Debunking the 'curse of oil'

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A paper co-written by an Indiana University economics professor takes issue with the widespread idea that there is a "natural resource curse" that puts countries with oil or mineral wealth at a disadvantage when it comes to economic growth.

The paper also shows that a common explanation for the curse -- that an abundance of oil or other point-source resources causes countries to have lower-quality civic institutions -- isn't true.

Having such resource wealth "may not improve institutions, but it doesn't make them worse. It doesn't affect them one way or another," said Michael Alexeev, professor of economics at IU Bloomington and co-author of the paper with Duke University economist Robert Conrad.

The paper, titled "The Elusive Curse of Oil," has been accepted for publication in the Review of Economics and Statistics. It has not yet been published.

In the 1990s and early 2000s, a series of economics publications made the claim that an abundance of point-source resources, such as oil, gas, gold and diamonds, was associated with weak economic performance. The idea came to be widely accepted, and the term "natural resource curse" was coined to describe it. Further research focused on the reason for the curse, and the most convincing answer seemed to be that, for a variety of reasons, nations with an abundance of point-source resources tended to have worse-than-average governments and other institutions.

But Alexeev and Conrad found no correlation between natural resource endowments and the quality of institutions if the calculations are done correctly. Previous analyses that found such a link, they say, were skewed by using per-capita gross domestic product (GDP) as a controlling variable. That approach resulted in comparing countries with high GDP and strong institutions with those that have high GDP purely because of resource wealth: comparing Portugal with Kuwait, for example.

"In essence," Alexeev said, "the logic of the earlier work was as follows: Most countries with high GDP have good institutions. Natural resource-rich countries, however, have high GDP but poor institutions. Therefore, natural resources must lead to poor institutions."

In their analysis, the authors calculated what they believed countries' GDP would be if they didn't have oil. With oil-driven increases in GDP removed from the equation, the presence or absence of oil had no impact on the quality of national institutions.

The authors also made use of "a kind of natural experiment," comparing Russia, Ukraine and Belarus, three geographically similar Slavic countries created by the break-up of the Soviet Union. Russia has extensive deposits of oil, gas and minerals; Belarus has almost none; and Ukraine is in between. If there were a natural resource curse, Russia would be expected to have the worst institutions and Belarus the best. In fact, Russia and Ukraine have similar scores for institutional quality, and Belarus scores much worse.

"The fact that growth based on natural resource wealth does not improve institutions is a drawback of this type of growth," Alexeev said. "But it does not make it a curse."

The paper also disputes the very concept of a natural resource curse,

pointing out that countries possessing significant point-source resources tend to be wealthier than other countries. While resource-rich countries may not have experienced strong economic growth in recent years, they write, those countries did grow at a faster rate when their oil or other resources were being developed.

"After all," Alexeev said, "long-term growth is everything until now," not just growth that has taken place since an arbitrary starting point of 1960 or 1970.

Alexeev said it's important to have an accurate understanding of the effect of point-source resource wealth on economic growth and institutional quality. The World Bank and other institutions make decisions about guiding and encouraging the development of point-source resources based in part on whether officials believe there is a natural resource curse, he said.

A preliminary copy of the paper "The Elusive Curse of Oil" can be seen on Alexeev's Web site at mypage.iu.edu/~malexeev/ .

Source: Indiana University