem to be immune to some of the 'spells' while other 'spells' do not apply: e.g. commodity price volatility is less problematic for a country with a diversified private sector, where the non-resource tax base is large enough to balance the government's books on its own.⁴

Authoritarianism: empirical studies find that countries which derive higher proportions of their GDP from extractive natural resources, tend, on average, to be less democratically governed (Ross 2001). This finding is contested for longer time periods (Haber/Menaldo 2011), but holds for the period since 1980 (Andersen/Ross 2014).⁵ A peculiar regional exception to this rule seems to be Latin America where natural resource wealth has no discernable negative effect on democratisation. Thad Dunning (2008) argues that Latin America's exceptionally high inequality may have given elites the security that democratisation would not lead to their disenfranchisement (Dunning 2008, 128-129, 210ff).

Civil war: the flipside to the rigid stability of suppressive authoritarianism is that political contestation, when it occurs, takes the form of violent conflict more often than in non-resource dependent countries (Le Billon 2001; Ross 2004b; 2004c; Collier/Hoeffler 2004; Fearon 2005; Humphreys 2005). This finding is robust, but qualified by intermediate variables – i.e. resources have the greatest likelihood of fuelling civil wars if they are easy to extract and located in areas already contested by local minorities (Fearon/Laitin 2003). For example, second grade diamonds, near or on the surface (and thus easier to extract), are more dangerous for political stability than underground first grade diamonds (Lujala et al. 2005). No correlation, on the other hand, has been found between offshore extraction and civil war (Lujala 2009). Much of this literature concentrates on certain sub-questions regarding not only the *types* and *locations* of resources, but also their respective effects on conflict onset (Lujala et al. 2005), conflict severity (Lujala 2009), or conflict *duration* (Lujala 2010). Furthermore, the risk of conflict seems to stand in an inverted U-shaped relationship with extractive resource wealth: there seems to be a tipping point, at which, the more resource wealth a country has, the less likely an outbreak of civil war becomes (Basedau/Ley 2009).

2.3 The social & ecological resource curse

Inequality: The highest income bracket in resource-rich countries seems to profit disproportionately from resource wealth. An indication for this is the frequent media reports on the extravagant lifestyles that elites of resource rich countries live. There is, in fact, a significant negative statistical relationship between countries' resource wealth and the inequality *data* they make public. While suspicious, all this means is that the actual effects of resources on inequality are difficult to measure (Ross 2007, 238). Gylfason/Zoega

(2003) have used the incomplete data that does exist to show a significant negative relationship. Fum/Hodler (2010) find that the impact of resources on inequality is mostly limited to ethnically diverse settings. On other nuances see Goderis/Malone (2012).

Human development: Gylfason (2001) sees the core relationship between natural resources and poor social outcomes in a lack of education in resource rich countries. This comes about in two ways: (a) the enclave nature and Dutch disease effects from the resource sector provide for few linkages and little opportunity for learning by doing in other (crowded out) sectors (see above); and (b) governments reliant on natural resources seem to invest less in education. But refuting the underlying data, Ross (2012) shows that school enrolment rates present a peculiar pattern: Middle Eastern oil exporters outperform their peers, while Latin American oil exporting countries score on par with non-oil countries, and in Sub Saharan Africa, oil exporters lag behind other countries' enrolment rates. For health, however, more sweeping findings have recently been made, regarding resource rich countries' lower health spending in general (Cockx/Francken 2014) and weaker institutions to fight HIV/AIDS in particular (de Soysa/Gizelis 2013).

Environmental degradation: almost inseparable from the 'health spell' are (a) the great threat of global warming – often discussed separate from the resource curse literature – and (b) the many local concerns regarding mining's negative externalities. Globally, the main concern is if, in the face of rising temperatures, it is even sustainable to extract more carbon-emitting fossil fuels (Rockström et al. 2009). Locally, environmental concerns range from the side-effects of hydraulic fracking in the USA; the marine biology consequences of accidents such as the Exxon-Valdez spill in 1989 (Malakov 2014) or the Deepwater Horizon spill in 2010 (King et al. 2015); to deforestation in South-East Asia (Ross 2004a); to undetected air pollution by mines in Ghana (Aragon/Rud 2012); or unpunished water and wetlands pollution in Ecuador or Nigeria (Maass 2009).

Gender disparity: a new strand in the resource curse literature emphasises the negative impact of a country's natural resource wealth on women's economic and political emancipation, as tragic in its own right, but also as an important link for explaining other resource curse phenomena. Natural resource extraction provides overwhelmingly male dominated jobs, e.g. in the construction sector. Furthermore, the Dutch disease effects crowd out export manufacturing, which happens to provide the most employment and social mobility for

women. These effects *could* be compensated for by employing more women in the services and government sectors (which grow disproportionately large in resource-driven countries). Yet, if a resource-driven country is patriarchal to begin with (which many low income countries and particularly most Middle Eastern countries are), women are often prohibited from working in such interactive service jobs (Ross 2012). In the Middle East, this prompts two developments: local women who marry early and then stay at home (leading to higher fertility rates), and inbound labour migration from poorer countries. Both of these factors have been found to lead to higher population growth rates, which in turn slow per capita income growth rates (Ross 2012; Cotet/Tsui 2009; Jamal et al. 2010).

Instead of allowing a sweeping conclusion from this vast literature, the above shows that the resource curse is harder to pinpoint than early contributions to the literature had suggested. Jeffrey Sachs and Andrew Warner's milestone studies (1995, 1997, 2001) had claimed that resource rich countries grow slower, economically, than resource poor ones. This has been rebutted, prominently by Mehlum et al. (2006), who inserted that a country's governance institutions are the critical intervening variable (well-governed resource-rich countries grow fast, and poorly governed ones grow slow or not at all). Other scholars have turned to historical cases, showing that resource-led industrialisation had indeed occurred in several Western countries (Wright/Czelusta 2004). Building on this, a series of qualitative studies seeks to show that extractive sectors in several Sub-Saharan African countries can provide the basis for industrialisation, mainly via backward linkages (for a synthesis of these studies see Morris et al. 2012). Meanwhile in the quantitative realm, two widely cited studies – Brunnschweiler/Bulte (2008), and Alexeev/Conrad (2009) – outright dismiss the 'resource curse' as a statistical artefact. This, in turn has been rebutted (van der Ploeg/Polhekke 2009; van der Ploeg 2011). And the majority of contributions to the field still find that extraction-led developing countries face severe problems that seem to come with the sub-soil sources of their revenues. Hence, a review of this literature suggests that the resource curse is more nuanced than originally claimed, but that its problems do indeed exist, particularly in the forms of difficult revenue volatility, Dutch disease effects, governance problems, and gender disparity. More difficult than pinpointing these empirical symptoms has been to decipher their underlying *causal* mechanisms. For this, political economy frameworks can prove helpful.

Political Economy Theory – adding value and avoiding violence

3



A recurring theme throughout this paper is violence.⁶ To understand a developing country's political economy is to understand that country's threat of internal violence, more specifically: of outbreaks of violent conflicts between powerful elites. Power clashes between elite factions are the single greatest hazard for a country's social, political, and economic development, they are "development in reverse" (Bannon/ Collier 2003, 1). The way violence is *organised* and *regulated* is key to understanding the difference between technologically advanced countries, associated with the Organisation for Economic Co-operation and Development (OECD), converging middle-income countries, and fragile low-income countries, known as the 'bottom billion'⁷ (North et al. 2009). Countries at the top end of the spectrum, those in the OECD-world, have managed to establish rules for when, how, and by whom violence can be legitimately exercised. Such rules are regularly refined by parliamentarians, neutrally applied by judges, and impartially enforced by the police. These state officials are, in turn, checked by one another (institutional balances), by the media (as the fourth estate), and by citizens (e.g. via periodic elections). These rules and their enforcement mechanisms are so firmly entrenched, that for most OECD-world citizens, the constant threat of violence by other citizens or by the authorities, while still existent, has moved far to the background of everyday life.

In contrast, most citizens of low-income countries hold recent and vivid memories of violent acts that were illegal but left unpunished by the state. Laws that the state cannot enforce are easy to break. Powerful groups with a particular potential for violence (North et al. 2009) or an ability to hold out long in conflicts (Khan 2010) have to be dealt with by other means. The state has to acknowledge their power and accommodate them. In trying to persuade them that refraining from disrupting the social order is in everyone's best interest, the state, as it is unable to fight them off, has to share resources with these groups. Citizens, for their part, usually grapple with the threat of such groups by joining one. Together, these two dynamics are mutually reinforcing (i.e. the upside of to states seeking to co-opt powerful groups and citizens seeking to join powerful groups is that groups with more members and larger shares of state resources are also more powerful).

This dynamic creates patron-client networks that are best visualised as pyramids with a patron at the top, and various cascading patron-client links throughout. Such arrangements take on different forms, but the *modus operandi* of these structures is found throughout the developing world. Belonging to a group provides its members (or 'clients') pro-

tection against outside attackers; access to material benefits directly generated within the group; and an identity linked to the group's reputation that can ease trade relations with outsiders.⁸ A group's leader (or 'patron') generates wealth in one of three ways: by either (a) *adding value* – i.e. letting most group members produce or trade goods and services, and keeping only a small cadre of 'violence specialists' to protect and collect membership fees from the majority of the productive members; by (b) *blackmail* – i.e. demanding that the state allocate the group a greater share of resources in acknowledgement of the group's organisational power to disrupt the social order; or (c) *confrontation* – i.e. by expanding the number of 'violence specialists' within the group in order to prey on other groups that are less militarised or by confronting the state directly to demonstrate violence potential, and hence the 'right' to a greater share of resources.⁹

'Powerful groups' can take on different shapes, depending on a country's historical or geopolitical trajectory (e.g. they can be political parties, rebel factions, ethnic groups, clans, religious or educational organisations, trade unions and business associations, or criminal cartels). Their respective blackmail strategies can be *soft*: a group whose *adding-value activities* are particularly needed can threaten to stop generating rents (e.g. worker strikes, or plant relocations). Or they can be *hard*: a group whose *violence potential* is undisputed can threaten to make use of it to start a confrontation (e.g. army coups, riots, or regional secessions). A country that functions well is one where the relevant powerful groups stick to a combination of *soft* blackmail and adding value. An adding value strategy in turn becomes more viable if the state can effectively protect productive groups from predators (e.g. by enforcing their property rights). The higher the focus of powerful groups on adding value (and hence shunning confrontation), the greater the country's potential for productivity growth and eventual structural transformation of the economy.

At the outset, the 'state' is itself nothing more than an amalgamation of powerful groups that have the potential to be disruptive, but have decided, for the time being, to cooperate in adding value instead. This means that the state consists of loosely affiliated patrons who have agreed to engage in wealth-generation and rent sharing within a joint territory. These patrons become the country's elite. Thus, a group's level of productivity is not the only determinant for that particular group's informal 'right' to rents.¹⁰ Another group may contribute less, economically, but can instead more credibly threaten to disrupt the social order. This group needs to be accommodated just as urgently. (This is in the interest of all involved, even the economically more productive groups,

since an actual demonstration of violence potential, in form of a power clash, would be more detrimental than a steady stream of rent-sharing.)

The crux of this system is that a society stuck in an unproductive zero-sum equilibrium between powerful groups (where most groups engage in strategies of hard blackmail and confrontation), cannot easily shift to a productivity-enhancing, positive-sum equilibrium (where most groups primarily engage in adding value).¹¹ Such a shift entails a delicate balancing act of checking and accommodating powerful groups. Yet, a shift back to the confrontation equilibrium (i.e. to civil war) can occur whenever groups overestimate their own strength, or underestimate that of others. The trajectory of this process can be traced by examining three relationships. These are in reality often indistinguishably enmeshed, but heuristically, they can be depicted separately as:

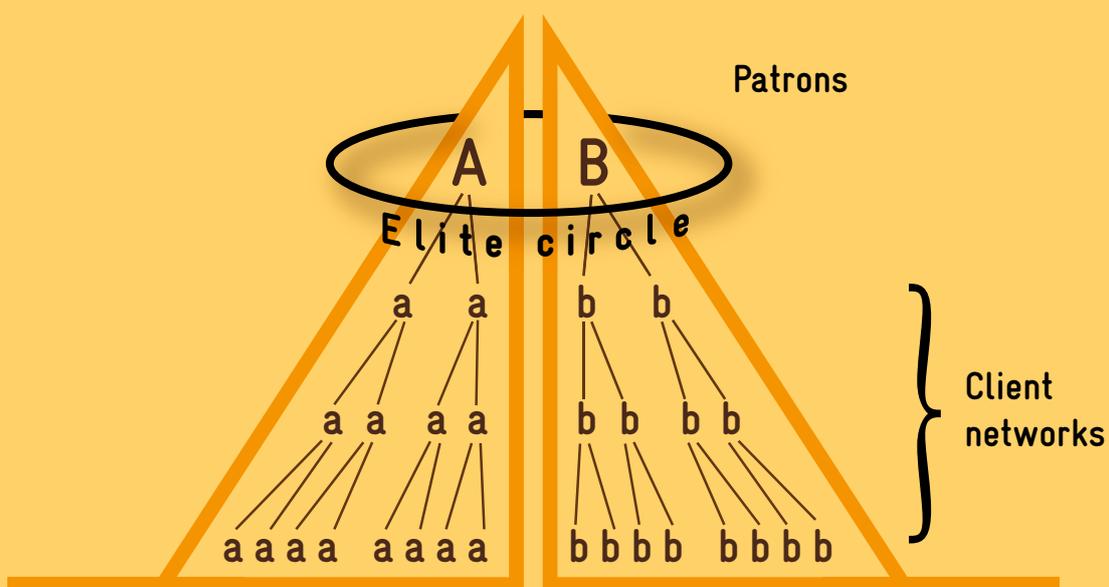
- the relations among the groups that constitute the national top-echelon of elites, effectively the ruling coalition (and in special circumstances, the relations of this ruling coalition

with groups that are excluded but nonetheless powerful); the relationships between these national top-echelon elites with elements in society that are (or have the potential to become) economically productive; and

- the relationships between top-echelon elites with lower-level elites (and the focus here will be on local politicians in peripheral extraction regions).

To examine these three sets of relationships, the following sub-sections introduce our three related strands of political economy approaches. Sections 3, 4, and 5 then show the peculiar effects that sub-soil resources bring to each of these relationships. By extension, this is linked to the TC Guidelines' three focus areas: the Limited Access Order framework best illuminates the political economy of strategic planning; the Politics of Industrial Policy framework best shows the political economy involved in employment creation; and the Theory of Political Settlements with regional elites best shows the political economy involved in strategies for local economic development.

Figure 1: The Limited Access Order



Source: author, based on North et al. (2013, 5).

3.1 The Limited Access Order

Nobel Laureate Douglass North and colleagues John Wallis and Barry Weingast have examined the historical evolution of societies and derived at what they call a Limited Access Order framework for describing the connections between political stability and economic development (North et al. 2009). The term ‘limited access’ refers to the top-echelon elite-circle that every developing country has and to which membership, or ‘access’ is limited. This framework gives little credence to formal rules that exist on paper but cannot be enforced. Anyone who can credibly threaten to mobilise a following strong enough to disrupt the social order is, per definition, a top-level elite and has to be included in the circle of rent-sharing patrons at the top of the patron-client pyramid.¹²

Elites strive to maximise their respective shares of rents, and have a common interest in blocking the rise of new elites (i.e. of a new patron who has managed to develop a following of clients that is significant enough to be reckoned with). Existing elites thus cooperate in keeping their circle closed to outsiders. Such outsiders are usually not ‘start-up’ patrons, the most threatening newcomers are former second-in-command or regional mobilisers closer to the very top of existing patron-client networks (often just below an elite patron). In practice, this means that each patron in the circle is only tolerated by the others if she commands a following that either (a) provides a large fraction of the shared rents (and can threaten to withhold these), or (b) has the violence potential to disrupt the social order. Once a patron has made it into the circle of elites, the other elites help this patron stay at the top of her clientelist network. Elites can call upon one another as third-party enforcers of the status quo. Figure 1 depicts this relationship in its most simplified way, where A and B represent the patrons, the horizontal ellipse represents their limited access elite circle, and the vertical triangles their respective networks of clients (the a’s and b’s) that constitute the ‘slivers’ of the larger patron-client pyramid.

This tit-for-tat insurance arrangement between top-level elites gives the members of their limited access circle incentives that easily lead to economic rigidity (once a patron has a permanent seat at the elite table, she has little incentive to put effort into adding more economic value by learning to be globally competitive or making risky investments in innovation). Yet, this is the system that survived and reappeared, according to North et al. (2009), throughout the 10,000 years of sedentary human existence, which suggests

that its benefits outweigh its downsides. Its greatest benefit is that this system provides stability. In latent form, a patron’s capabilities to disrupt the social order or hold out in a violent conflict can only be vaguely estimated.¹³ The only time such capabilities can really be measured is in an actual violent conflict between factions – a power clash. This is a tremendously costly undertaking for all (violence disrupts the economy and thus lowers rents for all, which can undermine other patron-client networks, setting in motion a run-away process of destabilisation). Limiting access to the elite circle from the start counterweighs the system’s Achilles heel: its inability to measure power abstractly. In contrast to open access orders of the world’s most advanced countries (the industrialised, liberal democracies of the OECD-world), in the limited access orders of developing countries, power cannot be measured in monetary terms or by counting votes, since smaller or less endowed groups can often be more disruptive than larger or richer groups. This is because members of poorer groups are often more willing to make sacrifices and thus be more disruptive and hold out longer in conflicts.¹⁴ Recall that all this takes place in developing country environments where the state’s violence organs (police, military, etc.) are not sufficiently insulated and equipped to pre-empt elite power clashes, or to impartially terminate such clashes once begun.

This illuminates the core systemic reason for blocking elite mobility in and out of the top-elite circle. It is not primarily because existing elites want to share rents with fewer rather than more patrons – under a more stable logic, a greater circle of elites would actually be desirable for them. It is because when the size of the elite circle changes, the allocation of rents will have to change accordingly. This entices elites to pre-emptively advertise their disruptive potential to one another, which, in turn, threatens the stability of the system.

The same logic applies if the number of elites in the limited access circle stays fixed, but the size of their available resources changes up or down. Section 4 examines the empirical impacts that such shifts in natural resource rents have on the constellation and stability of limited access elite circles in three fragile developing countries: Equatorial Guinea, South Sudan, and Chad.

3.2 The Politics of Industrial Policy

Zooming in on the mechanisms inside the peak of the patron-client pyramid, another political economy theory complements the Limited Access Order framework. Copenhagen-based researchers Lindsay Whitfield, Ole Therkildsen,

Lars Buur, and Anne-Mette Kjær examine the conditions that allow developing-country leaders to engage in successful industrial policy. Their *Politics of Industrial Policy* framework (Whitfield et al. 2015) suggests that industrial policy succeeds or fails within a triangle of (i) ruling politicians, (ii) economic entrepreneurs, and (iii) state bureaucrats. Political leaders must have some interest in productivity-enhancing economic activity; bureaucrats must have a modicum of capacity (i.e. some bureaucratic pockets of efficiency must exist); and entrepreneurs must have a genuine interest in (and a realistic chance for) becoming globally competitive (see Figure 2). The complexity of this triangle becomes clear with the actors' relationships to one another.¹⁵

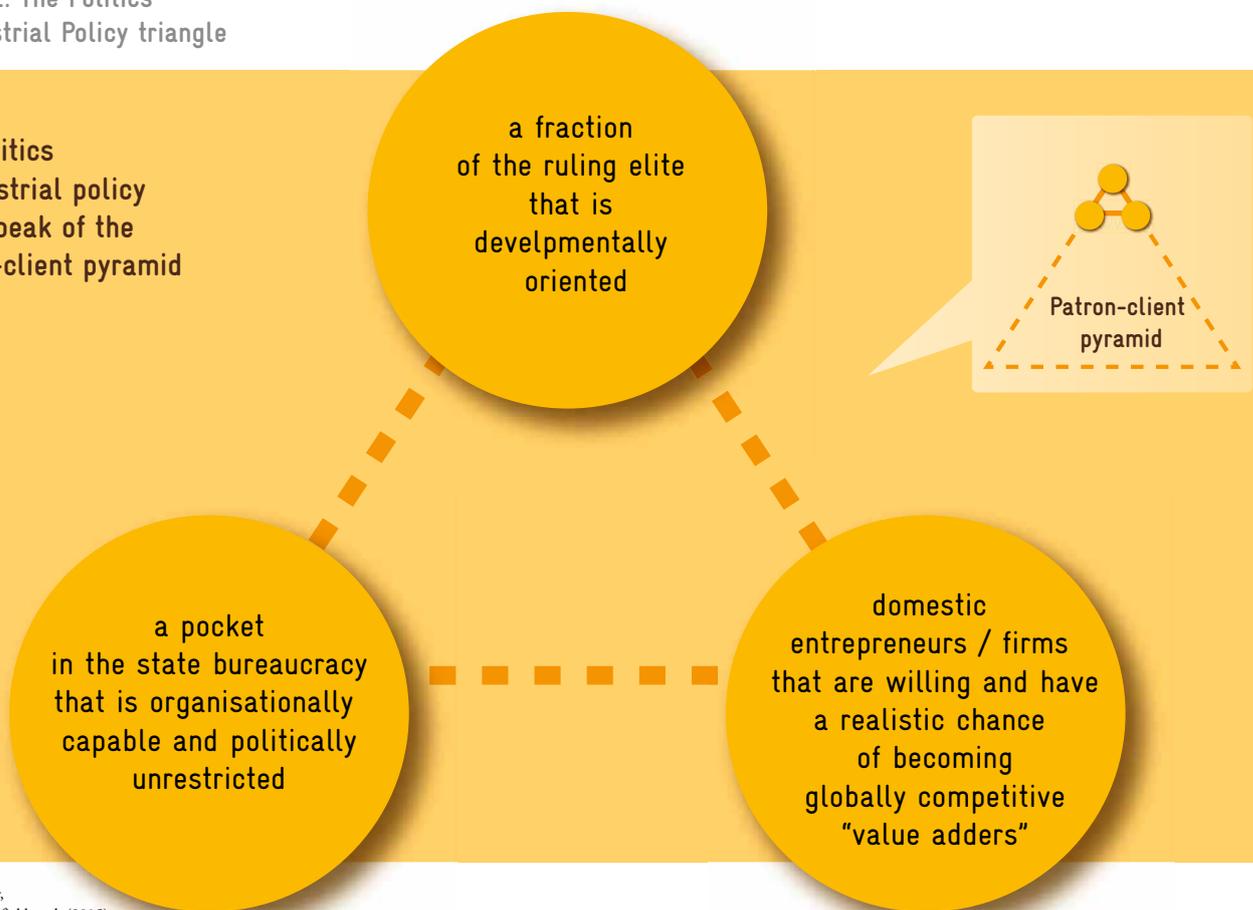
The relationship of political leaders vis-à-vis economic entrepreneurs entails that both see a tangible benefit for themselves if the firm's productivity is enhanced, preferably to an extent where it becomes globally competitive and gains the means to shift to making ever-more sophisticated prod-

ucts. For politicians, supporting such ventures involves risks. Economically, the resources spent on easing a chosen firm's path to competitiveness are not guaranteed to bear fruit: the 'picked' firm could fail, or, due to unforeseen changes in the global economy, the chosen sector could turn out to be a 'blind alley.' Yet, to nudge an economy toward productive activities more generally (i.e. to induce structural transformation), such speculative investments in particular firm's and sectors' long-term economic productivity are needed.¹⁶ But such investments are also costly in political terms, as the opportunity cost is to forgo consumption-spending that lubricates the elites' patron-client networks.

Moreover, any domestic entrepreneur in a position to become globally competitive will most likely be linked to a patron-client faction near the top of the political power structure to begin with (recall the pyramidal network introduced in the last section).¹⁷ This means that building up a firm's economic strength can create a potential shift in the elite

Figure 2: The Politics of Industrial Policy triangle

The politics of industrial policy at the peak of the patron-client pyramid



Source: author, based on Whitfield et al. (2015).

circle.¹⁸ Empirically, this explains why political support for productive firms in developing countries most often occurs for close kin relations or if the political elites and the economic entrepreneurs are indeed the same individuals. This can have positive outcomes, as it apparently did in Indonesia and may yet have in Angola and Nigeria (discussed below).¹⁹ But firms, by their nature, are interested in making profits, and avoiding unnecessary risks and investments. While firms mostly welcome state support, they are often inclined to try to avoid exerting the additional effort needed for becoming globally competitive. Hence, the political elites' support for firms often results in economic failures of the types witnessed in the import substitution industrialisation strategies of the 1960s, where firms continued to seek protection in spite of stagnant productivity levels. This happened at the expense of domestic consumers, who were limited to inferior and often more expensive goods, and domestic producers from other sectors, such as agriculture, who were taxed to finance the industrial policy (Bates 1981). More promising industrial policy paths were those of Korea or Taiwan, where support was contingent on firm success: protection of unsuccessful firms was discontinued.²⁰ But for this to come about, the third corner of the triangle is crucial.

State bureaucrats, tasked with supporting the entrepreneurs' development, have the particular role of gaging whether or not a firm is on its way to becoming competitive, whether it needs more time, more support, more pressure, or if it needs to be cut loose because it cannot deliver the promised results. For this, bureaucrats need substantial organisational skills, insights into the particular industry, and influence with the political elites who back this industrial policy. Remember that this triangle of relations sits at the peak of a patron-client pyramid where groups compete for rents. The developmental leaders who support the industrial policy must fend off competing elites who seek to shield certain firms from performance pressures (either because a firm is directly owned by an elite in the circle, or because the firm's profits otherwise finance an elite faction's rents). Alternatively, the nagging state bureaucrat can be approached directly by an elite/firm and influenced with a bribe, a threat, or both. Operating in a limited access order logic, a certain degree of stability, good will, trust, and probably luck is needed for this triangle of political elites, bureaucrats, and entrepreneurs to produce successful industrial policies. This explains why, over the course of history, most societies have managed to concentrate on adding value strategies for only short periods of time, before reverting to blackmail or confrontation, and why only a few countries have so far become technologically advanced.

As rents from extractive natural resources come into the picture, the odds against successful industrial policy initiatives become yet significantly greater. Chapter 5 provides the examples of Mozambique, Angola, and Nigeria that show some local content and local ownership policies, which look promising on paper, but have been warped to fit the political power structures. Yet, at least in Nigeria, recent linkage policies also seem to induce a turnaround toward more competitive local oil services companies.

3.3 Political Settlements Theory and regional elites

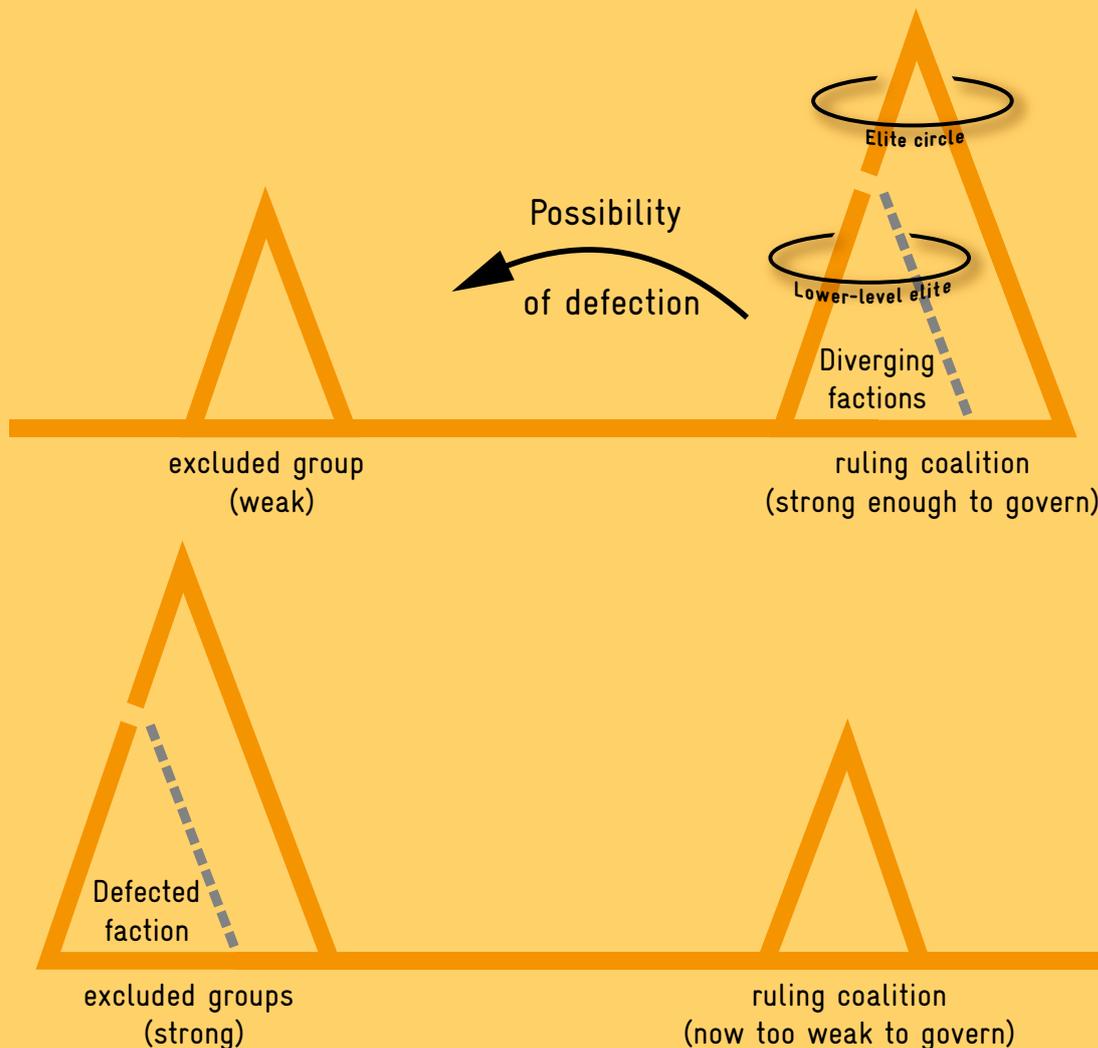
This is the last of the theoretical sections, and it examines the relationships between top-level elites and lower level-elites, i.e. patron-client ties going vertically down into the pyramid. This analysis is based on University of London Professor Mushtaq Khan's Political Settlements Theory. Much of Khan's work also underpins both the Limited Access Order and the Politics of Industrial Policy frameworks. For example, the emphasis on elite "violence potential" in North et al., is very close to Khan's notion of "holding power," which measures elite power in developing countries by the length of time a faction is able to hold out in a confrontation.²¹ One of Khan's insights is that the top-level ruling elites (at the peak of the pyramid) are dependent on lower-level elites.²² These are clients (when viewed from above), but also mid-level patrons (when viewed from below). They are the a's and b's in Figure 1 that provide factions with the organisational muscle. These can be members of the urban middle class who are politically active. Oftentimes, they are semi-autonomous regional politicians, such as provincial governors, mayors, or even traditional chiefs, who represent geographically and/or ethnically distinct sub-factions of a larger sliver of the pyramid. They introduce a further element to the balance of power: the risk that lower-level elites may break away and join excluded factions to contest the ruling coalition (Figure 3).²³ In Figure 3, the ruling coalition, depicted as the larger of the two pyramids, can shrink if a large enough 'sliver' of its coalition breaks away to join excluded groups. If, as a result, the excluded groups become more powerful than the rump of the ruling coalition, as depicted in the second part of Figure 3 (where the two pyramids have reversed in size relative to one another), a changeover of power is immanent.

So far, the discussion was restricted to a single patron-client pyramid made up of coalitions that constitute the political settlement of power relations in a country. This is a *dominant & inclusive clientelist system*: a state that incorporates

all regional/ethnic factions and faces few outside threats. Alternatively, there can be a *dominant & exclusive clientelist system*: a state that suppresses the organisation of external groups (e.g. a tightly authoritarian regime), or a *competitive clientelist system*: a state where power regularly shifts between mutually exclusive networks (e.g. a developing democracy with equally strong and competing factions).²⁴ Yet, observers must be careful to avoid the trap of taking a country's formal institutions at face value – as literally depicting the country's power relations among elites – when in fact, hidden informal institutions are more powerful and indeed arrange *all* powerful elites into one single limited access order pyramid. Box 1 provides three examples of this.

These three sections show that limited access order elites face, individually, the constant risk of power clashes within the elite-circle if rents are not divided according to violence potential; while, collectively, they face the constant threat of lower-level/regional elites breaking away to establish new networks that contest the entire elite-circle's hold on power. The challenge, then, is how, in such contested political environments, elites can entice more value-adding activities by getting firms to increase their productivity in fields that lead to structural transformation. This is a daunting task. And it is not surprising that many developing countries have had difficulties mastering it. The following three sections show the ways in which natural resource rents can yet substantially amplify these difficulties.

Figure 3: Political Settlements with lower-level elites



Source: author, inspired by Khan (2010, 62, 65).

Box 1: The inclusion of (formally) excluded elites

The literature somewhat diverges on the salience of ‘excluded top-level elites.’ Mushtaq Khan (2010) depicts a ruling coalition’s power vis-à-vis lower-level elites in the pyramid (vertical power), by noting that lower-level elites can detach, and join excluded elites (horizontal power). North et al. (2009) do not mention excluded elites, presumably because they do not believe in the existence of truly powerful elites that are nonetheless entirely excluded from the state’s rent accumulation. If this were the case, confrontation would ensue. Indeed, when empirically examining the relationship between governing coalitions and ‘other elites,’ ones that are seemingly excluded (e.g. via lost elections), one often finds a mixture of these two positions: various hybrid-types of *partially* excluded elites.

In Angola, the People’s Movement for the Liberation of Angola (MPLA) government regularly pays out individual bonuses to selected National Union for the Total Independence of Angola (UNITA) Members of Parliament (MPs), sums that can exceed the latter’s official salaries. The criteria for these bonuses are not stipulated, but observers suggest that these are pure co-optation payments (Amundsen 2014, 180-181). This shows that even in the authoritarian dos Santos regime, opposition elites (UNITA MPs) are not entirely ‘outside’ the peak of the pyramid. To keep them from disrupting the social order, these elites are accommodated by some inclusion in rent-sharing.

In Ghana, in spite of being hailed by many as Africa’s model democracy (e.g. Kopinski et al. 2014), informality still determines political relations. The power of Ghana’s president has been described by many observers as enormous (Ayee et al. 2011). Opposition politicians hardly ever veto the president’s bills, since all MPs seem keen on gaining a ministerial position, which the president alone can bestow (often rewarding not only loyal affiliates but also ‘cooperative’ opposition parliamentarians). In much of the literature, Ghana’s strong presidency is described as a problematic downside to Ghana’s otherwise exemplary democracy (Ayee et al. 2011; Standing/Hilson 2013). But a political economy framework helps observers take a more nuanced perspective: what appears on the surface as a rather one-way relationship – between MP ‘clients’ who hope for carrots and the president ‘patron’ who dishes them out arbitrarily – may instead be a delicate two-way mechanism of keeping the peace within the circle of powerful elites.

In Kenya’s democratisation phase, the most powerful excluded elites were arguably Odinga Odinga (a Luo, fighting as the main opposition leader for multiparty elections in the early 1990s), and Mwai Kibaki (a Kikuyu, and one of President Moi’s staunchest opponents from 1988, when he left the ruling Kenya National Union Party (KANU), until his landslide election victory in 2002). In the midst of the democratisation wave in the early 1990s, the fledgling opposition’s leader Odinga Odinga stood for a clean break with the Moi regime’s autocratic and corrupt rule. Yet, it was later found, that while Odinga campaigned for replacing the ‘corrupt old’ government with a new ‘clean one,’ he was himself one of 1,115 beneficiaries from a grand corruption scheme (the Goldenberg Affair undertaken by President Moi’s closest affiliates) that nearly bankrupted the country (Throup/Hornsby 1998; Wrong 2009, 63; Branch 2011, 220). Mwai Kibaki, for his part – who had won the presidency in 2002 by running on a ‘zero-tolerance-for-corruption’ campaign – seamlessly took over an ongoing grand corruption scheme (the Anglo Leasing Affair, begun under President Moi). Kibaki (or his closest aids) apparently not only covered for, but most likely compensated Moi and his henchmen for smoothly handing the scheme over.

Some observers of African politics suggest that such anecdotes reveal the charade that programmatic election campaigns really are (e.g. Chabal/Daloz 1999). But a political economy reading of these events suggests that in spite of the ‘anti corruption’ efforts, another dynamic is at play that does not allow ‘truly powerful’ elites to be entirely excluded or exposed.

In the first two of these examples, Angola and Ghana, the rent-sharing mechanisms have been formalised and are thus out in the open. These are often criticised as being blatantly undemocratic features of co-opting the legislature (Amundsen 2014; Ayee et al. 2011). In the Kenyan case, such mechanisms are kept entirely informal, which is arguably closer to the norm in many developing countries. When they are discovered, the media, international partners, and the producers of global country rankings rightly condemn these as corruption. But observers are also often taken aback and react with bewilderment when discovering that some of the most progressively reform-minded opposition leaders were involved in such schemes. This is then simply explained by ‘personal temptation,’ ‘weak individual character,’ or even the ‘remnants of backward culture.’ Yet the framework introduced here can help assess these mechanisms more accurately by pointing to the systemic logic of keeping stability by avoiding power clashes.

The Limited Access Order and natural resources

4



Strategic planning at the national level presupposes a degree of cohesion and stability within the elite circle that allows the respective patrons the ‘luxury’ to try out new ways of nudging their factions towards more adding value strategies and away from hard blackmail and confrontation. The discovery of a common pool of non-tax resources (Ostrom 1990) makes this substantially more difficult.

Psychology studies have found that cattle herders tend to act more aggressively than farmers. The reason is that a herder’s entire livelihood – his cattle – can be taken away in a single night, while a farmer’s wealth, dispersed across large fields, is much less vulnerable to theft. A way for the cattle herder to pre-empt theft is to advertise a readiness to confront anyone who crosses him; hence the notion of a cowboy as bar-fighting gunslinger (Cohen/Nesbitt 1994). Governments that derive their revenues from ‘point source’ minerals tend to act like cowboys, while governments that derive their revenues from a dispersed private sector tend to act like farmers: the one sits idle, is armed, and lurks into the night, expecting predators. The other toils hard during the daylight hours, wanting to facilitate widely dispersed growth.

This section and the following two explain the empirical findings in the resource curse literature (see Section 2), using the political economy logic introduced in Section 3. The Limited Access Order framework shows why extractive governments tend to resemble Cohen/Nesbitt’s cowboys. Recall that in any limited access order (be it resource rich or resource poor), the elite circle consists largely of individuals who can muster great violence potential by mobilising their groups in the event of a power clash between factions. This is their *primary* ticket for the seat at the elite table, more so than the actual rents which their respective factions contribute to the circle. Rents derived from the various factions’ adding value activities are shared by the elites according to their respective power to hold out in the event of a conflict, not according to actual productivity levels. This is the logic of redistribution from the productive to the potentially violent that blocks the incentives for all involved to concentrate solely on adding value activities – some hard blackmail and readiness for confrontation has to be part of any portfolio for limited access order factions.

In this political environment, new rents from newly discovered sub-soil resource deposits have three effects that are immediate and distinctly recognizable: (i) the changed size of the rent-pie, which is to be distributed among elites, demands that the particular allocations are recalculated – this can be dangerous for political stability. (ii) The new source of

rents makes the elite circle instantaneously less reliant on the revenues generated by productive firms. Factions within the pyramid that, in the past, have concentrated more on adding value activities become less important to the others. As the adding-value factions are less needed, their soft blackmail strategies (i.e. to withdraw from adding value if mistreated) become ineffective and they are easily pushed to the edge or altogether out of the elite circle. (iii) Others within the elite circle, those closer to the new source of the rents, find themselves suddenly in a new, much elevated but difficult position. Their power increases substantially, but their position within the circle also becomes much more contested. They seemingly have more discretion over the allocation of rents, but in reality have to carefully estimate who among the competing elites in the circle is capable enough and most likely to try to take over their position at the gate to the new rents. Jockeying for positions inside the elite circle takes on an entirely new dynamic.²⁵

The international development community often encounters leaders of newly resource rich countries who seemingly squander their unique opportunities to invest in pro-poor initiatives. This is often met with bewilderment and attributed to ‘personal greed’ on behalf of the leaders. While such disapproving responses are understandable, the framework here shows the systemic logic at play: Newly created rents need to be invested in clienteles that stabilise the elite circles. The case studies below depict the fragility of Equatorial Guinea, South Sudan, and Chad. All three are oil states and all three are on the brink of collapse, albeit in uniquely different ways.

Looking at Equatorial Guinea, South Sudan, and Chad makes the first part of the political economy framework (Section 3.2) tangible. These African oil countries are limited access orders of the most fragile kind. They represent archetypal examples of the common ways governments in weak states attempt to deal with large revenue windfalls: repression, co-optation, and institutional reform.

4.1 Repression in Equatorial Guinea

Since independence from Spain in 1968, Equatorial Guinea has been one of the world’s most ruthless dictatorships, on par with Sudan and North Korea (Freedom House 2014). In an ethnically fractured country, the independence president, Macias Nguema, kept the governing elite to a close ethnic and where possible to a close family circle. He was mentally unstable, and in 1979 he executed (among many others) one

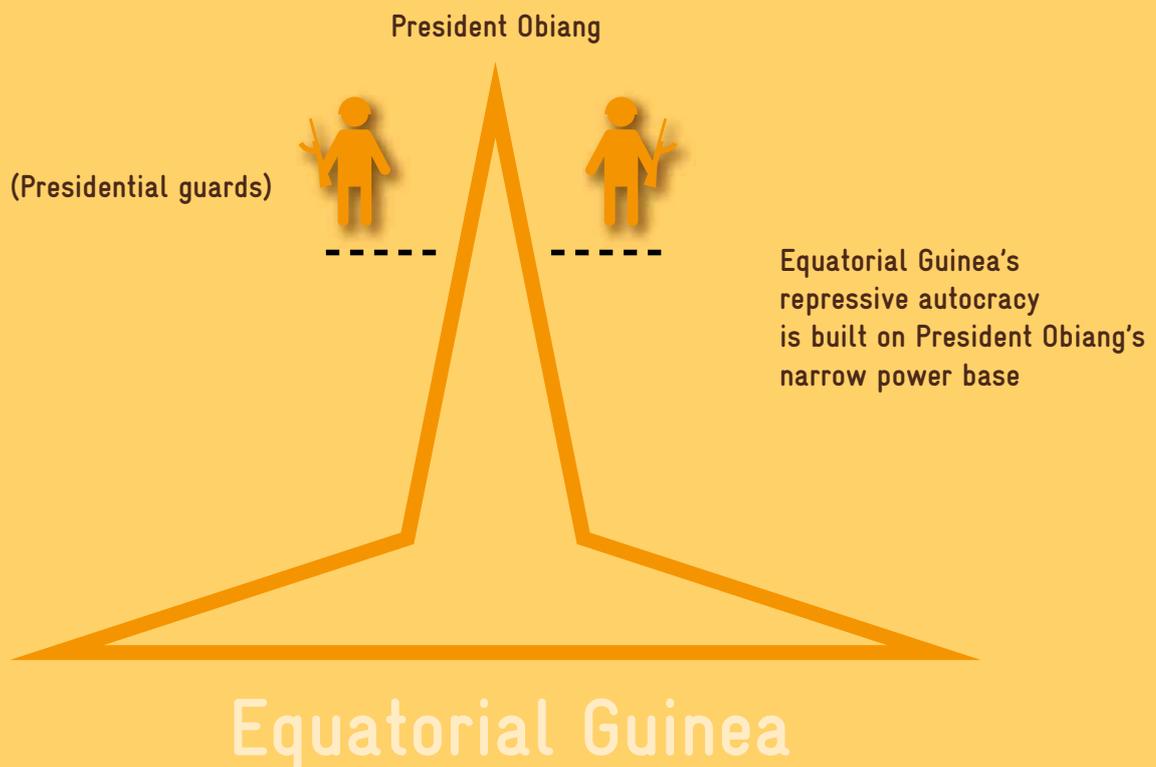
of his ministers who had also been his nephew. This prompted another minister and nephew, Obiang Nguema Mbasago, to stage a coup. Having succeeded in this, president Obiang has ruled Equatorial Guinea ever since. Yet, his rule has improved the fate of Equatoguineans only marginally: harsh dictatorial rule and economic mismanagement continue to this day.

When offshore oil was discovered in the mid-1990s, the small country's GDP started to grow rapidly (by an annual average of 16 per cent between 1997-2007). Contract conditions with foreign extraction companies (notably Mobil) were some of the world's most favourable for the companies, leaving little for the country. It was later found in a US court case, however, that these were coupled with gracious side-payments to the President and his closest aids and family. This means the president himself and his family managed the oil revenues informally. Money was stacked away in overseas accounts or invested in foreign estates (Frynas 2004; Wood 2004; Shaxson 2007, 27-40, 121-144). This is a rather com-

mon practice in weak states (e.g. see Kaunda in Zambia, Moi in Kenya, or Mobutu in Zaire). It is dubbed 'kleptocracy' and often attributed to the profligacy and greed of the leader. Yet, a look at the systemic reasons for this behaviour gives credence to how contested a political leadership position is, and how narrow the ruler's power base is.

Since Equatorial Guinea struck oil, Obiang had to avert several coup attempts. Some of the alleged plots may have been fronts for the president to pre-emptively cut emerging rival elites down. But others were real – one 2004 coup-attempt is particularly well documented as it involved foreign mercenaries (Roberts 2006). This suggests that one of the president's most urgent areas of attention, wanting to stay in power and indeed alive, is to strengthen his own violence capacity, and weaken that of potential opponents. Obiang's public appearances reflect his priorities. Journalist Peter Maass describes his impression of Obiang's visit to Ebebiyin, a town of 36,000 on Equatorial Guinea's mainland (the capital Malabo is on Bioko Island):

Figure 4: Equatorial Guinea's narrow power base



“... Obiang’s motorcade consisted of forty vehicles with enough firepower for a small war. In the lead were army-green trucks carrying elite soldiers in black ninja outfits. The jeeps in front of his armored Lexus SUV carried his Moroccan bodyguards—the president does not trust his own people to protect him—some of whom were perched on running boards, clutching machine guns aimed at the crowd. The president seemed to be invading rather than visiting. ... A few hours before the parade, several hundred soldiers— not the presidential battalion but underfed conscripts whose jungle checkpoints served as opportunities to cajole spare change from civilians—were ordered by the Moroccan bodyguards to break down their weapons to show they had no bullets. The Moroccans supervised this task with glares that made it clear that everyone they regarded was suspect” (Maass 2009).

This picture fits the power balance in Equatorial Guinea depicted in Figure 4. Power is centralised within an extremely narrow patronage pyramid. Threats to the president abound: anyone could try to topple the narrow pyramid by decapitating it – attacking the president. The greatest such threat comes from elites within or near the top of the patronage pyramid. From the president’s viewpoint, considering the country’s weak governance institutions and high risk of coups, it is rational to divert the oil money and keep much of it out the formal institutional channels, because (a) he needs to use much of the oil rents to reward his followers and repress potential rivals; (b) Equatorial Guinea’s institutions cannot provide the implementation capacity of genuine pro-poor spending programmes anyway, hence much of the resources would get lost to corruption; and (c) perhaps most important, assuming that he were to use major funds for the purpose of broad-based national development, those elites best positioned to embezzle development money could easily be *those same powerful elites who could plan the next coup against him*.

Obviously, such a politically narrow strategy makes for poor economic planning: Equatorial Guinea is today, in per capita terms as rich as an OECD-country, while the country’s Human Development Index rankings have hardly improved.²⁶ It is difficult to gauge how secure Obiang’s political situation is today, but the fact that after 35 years he is still in power shows that the strategy has worked for him thus far.

Other leaders in equally fragile countries have taken greater risks than Obiang has, in trying to govern more inclusively, be it because they saw this as the necessary strategy for

consolidating power (in South Sudan), or because they were persuaded by outsiders such as the World Bank (in Chad).

4.2 Co-optation and war in South Sudan

The 2013-14 civil war that broke out in the world’s youngest country has often been portrayed as a simple ethnic split between the Dinka of President Salva Kiir and the Nuer of former Vice President Riek Machar (Johnson 2014, 300). Yet, on its road to independence in 2011, Southern Sudan’s elite was split on many issues, notably, on whether to strive to become an independent South Sudan or to try to take power over Sudan via Khartoum. A 2005 Comprehensive Peace Agreement was signed with the Bashir government of the North and the South’s principal liberation leader John Garang. Garang passed away shortly after, and his deputy, Salva Kiir, took over. Kiir mainly attempted to (a) sooth relations with Khartoum, and (b) bring the different factions within the South together. Both South Sudan and Sudan-Khartoum are dependent on the South’s oil and on one another to export it. 80 per cent of the oil is located in the South, yet most of the infrastructure for exporting it leads through (and is owned by) the North (Natsios/Abramowitz 2011). The factions within South Sudan’s elite were split on how to proceed: some wanted to cooperate with Khartoum, others preferred to confront it (e.g. by attempting to economically cripple the Bashir regime in an oil production shut-down in 2012). Kiir’s main rival, Riek Machar, became Vice President as the country gained independence in 2011. Machar made no secret of wanting to succeed Kiir as soon as possible. Kiir’s strategy for pre-empting a hostile takeover of his government or civil war outbreaks in parts of the country was to share more rents. His practice of co-optation included disproportional salary increases to the military at crucial junctures (e.g. before the independence referendum in January 2011) and continuously turning a blind eye to the rampant corruption and human rights abuses committed throughout the SPLA (the army).²⁷ Alex de Waal (2014, 365) notes that “[w]hile he was at the apex of the system, Kiir was not in control of it.”

In mid-2013, Kiir then apparently sought to take a stronger stance against (a) those within the army who continued to block peaceful relations with Sudan-Khartoum, and (b) replace his belligerent cabinet with a more technocratic one, that would not contest his leadership as much. This resulted, five months later, in a coup attempt, which plunged South Sudan into civil war, with the two men, Kiir and Machar at the helm of the opposing sides (de Waal 2014; Johnson 2014; Natsios/Abramowitz 2011).²⁸ Figure 5 depicts this

scenario. In the early period of oil revenue flows, and in anticipation of a steady stream for the years and decades to come, two equally strong factions separate and rupture the country's power pyramid down the middle. This is the worst of all possible outcomes: both factions overestimate their relative violence potential or disregard the detrimental risks of confrontation, and civil war breaks out. If Kiir or Machar is more to blame – be it as morally ruthless or tactically naïve – is difficult to say. Kiir may have noticed that it was impossible for him to rule effectively with Machar (and others, e.g. Pagan Amum) by his side. Machar, for his part, must have recognised that with the onset of steady oil revenues to the government, he could not afford to be temporarily sidelined by Kiir, as this would most likely have led to permanent power consolidation by a Kiir-led government.

4.3 Institutional reform in Chad

In 1994, together with Exxon and the World Bank, Chad's President Idriss Déby had an elaborate plan for avoiding the resource curse: oil fields in southern Chad were to be connected to a pipeline leading to Cameroon's coast; the inflowing oil revenues would be managed externally in a London-based escrow account; and much of the proceeds were to be allocated to pro-poor initiatives according to a pre-stipulated

quota. With the World Bank largely as a guarantor (that Chad would not renegotiate after the initial investments), Exxon financed most of the operations.²⁹ All this and more (e.g. environmental and health safeguards and a future-generations fund) was stipulated in Chad's Petroleum Revenue Management Law, perhaps the most finely tuned legislation ever devised for avoiding the resource curse in a developing country (Frank/Guesnet 2009).

Once the oil started to flow, however, Déby reneged on this arrangement to use the money to instead pay civil servants and, particularly, soldiers. The budgeted money for salaries had been mismanaged (i.e. dispersed informally into patronage networks). In 2004, Déby saw that he needed to renegotiate: a rebellion from the eastern part of the country loomed and in March 2005 a military coup was averted, but in April, fire-fighting beset the capital “led in part by former government officials who sought ‘to control petroleum revenues’” (Winters/Gould 2011, 238, citing EIU). The Déby government diverted everything it could to military spending and intensified negotiations with the World Bank to transfer escrow account money directly to Chad's treasury (threatening to otherwise halt all oil production within three days). Déby's assertion that his government was under immediate threat of annihilation had to be taken seriously. The USA and France pressured the World Bank to give in.

Figure 5: South Sudan's rupture that led to civil war

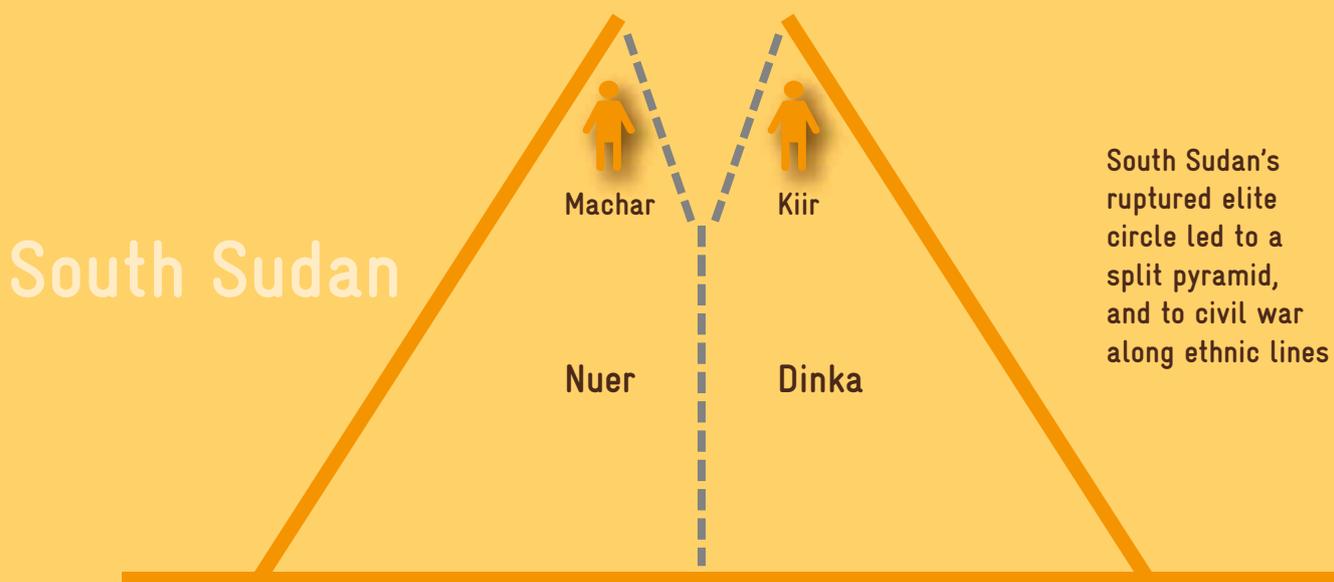
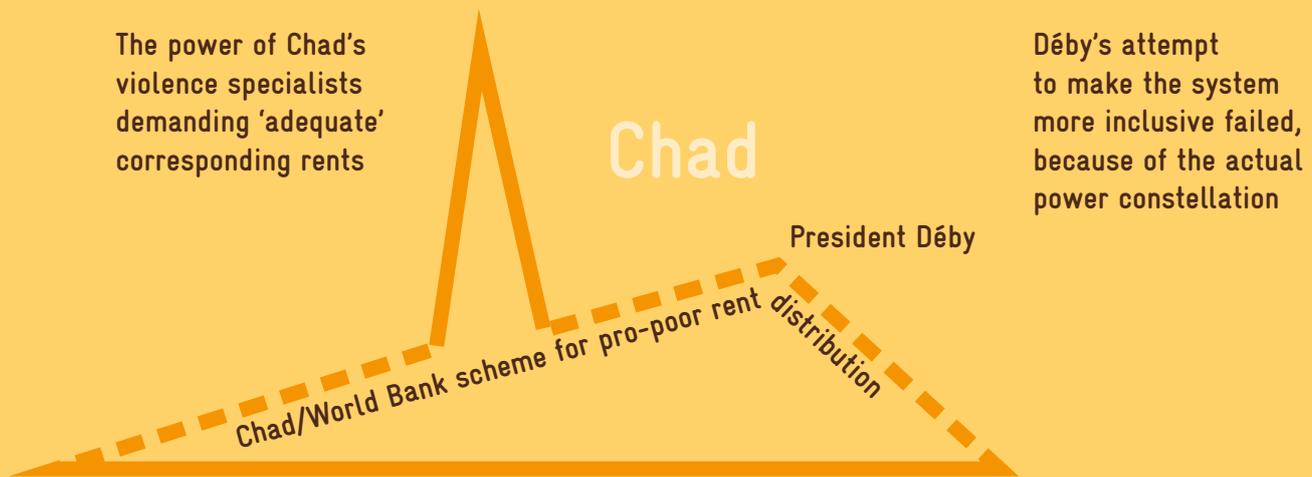


Figure 6: Chad's attempt to flatten the power structure



Source: author.

After repeated hard-fought renegotiations and several more concessions, the World Bank finally pulled out of the project altogether in September 2008.

This has been interpreted as Déby rationally taking advantage of his strengthened bargaining position: once his foreign partners had sunk costs that essentially committed them to continue, Déby could exploit them, confident that they would not withdraw, even under worse circumstances (Gould/Winters 2007).³⁰ Similar accounts accord the project's failure to poorly designed rules (Pegg 2006, 2009; Winters/Gould 2011). Yet, a political economy perspective draws attention to the clear messages Déby received from various members of the elite circle: that factional violence potential was about to be demonstrated if Déby did not 'come to his senses' and allocate the inflows according to the formula of matching the country's powerful groups' respective holding power with adequate rents. Déby realised that the political settlement he operated in did not allow him the 'luxury' of spending sizable portions of the rents on pro-poor growth initiatives. Policies that were economically and developmentally sensible were, in fact, politically impossible. The dotted line in Figure 6 depicts Déby's attempt to make the system more inclusive, only to realise that the actual power constellation (the narrow peak, towering above his flattened construct) would not permit this.

The mechanisms at play in these three countries are entirely informal but no less real. It is no coincidence that this study chose to illustrate informal power by pointing to some of the

world's most fragile states.³¹ This is where the informal system comes to the surface. What makes informal institutions so difficult to grasp for outside observers is that, even here, on the brink of collapse, they are not in plain sight. Larson et al. (2013) cite a donor official in South Sudan who

"distinguished between the 'Real Ministry of Finance' and the 'Fake Ministry of Finance.' The 'Fake Ministry' is the one working with the donors and technical advisors on budget allocations, promoting the outward appearance of high functionality, while the 'Real Ministry' is operated through backdoor dealings between South Sudanese officials, concealed from donor view. As the donor official says: 'The technical advisors help prepare budget allocations, but then the army generals wheel into the minister's office, and they make the real allocations.'" (Larson et al. 2013, cited in de Waal 2014, 359-60).

In countries that are more stable than Equatorial Guinea, South Sudan, or Chad, these informal mechanisms are more concealed. Rule-of-law institutions, copied from the OECD-world, hide the actual rules of the game. Such 'isomorphic mimicry' makes it difficult for outside observers to see that the informal institutions of accommodating factional patrons still lie at the core of political conduct.³² The next two sections depict more stable cases where the signs are subtler, but the same logic is at work.

The Politics of Industrial Policy and natural resources

5



Creating sustainable employment for large segments of the population has to be at the core of any inclusive growth strategy, be it with or without extractive resources. This means nudging elites toward specialising in adding value activities. To recap, the mechanism that keeps developing countries peaceful is that rents generated by productive groups are continuously shared with groups that threaten to otherwise disrupt the peace. This is obviously a second-best solution: a more efficient solution – one exercised throughout the OECD-world, but one for which the state in developing countries lacks the organisational capacity – would be to punish unproductive blackmail and confrontation activities, while rewarding only adding-value activities by letting producers keep more of their rents. The second-best equilibrium in developing countries can only be overcome if hard blackmail and confrontation become less worthwhile strategies. The Politics of Industrial Policy framework (introduced in Section 3.2) depicts the triangular relationships between political elites, economic entrepreneurs and state bureaucrats that provide the conditions needed for *getting from here to there*. The exact mechanisms of how this emerges and unfolds are not yet well understood. But historical cases suggest that it is a piecemeal process that is prone to reversals.

A common pool of rents derived from extractive point-source resources distorts all three corners of the triangle away from adding value: most essentially, political elites, to survive at the top of resource-driven economies, *no longer depend on revenues from value adding firms*. Instead, elites need to carefully balance the resource rents among the members of the elite circle. Diverting rents toward industrial policy initiatives solely on an efficiency criterion can (i) distort the power equilibrium by creating new strong forces that then have to be reckoned with politically, and, more importantly, (ii) create anxiety among other elites, who feel they are being passed over if part of ‘their share’ of the rents is allocated elsewhere. Such anxiety is not simply based on material greed or paranoia: a patron whose faction’s holding power is noticeably larger than the share of the rents she draws, will be expected to address this misalignment. This, in turn, makes it harder for entrepreneurs, together with the Dutch disease effect, to concentrate solely on adding value. The alternative strategies of blackmail and confrontation become more viable. Lastly, state bureaucrats for their part, no matter how competent, can only ever act upon a developmental vision if political elites genuinely endorse it. Building on Figure 2 above, Figure 4 illustrates how extractive resource rents shrink the space for adding value activities and genuine industrial policy in all three corners of the triangle (depicted by the the circles filled with the bad incentives that come with resource rents).

By using examples from Mozambique, Angola, and Nigeria, the case studies below show different ways this dynamic can unfold.

5.1 Collusion in Mozambique

As a Portuguese colony, Mozambique was one of sub-Saharan Africa’s eight most industrialised countries (Buur 2014), but shortly after gaining Independence in 1975, the two regio-political factions – FRELIMO (strong in the more developed south of the country) and RENAMO (strong in the poorer rural centre and north) – plunged Mozambique into a 16-year civil war (Levy 2013, 132-133; Pitcher 2002, 172). This completely destroyed Mozambique’s industry. After the war, the Cahora Bassa mega dam (comparable to the Hoover Dam in size and electricity generation) was repaired by 1997 (Xiong 2014, 26), which provided enough power to build a large-scale, multinational company-driven smelter, MOZAL (begun in 1998) that turns imported bauxite to aluminium ingots.³³ Mozambique has also recently discovered large quantities of natural gas and coal, and is thus expected to become the world’s eighth largest exporter of both liquefied natural gas and coal (Xiong/Melina 2014, 143). To date, MOZAL aluminium exports are still at the core of Mozambique’s economy.

Mozambique’s industrial policy began with MOZAL’s two construction phases (1998-2000 and 2001-2003), and a series of initiatives that followed in 2001 (the SME Empowerment & Linkages Programme by BHP Billiton), 2002 (Mozlink I), and 2007 (Mozlink II), which sought to provide linkages to the mega-project by binding local ownership stipulations to SME supplier firms (Krause/Kaufmann 2011, 49ff). The International Finance Corporation and other donors helped, particularly by attempting to create pockets of efficiency in the state bureaucracy.

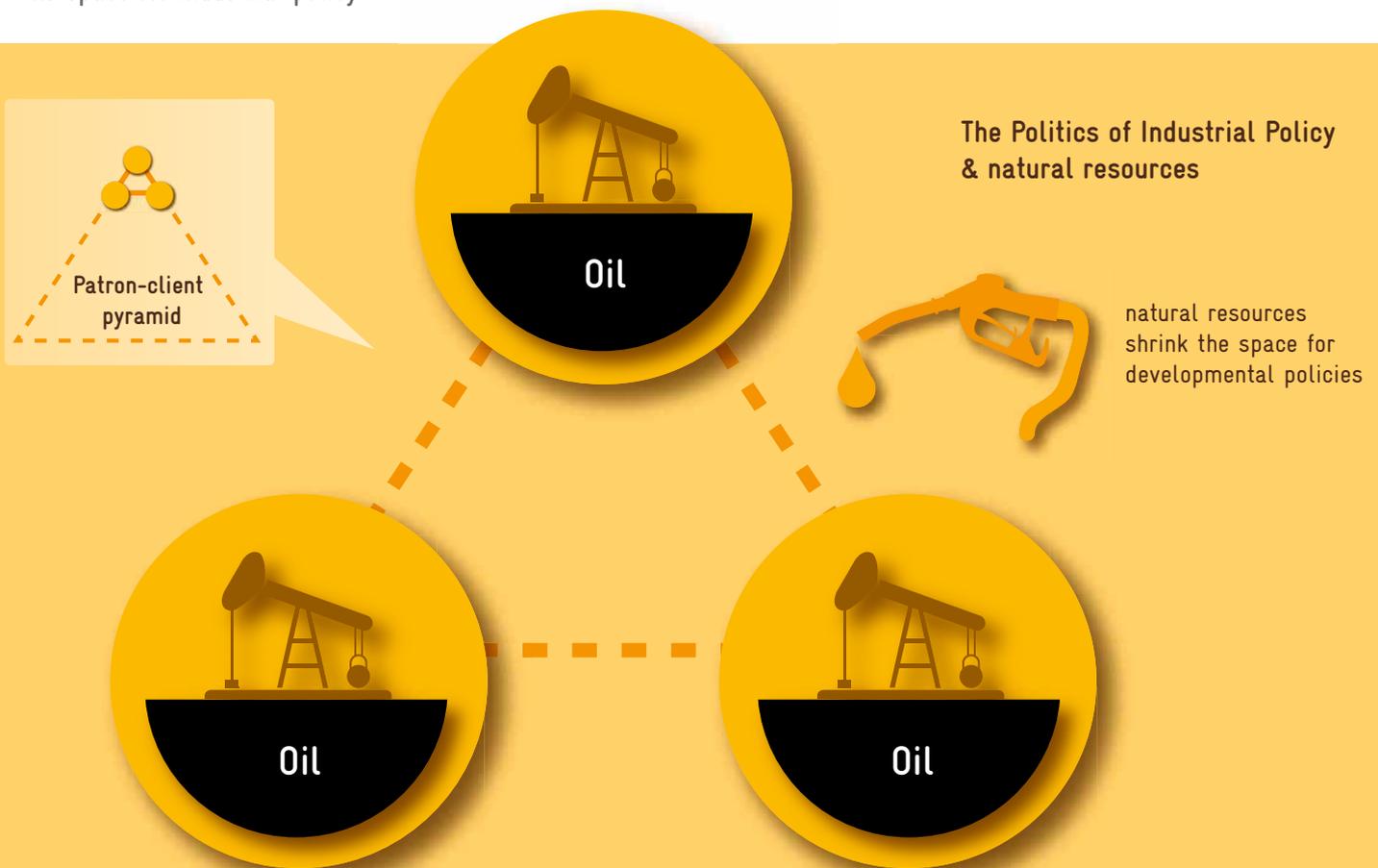
Initially, under President Joaquim Chissano’s leadership (1986-2005), power within the ruling FRELIMO was fairly balanced across different factions. But under his successor, President Guebuza (2005-2014), power became more narrowly concentrated within the ‘Guebuza faction’ (Buur 2014, 19). Chissano was generally seen as the wiser and more developmental leader. He had ended the war, initiated successful disarmament, and brought the large-scale industrial policy projects underway. His wife hailed from Northern Mozambique, and, known for his openness to dialogue, Chissano was trusted by RENAMO leaders. After his decision not to run for a third term, he received the

first-ever Mo Ibrahim Prize for African Leadership in 2007 (*The Economist* 25th Oct. 2007, and 9th Nov. 2013).

President Guebuza, by contrast, had been a southern business tycoon, whom northerners regarded with suspicion even before he came to office. He was associated with a more chauvinistic FRELIMO faction, and, once in power, he swiftly tightened the circle of elites around him. This coincided with a 2005-2007 up-scaling of extraction FDI for coal and limonite explorations. In 2005 alone, the amount of extraction-related FDI that came into Mozambique was a quarter of the country's GDP (*The Economist* 29th Nov. 2007). While it cannot be proven that the new resource rents played any role in it, the tightening of the Guebuza faction's grip on power did coincide with this inflow of new revenues.³⁴

The responsible state bureaucracy and those in the private sector who received industrial policy support were all closely enmeshed with the Guebuza network. SMEs approved by the state for MOZAL providers were often created for the purpose. Similarly, in anticipation of future gas extraction, in the state bureaucracy, "all the top senior government officials and bureaucrats in the INP [the National Institute for Petroleum], ENH [the state-owned oil company] and MIREM [the Ministry of Mineral Resources] have established companies that can service the oil and gas sector, because they enjoy 'privileged access to information on the country's natural resources'" (Buur 2014, 21, citing CPI 2010). Foreign companies have little choice in picking from a small pool of politically connected domestic partners (Buur 2014; Nuvunga 2009). The state's pockets of efficiency are arguably ineffective because they were externally induced (donor-driven). As Buur et al. (2013, 72) note:

Figure 7: Natural resource rents minimise the space for industrial policy



Source: author, based on Figure 2 (above), and on Whitfield et al. (2015).

“Over the last ten years, Norway has specifically concentrated its support on the National Petroleum Institute, as well as the Mozambican tax authorities (in the latter case, together with other donors). Nevertheless, major decisions have been taken by the Executive without much usage of the competent institutions: their advice has even been wholeheartedly ignored in the case of linkage creation policies. For gas and mining contracts, while capacity has indeed been created, competent agencies often end up playing ‘catch up’ using acquired knowledge and skills to justify or mitigate decisions taken by the executive instead of informing such decisions.”

However, as the case of Angola will show, genuinely home-grown state efficiency is no panacea either. To the contrary, powerful state pockets of efficiency can help entrench economic inertia just the same.

5.2 Abused state efficiency in Angola

Angola’s \$104bn GDP is mainly derived from the roughly \$70bn of its annual oil exports (APP 2013, 43, 48).³⁵ In the triangle of political elites, economic entrepreneurs, and state bureaucrats, Angola’s oil sector is remarkable for the latter. Since Independence from Portugal in 1975, Angola’s state-owned oil company, Sonangol, has consistently grown in size and efficiency. Beginning with a smooth transition from the Portuguese Petrogal, Sonangol was led by practically minded technocrats who carefully sought out a diversity of external advisers (e.g. Algeria’s SONATRACH, Italy’s ENI, or Arthur D. Little Inc.). Throughout its 29-year existence, Sonangol’s leadership has been closely enmeshed with and trusted by the political elite around Presidents Neto and dos Santos. In the international oil industry, Sonangol has gained the reputation of a competent and reliable (if secretive) business partner. This allowed Sonangol to attract numerous foreign partners to Angola, and to become an exceptionally tough negotiator. Sonangol has also diversified up- and down-stream, and into a myriad of other fields at home and abroad (many entirely unrelated to oil, such as airlines, luxury home building, or telecommunications). It has also established a parallel state apparatus for services (notably financial services), which the rest of Angola’s dilapidated bureaucracy could never provide. This ‘efficiency miracle,’ remarkably, took place in complete insulation from the ruling MPLA’s otherwise socialist ideas that dominated the rest of the Angolan economy into the 1990s (Sonangol was able to reassure American oil companies, Gulf Oil and Chevron, that their investments were safe), and, more surprisingly, this happened in the midst of

an intermittent but devastating civil war that only ended in 2002 with the death of UNITA’s rebel leader Jonas Savimbi (Soares de Oliveira 2007, 596-7).

Tellingly, only one other branch of Angola’s state is as well-equipped as Sonangol: security. Angola has one of Africa’s largest militaries, several internal security organs and a sophisticated intelligence service (Soares de Oliveira 2007; Amundsen 2014, 179). This suggests that the Sonangol ‘efficiency-island’ serves a narrow political elite. And indeed, for all the wealth generated by Angola’s oil industry, strikingly little, even compared with other low-income oil exporters, has trickled down to Angola’s poor. While *The Economist* (8th Feb. 2011) ranked Angola’s capital Luanda ‘the most expensive city in the world,’ most Angolans remain among the world’s poorest: 70 per cent live under the poverty line (Amundsen 2014, 174). Average annual GDP growth has been 10 per cent from 2000 to 2010, but Angola’s human development rank is 148th, average life expectancy is 51 years, and child mortality and maternal health rankings are among the worst in the world (APP 2013, 22-27). Soares de Oliveira writes:

“Sonangol’s undeniable competence and sophistication are not, and have never been, put at the service of Angolan development, however defined. Instead, the company is the pivotal tool for the interests of the presidential clique known as the Futungo de Belas. The Futungo, a nebulous group of unelected officials and businessmen around President Eduardo dos Santos, became the key structure of power in the 1980s, in tandem with the relative sidelining of MPLA party organs and formal state structures. Sonangol essentially exists to harness and further their agenda” (2007, 606).

Furthermore, in stark contrast to Sonangol’s good reputation in the oil industry, Soares de Oliveira describes: “it is impossible to engage in [Angola’s economy outside the oil enclave] without encountering its rentier, unproductive dominant logic” (2007, 612). Other than Sonangol’s efficiency in the business of oil rent extraction, the elite tightly controls the home market and has no discernible interest in becoming globally competitive. He notes:

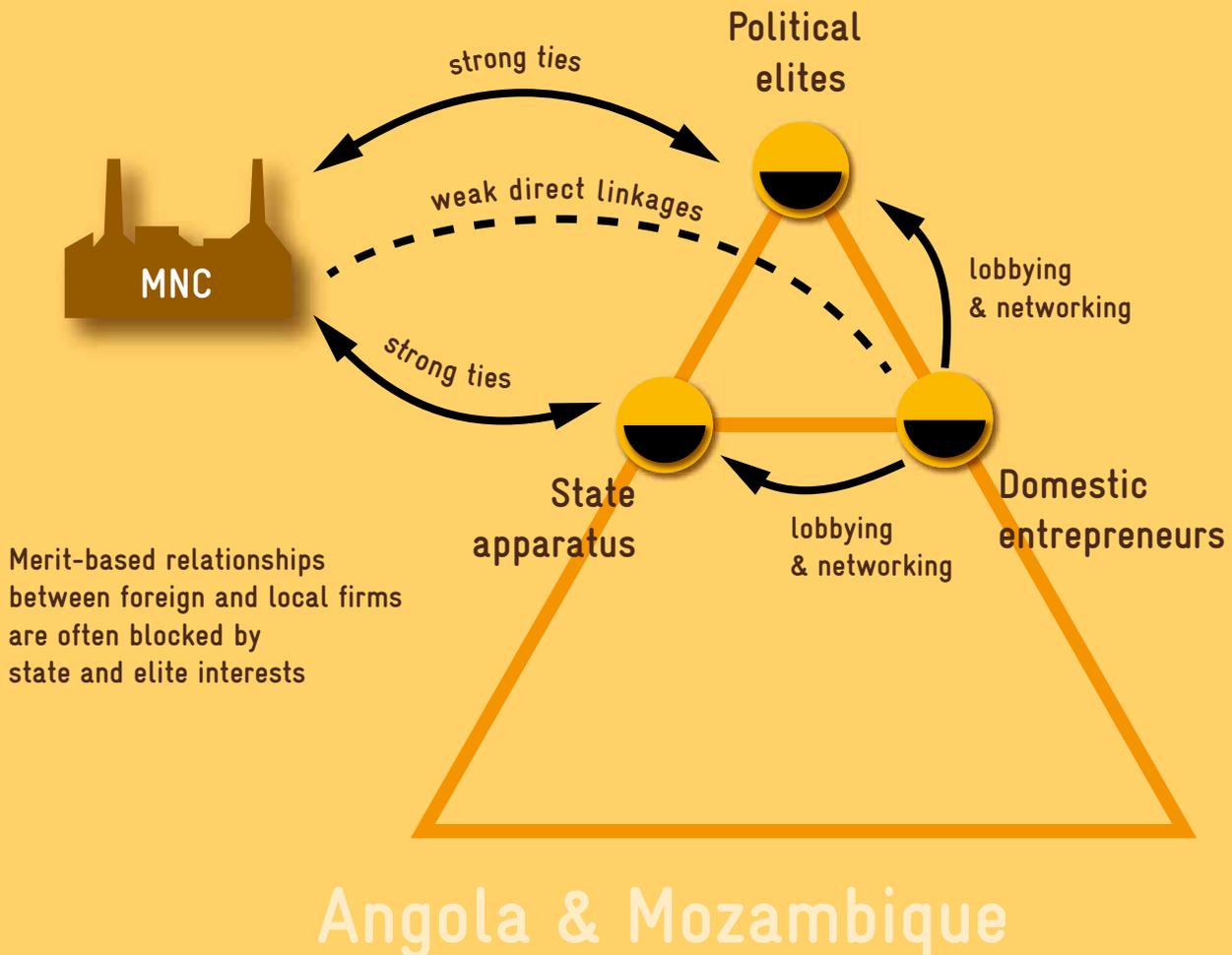
“A look at many characters benefiting from this sort of uncompetitive behaviour is a veritable who’s who of the Futungo and the upper ranks of the bureaucracy, the military, the party, and their families. Unsurprisingly, it also includes most current or past senior technocrats of Sonangol itself. Indeed, while interviews with many of these officials are replete with formulaic expressions of a

desire to roll back the patrimonial character of Angola's political economy, they do not actually envisage having to compete in a genuinely open market. ... Sonangol is busy creating opportunities for well-connected but non-entrepreneurial individuals with little value added for Angola, while genuine entrepreneurs face formidable hurdles in all lines of business. This strategy essentially aims to secure continuing support for the presidency by sharing rentier opportunities and some of the spoils of the oil boom across the elite" (Soares de Oliveira 2007, 608).

This verdict of Angola as a failed but nonetheless (for the elite) successful state is shared by other observers (e.g. Amundsen 2014; Shaxson 2007, 41-62) but is relativised by slightly more optimistic accounts by Ovardia (2012a) or Teka (2012), who see some progress in Angola's linkage promotion policies. Ovardia finds that:

"[t]he promotion of Angolan ownership can lead to a variety of outcomes, since there are good Angolan partners and bad ones. Some companies pay an Angolan face to do what they want or simply to do nothing at all, while other Angolan partners do a great deal of work for their 51 per cent of the company" (2012a, 412).

Figure 8: Mozambique and Angola – The state blocks adding value collaborations



Source: author, based on Figures 1, 2, and 7 (above).

Yet, the Angolan state's dominance, economically via Sonangol and coercively via the security apparatus, is undisputed. This *would* provide the political elite with the needed stability to engage in long-term economic planning for increased value addition, but the oil revenues seem to quash any incentives for this. Sonangol serves as a warning for those who see weak state capacity as the core obstacle to development: in the service of Angola's crony elite, it is Sonangol itself that, for the time being, crowds out any notion of entrepreneurship for adding value to Angola's economy. Figure 8 shows the triangle of political elites, the state apparatus, and domestic entrepreneurs within the peak of the patron-client pyramid. In Mozambique and Angola, strong ties between multinational companies (MNCs) and both, the political elite, and the state apparatus do exist (shown by the solid two-way arrows between them). Yet, between MNCs and domestic entrepreneurs, only weak direct linkages exist (shown by the dotted line between them). Domestic entrepreneurs cannot freely partner with MNCs on the basis of their good ideas and honest work alone. Rather, to get selected for such partnerships, they must have patrons among the elite, or in Angola's case within Sonangol. This creates an incentive-blockade against efficiency-enhancing activities among domestic firms. A strategy of lobbying and networking serves them better than a genuine adding-value strategy.

5.3 From blackmail linkages to real linkages in Nigeria

Africa's largest country (for long measured in population and as of 2014 also in terms of GDP) is perhaps the most commonly cited example for the 'resource curse' (e.g. Sala-i-Martin/Subramanian 2003, 2013; Lewis 2007, 238-267; Shaxson 2007, 9-26). Exporting \$100bn of oil annually, Nigeria is almost as oil dependent as Angola (APP 2013, 43). But with a population of roughly 170 million (seven times that of Angola), Nigeria's political elite consists of a more heterogeneous circle. The regime is, compared with Angola's, also noticeably more open to political competition. The governments of Presidents Obasanjo (1997-2007) and Jonathan (2010-2015) have repeatedly appeared refreshingly democratic and reform-minded. But Nigerian governments have also often brazenly reverted from this, which leaves observers with the impression that the periodic 'good governance' reforms are smokescreens. (Angola, by contrast has, until recently not bothered with smokescreens) (Shaxson 2009; EIU 2014b).

Over the course of its oil-exporting years (since 1956), Nigeria has particularly suffered from corruption and political instability. In Angola, the war had been financed by foreign powers and conflict diamonds, but its offshore oil provided, if anything, stability to the government. This was different in Nigeria. The 1967-70 Biafra War was an attempt by the eastern Igbo to secede with the oil rich Niger Delta. Two million Nigerians died in this war, mostly civilians, starved by blockades.

With the war's end in 1970, oil production picked up, and the government attempted to make the enclave oil industry into a driver of national development. The Petroleum Act of 1969, the Joint Operating Agreements (1991), and Production Sharing Contracts (1993) were attempts to elevate Nigerian firms and workers. Yet, these policies exclusively served the top-echelon elites, without discernable 'trickle-down' effects to other Nigerians. Xavier Sala-i-Martin and Arvind Subramanian (2013) have captured this predicament in numbers:

"Over a 35-year period [1965-2000], Nigeria's cumulative revenues from oil (after deducting the payments to the foreign oil companies) have amounted to about US\$350 billion at 1995 prices. ... Between 1970 and 2000, the poverty rate, measured as the share of the population subsisting on less than \$1 per day, increased from close to 36% to just under 70% ... [This kept] Nigeria among the 15 poorest nations in the world for which such data are available. ... Similarly, mortality under 5 was of 186 for 1,000 live births in 2000, the seventh worst position in the world. ... To illustrate, whereas in 1970 the top 2% and the bottom 17% of the population earned the same total amount of income, in 2000 the top 2% had the same income as the bottom 55%. ... In 1965, when oil revenues per capita were about US\$33, per capita GDP was US\$245. In 2000, when oil revenues were US\$325 per capita, per capita GDP remained at the 1965 level. In other words, all the oil revenues—US\$350 billion in total—did not seem to add to the standard of living at all" (Sala-i-Martin/Subramanian 2013, 571, 572, 573).

In the teeth of these statistics, political stability was always fragile, particularly in the poorer regions of the predominantly Muslim North (see e.g. the menace of Boko Haram), and in the oil-producing swamplands of the South, the Niger Delta. Since the 1990s, anti-regime activities sprang up in the Delta, prominently inspired by the Ogoni activist Ken Saro-Wiwa. Since his controversial execution in 1995, several militia groups have taken over, wreaking havoc in the Delta to this day. Initially led by Alhaji Dokubo-Asari (an

Ijaw) and the Movement for the Emancipation of the Niger Delta (MEND). These groups make a living from a peculiar mixture of fighting and protecting the foreign companies operating in the Delta. Michael Ross writes:

“[Dokubo-Asari’s] deputy, Alali Horsefall, told a Crisis Group researcher he had earned upward of \$7,000 a month from Shell contracts held by his company, Du-koaye Security Services, for security, surveillance, and community development—as well as oil well services such as generator repair which, he admitted, it had no capability to supply. He also said he had contracts with oil service contractors Daewoo, Nissco, Willbros, and others. When asked how a leader of what was then the Delta’s most feared militant group had acquired contracts with foreign oil companies, he replied: “If they don’t want to, then I will fight them” (2012, 122, citing ICG 2011).

The Nigerian government tried to undermine such blackmail by periodically launching military offenses in the Delta. A 2009 amnesty declaration then brought about a ceasefire that has reduced militant attacks on companies, but this impunity also greatly increased crude theft. It is an open secret that large parts of the state apparatus also cooperate with these rebels in systematic crude theft. The regular barge traffic that takes looted crude to sea, for example, could not otherwise continue as smoothly as it does (Katsouris/Sayne 2013).

This type of collusion in unproductive rent seeking also led most of Nigeria’s earlier linkage policies to fail. In the 1970s, local content in the oil and gas industry was around 4 per cent, and by 2004, this had risen to only around 20 per cent (UNCTAD/CALAG 2006, cited in Adewuyi/Oyejide 2012). Several other industrial policy initiatives also failed. “Oil revenues financed the building of the famous Ajakouta steel complex in the 1970s, which until today has not produced a commercial ton of steel” (Sala-i-Martin/Subramanian 2013, 596).

Yet, in spite of all this, more recent efforts to promote genuine Nigerian content in and around the extractive sector seem to be more successful. By 2009, local content stood at 39 per cent (Adewuyi/Oyejide 2012). This is still lower than in Brazil, Malaysia, or Venezuela, where local content is 45–75 per cent, but much higher than in Angola (Morris et al. 2012, 89). In 2005, a set of 23 Directives for low technology sourcing on-shore has, according to the Nigerian National Petroleum Corporation (NNPC), made a substantial impact between 2005 and 2008. Some of the major achievements

over this period were listed as: a sevenfold increase in fabrication tonnage in Nigeria; a five- to tenfold increase in fabrication yard lifting capacity; a 12-fold increase in the number of engineering person-hours performed in Nigeria; and two international engineering firms having set up shop in Nigeria (NNPC 2008; cited in Ovidia 2013a). The executive secretary of the Nigerian Content Development Monitoring Board, Ernest Nwapa, asserted in a 2010 interview “that engineering ‘manhours’ performed in Nigeria are now ‘in excess of 3.5 million’ (out of a total of roughly five million hours per year available)” (Ovidia 2013a, 264, quoting Nwapa). In 2010, the government also followed up with an extremely ambitious Nigerian Content Act (NCA). It may be too early to gauge the NCA’s short-term impact, but two recent studies (Adewuyi/Oyejide 2012, and Ovidia 2013a) have reached tentatively positive conclusions. An earlier study (Heum et al. 2003) had found that, of Nigeria’s extractive linkage sub-sectors, seven³⁶ revealed local capabilities that were closest to the needs of the oil and gas industry. Of these seven, Adeolu Adewuyi and Ademola Oyejide (2012) examined three: fabrication & construction; well construction & completion; control systems & information-communications technology (ICT). Using standardised questionnaires, they obtained information from 12 large, mostly foreign oil companies (of a total of 45 such companies operating in Nigeria), and from 80 local oil and gas services firms (of a total of approx. 230 companies). While the local services firms rated the quality and frequency of contacts with the large lead companies as ‘on an arm’s length’ basis, and wished for more contracts, nine of the 12 large oil companies claimed to be purchasing more than half of their goods and services locally in Nigeria and to have ‘good working relations’ with their local first tier suppliers.

Yet, multinational companies’ claims to be sourcing above 50 per cent locally may, on its own, be less promising than it seems. Multinationals are keenly aware of the pressures they face in Nigeria, especially since the Nigerian Content Act. Such questionnaire responses are difficult to validate and the numbers could be inflated.³⁷ Assuming this 50 per cent figure correct, first-tier supplier firms could still merely be owned by Nigerians who are paid to act as façades for foreign firms. The local-content literature is replete with examples of such Potemkin-village firms throughout the developing world, and Nigeria has seen its share of them in past decades (Ovidia 2012b).

Adewuyi/Oyejide’s most promising finding is thus not the link between multinational extraction companies and their first-tier suppliers, but the link between first-tier suppliers and second-tier suppliers. In two of the three sectors

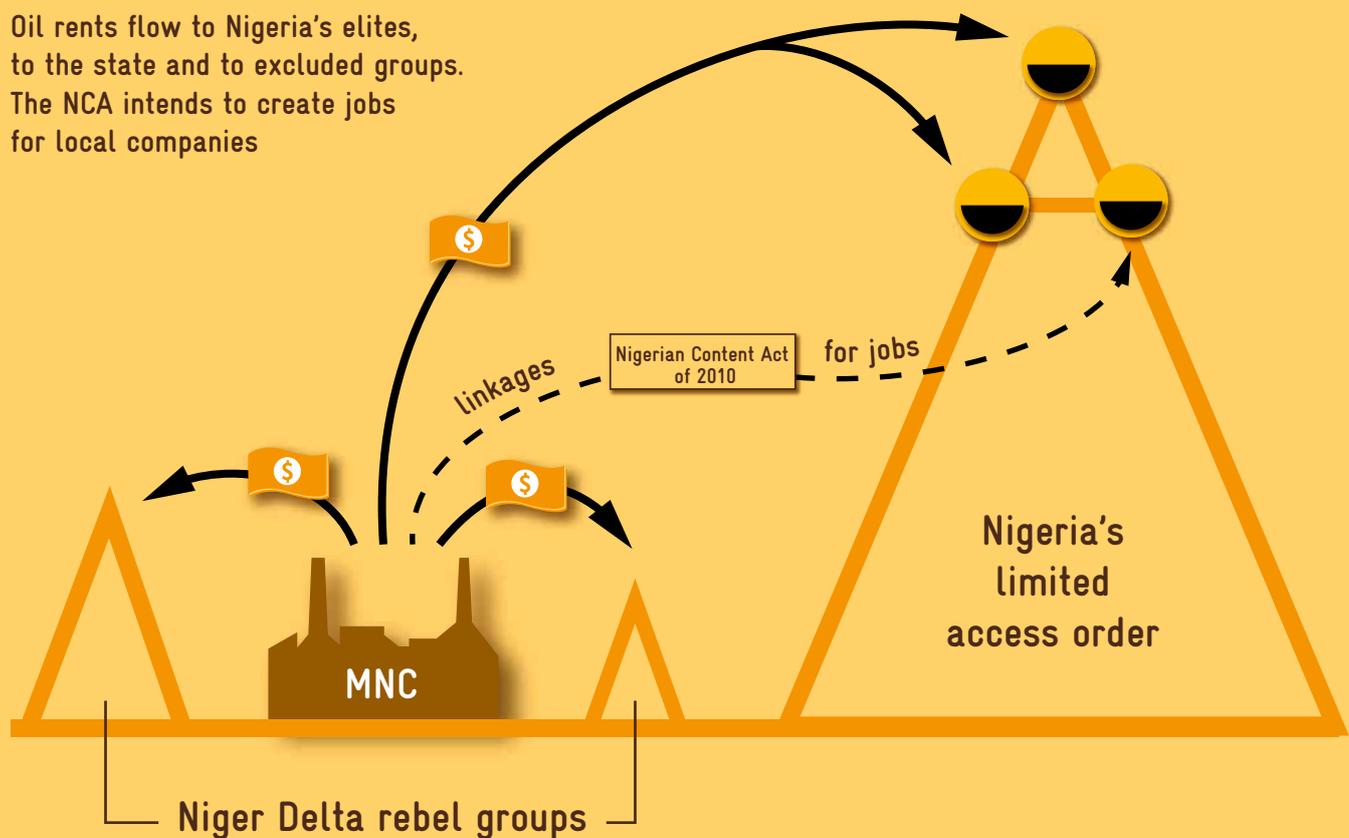
examined, they found that sizable linkages to second-tier supplier firms did indeed exist: 41 per cent of the responding well-construction and completion firms, and 46.5 per cent of the responding fabrication and construction firms claimed to source *more than three-quarters of their inputs domestically*. This figure, if accurate, suggests tangible headway in Nigeria's local linkage formation in these two sectors.

Indeed, a wider turnaround seems to be underway in the entire oil services sector. Jesse Ovadia notes a general change in perception among those active in Nigeria's oil and gas industry. He quotes an NNPC official who notes: "The

major thing is that you can no longer ignore it. [E]veryone in the industry must think about our [NNPC's] goals in terms of local goods and services." (Ovadia 2013a, 265). This same NNPC has long been infamous for embezzlement and collusion with the elite,³⁸ but the sentiment of an ongoing change in Nigeria's oil industry is not limited to spokespersons of state-owned enterprises. Citing interviews with private oil services companies, Ovadia goes on to note:

"The shift, according to many Nigerians in the industry, is already occurring from rent-seeking to productive enterprise. According to Fabian Ajogwu: 'I think if we

Figure 9: Nigeria's fractured Delta, and linkages to the oil sector



Source: author.

don't truncate what has been started in the next two to three years, we'll see the direct results ... a shift to a more capitalistic form of business with emphasis now on participation rather than rent-seeking. You will not be able to sit and collect rent. You will have to now go at it, work it, do it yourself'. Ajogwu also confirms that the shift is already underway: 'I already see my friends getting involved, bringing in rigs. There are all kinds of transactions coming in now ... It's already occurring'" (Ovadia 2013a, 269).

This economic development is cause for optimism. And it is reinforced by a more recent political event that leaves most Nigerians hopeful for progress. Contrary to many outside observers' expectations (Moss 2015; *The Economist* 1st Apr. 2015a; Campbell 2015), Nigeria's 2015 presidential elections have led to a democratic and peaceful changeover of power from President Jonathan, who accepted defeat to his northern challenger Muhammadu Buhari. Buhari's campaign was centred on fighting corruption and creating a society that is less collusive and more merit-based, and his modest personal lifestyle and past political record (as military head of state 1984-1985, and his 'war against indiscipline') make this claim believable for many Nigerians. The large numbers of southern Christians who cast their vote for Buhari also surprised observers (*The Economist* 1st April 2015a). Together, these two developments – Nigerian Content successes in oil and gas, and the prospect of more rigorous leadership in State House – may spark the turnaround that Africa's largest country has long awaited (cf. *The Economist* 11th April, 2015).

Figure 9 depicts the decentralised rent-seeking, where excluded groups in the Niger Delta (the smaller pyramids) compete for rents from the oil sector with the country's state and elite (depicted by the money-arrows flowing from the multinational extraction company). Simultaneously, Nigeria's linkage policy (most notably the Nigerian Content Act of 2010), seeks to create linkages between the multinational companies and the domestic entrepreneurs. [preferred location for Figure 9 is here]

These three case studies show that with natural resource rents, it becomes more difficult to kick-start the elite-bureaucrat-firm triangle in the direction of genuinely adding value. In Mozambique, development partners were unsuccessful in their attempts to create bureaucratic pockets of efficiency, insulated from the political elite, even before the resource rents started to flow. The Sonangol 'efficiency miracle' – which enjoys complete trust and autonomy from the Angolan political elite, but nonetheless hampers the rest of the economy's development – shows that pockets of efficiency alone are not enough to set a country on the path toward adding value. In both, Mozambique and Angola, the state blocks fruitful collaborations between technologically advanced foreign firms and domestic firms ready to learn and add value. Nigeria's case shows that without the state's hand, different, but equally grave problems can emerge: in the Delta, what looks like linkage creation via local maintenance and security services on paper is, in reality, a confrontational protection racket. Yet the Nigerian case also shows that even in a fractured society, policy efforts for local content can lead to the desired outcomes. The next section delves deeper into the difficulties faced in sub-national extraction localities.

6

Regional politics and natural resources



Approaches to local socio-economic development near extraction sites have primarily taken two forms: (a) corporate social responsibility measures by foreign extraction companies directly, and (b) development via local political leadership. International donors often support both approaches, but while corporate social responsibility measures are, by their nature, limited in scope and longevity, fiscal decentralisation to lower levels of government are more sustainable and widely viewed as more aligned with the aid effectiveness principle of local ownership. This section picks up where the Niger Delta problems in the Nigerian case study left off, and examines the decentralisation of extractive resource revenues, and the political economy relations between the central government's top-level elites and the lower-level elites of resource rich regional governments.

Recall from the political settlements analysis in Section 3.3 that the top-level elites base their power in great part on the allegiance of lower-level elites. If the latter are regionally based, they will demand a share of the rents for their region that is in accordance with their holding power (the region's patron's disruptive capacity). If natural resource reserves come into play, the dynamic is changed, and substantially so for the particular region underneath which these resources happen to be located. The holding power of that region's patron exponentially increases, as a successful secession would promise this patron nearly 100 per cent of the resource rents.³⁹ This is why co-optation alone is not deemed enough for many limited access order top-level elites. In Nigeria the top-level elite regularly combines informal co-optation (letting the oil theft continue or even cooperating in it), and repression (via occasional military raids in the Delta), and divide and rule (by explicitly fuelling animosities between particular local groups) (Shaxson 2009; Watts 2007).

As in Nigeria, many countries have tried to constitutionally co-opt their resource rich regions via decentralisation measures. The case studies below depict the decentralisation experiences from Peru and Ghana and give a glimpse of what could be in store for Kenya in the near future.

6.1 Decentralised violence in Peru

Peru has recently scaled up its longstanding mining activities. Today Peru extracts sizable quantities of tin, lead, molybdenum, gold, and is the world's largest producer of silver, and the world's second largest producer of copper and zinc. Throughout the 2000s, Peru's macroeconomic management was sound and poverty levels plummeted from 54

per cent in 2002 to 36 per cent in 2008 (Peru 2009, INEI 2009, cited in Arellano-Yanus 2011, 620). In 1992, a fiscal decentralisation law stipulated that 20 per cent of extraction company income tax payments were to be devolved to the resource rich regions. In 2001 this was increased to 50 per cent, and in 2004 another amendment stipulated that yet more specific recognition was to be given to the particular *localities* in which extractive activities take place (i.e. more funds would go to the third and lowest tier of government). This led the bulk of the transfers to mining areas, inhabited by less than one fifth of Peru's population. It also coincided with enormous commodity price booms for these minerals. Arellano-Yanus writes: "these transfers amounted to an average of nuevos soles 426 (US\$142) per capita for the country as a whole, but close to nine times that level for the Moquegua and Tacna mining regions" (emphasis added). Yet, "the frequency of social conflicts in the country has increased considerably, from 47 conflicts in February 2004 to 197 in December 2008; and [...] these increases are heavily concentrated in the mining regions" (2011, 623, 624). In his award-winning study, Arellano-Yanus was able to show that these preferential treatments of mining localities not merely coincided with, but actually *caused* prolonged violent conflicts. These conflicts took several different forms: some were of the type that is widely documented in the literature, where local community activists protest the presence of mining companies. Yet, more frequently, extraction related conflicts had to do with sub-national border disputes, particularly around extraction sites. This implies that the rent stream coming down from the central government, instead of having the democratising effect of bringing government closer to the people, actually incentivised local politicians to incite violence against neighbouring communities, with the aim of, eventually, redrawn sub-national boundaries at extraction sites (Arellano-Yanus 2011, 632-633). Such experiences lead Oxford economist Paul Collier to advocate equal national shares of mining rents, with no preferential treatment for mining regions (apart from compensating for environmental degradation and relocation schemes), because this could easily incentivise a run-away process of demands for preferential treatment in ever-smaller areas (Collier 2010). A related problem with decentralising mining revenues is often increased corruption and collusion with foreign companies as seen in the case of Ghana.

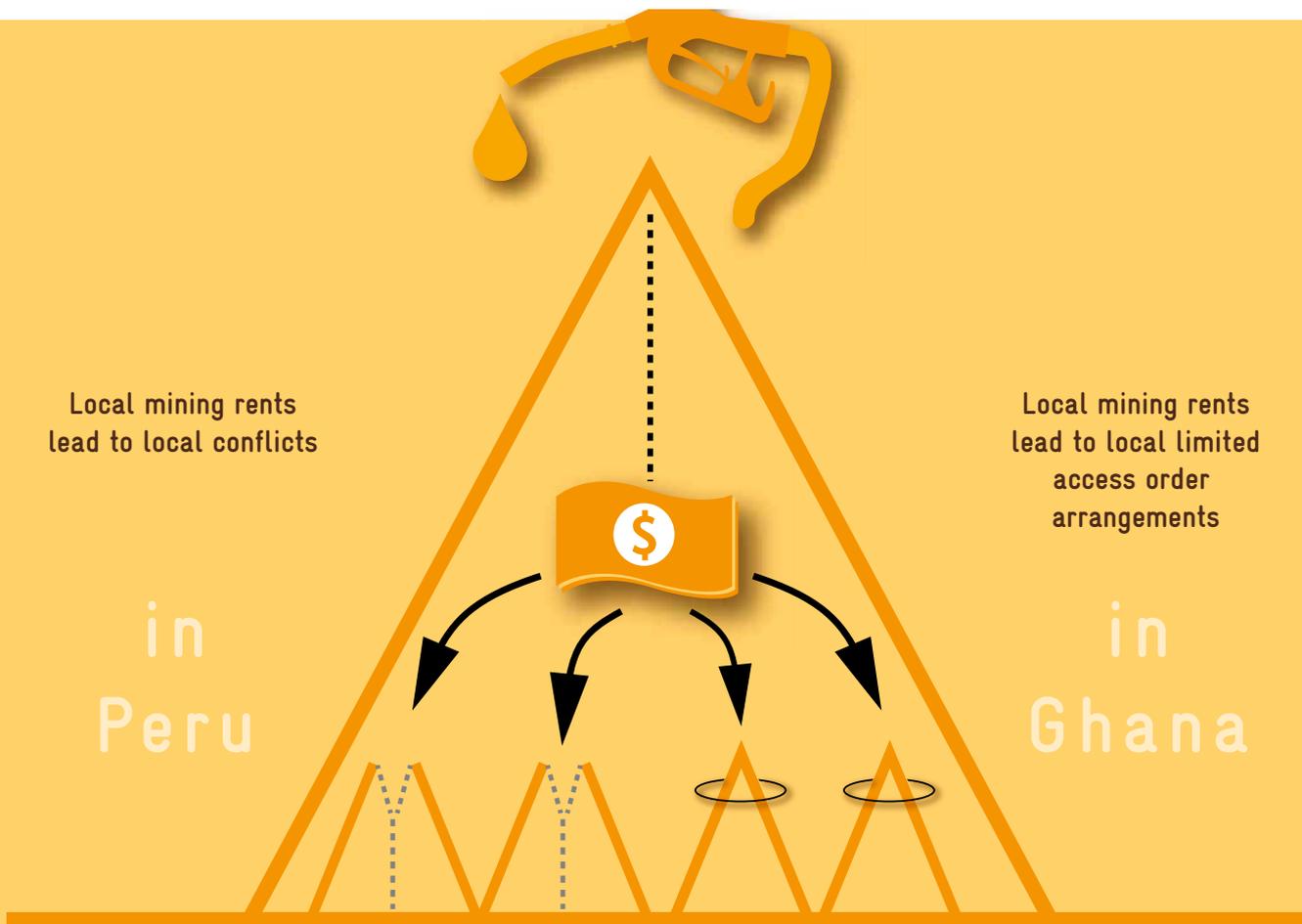
6.2 Local Chiefs in Ghana

Ghana's gold mining revenues come mainly from a 5 per cent royalty tax (increased in 2010 from 3 per cent), which

accounts for roughly 14 per cent of the national budget. Of this, 80 per cent stays in the national coffers, 10 per cent flows into a Mineral Development Fund (for compensation and development projects in the mining areas), and the remaining 10 per cent is devolved to local governments in the mining regions. Ghana's local governments are comprised of 95 paramount chiefs in rural areas, presidentially appointed district chief executives, and district assemblies (two-thirds elected and one-third presidentially appointed members). The active chiefs hold *stools* (all chiefs are addressed with the prefix *Nana* but only those presiding over a *stool* act as informal local executives). In gold mining communities, the devolved revenues are split 45-55 between *stool* (i.e. chief)

and assembly. Ghana's constitution is ambiguous about what chiefs and assemblies are supposed to spend this money on. Critical observers found that chiefs have spent lavishly on "limousines, jewellery and ceremony" and little on community development projects (ICMM 2007, cited in Standing/Hilson 2013; see also Opoku 2006). Chiefs, in particular, are said to have misinterpreted the clause that "Stool Land revenues are to be used to maintain the stool in keeping with its status" to mean that, as the chief personally represents the community, he has to keep up his personal 'status.' Furthermore, a dispute between Chief Nana Bonin Abankoro and his de-stooled predecessor, Nana Ntiamoah Berdiako, over mining royalties, is reported to have led to injuries between

Figure 10: Peru and Ghana - Local effects of decentralised mining rents



Source: author.

community members of their respective factions (Standing/Hilson 2013, 8). Other chiefs are accused of having made agreements with mining companies without consulting their communities (Greenspan 2012, cited in Standing/Hilson 2013).

Similar criticism has been heralded at the district assemblies: being only two-thirds democratically elected, these bodies have the reputation of scrupulously misappropriating funds, of being vehicles for patronage and cronyism (Standing/Hilson 2013, 9), and being of little use for negotiating their communities' interests (Meyers/Vermeulen 2002; Marfo et al. 2012; Larson et al. 2010). Neither of the two institutions is seen to be particularly capable of or interested in protecting community rights against foreign mining companies. To the contrary, a survey found that 85 per cent of respondents deemed that projects financed via district assembly were of no use to citizens (Debrah 2009, cited in Standing/Hilson 2013, 10).

Standing/Hilson (2013), on whose work this account draws, categorically condemn the undemocratic behaviour of Ghana's chiefs and district assembly members. They suggest that "policy makers and the international development community working in Ghana have yet to review the appropriateness of the Chief's inclusion," and cite a study that notes "[t]here is strong evidence that the payments to traditional councils and stools tend to finance expenditures other than those that benefit the local communities involved" (Standing/Hilson 2013, 8, 7, citing ICMM 2007).

Yet, from a political economy perspective it cannot be ruled out that the opposite is true: Ghana's 'model democracy' at the national level would perhaps not be as stable and thus could not function as well as it does without certain co-optations of lower-level elites. One way of looking at this profligacy (which is doubtlessly blatant, but at 1.4 per cent of the national budget also comparatively minor) is that letting lower-level elites 'maintain their status' keeps the national regime stable enough to engage in the industrial policy undertakings (Section 5) necessary to provide the jobs that make Ghana's narrowly commodity-driven economy into a more diversified one. Figure 5.2 depicts the rent dispersion from top- to lower-level elites in both Peru and Ghana. In Peru, the localised jockeying for rents has led to strategies of local confrontation, (depicted by the fractured local pyramids on the left of the image, akin to the images of South Sudan's national level). In Ghana, meanwhile, the devolution of resource rents has created miniature versions of the limited access order: keeping the stools in line with the broad

national agenda, at the expense of the excluded local community (depicted by the small limited access order pyramids on the right side of the image).

6.3 Threats of local violence and secession in Kenya

Like the rest of East Africa, Kenya was long seen as rather resource poor. But in March 2012, Tullow Oil discovered sizable oil reserves in Kenya's north-western periphery, Turkana (Blocks 10BB and 13T). And on the other side of the country, prospectors suspect offshore gas reserves in the Indian Ocean, near Lamu, bordering Somalia (Blocks L-5, and L21-25) (Patey 2014; Reitano/Shaw 2014). The resource curse literature on violent conflicts finds that new resource discoveries are particularly dangerous if made in areas with pre-existing conflicts (Fearon/Laitin 2003). Kenya's Northwest has long been plagued by ethnic rivalries. Armed back-and-forth cattle raids between bands of youths – mainly from the Turkana, Pokot, and Samburu communities – take on the forms of deadly feuds. They spread into several adjacent counties but their epicentre lies in Turkana, immediately south of Blocks 10BB and 13T. With little economic productivity in Kenya's periphery, these cattle raiders are embroiled in enduring zero-sum games of honour and revenge. They have often lent themselves to local politicians' strategies of confrontation over boundary disputes (Greiner 2013). Turkana's oil discoveries now set the stage for a new dimension of conflict in two ways: (i) Turkana locals are suspicious of the central government, whom many equate with the inland Kikuyu business elite. Watching their arrangements with foreign companies to 'remove' Turkana's oil, local youths seem ready to fight for a share of the proceeds; and (ii) border disputes between neighbouring Pokot and Turkana have long existed over grazing rights, and hostilities are likely to increase with the value of this contested land (Lynch 2014).

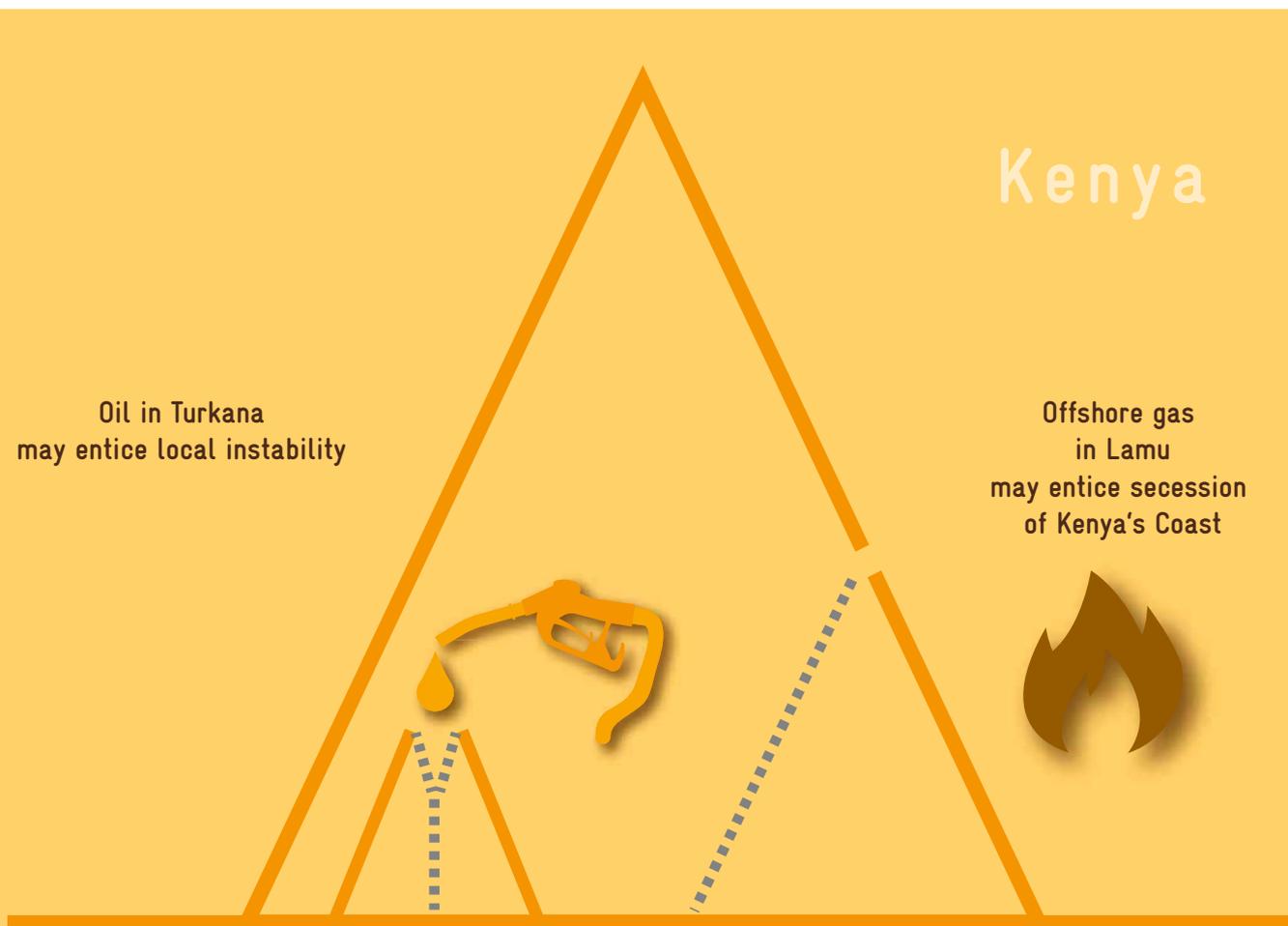
Over on Kenya's coast, the picture is different, but arguably no less dangerous. According to the literature, offshore resource discoveries have rather strengthened the central government's hold on power vis-à-vis regional insurgents as these are difficult for rebels to reach (e.g. Lujala 2010), but an exception may be secession attempts (Collier/Hoeffler 2006; Horowitz 1985). Kenya's Coast Region has long been a hot spot for tensions between indigenous Muslim Coast populations (Mijikenda, Swahili, and others) and inland Christians (mostly the Kikuyu business elite, who have come to own most of the valuable coastland, have built hotels, and now

dominate the tourism industry). Apart from a constant threat from the Islamist al Shabaab in nearby southern Somalia, resentments in Kenya's Coast Region simmer, and a real risk of secession attempts exists once oil and gas starts flowing.

Further problems are revealed when zooming in on the locality near which the gas fields are suspected. Lamu County is one of Kenya's ethnically most divided: Lamu West is home to a comparatively affluent Kikuyu settler community, constituting about 40% of Lamu's population,⁴⁰ while Lamu East – including the islands where most of the remaining 60% of the population live – consists mostly of regional natives who are much poorer. Lamu's Governor, Issa Timamy (a native Swahili) ran a confrontational election campaign

against Kikuyu business interests in Lamu, accusing 'government insiders' of land grabbing via faked title deeds, speculative land purchases, and opaque procurement. Ever since Timamy won the governorship in March 2013, the central government of President Uhuru Kenyatta (Kikuyu), in turn, has taken a confrontational stance, accusing Timamy of hate speech and, at one point, publically suggesting there was an alliance with al Shabaab (Interview with Timamy, Nairobi, 25th July 2013; *The Standard* 27th Nov. 2013, and 17th Jun. 2014). As extraction and construction projects planned for Lamu get underway, this conflict is likely to intensify. Figure 11 depicts Kenya's two trouble spots: the risk of Delta-like civil war in Turkana, and the risk of secession attempts at Kenya's Coast.

Figure 11: Kenya's oil and gas extraction may amplify existing tensions



Source: author.

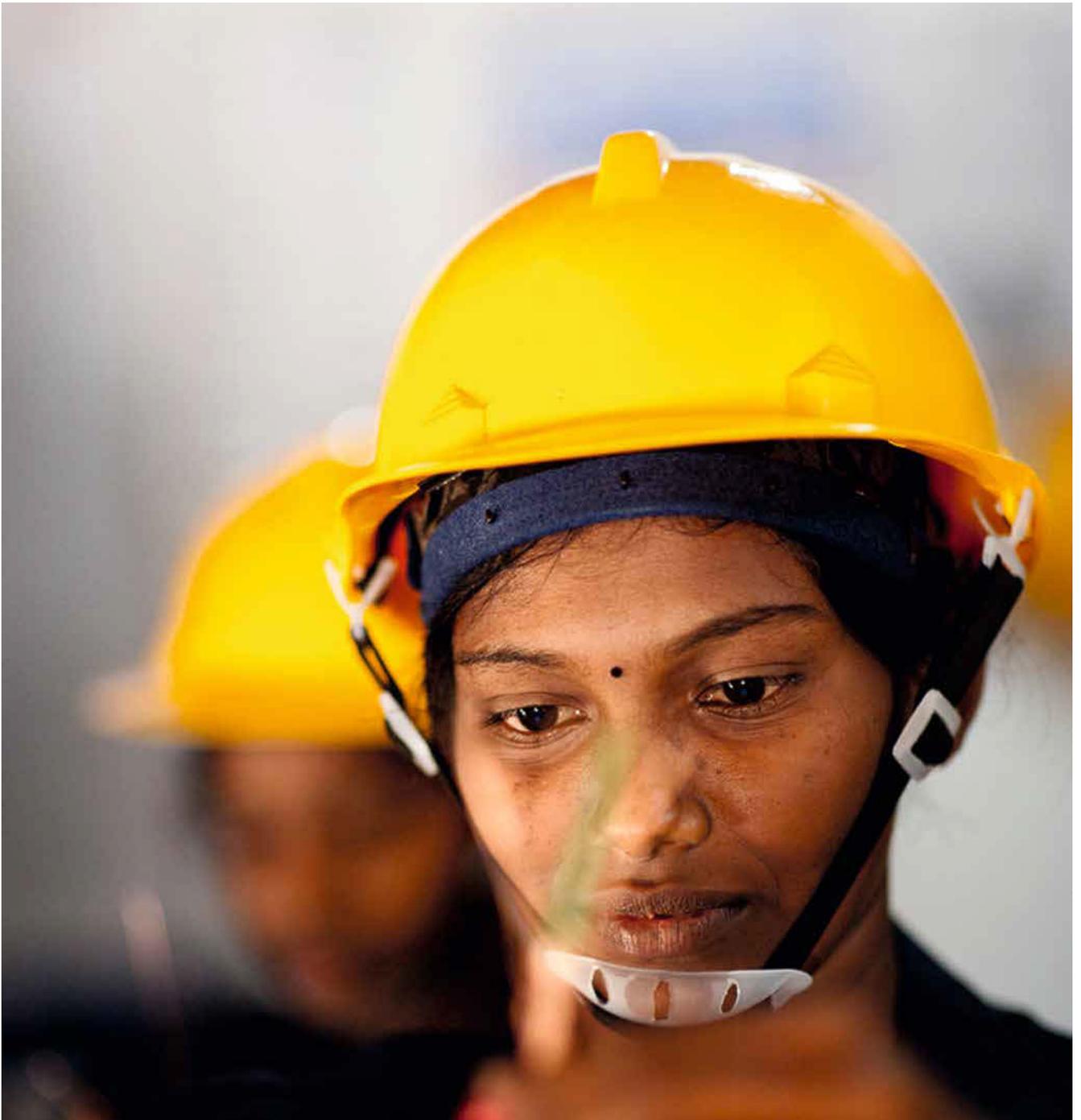
This completes the three substantive sections, and a note of direction may be in order. Simply leaving the resources in the ground is not an option. Some observers, perhaps overwhelmed with having studied the negative impacts depicted in some of the cases above, have advised countries to forgo extraction, until, at a future point in time, better institutions were in place for managing the windfalls (e.g. Gelb 1988; Ross 2012). Yet, these appeals neglect that what leads to mismanaging resource rents is the very same systemic mechanism that also leads to rushed extraction. Empirically, those countries whose governments are least ready to deal with resource rents are, without exception, also the countries whose elites have the greatest incentives to extract as soon and as fast as they can. The aim of this study, therefore, is not to bedevil natural resource extraction or to frighten

technical assistance agencies into avoiding the sector. To the contrary, as noted in the introduction, together with the TC Guidelines, this study aims to assist developing countries in making the best possible use of their sub-soil wealth. Rather than downplaying the existence of the resource curse (see e.g. UNECA 2013; Morris et al. 2012) this study seeks to provide the assessment needed for anticipating the political risks. With that, the next section examines resource-curse remedies, focusing on the possibilities provided by three particular policies for alleviating the resource curse with regard to national strategic planning, employment creation, and local development.



7

International remedies against the resource curse



Several sensible efforts are underway for curbing the resource curse. Most common is the macroeconomic assistance by the International Monetary Fund (IMF) for smoothing volatile revenue flows (i.e. countercyclical spending and longer-term natural resource funds). Yet, for the same reasons that elites cannot delay extraction and cannot easily spend the windfall gains on genuine development projects, they also have difficulties when it comes to saving these rents: elites in the circle need their share of rents to uphold their patronage networks. Even if all elites were to agree to set aside money for the future (which, in reality, many wholeheartedly try), the mistrust among elites that this money, as it begins to accumulate, could at any time be used to push some elites out of the circle, triggers a first-mover effect which leads to a self-fulfilling prophecy. Humphreys and Sandbu (2007), showing some of the limited access order incentives involved, illustrate the pattern of how, over time and across continents, natural resource funds in developing countries have systematically been mismanaged and depleted. Michael Ross suggests that a mechanism which turns this process on its head could help: development banks that lend to resource rich countries whenever the prices for their minerals are low, and peg the repayment rate to oil proceeds (Ross 2012).⁴¹

Beyond macroeconomic management, donors often provide governance assistance more broadly as seen in the Mozambican and Chadian cases (Sections 4.3 and 5.1). One recent development, inspired by Paul Collier, is geological mapping. Co-funded by the World Bank, this aims to counter the information asymmetries between global extraction companies and host countries (Iyer 2014; Collier 2010). Three approaches are examined in more detail here: (i) transparency and accountability, (ii) barter trades, and (iii) direct cash transfers to citizens.

Transparency initiatives aim to give host countries a stronger position in negotiations with foreign extraction companies that are often better informed, and to allow host country citizens to scrutinise the deals struck between their leaders and foreign companies. Proponents argue that this would reduce political leaders' opportunities to ask for personal kick-backs, embezzle the proceeds, or strike deals without adequately considering the local downsides of extraction, such as village relocations, environmental degradation, or local Dutch disease effects. This would allow citizens to get involved from the outset, which in turn, would make leaders in resource driven countries more accountable (Kolstad/Wiig 2009; Williams 2011; Corrigan 2014).

Barter trades refer to arrangements in which natural resources are traded directly in return for public infrastructural goods.⁴²

They were born from necessity: China's need for resources, and its need for reassurance that instable governments would not default on loans, coupled with (mostly) African countries' needs for infrastructure and a general desire to side-step the tedious conditions attached to loans from international financial institutions. Initially viewed in the West with scepticism, some observers have come to embrace barter trades as a possible model for western development aid, as this puts the onus of dealing with price volatility on the developer, and as this keeps rents from entering the elite circle and thereby insulated from misappropriation (Brautigam 2010; Dobbs et al. 2013; Collier 2014).

Direct cash transfers to citizens have existed in Alaska since the 1970s, and became popular as a development tool with Mexico's successful conditional cash transfers for school-attending children (Banerjee/Duflo 2011).⁴³ Several scholars clustered at the Washington based Center for Global Development eagerly promote direct cash transfers as the most promising tool for avoiding many of the resource curse's ailments (e.g. Birdsall/Subramanian 2004; Gelb/Decker 2011; Moss/Majerowicz 2013). At the core of their argument is that unconditionally transferring money to citizens creates a benign slippery slope, moving politicians away from patronage politics and toward programmatic competition. Political leaders who introduce this as a populist measure (for example in an election campaign) would find it difficult to reverse. Much as salaries are more difficult to embezzle than development spending, citizens would vehemently demand their transfers, thus laying the foundation for a modern social contract. The remainder of this section first describes the current-historical developments in these three areas of transparency, barter trades, and direct cash transfers, and then discusses these policies in light of the political economy insights gained from the case studies.

7.1 Transparency and accountability initiatives by Europe and the USA

After witnessing the devastating effects of the commodity boom-bust cycles of the 1970s and 1980s (e.g. Gelb 1988), European civil society organisations began to point to the secrecy and opacity of the international oil, gas and minerals sectors. In 1993, the formations of two nongovernmental organisations kicked this off: the Berlin-based Transparency International and a more sensationalist but exceptionally successful London-based Global Witness. Initially, Global Witness exposed Khmer Rouge's proceeds from timber logging in Cambodia and thereby substantially contributed to Pol

Pot's demise. It then turned to the issue of conflict diamonds in Angola (spurring the most remarkable anti-resource-curse achievement to date: the creation of the Kimberly Process Certification Scheme⁴⁴), and soon after, Global Witness focused on Angola's oil, producing two agitating reports (1999, 2002) that caught a wide audience (Shaxson 2007, 211). As extractive contracts were often extremely favourable for multinational companies, it seemed obvious that this was only partly due to the poor information and negotiating skills of host governments. Global Witness called upon companies to disclose their *actual* payments to host government agents, including signing bonuses, etc. When in 2001 British Petroleum tentatively tried this out, regarding its operations in Angola, Sonangol reacted with a threatening letter, copied to the rest of the industry. Voluntary initiatives by individual western companies were thus soon equated with corporate suicide (Browne 2010, cited in Short 2014). In 2002, billionaire George Soros and his Open Society Institute got involved with a 'Revenue Watch' programme that established a network of transparency NGOs, urging extraction companies to 'Publish What You Pay' (PWYP) to host governments. This also called upon western governments to force companies to be more transparent. In mid-2003 the UK's Blair Government followed up by establishing the Extractive Industries Transparency Initiative (EITI). The EITI formalised the naming-and-shaming agenda by asking *both*, host governments and companies to sign up to the process. This put the onus on host governments, but still remained on a voluntary basis. Observers who followed the EITI process throughout the 2000s note that these initiatives were vastly outmatched by an overlapping interest of exporting country elites and multinational extraction companies (Buur et al. 2013; Karl 2008). The EITI helped identify those countries least willing to cooperate (Angola, Equatorial Guinea), but its minimal compliance standards were fairly lax, which in some cases backfired by legitimising regimes that paid lip service to the EITI with, in hindsight, little intention of ever fully complying with it (Azerbaijan, Nigeria) (Soare de Oliveira 2014; Shaxson 2009; Short 2014, 11; *The Economist* 13th Dec. 2014).

The 2008 global financial crisis, finally, led the many appeals for OECD countries to move past the voluntary and legislate for transnational transparency to come to fruition. The USA 2010 Dodd-Frank Wall Street Reform Act included a section (1504) that mandated that companies active in the extractive oil, gas, and minerals sectors and listed on the US Stock Exchange would have to publish all payments to host country governments on a project-by-project basis.⁴⁶ Challenged by the American Petroleum Institute, a Washington

DC court verdict vacated the clause in June 2013, which the government has not appealed. But observers anticipate that redrawn legislation is soon to follow (Hughes/Pendred 2014). Meanwhile, the European Union has passed a 2013 Directive, modelled on Section 1504 of the Dodd-Frank Act, and the governments of Canada and Australia have committed themselves to similar measures in June and July of 2013 respectively (*ibid.* 41).

Notwithstanding the teething problems associated with such legislation (accentuated by sophisticated backlashes from extractive industry operators),⁴⁷ these ongoing efforts depict a sea-change from lip service to concrete action by western governments to curb the extractive sectors' corruption. This internationally enforced revenue transparency is sought to stimulate host-government accountability. The importance and limitations of these initiatives are discussed together with the following two remedies in Section 7.4. An interesting contrast to transparency initiatives is China's form of a 'no-questions-asked' aid-trade hybrid.

7.2 Resources for Infrastructure deals by China

Since the early 2000s, China has increasingly financed infrastructure projects in partner countries. For resource rich countries, this is done with what has come to be known as 'barter' deals: China's EXIM Bank gives concessional loans with low interest rates (subsidised by the Chinese government) and reimbursement periods of up to 20 years (Alves 2012, 213). Mostly used for the construction of roads, railway lines, power stations, telecommunication lines, mines, factories, hospitals, or housing units, these projects are tied to Chinese companies (usually for 50 per cent), and sovereign guarantee by the host country is provided by backing the loan repayment with future resource proceeds. By 2008, one third of China's oil supply came from Africa (mainly from Sudan and Angola, van Dijk et al. 2010, 144). By 2009, China had financed infrastructure projects in 27 Sub Saharan African countries, but its largest investments were concentrated in Angola and Nigeria (20 per cent and 30 per cent of China's investments in Africa, respectively; Foster et al. 2009, 25ff).⁴⁸

In Angola, Chinese oil-backed finance began in 2002, initially small, but it substantially increased in 2004, with a \$2bn loan for various infrastructural and health and education constructions, backed by 10,000 barrels per day. Since this was the first such deal, this has come to be known as 'Angola mode.' Further oil-backed loans for infrastructure projects

followed in 2007 (for \$2.5bn) and in 2011 (for \$3bn) (Alves 2012, 216; Foster et al. 2009, 27; Corkin 2012).

In Nigeria, China's project finance runs to between \$5.4bn and \$12bn.⁴⁹ In 2002, China's ZTE and Huawei started Nigeria's National Rural Telephony Project, and in 2005, a first EXIM Bank loan financed the construction of three power plants. For this, Nigeria's National Petroleum Company would sell China's CNPC 30,000 barrels per day for one year. This was to be scaled up more than tenfold in 2006, with big EXIM Bank loans to co-finance multiple railroad projects, a hydro power plant, and the refurbishing of an oil refinery in Nigeria. President Obasanjo's successor, President Yar'Adua froze several of these projects in 2007, which frustrated the relationship between Nigeria and China. But by 2011, under President Jonathan, the Nigeria National Petroleum Company apparently signed an agreement with China's State Construction Engineering Corporation for a \$28bn mega-project that includes the building of three new refineries (to be 80 per cent financed by China), and another \$3bn loan in early 2012 for the completion of older projects (Alves 2012, 216; Mthembo-Salter 2009; Foster et al. 2009).

In the early 2010s, this model multiplied. China's multi-billion dollar barter deals continue to spread (e.g. to Ghana for pipelines, ICT, and social infrastructure; to DR Congo for greenfield mining projects, infrastructure and health facility constructions; or to Gabon for mine development in return for a 560 km railway line),⁵⁰ and Brazil's development bank has copied the model for its deals with Angola, Mozambique, and Ghana (Alves 2012).

7.3 Direct Cash Transfers in Mongolia

For its income bracket and geographical neighbourhood, Mongolia is remarkably democratic. This has been attributed to its relative resource scarcity (Fish 2001, 325ff). Yet, in 2001, the world's largest untapped copper reserves (and large gold reserves) were confirmed in Olu Tolgoi, and the world's largest coal reserves in Tavan Tolgoi, both in Mongolia's South Gobi near the Chinese border. The subsequent pouring in of extractive FDI, and a sharp rise in copper prices flooded Mongolia's tiny economy.⁵¹

With these developments underway, Mongolia also became a pioneer for introducing a direct cash transfer to citizens. In 2004, in the run-up to parliamentary elections, the MDP, an underdog party that wanted to shed its 'neoliberal' image (for having cut pensions after the Asian Financial Crisis),

campaigned on a Child Benefits Fund. This would transfer approx. \$9 monthly per child unconditionally. The idea was immensely popular. The MDP gained 32 seats in Parliament, coming just short of a relative majority over the MPRP. The two parties had to form a coalition government, and due to the proposal's popularity, the larger MPRP coalition partner went along with it (Fritz 2014, 57). A small cash transfer, targeted at poor families, was introduced in 2005, and in 2006 an untargeted child benefits transfer to families of all income brackets was introduced, coupled directly to a new windfalls tax. Some other pay-out schemes (for new-borns and for newlyweds) followed, and in 2007 the Child Benefits money was increased by \$85 annually. Much like in Alaska, (where a direct cash transfer has existed since 1976) the policy was so popular that few politicians dared to oppose it. To the contrary, in the run-up to the 2008 elections, the two parties outbid one another: the MDP promising a \$900 annual pay-out to all citizens and the MPRP promising a \$1,300 payout (Mongolia's annual GDP per capita was then just below \$2000!). After the elections, the price slump in the 2008 financial crisis, led to a balance of payments crisis, which brought in IMF austerity measures that temporarily scrapped all cash transfers. But in 2010 each citizen received \$90 unconditionally, increased to \$190 in 2011. In 2012 amendments promised targeted transfers of \$900 annually to pensioners and the disabled, and \$600 to students. This was reversed in late 2012 and the Child Benefits Money was also again reduced (Fritz 2014, 55). The World Bank noted that these were populist campaign promises, not based on perceived socio-economic necessity but purely on political rationale (ibid. 59-60). Their technical implementation was also wrought with difficulties (e.g. the transfers were directly tied to windfalls, and thus highly unpredictable).

Nevertheless, the cash transfers did have the effect that its academic proponents had hoped for: here was an institution that led politicians to use an alternative to their patron-client networks in which little trickles down to the base of the pyramid. Once begun, it was difficult for elites in a competitive clientelist system to turn against it – the 'cash transfer virus' had been released. (However, the two parties subsequently agreed to 'no populist' campaign promises ahead of the 2013 presidential elections). As Mongolia's cash transfer roller-coaster ride stabilises in the future, it should greatly benefit the population.

Could this system be implemented elsewhere, or is there something particularly cash-transfer-suitable about Mongolia? Mongolia is ethnically homogeneous, and has long been internally cohesive and peaceful, perhaps also due to latent

external threats from its large neighbours (Russia to the North and China to the South). Other than this, Mongolia has all the hallmarks of a limited access order: clientelist networks, nepotism, and grand corruption at the top elite level abound (*The Economist* 23rd June 2012).

With increased natural resource revenues, the jockeying around the new rent gate within the elite circle has intensified: on 12th April 2012 (four months before parliamentary elections) opposition leader and former President, Nambariin Enkhbayar, released documents that implicated the sitting president, Tsakhiagiin Elbegdorj. That same evening, police and the anti-corruption authority raided Enkhbayar's home and carried him out. He was jailed for 2.5 years for relatively minor corruption offences (*The Economist* 28th April 2012).⁵² This tussle is in line with the logic of a limited access order with natural resources (although the severity of the measure, paradoxically, indicates the regime's stability: in a more fragmented society, only narrowly authoritarian governments, such as Obiang's in Equatorial Guinea, could have confronted a top-level elite in such a harsh manner without sparking a violent power clash among factions).

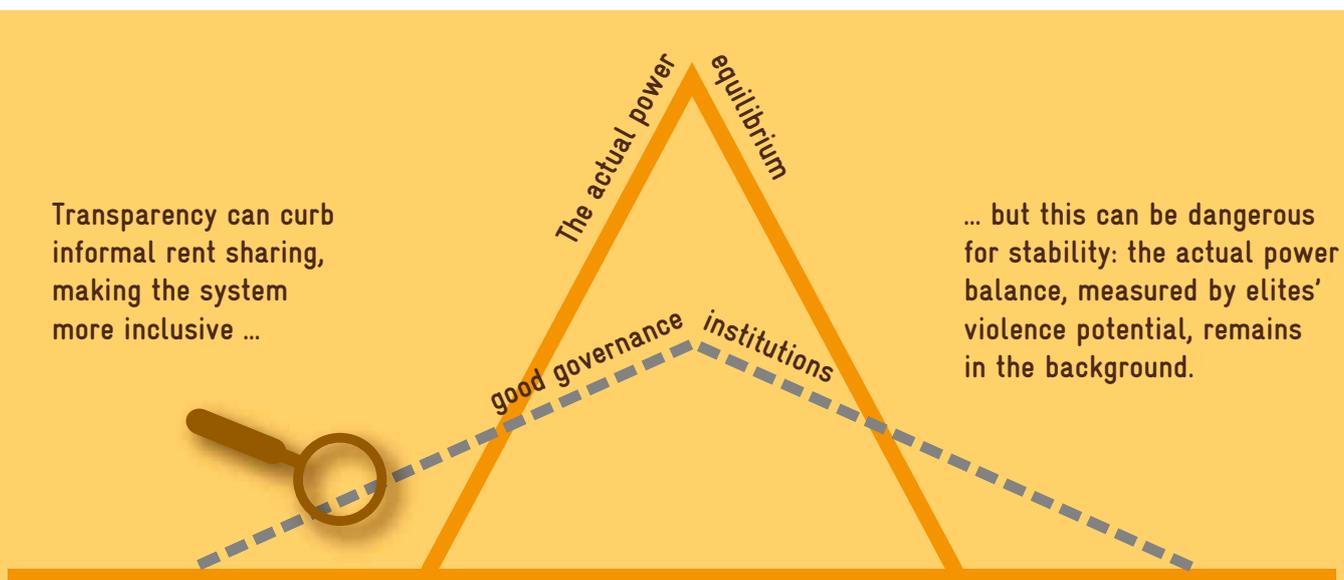
One aspect, however, that sets Mongolia distinctly apart from most other resource driven low income countries is decisive: the expected *size* of its resource rents. In spite of its great landmass, taking the resources-to-population ratio,

Mongolia resembles a small Emirate. Its sub soil assets amount to an estimated \$3tr, which translates to roughly \$1m per person (*The Economist* 11th Oct. 2014). Recall the inverted U-shaped relationship (found by Basedau/Ley 2009) between resource wealth and conflict. This may well hold for the wider resource curse as well, not merely for conflict: above a certain point, elites have the security that sharing with everyone in the country will not destabilise their position. As long as a consensus exists within the elite circle to refrain from serious confrontation, all will prosper, and there is even enough stability to spend sizable amounts on the poor via cash transfers. Many now call for such a measure to be introduced elsewhere.⁵³ But could this work in a political settlement that is (a) less cohesive and has (b) a drastically lower resource-rents-to-population ratio, such as Ghana or Nigeria? All three remedies are discussed in the next sub-section.

7.4 Discussing the remedies

This study outlined some of the main political economy hurdles involved for resource-driven low-income countries that try to create a national strategic plan that is workable and sustainable; create meaningful employment for sizable parts of the population; and provide local economic development in mining areas. The case studies in Sections 4-6 provided windows into some of the recurring issues, and this section

Figure 12: Transparency and accountability to fight corruption



introduced three potential remedies for avoiding the resource curse. This final sub-section links the remedies to the insights collected in the case studies on the Limited Access Order, the Politics of Industrial Policy, and Political Settlements with regional elites. Ideally, this should help policy makers and TC practitioners gauge these remedies' respective usefulness for strategic national planning, employment creation, and local economic development.

Transparency and accountability for limited access orders?

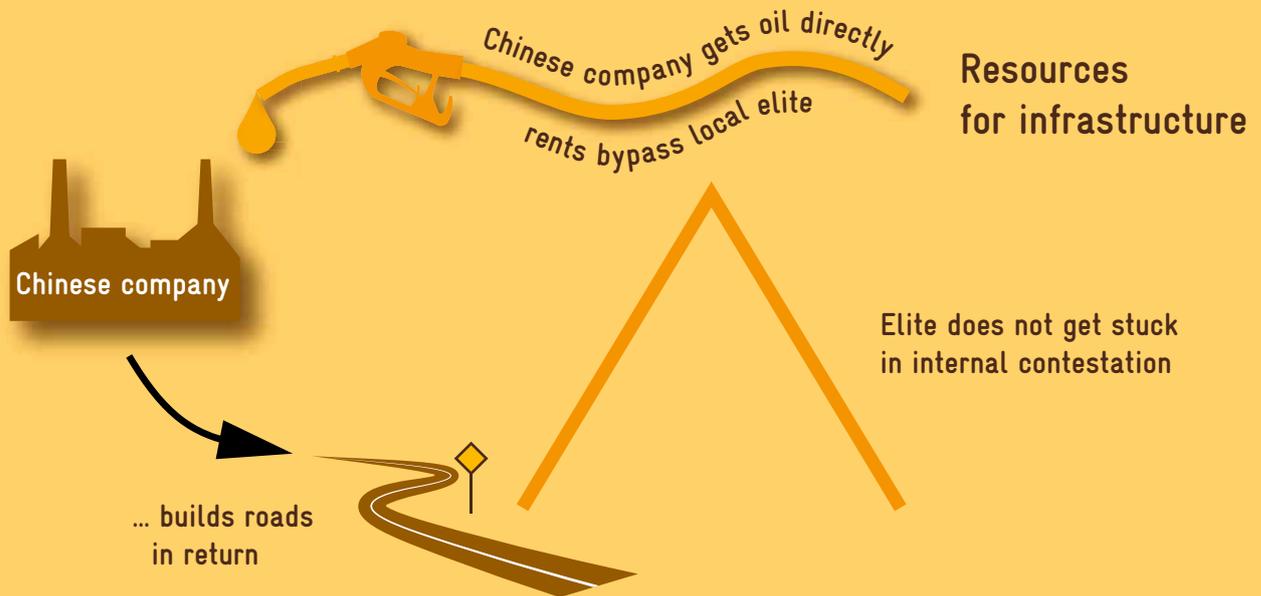
Highlighting structural reasons for the resource curse, as this study has done, runs the risk of relieving human agency of responsibility. Many analysts steer clear of structural explanations, because the resulting policy advice could condone corruption. Yet, as systemic currents have generated patterns of similar undertows in many countries, simply calling for 'better leadership' falls short of the mark. Understanding the structural mechanisms, instead of excusing corruption, can thus fine-tune the governance tools that seek to mitigate it. For this, it may help the observer to imagine the elite power equilibrium as a heavy rock, and the country's formal institutions as ropes that stabilise this rock. If, by tightening and relocating the ropes, the rock is to be moved from one position (e.g. a limited access order) to another (e.g. an open access order), particular attention has to be paid to the shape, position, and size of the rock, and the gravitational force acting upon it. If one rope snaps, the others may not hold the weight, leaving the rock to fall back uncontrollably, destroying everything that had grown in its shade. The cases of Chad and South Sudan are instructive: a limited access order on the brink of collapse cannot implement overly inclusive institutions, no matter how well thought out they are. Critics of the Chad-Cameroon pipeline project have focused on the flawed institutional design (i.e. on an incorrect placement of the ropes) (Pegg 2009), and omitted to study the shape and weight of the rock itself (President Déby's narrow power base). Similarly, in South Sudan, critics have faulted President Salva Kiir's lax handling of corruption as a cause of South Sudan's predicament (de Waal 2014). This study suggests that his approach was, instead, the only means of dealing with the predicament of instability. With his attempt to reform in June-July 2013, the system collapsed five months later.

This is not to suggest that the transparency and accountability agenda is doomed, only that it needs to pick its battles carefully and strategically. The international agenda for making the proceeds of resource extraction deals more transparent goes in the right direction. It gradually takes the secret funds away, allowing elite factions to agree on earmarking

certain portions of a more transparent budget to development projects. This pushes the political settlement (the rock) slowly toward more programmatic competition, and away from clientelist competition. Calls from western researchers to go substantially beyond transparency in revenue *generation* (host country elite contracts with foreign extraction companies) and into total transparency in revenue *distribution* (open budget initiatives where the movement and allocation of every cent is made transparent) (e.g. Kolstad/Wiig 2009, Amundsen 2014) can, while desirable in principle, be dangerous for political stability. Figure 12 illustrates the attempt to make a limited access order pyramid more inclusive via 'big-push' transparency measures (the dotted-line pyramid). The actual power balance will become informal, but nonetheless remain strong in the background (depicted as the narrower, taller, and solid-line pyramid).

Resources-for-infrastructure to bypass the Politics of Industrial Policy? Much in contrast to the above, China's barter arrangements have often been seen as the opposite of Western donor conditionality, and have been called 'no-questions-asked' deals. Most notably, when US companies withdrew from Sudan, due to the al Bashir government's human rights abuses in Darfur, Chinese partners quickly filled the void. Yet, barter deals, examined separately from China's ethical approaches, also bring succinct advantages for public-goods-provision in limited access orders. Locking future resource rents into public goods helps developmentally oriented elites get projects underway quickly, that otherwise would get bogged down by internal contestation. Like a gambler who assigns a friend the task of making large purchases for him in advance, in return for access to his bank account: as soon as money comes into the account, it cannot be squandered because it already belongs to the friend. Paul Collier suggests that in combination with transparency initiatives, such barter deals could provide a suitable model for western donors interested in helping resource-driven low-income countries develop. Procurement could be undertaken as transparent barter tenders: development banks or bilateral assistance agencies could partner with western extraction companies in bidding for resources-for-infrastructure barter deals, offering a list of pro-poor and non-pro-poor investments. This could have secondary effects of moving host governments into a social contract with local citizens. Giving host countries a transparent choice between one barter deal that promises a large sports stadium and a new party headquarters sky scraper built mostly by foreigners, and another barter deal that instead promises a sewage system and rural feeder roads built mainly with the use of local labour, could push populist elites toward choosing the latter (Collier 2012). Such developmentally oriented

Figure 13: Resources for infrastructure - Barter trades with China



Source: author.

barter deals, in combination with the adequate local content stipulations, and transparent procurement procedures, could lead to several positive outcomes: infrastructure would get built, which opens up generic space for growth of many other sectors; the local content stipulations, if they have traction, induce technology/skills spill-overs from foreign to domestic firms; and, most importantly from a political economy perspective, a more regularised and open barter trade could help host country governments move slowly toward more programmatic and transparent development spending.

Yet, some problems remain. The Chad-Cameroon pipeline project showed that spinning barter deals in a pro-poor direction has to be done in a piece meal measure. Such projects, if too ambitious, may, as happened in Chad, fail altogether. Furthermore, while Angola's 'successfully failed state' (with its strong extractive institutions but hardly any redistribution to the poor) profits greatly from barter deals with China – the *types* of construction projects agreed upon between the two governments disproportionately benefit Angola's most affluent. If this 'tide' can, eventually, also raise the living standards of Angola's poor remains to be seen. Sonangol's strong negotiating power may in the long run lead to real linkages via local content and Angolanisation stipulations, even if, for the time being, they mainly serve the elite's rent-seeking activities. Figure 13 illustrates the concept of 'outsourcing' revenue management for infrastructure investments by keeping oil rents away from the elite circle. In the figure, an extended

fuel pump hose leaps across the limited access order pyramid, directly to the foreign company, which in turn builds a new road that benefits all.

Direct cash transfers instead of fiscal devolution? The direct cash transfer scheme is a libertarian silver bullet that certainly has its charm. That such a simple institution could entice political elites to move away from lubricating their clientelist networks, and toward promising ever-greater direct cash transfers to all citizens on an impersonal basis, sounds almost too good to be true. A reliable and impersonal income for all would allow citizens the financial security to look more to the left and right (for trading and adding value with other citizens), and less upward (awaiting favours from a network's patron). Technically, some problems do exist. Just as barter deals are prone to prestige projects, cash transfers are liable to volatile swings and fiscal mismanagement. The World Bank team in Mongolia lamented (a) that the cash transfers were directly coupled to resource windfalls, and were thus equally volatile, and (b) that 20 per cent of poor families did not receive their money from the initial trial transfer (Fritz 2014, 64). The first of these – volatility – is a solvable technical issue. Most developing countries have greatly improved their macro-economic management in the past two decades, and this should be manageable as well.

The second problem – of actual arrival of transfers – goes more to the core of this study's theme: why would elites in

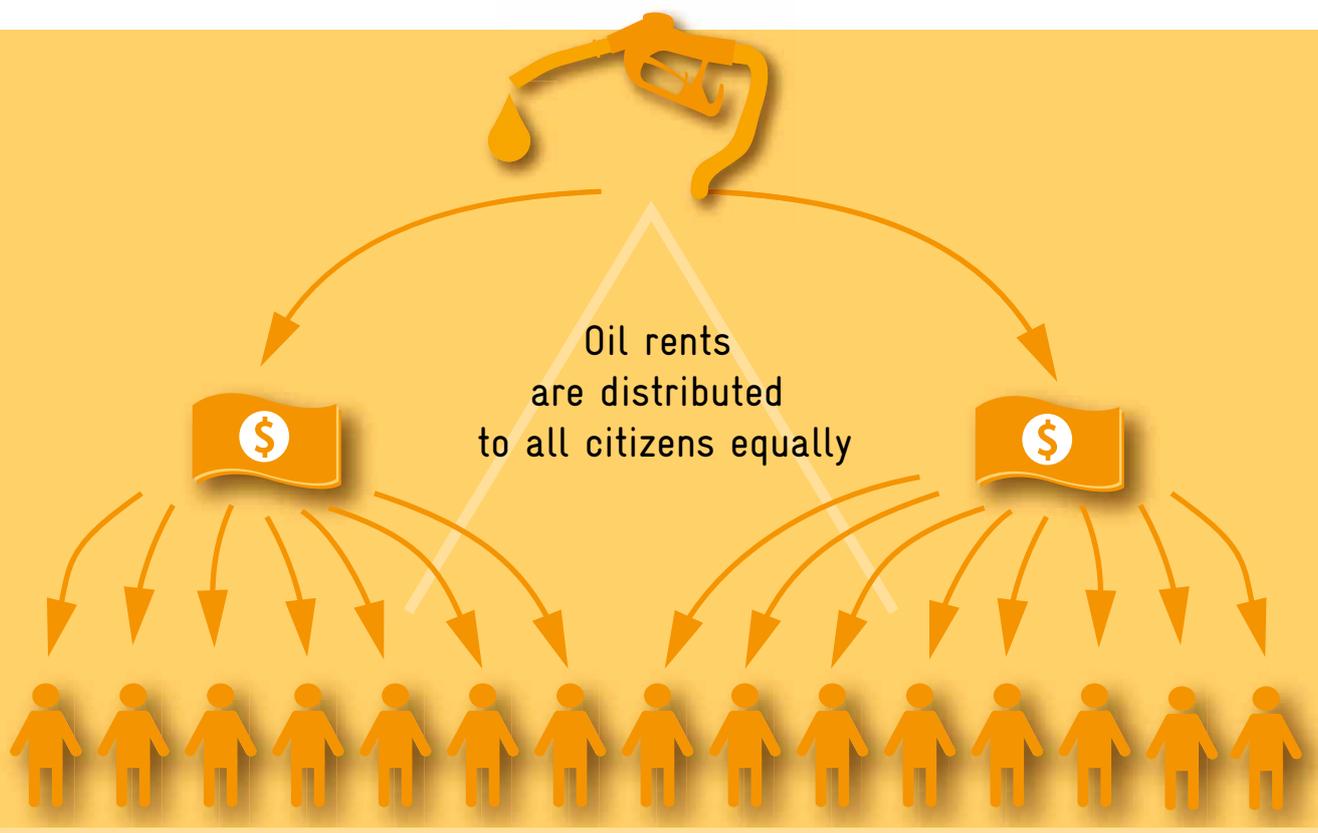
limited access orders agree to give money to citizens who have effectively no bearing on the power constellation of the elite circle? Seen in this light, an initial 80 per cent success rate is a remarkable achievement,⁵⁴ one that may not be replicable in countries with (a) a more fractured society (and thus a more fractured elite circle), and (b) much less natural resource wealth per person. Recall that Mongolia can anticipate as much resource revenue per citizen as an Emirate city-state. This may give the elites enough of a cushion to experiment with such initiatives. In countries with fewer resources or larger populations, elites have less of a cushion, and are less likely to go along with such a scheme. If a reform-minded faction implements it, others would most likely contest it. This suggests that, while large cash transfers would be ethically most desirable, beginning with small cash transfers could be more successful. Technological advances, such as biometric identification, hold the promise that, once cash transfers have been cemented, they can be scaled up at a later point in time (Gelb/Decker 2011). Figure 14 depicts that direct cash transfers benefit all citizens equally, those lucky enough to have found their place within the existing patronage network (shown as those individuals sheltered under

the limited access order pyramid), and those left outside it.

Two problems remain: (a) governance structures need to be strengthened nonetheless, as this scheme cannot entirely replace revenue streams to decentralised units of government; and (b) direct cash transfers have, on their own, no effect on market failures that have to be tackled with coordinated public investments. Yet, these 'problems' only apply to a radical big-push approach to a cash transfer scheme. In combination with better international transparency; barter-contracts coupled with proper local-content stipulations schemes that help nudge developing country elites toward making better use of resource revenues; direct cash transfers can be a promising tool for decentralised pro-poor growth and poverty alleviation.

This study favours a nuanced approach to reforms in general and to cash-transfer schemes in particular: Cash transfers have to be treated as one of several tools needed to curb the resource curse. Finding the right combination of remedies for each country is a trial-and-error process, a roadmap that has to be flexible for path corrections once the journey has started.

Figure 14: Direct cash transfers to all citizens



Source: author.

Implementing the German TC Guidelines: Political Economy Recommendations

8



The above chapters gave general insights to the political economy forces in developing countries and showed the amplifying effects that natural resource rents can have on such forces. As this study is a supplement to the Technical Cooperation (TC) Guidelines – *Sustainable Economic Development in Resource Rich Countries* (GIZ 2015) – this final section provides political economy conclusions with regard to the Guidelines. Much like the TC Guidelines themselves, this section aims to give concrete advice to TC practitioners who are active in facilitating resource-driven development. It may be helpful for readers to keep the TC Guidelines nearby for cross-references.

When a country embarks on a resource-led development path, human lives are affected in numerous ways. The TC Guidelines are therefore linked with several adjacent issues that overlap with Sustainable Economic Development (SED) goals but that, in terms of German Development Cooperation, belong to other TC areas (e.g. Good Governance, Environment and Climate, or Security, Reconstruction and Peace). If technical cooperation is to be successful, all must be viewed through the lens of political economy. But the core focus of the TC Guidelines is on (i) creating economic linkages between extractive resource sectors and other, nearby sectors; and (ii) more broadly, structurally transforming an economy toward higher value-adding activities. This section focuses more on these two core SED intervention aspects and touches upon some of the Guidelines' suggested approaches. The TC Guidelines address these approaches first generally, then within the three thematic fields of *strategic planning* (GIZ 2015, pp. 24-28), *employment creation* (ibid. pp. 28-36), and *local economic development* (ibid. pp. 37-48), and, lastly, by separately examining the possibilities for *cooperation with extractive sector companies* (ibid. pp. 50-53). In line with this structure, the sub-sections below will examine a few of the TC Guidelines' features through the lens of political economy.

In a nutshell, the political economy trick for technical cooperation is to help resource rich countries create linkages and transform their economies without getting pulled into local resource conflicts. The trick is to help create jobs in and induce linkages to the extractive sector without getting the country stuck in a dead-end path of dependence on a dying sector. The trick is to partner with multinational extraction companies to create local economic development, without getting involved in worker exploitation, human rights abuses, or environmental pollution. And the trick is to help countries make use of resources-for-infrastructure barter deals with external partners – without spurring unsustainable

dependency relationships that leave behind another generation of unused *white elephant* structures.

8.1 SED, linkages, and structural transformation

Gavin Wright and Jesse Czelusta (2004) have shown that, historically, extractive sectors can be drivers for economic development: resource extraction has often led to technological learning and structural transformation, e.g. in the USA, Chile, or Australia. Today, the overarching SED objectives for turning subsoil extraction into a development driver are *linkage creation* and *structural transformation*.

Linkages for structural transformation: The *TC Guidelines* distinguish between a mining sector's employment effects as *direct* (in the mine), *indirect* (via jobs created up- or downstream from the mine), and *induced* (via jobs created in more distant sectors merely by the increased economic activity). In the linkage-creation language, indirect jobs come about via backward, horizontal, or forward linkages (i.e. inputs such as extraction machinery maintenance are backward linkages; laundry, catering, or entertainment services for miners are rudimentary horizontal linkages; and output value addition such as gemstone beneficiation or packaging are forward linkages). *Induced* jobs come about via consumption or fiscal linkages (i.e. as new jobs in this field increase the bulk of salaries, they increase the demand for various consumer products, thereby leading to yet more jobs – this is called consumption linkages; and the government's use of proceeds from mining to invest in health, education, or industrial policy programmes is known as fiscal linkages). The goal of nudging an economy toward evermore sophisticated and globally sought-after activities has been achieved via any of the above: Norway has, via backward linkages to its oil sector, created world class extraction machinery (Hunter 2014); Botswana has, via local content laws vis-à-vis DeBeers, established a significant diamond beneficiation industry (Mbayi 2013); and the USA's work in petroleum geology has created world class institutions of higher learning, such as UC Berkeley and Stanford University (Wright/Czelusta 2004, 21). Yet, any of these initiatives can easily fail or work against one another. The ingredients to successful industrial policy are hotly debated in the literature and are most likely very context specific. In broad terms it can be said with some confidence, that structurally transforming an extraction-led economy demands coordinated government planning and intervention.⁵⁵ But from a political economy perspective, any of these strategies run the risk of failure: creating a backward

linkage industry succeeded in Norway, but largely failed in Mozambique: Krause/Kaufmann (2011) show how SMEs providing inputs to the large aluminium smelter, MOZAL, became too specialised for the Mozambican market: once the project was completed, these SMEs had to scale down their sophistication in order to be competitive. Beneficitation worked in Botswana's diamond sector, but failed in numerous other countries, where heavy-handed government attempts to force domestic processing of local raw materials made little economic sense: one common obstacle was that the needed infrastructure was not in place, and plunging ahead without it hopelessly overstretched the existing infrastructure (particularly regarding power supply). In the process this often choked out of existence the small domestic industrial sector. This essentially led to negative structural transformation – the opposite of what was intended (Lin 2012). Fiscal linkage creation (i.e. using revenues from a primary sector to invest in other sectors) is the most straightforward approach to inducing structural transformation. Dubai and other Emirates are prime examples of attempts to push into financial and other high-end services. But examples of catastrophic failures from the import substitution industrialisation era also abound. For Africa, one seminal study showed how taxing primary sectors (cash crop agriculture) to finance fledgling industrial sectors led to little more than urban profligacy at the expense of rural misery (Bates 1981). Using extractive resource rents for structural transformation (i.e. as fiscal linkages) can thus equally lead to success or failure. In contemporary Angola, the president's daughter, Isabel dos Santos, is Africa's first female billionaire, and has established herself as an investor in telecommunications, banking, and media firms that seem to be competitive in several countries. This indicates that using oil rents for diversification into other, more future-oriented sectors can indeed occur, even if the concrete shape this takes can be more reminiscent of Don-Corleonean white-washing than of Schumpeterian boot-strapping.

The danger with such industrial policy plans, from a political economy perspective, is that in limited access orders few safeguards for correcting poorly devised plans are in place.⁵⁶ Local content policies that are meant to stimulate linkage creation can easily be perverted to serve narrow interests. They then generate pseudo-jobs and contracts for non-performing cronies that may overly frustrate and drive foreign investors away. The Nigerian case studies (Section 4) indicate that local content can lead to both, local success stories, and increased rent seeking (Adewuyi/Oyejide 2012, cf. *The Economist* 1st April 2015b).

Can Linkage creation lead to path-dependence on a dead-end mining sector? A commonly held political economy fear, regarding linkage creation, is that, once forward or backward linkages have been established, the lifespan of the mining cycle is near its end (Collier 2010). And, along with these new domestic firms that have specialised on the mining industry, new political forces have been created that jealously seek to keep investments and subsidies within the primary sector – thus having essentially created 'anchors' that lock an economy in place instead of structurally transforming it. Yet, this fear may be unwarranted. Once the initial hurdle has been taken – of creating truly productive and competitive domestic firms – such firms often manage to find new markets or manage to tweak their expertise sufficiently to realign it with the changed domestic market. Historically, such 'expertise tweaking' is what kept the initial mining cycle from being a dead-end sector: as firms were forced to find new resources or make better use of the existing but dwindling ones, technological advancements have led to new discoveries, new extraction techniques, or new processing innovations (Wright/Czelusta 2004). Inspired by these encouraging historical observations, the Open University's and University of Cape Town's joint research programme for linkage creation – *Making the Most of Commodities (MMCP)* – followed Wright/Czelusta's lead by investigating if the beginnings of such transformation developments could today be found in contemporary resource extracting sub-Saharan African countries. The researchers found that in several countries, such as Nigeria and Ghana, these did indeed exist (or had the potential to), and the flagship MMCP publication came to be called *One Thing Leads to Another* (Morris et al. 2012), which refers to Albert O. Hirschman's notion that one sector (i.e. extractive) can lead to another (i.e. industrial).

Having established that linkage creation is unlikely to glue a country to the low-value-added primary sector, and that it is thus indeed a desirable policy agenda for initiating structural transformation, the rest of this chapter skates down the TC Guidelines' sections to give political economy pointers on some of its intervention recommendations.

8.2 Planning visions and implementing strategies coherently (GIZ 2015, pp. 24–28)

Long-term prudent strategy development: For creating trans-sector vision plans, the TC Guidelines note: "the pursuit of an economically sustainable form of mining, which also opens up future options for development, can only suc-

ceed through cross-sectoral approaches. In the real economy this calls for a high degree of coordination and cooperation between the key stakeholders in various technical disciplines, administrative structures and economic fields” (GIZ 2015, 23). The TC Guidelines reiterate that this provides suitable intervention points for German TC to facilitate communication channels and platforms.⁵⁷ This study – the theory section (particularly in Section 3.1) and the case study sections (particularly in Section 4) – described that successful long-term and prudent planning presupposes, first and foremost, the political stability that allows for a reform consensus among elites.

In the early 2000s, many developing country governments decided (or were urged by donors) to acquire all-encompassing quarter-century vision documents for their countries, mostly modelled on successful East Asian visions.⁵⁸ For this, many governments hired external consultant firms (e.g. McKinsey & Co.) to undertake the needed feasibility studies and produce the manuscripts. Such outside consultants are usually western-educated policy experts, who are knowledgeable in (i) contemporary OECD-country reform-agenda case studies, and (ii) the growth miracles of the East Asian Tiger countries. Whereas their predecessors tended to take for granted the soft infrastructure – i.e. a functioning legal system, adequate property rights, reliable and impartial law-enforcement – that is so readily available in advanced countries but sorely lacking in low-income countries, this new generation of consultants based their road-maps more on the trial-and-error approaches of other developing countries. This was an improvement, because learning from successful limited access orders is more promising than trying to duplicate open access order reforms that underlie a different political economy dynamic. Yet, two core problems remained: the notions that vision planning is (a) essentially a technical economic undertaking that (b) could be copied from other parts of the world are most likely both incorrect. Much has been written about the failures of western ‘fly-by’ consultants whose reform-plans tried to use the blueprints of Asian success cases for client governments of low-income countries elsewhere (e.g. Andrews 2013; Kellsal 2013, Whitfield et al. 2015). The essential difference between the original success visions and their failed duplicates is that the former were devised by local insiders, who understood which reforms were politically attainable. The basic groundwork for drafting successful vision documents is the political give-and-take among the leaders of powerful groups. Fragile political settlements cannot sustain overly progressive reform-plans that go against the interests of powerful groups.

Interface management & consensus-finding processes: From the viewpoint of TC practitioners, the above creates the dilemma that the politically powerful groups needed to make vision-implementation successful, are not the same as the affected stakeholders whom TC practitioners would like to see empowered. To the contrary, they are often the landed oppressors, the cartels that act as middlemen, or the state officials who profit from existing red tape and legal loopholes. As reform-minded elites in weak states have limited options for dealing with such groups, they have to co-opt some of them, to be able to confront others. In such political environments it can be difficult for outsiders to decipher what developmental leadership entails. It is often too simplistic to interpret a heavy hand or an ignored corruption scandal as signs of despotic or dishonest leadership. And it can be difficult for reform-minded elites to speak openly with TC practitioners about the informal political constraints they face when genuinely trying to implement a particular reform policy. This is because, to some extent, TC practitioners’ hands are tied. Operating as they do under the mantle of ‘good governance,’ they could not go along with many of the actions needed to implement reforms in a limited access order. But TC practitioners who understand and are sensible to the political economy dynamics involved will most likely create a less pejorative and more cooperative atmosphere with domestic reform partners. This makes it easier to listen for subtle cues regarding what is and what is not feasible in a given political settlement.

8.3 Activating & expanding employment potential (GIZ 2015, pp. 28–36)

The TC Guidelines offer several intervention points for TC practitioners in the realm of employment creation. This section addresses two of them: (i) assistance in providing sector-relevant skills and qualifications training, and (ii) providing platforms for firms and workers to organise, articulate their interests, and address bottlenecks for employment creation vis-à-vis the government.

Technical and vocational education and training (TVET) is arguably as important in limited access orders as it is in open access orders. Yet, in the former, results of such training are often not as obviously discernible at the outset, and TC practitioners are likely to experience distinct backlashes from both employers and employees. Understanding the mechanisms behind these backlashes, and hence being able to incorporate them into planning and expectation management, can save TVET facilitators from unnecessary frustration. To

recap, compared to the open access orders of advanced countries, the incentive system in limited access orders of developing countries is such that merit is less important and personal connections are more important. If it is informally decided who receives jobs or procurement contracts before merit issues are even considered, those TVET recipients who happen to enjoy the needed connections may see technical training as a nuisance, while those TVET recipients who do not have these connections may see technical training as a hopeless waste of their time. For TVET facilitators and instructors, this can sometimes result in abstruse circumstances that are difficult to manage. For example, trainees who are sure of their position in the network of political connections may send others to sit through class in their stead.⁵⁹ Conversely, those who lack the needed political connections to score a job or a contract can have the intuition that taking part in TVET is not going to improve their chances. Hence these ‘outsiders’ may be more interested in the daily allowances/stipends or travel opportunities than in the actual contents of a given workshop.

Thus, in comparison with TVET in the OECD-world, the benefits of such initiatives can be less straightforward in limited access orders. But it would be a mistake if TC practitioners despaired and attributed the encountered problems to primordial cultural traits. As North et al. (2009) note, only 300 years ago, *every* social order on earth was a limited access order. Letters from British travellers to Germany attest that, in the 19th Century, Germans were seen as ‘a dull and heavy people’ who ‘never hurry.’ In Japan, a 1911-12 British traveller observed ‘objectionable notions of leisure’ and ‘evidently no desire to teach people to think’ (Hodgskin 1820, Shelly 1843, Webb 1986, all cited in Chang 2007, 183). And in the early 20th Century non other than the great sociologist Max Weber wrote that Confucianism was incompatible with capitalist development (Fukuyama 1995). Yet, since then, Germany and much of East Asia have caught up successfully. And a historically broad view shows that all limited access orders are currently opening, some faster, others slower (and all doubtlessly with regressions) (Pinker 2011; Diamandis/Kotler 2012; Naim 2013). As the world becomes more meritocratic, TVET is immensely important as it has various direct and indirect effects: i.e. some entrepreneurs who are well-connected may nonetheless seek to exert the effort needed for entering new markets; some hitherto unconnected job-seekers may use their newly acquired skills to pursue careers abroad and return home some decades later as quasi-foreign direct investors; others may combine their newly gained adding-value skills with a capability to engage with a new patron to elicit protection, thus being able to

establish a successful new firm. Many of the recently arrived Chinese micro-entrepreneurs in Africa are seemingly on their own, without backing from the Chinese state. Their successes attest to such possibilities (French 2014).

Hence, it may help to keep in mind that adverse cultural traits are not causal, but at best, intermediate variables; that technological learning has historically been *the* mechanism for structural transformation (Wright/Czelusta 2004; Stiglitz/Greenwald 2014); and that, in the greater picture, almost all low-income countries are currently changing and developing at historically unprecedented rates. Hence extraction sector TVET initiatives are well worth the effort, as they are very likely to eventually bear fruit in one form or another.

Coordination among unions and business associations: An important TC intervention tool is to support the establishment of new or strengthening of existing business associations. Such efforts are well invested: local business associations can help formalise state-business relations and thus bring some transparency to the lobbying process. But when aiding from the outside, TC practitioners have to keep in mind that such (often newly established) associations do not fill a vacuum. Rather, they compete with existing networks that are informal, but (i) are entrenched with the local population, and (ii) are well-connected to powerful political patrons. Thus, throughout the developing world, two forms of private sector organisations exist: formal (i.e. unions, private sector alliances), and informal (i.e. ethnic or religious affiliations and fraternities). The former are often quite visible in urban areas, run by articulate middle class activists and often supported by donors. But when it comes to actual political influence, many formal organisations are rather weak.⁶⁰ Exceptions exist: some formal organisations thrive on their great numbers (e.g. teacher unions or, to a lesser extent, health worker associations), others thrive on the fact that powerful elites personally invest in a particular sector (e.g. transport associations can be strong if the owners of private minibus fleets are also high-ranking politicians). Dismissing formal private sector alliances in low-income countries as mere urban charades (Chabal/Daloz 1999) is therefore much less accurate for the current growth period (1995-2015) than it was for an earlier period of stagnation (1975-1995). Yet, informal networks are arguably still stronger in many sectors. Especially when it comes to extractive resources, much is still done informally. The deals made, for example, with Chinese extraction and construction companies usually go directly through a country’s president (Burgis 2015, 81-102; Soares de Oliveira 2015, 184-192). The problem from an outside observer’s perspective is that, like secret sororities, such net-

works are hardly visible. Thus, it is often cloaked in obscurity which domestic entrepreneurs benefit from extraction deals and for what reasons.

For TC practitioners, helping to forge new private sector alliances (or strengthening existing ones) is nonetheless a worthwhile initiative for bringing more transparency and eventually fairness to an economy. But, especially in the extractive sector, formalising business relations must be seen as a longwinded and piecemeal process that is prone to experience backlashes from the informal system. To start with, it is good if TC practitioners are aware of the existence of such parallel alliances, and it may help to approach them for limited cooperation. They are the vehicles for nepotism, but they do not necessarily have to be viewed as entirely disruptive or economically ‘backward.’ Seen in a different light, these are informal institutions that uphold the societal glue of trustworthiness according to personal group membership, as long as the impersonal legal system is too weak to do so. Historically, whenever a legal system became strong enough, such groups morphed into formal organisations or disappeared (Greif 2006). More troubling alternatives to such informal state-business collusion sororities appear in less stable countries and territories: decentralised quasi-warlords of the kind found in Nigeria’s Delta. Section 5 gave the example of a protection racket – Alali Horsfall’s Dukoaye Security Services – that operates independently from the state, not because Nigeria tops the Doing Business charts, but because narrow interests and informal networks have infiltrated the state to a degree that makes it unable to enforce the country’s laws.

8.4 Developing sites and their surroundings (GIZ 2015, pp. 37-48)

Much of this TC Guidelines section focuses on the societal and political effects near mining sites, thus going beyond the narrowly economic focus. These broader SED goals sometimes lead directly to better linkage creation and structural transformation. But often, they serve indirectly, by protecting the human rights of locals, ensuring that other measures for linkage creation and structural transformation do not agitate delicate socio-political issues. Three of the Guidelines’ suggested approach angles are discussed here from a political economy perspective: (i) providing information, (ii) supporting political decentralisation, and (iii) creating social capital.

Eliminating information asymmetries: The TC Guidelines note that with regard to available local SME capacity a “[l]ack of information concerns all stakeholders in equal mea-

sure.” While this is true, TC practitioners have to be aware that in any limited access order situation, some stakeholders are interested in keeping information obscure: be it because they or their close affiliates enjoy a quasi-monopoly which they see threatened; because they want to keep a loophole open for corruption; or simply because they fear that more transparency would expose their past ineptitudes. In some instances the lack of information is indeed an apolitical, technical circumstance. But generally, information asymmetries are a tool for limiting access. Trying to rectify this, falls squarely into the category of opening access: i.e. democracy promotion. Shining a light on the plight of local populations is utterly needed and desirable. Yet, from a political economy point of view, it helps to keep in mind that this space is as politically contested as any other. As soon as outsiders have entered the theatre – be it in the form of politically alert TC, or western advocacy or human rights organisations – their influence alters the existing power equilibrium, and thus, often unknowingly, becomes a cog in the game of jockeying for power. In the best cases, local communities with genuine grievances can use the new spotlight to protest and complain. Yet, since local elites (and local elites in waiting) usually have a better grasp on events on the ground, they can easily manipulate existing community grievances and desires to initiate protests for causes that suit their political agenda and would not otherwise have existed. Examples of such cases of politically motivated grievance displays abound.⁶¹ Such warnings are not meant to discourage TC efforts to empower local communities in mining areas; the benefits of transparency certainly outweigh. It is, however, helpful to go into such endeavours with a firm grounding in the various mechanisms that await below the surface of otherwise seemingly straightforward disputes. Helping local communities in any locality means to enter not a vacuum but a highly politicised space.

Political decentralisation: While the TC Guidelines do not directly recommend decentralising mining revenues, the spirit of decentralisation is an implicit foundation to many of the suggested approaches. Decentralisation has long been a focus area of German Technical Cooperation and the core implementation problem has rightly been located at the central level: with interested central government power holders. With regard to decentralising mining revenues, the stakes are significantly higher, and backlashes against decentralisation reforms are likely to increase accordingly. However, the case studies of Peru and Ghana (Section 6) show that once the initial hurdle has been cleared – of getting decentralisation reforms passed by the central government – new challenges arise at the local level. Enhancing the capacity of local level state agencies, be it merely administrative or political, may or

may not end up benefiting the impoverished local community (see Eaton et al. 2010). Successful decentralisation is a thin line between giving the local community too little autonomy, thereby risking unrest (Lijphart 1977), and handing over too much autonomy, thereby risking secession attempts (Horowitz 1985). In any event, bringing government closer to citizens does not guarantee that the distribution of resource revenues will be made more equitable. It merely brings the limited access order logic from the national to the local level.

*Facilitating dialogue & strengthening social capital.*⁶² The TC Guidelines emphasise the role of local change agents. Supporting progressive movements to make revenue distribution more equitable or political processes more inclusive is a central role for good governance initiatives. But from a SED perspective that is political-economy sensitive, two points must be kept in mind: (i) in many countries, economic change, in the form of structural transformation, did not necessarily spring from policies that were initially designed as inclusive or pro-poor. Quite the opposite, companies that started out as nepotist structures of zealous state-business collusion often turned out to be, in hindsight, the drivers for structural transformation (Khan/Jomo 2000; Kang 2002). (ii) local ‘change agents’ who can change the political settlement in a desired direction may be difficult to spot at the outset. In the past, individuals who challenged the status quo, by championing democracy and equal rights for all, have often failed to stick to these values once given the opportunity to apply them (Lemarchand 1992; Callaghy 1994). Yet more sinister readings suggest that many who pose as local change agents do so for the opportunity thus granted by outside supporters who, in transferring their own OECD-world experiences, misunderstand the local political settlement and can easily be deceived by familiar slogans (Kasfir 1998; CFS 2010). Here too, these warnings are not meant to discourage TC practitioners from supporting local communities, or to make them overly sceptical of local grievances. Often hopelessly overpowered by a network of foreign extraction companies, central elites and local elites, such small groups are indeed nearly voiceless and could use all the outside help they can get to make grievances heard.

8.5 Extractive sector companies as levers for development cooperation (GIZ 2015, pp. 50-53)

Partnering with western multinational companies: Western extraction conglomerates that invest in limited access order

countries often find themselves in the peculiar position of having to cater to the incentives of (i) their shareholders; (ii) their democratically elected home governments; and (iii) their contractual partners: local limited access order elites. For the local elites, rather than rely entirely on foreign multinationals, it is more profitable and hence more desirable to have a well-run state-owned resource company such as Sonangol.⁶³ But elites in fragile limited access orders often have no other opportunity than to work with foreign companies. An extreme example of this is Equatorial Guinea’s obscure holding company, Abayak S.A., which apparently ran from President Obiang’s home as a silent partner to MNCs, eliciting large payments for inexistent services (Maass 2009). For western extraction companies, once they have decided to become active in such a difficult political environment, it can become next to impossible to act in accordance with all three of the above principals (company shareholders, democratic home governments, and domestic leaders).

Quantified project objectives, as mentioned by the TC Guidelines in an example of Mozambique and Madagascar, include targets to “increase of 30 percent SMEs providing goods and services,” “at least three vocational training centres,” or “at least five market oriented rural development projects” (GIZ 2015, 52). These may be needed as rudimentary benchmarks. But the actual cooperation benefit will most likely come from more qualitative achievements that go beyond this, are case specific, and only emerge when the different actors’ incentives for cooperation genuinely overlap. One interesting finding from the Making the Most of Commodities Programme is that first tier suppliers (original equipment manufacturers such as Caterpillar) employ procurement managers who tend spend minimal time periods in country but have a global network of tried and tested suppliers for everything from spare parts, to laundry, to catering services. These procurement managers, in turn, have strict quantified directives from head office that dissuade procurement managers from taking a chance on a new local supplier. Here, TC practitioners can help by (i) convincing companies that they would fare better, in terms of their ‘social licence to operate,’ if they gave procurement managers more leeway for trying out new local suppliers; by (ii) cooperating with companies in building the local capacity to supply, e.g. via technical and vocational training; and by (iii) assisting host countries in devising local content legislation that is at once flexible enough to allow for realistic operationalisation, and ridged enough to gain traction by taking away the procurement managers’ easiest option of contracting established foreign firms for even the most rudimentary services.

Resources-for-infrastructure: The TC Guidelines also mention the possibility for German TC to get involved in resources-for-infrastructure barter trades (GIZ 2015, 42). Section 7.2 above discussed the pros and cons of such arrangements in some detail. In brief, from Germany's TC perspective in general, and from a Sustainable Economic Development perspective in particular, the following should guide the decision on whether to engage or not, and if so, what to look out for:

- On their own, Chinese resources-for-infrastructure deals often stand in direct conflict with linkage creation, transparency, and pro-poor development spending. Most Chinese projects were built by Chinese companies, via local blue-collar workers, but exclusively via Chinese managers and engineers (French 2014). They have built infrastructure projects that often disproportionately catered to the elite and urban middle classes (Alves 2012). And some of them have been extremely opaque, involving such dubious 'gifts' as gigantic sports stadiums (which happen to be ideal for elites' political rallies).
- With German TC getting involved as an honest broker, such deals would have to manage a balancing act between (i) including realistic and water-tight local content stipulations, as well as taking all of the World Bank's Chad-Cameroon Pipeline Project's stipulations on board, regarding prudence, pro-poor spending, and transparency; and (ii) based on the knowledge that big-push good-governance reforms cannot be implemented in weak-state low-income countries, all the above stipulations must be carefully engineered as piece-meal conditions, and all relevant domestic partners must be involved.

8.6 Conclusions

TC practitioners tasked with assisting low-income resource-driven countries may be discouraged by this study. Yet its aim is not to deem their work futile. By outlining the involved difficulties, the study seeks to help readers prepare. Resource-driven development is possible, several countries have done it in the past, several others are doing it in the present, and more will doubtlessly follow in the future. This study has mostly been concerned with showing the obstacles. Further research should illuminate what the countries that managed to overcome the resource curse had in common. Looking through the political economy lens introduced in this study, it can be said with some certainty that their reformers must have had two things in common:

- (1) They must have taken the informal system of accommodating powerful elites serious and must have adequately incorporated these elites into their reform agendas. If merely implicitly acknowledged, or explicitly formulated, these reformers, when breaking the mould, must have worked with the grain (Kelsall 2013; Levy 2014).
- (2) They must have delivered their reform policies in carefully dosed and well-timed combinations of several of the introduced above tools. More important than choosing the right reform tools, is to flexibly implement the chosen tools, adjusting them to the country's political settlement. Single big solutions hardly ever lead to the desired outcomes, especially when taken as blueprints, copied from other parts of the world (Andrews 2013).

(1) Take serious the informal system that accommodates powerful elites: It is no coincidence that developing country politics has long revolved around consensus-finding. As an outsider, one should be careful not to overestimate the powers of domestic reformers. TC fails when it consists of coming into a limited access order with an open-access-order mind-set, seeking to help reformers devise laws that resemble those of the OECD-world (Andrews 2013; Grindle 2007; Kelsall 2013; Booth 2012; CFS 2010). Development in limited access orders may be comparable to a cold war, where several nuclear powers possess the power to destroy everything. Powerful groups have to be included in any development strategy. TC practitioners may once find themselves in a situation where the claims or ideas of particular individuals at a negotiating table seem too backward to be considered. Yet the political leader, in the name of 'finding a consensus' seeks to include them anyway. As wrong as this may seem, before advising the leader to push through and exclude some from the negotiation table, it helps to recall the limited access order logic. These are political decisions that leaders will have to take, weighing all the informal channels, all the unspoken possible consequences. This field is complex, and developing country leaders are experts at navigating it. Which elites have to be included and which ones can be excluded falls squarely outside the realm of technical cooperation advice. Pressured into a wrong decision, the outcome may fall in the realm of disaster relief.

(2) Start modest, combine reforms, and implement them via trial-and-error: Nigeria will serve as an example: The Petroleum Minister is widely quoted for a claim he made in 2010: the Nigerian Content Act would, by 2015, provide 30,000 jobs for Nigerian professionals. Spread among the roughly 170 million Nigerians, this would, were it achiev-

able, provide one oil job for every 5,667th Nigerian – a drop in a tanker. By contrast, Sala-i-Martin/Subramanian (2013, 603) came up with a direct cash transfer calculation for Nigeria that would pay every Nigerian, every year, the purchasing power parity of roughly US\$800. The first measure is extremely elitist, providing management and engineering jobs for professionals who would otherwise most likely leave the country in search of work abroad. Yet these few could be the Schumpeterian entrepreneurs needed to pull Nigeria's economy up the latter by turning the enclave oil sector into a development driver. The second measure is perfectly egalitarian – it would eradicate poverty in a single swoop. Both measures are important. But both measures are also too ambitious to be achieved. The Petroleum Minister's figure is based on local content requirements of which, as Ovardia (2013a, 263), based on a consensus among industry experts concludes: “many are completely unrealistic, it is reasonable to expect that the NCDMB [Nigerian Content Development Monitoring Board] will be issuing waivers to the requirements on a regular basis, which brings into question

the rationale for the guidelines in the first place.” Sala-i-Martin/Subramanian's figures are arguably even less realistic. The authors' argue for a big-push cash transfer scheme that would give away all of Nigeria's oil revenues to citizens. From a political economy viewpoint, this idea would be difficult to implement in Norway. To suggest it for Nigeria seems odd. In principle, however, both of these measures are important, and less ambitious versions of them would even be compatible. This goes for the other remedies as well. Using Chinese barter deals for opening particular infrastructural bottlenecks – e.g. building a seaport or paving a road between two cities – may bring about so much economic activity that these projects are desirable even without local content stipulations. Using transparency initiatives can drain the theft in the Delta and the corruption in the state that makes the theft possible. But prior to this, real adding value alternatives have to be put in place, lest those who fear their loot foregone decide to demonstrate their holding power. Here, local content stipulations, linked to a barter deal, could prove useful.

Notes

- ¹ Readers active or interested in the thematic field of National Economic Planning are invited to consult the Limited Access Order framework (Section 3.1 and Section 4). The field of Employment Creation is best addressed by reading up on the Politics of Industrial Policy (Section 3.2 and Section 5). And Local Economic Development is most closely associated with the Political Settlements Theory applied to regional elites (Section 3.3. and Section 6).
- ² A debate in the literature is concerned with measuring and categorising resource wealth and resource dependency. ‘Resource rich’ usually refers to a country’s absolute resource wealth. To exclude the diversified economies (e.g. Australia, Norway, USA) that have fewer difficulties with the resource curse, the terms ‘resource driven’ or ‘resource dependent’ are used. How resource driven/dependent a country is, can be measured as a percentage of either government revenue or of total exports (IMF 2012, 61). Some advocate measuring resource wealth in per capita terms (see Ross 2012).
- ³ The term ‘Dutch disease’ refers to the Netherland’s predicament from offshore gas discoveries in the 1960s. It was coined by *The Economist* (1977) and formally modelled by van Wijnberg (1984) and discussed by many others since, e.g. Krugman (1987), Sachs/Warner (1995), Matsen/Torvick (2005).
- ⁴ Norway’s mechanisms for counter-cyclical spending and its safeguards against political corruption keep it on course as one of the richest countries on earth (Hodler 2013).
- ⁵ Before 1980, seven large western oil companies dominated the sector, which left host governments with a much *steadier* stream of much *smaller* revenues. Since then, the OPEC cartel allowed national oil companies to derive a much greater (and much more volatile) portion of the revenue stream. Today the likelihood for a country to be governed by an autocrat is 50 per cent higher in an oil state than in resource poor countries (Ross 2012).
- ⁵ This section draws equally on insights from Mushtaq Khan (2010) and on North et al. (2009, 2013). The notion that ‘violence’ is the key explanatory variable comes from North et al. (2009). But Khan’s notions of ‘stability’ and ‘holding power’ are closely related.
- ⁷ The term ‘bottom billion’ is Collier’s (2007), and refers to the world’s approx. 44 least-developed countries.
- ⁸ See Greif (2006) and Fafchamps (2004) on group-reputations that compensate for weak legal systems.
- ⁹ The term ‘violence specialist’ is used by North et al. (2009) and refers to those who substantially invest in honing their violence potential.
- ¹⁰ The term ‘rent’ is used in its broad and original form: as the return on an activity minus the value of alternative activities forgone (North et al. 2009, 19). In the literature cited here, this term is used interchangeably with state revenues that are shared according to formal or informal arrangements.
- ¹¹ This explains the empirical finding that countries which have experienced a civil war in the recent past are more likely to face a renewed outbreak of war than are countries with a more peaceful history (see Collier/Hoeffler 2004).
- ¹² Section 3.2 will introduce a variant of this arrangement where some powerful factions are excluded from the ruling coalition.
- ¹³ This is why wars are often longer (Vietnam) or shorter (Six-Day) than anticipated: one’s own strength relative to that of an opponent is hard to measure in peacetime.
- ¹⁴ This particular notion, while it complements the limited access order theory, is Mushtaq Khan’s (2010).

¹⁵ [a triangle of three circles: 1. 'a faction of the ruling elite that are developmentally oriented', 2. 'Domestic entrepreneurs/firms that are willing and have a realistic chance of becoming globally competitive', 3. 'a pocket in the state bureaucracy that is organisationally capable & politically unrestricted'].

¹⁶ This is a heuristically simplified version of industrial policy, supporting one single firm. These relationships usually include several firms in one or more sectors, or in a cluster.

¹⁷ According to this framework, SMEs that have no relationship with the elite could not be in a position to become globally competitive. Unaffiliated, their paths would be severely blocked by the power structure. An interesting test for this is the many independent Chinese SMEs currently trying their luck throughout Africa (see French 2014).

¹⁸ A vivid example from the oil sector is the oligarchs in Russia who, after privatisation, became a political threat to the Kremlin elite.

¹⁹ For Indonesia see Lewis (2007). The Angolan president's daughter, a media and telecommunications entrepreneur, recently became Africa's first female billionaire (*The Economist* 12th April 2014; APP 2013, 20).

²⁰ In extreme cases, entire plants were transferred to new owners (Chang 1994; Lee 1991, cited in Khan 2003, 178; Kang 2002). However, as this chapter will show, it is not the simple act of applying pressure to firm-management that *causes* East-Asian-like successes. Rather, it is a combination of fortunate developments which makes applying such pressure possible in the first place. Hence the difficulties often encountered when attempting to transplant 'best practice' reforms from one political settlement to another (Andrews 2013).

²¹ Khan's term is broader and therefore more widely applicable as it includes non-violent confrontations such as strikes and sit-in protests. This provides the insight that a group's power is not merely measured by its violence potential, but also significantly by its members' readiness to endure losses. This makes large groups of poor members often more powerful than affluent groups. The latter usually have superior means to fight (i.e. to employ violence specialists) but because they also have more to lose, materially, in a violent confrontation, they tend to give in easier to their adversaries' demands. This means that, in spite of richer group's superior violence potential, they sometimes command less holding power than poorer groups.

²² The other two frameworks also discuss the power relations between top-level and lower-level/regional elites, but Khan most concretely spells out who the lower-level elites are (e.g. urban middle class professionals) and what the dynamics between them and the country's top-level elites are.

²³ Section 6, below, uses the concept of 'inclusion of excluded elites' to explain the dynamics of 'political settlements with regional elites' in Peru, Ghana, and Kenya. While excluded elites can also be based on urban classes, factions, or religions, this study seeks to explain those based on particular regions (i.e. resource extraction regions).

²⁴ See Barma et al. (2012) for more on these categories regarding resource rent management.

²⁵ This new dynamic starts with the mere prospect of new rents (i.e. the announcement of a sizable new find), even if the rents are not available for several years. A simple game theory model explains this: with even a slight first-mover advantage, the mere expectation of future resource rents sets the new dynamic in motion.

²⁶ Equatorial Guinea's 2011 PPP GDP per capita was 45th in the world; its HDI rank was 136th (APP 2013, 22).

²⁷ This is in line with a wider culture of gift-giving throughout the SPLA of South Sudan, where senior officers misappropriate funds and personalise the military loyalty codex by e.g. paying the dowry for subordinates who could not otherwise afford to marry (Pinaud 2014).

²⁸ Observers are divided over whether this coup attempt was real, or if Kiri's allegations were a pre-emptive move against Machar. For the purposes of this study it does not matter who actually started the war.

²⁹ ChevronTexaco and Petronas were also substantially involved. Exxon had approached the World Bank as guarantor, because Chad seemed unstable as Deby himself had only come to power in 1990 via a coup d'état; the World Bank in turn came up with the elaborate conditions for the project. (Exxon merged with Mobile in 1999.)

³⁰ This mechanism is often called 'obsolescing bargain,' a term that is attributed to Vernon (1971).

³¹ Readers may object that Equatorial Guinea's regime – with President Obiang having been in power for 35 years – is stable. Yet, it is argued here that Obiang's narrow power base

and his tightly authoritarian rule are so exclusionary, that the society is locked in rigidity. The systemic vulnerability is such that the government can focus on little else besides avoiding its own demise.

³² ‘Isomorphic mimicry’ describes how formal institutions, transplanted from other parts of the world, act as fronts that outwardly appear like OECD-world laws, but inwardly function, if at all, to a different, informal logic (Pritchett/de Weijer 2010). The hybrid system between formal and informal institutions is also a prevalent theme in the neopatrimonialism literature (see e.g. Bratton/van de Walle 1997).

³³ BHP-Billiton owned 66 per cent of MOZAL, South African Industrial Development Corporation owned 20 per cent, Mitsubishi 12 per cent and the Government of Mozambique 2 per cent (Krause/Kaufmann 2011, 48).

³⁴ In 2014 President Guebuza was succeeded by the current president, Filipe Nyusi (former defence minister). Nyusi was selected from a group of only three, who were all tight Guebuza allies. Some observers see President Nyusi as a weak proxy for Guebuza who continues to wield substantial power behind closed doors (EIU 2014a).

³⁵ Angola is Sub Saharan Africa’s second largest oil exporter behind Nigeria: \$100bn annually (ibid.).

³⁶ These seven are: (i) fabrication and construction; (ii) well construction and completion; (iii) modification, maintenance and operations; (iv) transportation; (v) control systems and information and communications technology (ICT); (vi) design and engineering; and (vii) consultancy.

³⁷ Ovadia notes, quoting an interviewee: “For many public officials, there is a general sense that what the IOCs [International Oil Companies] report is simply not a reflection of what is actually occurring on the ground: ‘but how do you confirm that? ... I told you there is an issue of sincerity. It’s not there. How do you validate?’” (2013a, 267).

³⁸ In early 2014, Nigeria’s Central Bank Governor Lamido Sanusi submitted a claim to a Senate investigatory committee that some US\$20 billion went missing in NNPC over the past years. Petroleum Minister Diezani Alison-Madueke was outraged, and President Jonathan suspended Sanusi (*The Economist* 1st March 2014).

³⁹ This view assumes that regional patrons face competition from within the regional pyramid, and that a display of modesty toward the central government could see a regional patron replaced by an adversary.

⁴⁰ The Kikuyu in Lamu are geographically concentrated around an agricultural settlement in Mpeketoni, which was established in 1973 for landless Kikuyu, with the help of Germany’s GTZ.

⁴¹ Lower mineral prices would then simply lead to slower loan repayments.

⁴² Technically, most barter deals are merely EXIM Bank loans that are backed up by host country’s future oil proceeds. Oil provides the means for countries not to default, international credit ratings provide the incentives.

⁴³ In 1997, Mexico’s government began several successful cash transfers for poor mothers who bring their toddlers to medical check-ups, and make their children attend school regularly. This had initially nothing to do with natural resource revenues. But its great success as a poverty-reduction tool led a number of development policy advisers to advocate for oil-to-cash schemes in resource rich countries.

⁴⁴ The Kimberley process managed to significantly curb the sale of conflict diamonds, defined as “rough diamonds used by rebel movements to finance wars against legitimate governments” (www.kimberleyprocess.com). It was established collaboratively by NGOs, governments, and the diamond industry (cited in World Bank 2010, 33).

⁴⁵ To counteract these problems, the EITI Standard has last been refined in May 2013. Opinions on EITI’s usefulness diverge. While some observers seem optimistic about the new Standards and see a continued role for EITI as complementary to legislation (e.g. Collier 2014; Short 2014, 13; on the new EITI Standard see Short 2014, 10-11), others indicate that they feel the EITI has outlived its usefulness with the emergence of widespread legislation (e.g. Soros 2014; Soares de Oliveira 2014). Yet others, notably from the extractives industry, instead, see Western unilateral legislation as doomed, and see the only viable future in the EITI process, because it does not discriminate against companies depending on their origin (Rees [on behalf of Shell] 2014). As of June 2015, of the 48 countries having joined EITI, and implementing the Standard, 31 have reached ‘compliant’ status of meeting all EITI requirements, five

countries have been temporarily suspended (www.eiti.org/countries; see also (Short 2014, 11).

⁴⁶ See Hughes/Pendred (2014) for details.

⁴⁷ These mostly come in two related forms: (a) western extractive companies' diminished competitiveness vis-à-vis developing country competitors; and (b) concerns regarding breaches of host country law (see Rees 2014).

⁴⁸ See also Patey (2010, 622). Other observers give more weight to Sudan (van Dijk et al. 2010, 67).

⁴⁹ See Foster et al. (2009) and Alves (2012) for these figures respectively.

⁵⁰ Yet, Alves (2012) notes that the DR Congo and Gabonese projects have been particularly marred with difficulties.

⁵¹ In 2012, GDP growth rates were estimated to be 14 per cent annually until 2016 (IMF, cited in *The Economist* 21st Jan. 2012). Yet, problems arose: growth in 2014 was 7.8 per cent and is now expected to be merely 3 per cent in 2015, and 5 per cent in 2016 (ADB 2015, 158-61). This is mainly due to an ongoing legal dispute with Rio Tinto, the foreign investor responsible for bringing the Oyu Tolgoi copper mine on stream, and due to China's lower demand for coal – which is still Mongolia's main export (*Economist* 11th Oct. 2014).

⁵² Enkhbayar's home was under siege over night, and live TV footage showed masked anti-corruption authority agents enter the next morning to carry him out, his bare feet above their heads (see: www.youtube.com/watch?v=n_32V8_cMs4). At the time of this writing the aging Enkhbayar is serving the rest of his sentence in hospital.

⁵³ For Nigeria, see Sala-i-Martin/Subramanian (2003, 2013); for Ghana, see Moss/Young (2009), Standing (2014); for Iraq, see Birdsall/Subramanian (2004).

⁵⁴ Compare this to the findings of a now famous study on expenditure tracking in Chad's health sector, where the authors tracked the proportion of non-wage allocations that arrived at their intended destination. The result: only 1 per cent of these funds ended up in the hospitals to serve their intended purposes. 99 per cent were 'lost' along the way (Gauthier 2006).

⁵⁵ Yet, even this broad statement is disputed by free-market proponents who contend that the harm of such state interventions mostly outweighs their benefits (e.g. Buchanan et al. 1980; Klein/Hadjimichael 2003).

⁵⁶ This is not to say that OECD-world industrial policy projects are failsafe. But differences do exist: recent cockups in Germany, such as Stuttgart's train station, Hamburg's philharmonic, or Berlin's airport, were all met with vehement public backlashes. By contrast, dwindling coco revenues were used in Cote d'Ivoire to build the world's largest cathedral in the president's home village. And in Dakar, Senegal's president had a gigantic bronze monument erected (of a family that curiously resembles his own), and he had a city tunnel built, which is frequently flooded and serves no discernable infrastructural purpose.

⁵⁷ A document that complements the TC Guidelines well, with regard to strategic planning in Africa, is the Africa Mining Vision (African Union 2009).

⁵⁸ For a discussion of these documents, see Kayizzi-Mugerwa (2013).

⁵⁹ They may feel they have the security to be able to learn on the job everything they need to know, or worse, believe that it is understood that the MNC, in return for being permitted to 'drain' the nation's wealth, should pay the local service providers while doing the outsourced jobs in-house underhand.

⁶⁰ Formal associations (sometimes called professional organisations) have evolved in the OECD-world as the middle classes grew larger and thus more powerful vis-à-vis the ruling elites. Low-income countries, per definition, have small to non-existent middle classes. Thus, their organisations have little to no effect when bargaining with the elite. A particular exception is when external supporters artificially increase these organisations' power (either directly by supporting them financially, or indirectly by pressuring the political elite).

⁶¹ For critical reviews of advocacy and civil society organisations in Africa see Lemarchand (1992); Callaghy (1994); Kasfir (1998); Chabal/Daloz (1999, 17-30); VonDoepp (2002).

⁶² The term 'social capital' is used by different scholars (e.g. de Tocqueville, Bourdieu, Coleman, or Putnam) to mean different things. Generally, the weaker a state, the stronger the social capital (e.g. see the strict informal communal/reli-

gious rules applied in near-stateless areas of Somalia or rural Afghanistan). This type of social capital, sometimes called bonding, is exclusive to in-groups: religious communities, ethnic fraternities, clan/family networks and thus not what TC practitioners seek to promote (which is inter-communal, or 'bridging' social capital).

⁶³ Before the OPEC cartel changed the game in favour of state-owned companies in the late 1970s, seven MNCs (the predecessors of ExxonMobil, BP, Shell, and ChevronTexaco) dominated the world oil market (Ross 2012). Today, daily oil and gas production by the big five (the above four and Total) account for around 11 percent of total daily global production. The rest comes from state owned enterprises (SOEs) or quasi-SOEs (Rees 2014).

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