

# WHY ECONOMIES SLOW

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## The Myth of the Resource Curse

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*Recent studies assert that natural-resource abundance (particularly of minerals) has adverse consequences for economic growth. But these two economists argue that it is inappropriate to equate development of mineral resources with terms such as “windfalls” and “booms.” Contrary to the view of mineral production as mere depletion of a fixed natural “endowment,” they argue that “nonrenewable” resources have been progressively extended through exploration, technological progress, and advances in appropriate knowledge.*

**M**ANY OBSERVERS BELIEVE THAT RELIANCE ON NATURAL RESOURCES has adverse consequences for economic growth. Consider Richard M. Auty. He writes flatly: “Since the 1960s, the resource-poor countries have outperformed the resource-rich countries compared by a considerable margin” (2001, 840). Although concern over the efficacy of resource-based development is centuries old, the recent cycle begins with Sachs and Warner (1995, 1997), who pre-

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sented evidence of an inverse statistical relationship between natural-resource-based exports (agriculture, minerals, and fuels) and growth rates during the period 1970–90. Summarizing and extending this research (to 1989) several years later, Jeffrey Sachs and Andrew Warner conclude: “What the studies based on the post-war experience have argued is that the curse of natural resources is a demonstrable empirical fact, *even after controlling for trends in commodity prices*. . . . Almost without exception, the resource-abundant countries have stagnated in economic growth since the early 1970s, inspiring the term ‘curse of natural resources.’ Empirical studies have shown that this curse is a reasonably solid fact” (2001, 828, 837). This thesis has been widely disseminated and is now often encountered in the popular press.

In this paper we subject the notion of a “resource curse” to critical scrutiny. We concentrate on minerals, in part for reasons of our own expertise but also because oil and other minerals have been fingered as the primary culprits in this melodrama.<sup>1</sup>

The resource-curse literature pays little attention to the economic character of mineral resources or to the concept of “resource abundance.” Theirs is indeed a black box approach. Virtually without exception, these studies equate the *export* of mineral products with “resource abundance,” seen as a simple reflection of an exogenously given geological “endowment.” When the revenues from this activity are described, terms such as “windfalls” and “booms” are generally not far behind. This synonymy is a matter of implicit assumption rather than analysis or demonstration, generally unquestioned, and all too often unrecognized. On closer scrutiny, each step in this chain of equivalences is questionable.

To begin, comparative advantage in resource products is not equivalent to “resource abundance.” The elementary theory of international trade teaches that every country has a comparative advantage in something. A comparative advantage in natural resources may simply reflect an absence of other internationally competitive sectors in the economy—in a word, underdevelopment. Since indices of “development” are inherently imperfect, this statistical bias is not addressed by adding a host of additional variables into a cross-country regres-

sion. Studies that use more appropriate measures of mineral abundance (such as reserves per capita or the level of natural resource exports per worker) do not find that these variables are negatively associated with growth rates (Maloney 2002; Stijns 2003).

Historical studies show that successful resource-based development is not primarily a matter of geological endowment. The United States was the world's leading mineral economy in the very historical period during which the country became the world leader in manufacturing (roughly between 1890 and 1910). Resource intensity was a pervasive feature of U.S. technological and industrial development. But with the aid of hindsight, we know that the country's mineral endowment was not particularly favorable. Instead, the United States developed its mineral potential well ahead of countries on other continents, including Latin America, on the basis of large-scale investments in exploration, transportation, geological knowledge, and the technologies of extraction, refining, and utilization. It is fair to say that the minerals sector constituted a leading edge of the knowledge economy in U.S. history.

The minerals sector is no less linked to advances in knowledge and technological capabilities in the modern world. Indeed, it is one of the high-tech industries of the global economy. Fears of impending scarcity have been overwhelmed by technological progress in exploration, extraction, and substitution over the past two centuries, a fact well known to resource economists (such as Krautkraemer 1998 and Tilton 2003), though it rarely arises in the resource-curse literature. Less well known is the fact that returns to investments in *country-specific* minerals knowledge have stayed high in recent decades, so that production and reserve levels have continued to grow in well-managed resource economies. Many other resource-based economies have performed poorly, not because they have overemphasized minerals but because they have failed to develop their mineral potential through appropriate policies.

These issues matter precisely because of their relevance for policy decisions. What doctor would offer the diagnosis that her patient's condition is hopeless and has been so from day one, attributing his

ills to an ill-fated factor endowment? Would lenders and donors consider as evidence of “reform” decisions to suspend programs of minerals exploration, curtail the training of mining engineers, and terminate contracts with international mining companies? Perhaps not, but how else should policymakers understand the implications of a thesis that a country would be better off not knowing about its underground wealth potential? On the other hand, perhaps an appreciation of the knowledge-based character of the minerals sector might lead resource-curse advocates to reformulate their position and rethink its policy implications. Our position is that investment in minerals-related knowledge is a legitimate component of a forward-looking economic development program. We support this position by examining cases of resource-based development, past and present.

### **The United States as a Resource-Based Economy**

Writing in 1790, Benjamin Franklin declared: “Gold and silver are not the produce of North America, which has no mines.”<sup>2</sup> By 1913, however, the United States was the world’s dominant producer of virtually every one of the major industrial minerals of that era. Here and there a country rivaled the United States in one mineral or another—France in bauxite, for example—but no other nation was remotely close to the United States in the depth and range of its overall mineral abundance.

Resource abundance was a significant factor in shaping if not propelling the U.S. path to world leadership in manufacturing. The coefficient of relative mineral intensity in U.S. manufacturing exports actually increased sharply between 1879 and 1914, the very period in which the country became the manufacturing leader (Wright 1990, 464–68). Louis Cain and Donald Paterson (1986) find a significant materials-using bias in technological change in nine of twenty U.S. manufacturing industries between 1850 and 1919, including many of the largest and most successful cases. A study of the world steel industry in 1907–9 put the United States on a par with Germany in total factor productivity (15 percent ahead of Britain), but the ratio of horse-

power to worker was twice as large in America as in either of the other two contenders (Allen 1979, 919). The American economy enjoyed abundant natural resources during the country's ascendance to world leadership, yet economists do not seem inclined to downgrade U.S. performance on this account.

There is good reason to reject the notion that American industrialization should be somehow discounted because it emerged from a setting of unique resource abundance: On closer examination, the abundance of American mineral resources should not be seen as merely a fortunate natural endowment. It is more appropriately understood as a form of collective learning, a return on large-scale investments in exploration, transportation, geological knowledge, and the technologies of mineral extraction, refining, and utilization. This case is set out in detail by Paul David and Gavin Wright (1997) and may be briefly summarized here.

For one thing, the timing of increases in production of a range of minerals in the United States is striking. Leadership or near-leadership in coal, lead, copper, iron ore, antimony, magnesite, mercury, nickel, silver, and zinc all occurred between 1870 and 1910. Surely this correspondence in timing cannot have been coincidental.

In direct contrast to the notion of mineral deposits as a nonrenewable "resource endowment" in fixed supply, new deposits were continually discovered, and production of nearly all major minerals continued to rise well into the twentieth century—for the country as a whole, if not for every mining area considered separately. To be sure, this growth was to some extent a function of the size of the country and its relatively unexplored condition prior to the westward migration of the nineteenth century. But mineral discoveries were not mere by-products of territorial expansion. Some of the most dramatic production growth occurred not in the Far West but in older parts of the country: copper in Michigan, coal in Pennsylvania and Illinois, oil in Pennsylvania and Indiana. Many other countries of the world were large, and (as we now know) well endowed with minerals. But no other country exploited its geological potential to the same extent. Using modern geological estimates, David and Wright (1997)

show that the U.S. share of world mineral production in 1913 was far in excess of its share of world reserves. Mineral development was thus an integral part of the broader process of national economic development.

David and Wright identify the following elements in the rise of the American minerals economy: (1) an accommodating legal environment; (2) investment in the infrastructure of public knowledge; (3) education in mining, minerals, and metallurgy.

It would be a mistake to view the encouragement to mining as flowing exclusively from a simple, well-specified system of rights and incentives, because much of the best U.S. mineral land was transferred into private hands outside of the procedures set down by federal law. Nearly 6 million acres of coal lands were privatized between 1873 and 1906, for example, mostly disguised as farmland. Most of the iron lands of northern Minnesota and Wisconsin were fraudulently acquired under the provisions of the Homestead Act. Nevertheless, whether through official or unofficial procedures, the posture of American legal authority toward mining was permissive and even encouraging well into the twentieth century.

This discussion may convey the impression that the rise of U.S. mineral production was an exercise in the rapid exhaustion of a non-renewable resource in a common-property setting. Although elements of such a scenario were sometimes on display during periodic mineral “rushes,” resource extraction in the United States was more fundamentally associated with ongoing processes of learning, investment, technological progress, and cost reduction, generating a manifold expansion rather than depletion of the nation’s resource base. A prime illustration is the U.S. Geological Survey (USGS). Established in 1879, the USGS was the most ambitious governmental science project of the nineteenth century. The agency was successor to numerous state-sponsored surveys and to a number of more narrowly focused federal efforts. It was highly responsive to the concerns of western mining interests, and the practical value of its detailed mineral maps gave the USGS, in turn, a powerful constituency in support of its scientific research. The early twentieth-century successes of the USGS in petro-

leum were instrumental in transforming attitudes within the oil industry toward trained geologists and applied geological science.

The third factor was education. By the late nineteenth century, the United States had emerged as the world's leading educator in mining engineering and metallurgy. The early leader was the Columbia School of Mines, opened in 1864; some twenty schools granted degrees in mining by 1890. After a surge in enrollment during the decades bracketing the turn of the twentieth century, the University of California at Berkeley became the largest mining college in the world. The most famous American mining engineer, Herbert Hoover—an early graduate of Cal's cross-bay arch rival, Stanford—maintained that the increasing assignment of trained engineers to positions of combined financial and managerial, as well as technical, responsibility was a distinctive contributing factor to U.S. leadership in this sector. A manpower survey for military purposes in 1917 identified 7,500 mining engineers in the country, with a remarkably broad range of professional experience, domestic and foreign.

### **United States v. Chile: The Case of Copper**

Between 1900 and 1914, copper mines in the United States produced more than ten times as much copper as did the mines of Chile, but this vast differential was not based on superior geological endowment. Chilean copper production exceeded that of the United States until the 1880s and nearly recovered its relative standing by the 1930s. During the 1880–1920 era of U.S. ascendancy, however, there was no comparison. The rapid growth of U.S. copper production illustrates the ways in which investment and technology can expand a country's resource base, effectively creating new natural resources from an economic standpoint.

The pure native coppers of the Great Lake region were indeed a remarkable gift of nature, but the capital requirements for profitable exploitation of this potential were immense. Along with the railroads, the copper companies of Michigan pioneered in the organization of the giant integrated business enterprise. Advances in the 1870s and



1880s reflected technological developments in drilling and blasting such as the use of nitroglycerin dynamite and rock-drilling machines powered by compressed air. Steam engines were adapted to hoist ore from the deepest mines in the country, as well as to stamping and other surface operations. Beginning in the 1870s, national totals were augmented by production from newly discovered deposits in Arizona and Montana, but Michigan copper continued to grow absolutely until the 1920s.

What truly propelled the copper industry into the twentieth century was a revolution in metallurgy, overwhelmingly an American technological achievement. In the 1880s and 1890s, the major breakthroughs were the adaptation of the Bessemer process to copper converting and the introduction of electrolysis on a commercial scale for the final refining of copper. These advances made possible a nearly complete recovery of metal content from the ore. The dramatic new development of the first decade of the twentieth century was the successful application of the Jackling method of large-scale, nonselective mining using highly mechanized techniques to remove all material from the mineralized area—waste as well as metal-bearing ore. Complementary to these techniques, indeed essential to their commercial success, was the use of the oil flotation process in concentrating the ore. Oil floatation called for and made possible extremely fine grinding, which reduced milling losses sufficiently to make exploitation of low-grade “porphyry” coppers commercially feasible.

Together these technological developments made possible a steady reduction in the average grade of American copper ore, from 3.32 percent in 1889 to 1.88 percent by 1910. By contrast, in copper-rich Chile—where output was stagnant—yields averaged from 10 to 13 percent between 1890 and 1910 (Przeworski 1980, 26, 183, 197). From these facts alone, one might infer that the United States had simply pressed its internal margin of extraction further than Chile, into higher-cost ores. But the real price of copper was *declining* during this period, confirming that the fall in yields was an indicator of technological progress. Indeed, the linkage between yield reduction and the expansion of ore reserves was exponential, because of the inverse



relationship between the grade of ore and the size of deposits. Advances in technology thus led directly to an expansion of American mineral wealth.

Historians differ on the reasons for the Chilean lag. In the mid-nineteenth century, the Chilean industry was comparable to and probably superior to that of the United States in its technological sophistication. But the supply of high-grade ores began to decline in the 1880s, and, in contrast to the United States, Chile did not respond to this deterioration with either new discoveries or technological adaptation. Political historians stress the lack of national consensus in support of the industry and the predominance of revenue motives in government policy. Economists tend to emphasize the obstacles posed by large fixed-capital requirements in transportation and other forms of infrastructure, as well as in mining and processing facilities. American copper benefited from much greater investment in engineering skills, geological knowledge, and transport facilities (Maloney 2002, 126–28). Scale economies were not independent of the legal and political regime, however; in Chile, for example, the mining code discouraged the consolidation of individual mining claims (Culver and Reinhart 1989, 741).

Whatever the precise mixture of explanations, the important point is that Chile's problem was not its mineral endowment but delay in developing its resource potential. The barriers were real, but large U.S. companies found profitable what the Chileans did not, and investments by Guggenheim and Anaconda after the turn of the century began the long-term reversal of the industry's fortunes. Through massive investments in railroads, roads, steamships, water, and housing, these private firms in effect created their own infrastructure.

### **Resource-Rich Underachievers**

What was true of Chilean copper was also true of other areas of the world that are now known to be richly endowed with mineral resources: Latin America, Russia, Canada, even Australia—a country whose early economic performance has been impugned for its excessive reliance on natural resources. European settlement of Latin

America was largely motivated by the search for precious metals, but the Spanish and Portuguese rulers had little interest in possible spillover benefits from gold and silver mining to broader mineral development. In contrast to the United States, the countries of Latin America had barely made a beginning at exploiting their potential in zinc, lead, bauxite, iron ore, phosphate rock, and petroleum.

Contemporaries and historians have found many rationalizations for this pattern of underachievement. But the proximate impediment seems to have been a lack of accurate knowledge about the extent and distribution of mineral deposits. A report issued as part of the 1910 survey of world iron-ore resources called attention to enormous undeveloped deposits of high-grade iron ore in Brazil and attracted great interest in that country. Yet even in the 1930s experts cautioned that “a belief that South America is a vast reservoir of untouched mineral wealth is wholly illusory” (Bain and Read 1934, 358). Somehow the illusions metamorphosed into real resource endowments within sixty years, as mining investments blossomed throughout Latin America in the 1990s.

Australia was a leading gold-mining country in the nineteenth century, but Australia was an underachiever with respect to virtually every other mineral, particularly coal, iron ore, and bauxite. As David and Wright (1997) show, Australia’s share of world production lagged well behind its actual share of mineral wealth (based on modern estimates). In a nation with a strong mining sector and a cultural heritage similar to that of the United States, why should this have been so?

Here, too, it is easy to identify adverse factors that may have discouraged resource exploitation. The population of Australia was small relative to its area, and the harsh climate of the large desert areas discouraged migration from the coast. But similar conditions prevailed in much of the western United States. States like Montana, Utah, and Arizona are not famous for their gentle climates. Australia did invest in geological research organizations, mining schools, and mineral museums, and indications are that “a viable and independent technological system did develop in the years approximately 1850 to

1914" (Inkster 1990, 43). Yet Australia lagged well behind other developed countries in engineers per capita (Edelstein 1988, 14), and was heavily dependent upon foreign science. Into the 1880s, most large Australian mines were managed by Cornishmen, who had much practical experience but were untrained in metallurgy and resistant to new technology. The emerging Australian technological system was distinctly informal, reliant upon outside science, and lacking in scale economies relative to the United States. In the early twentieth century, as Britain fell behind in minerals education and research, and as protectionist policies inhibited inflows of knowledge embodied in goods and people, the relative pace of learning in the Australian minerals sector appears to have decreased substantially. In a 1977 lecture at the University of Queensland, Raymond J. Stalker (a professor of mechanical engineering) stated that "on the eve of the Second World War, the 'self-image' of Australia was that of a relatively unsophisticated and technologically dependent dominion of the British Empire" (as quoted in Magee 1996, 31).

Arguably as a result of the above factors in conjunction with low mineral prices, by the 1930s Australians had become pessimistic about the possibilities for further expansion of their natural resources. W.A. Sinclair (1976, 201) speaks of "a greatly reduced willingness to underwrite a process of development based primarily on the exploitation of natural resources." In parallel with growing concerns in other countries about the extent of natural resource supplies, Australians deemed it prudent to conserve minerals for domestic industries.

Pessimism led to misguided policies and lack of survey effort. In 1938, when Australia had recently begun to export iron ore on a small scale and gave promise of expanding this traffic, the government imposed an embargo on all iron ore shipments in an effort to conserve the remaining supply—effectively raising a barrier to exploration that remained in place for the next twenty-five years. The policy was justified by a report to the Commonwealth in May 1938: "It is certain that if the known supplies of high grade ore are not conserved Australia will in little more than a generation become an importer rather than a producer of iron ore" (quoted in Blainey 1993, 337). As late as

the 1950s, the accepted view was that Australian minerals were fated to diminish over time. A 1951 report stated:

We have been utilizing several of our basic metals at an ever-increasing rate and, with the development of many of the so-called backward nations, it appears likely that that rate will not diminish in the future; demand is likely to increase. We have not an unlimited supply of these metals available to us by economic processes as known today, nor is there any indication that sources other than the kind of ore-deposits worked today will become available to us. The capacity for production of some metals cannot be increased indefinitely. . . . Periods of shortage such as we have experienced will recur more frequently. (Australian Bureau of Mineral Resources, Geology and Geophysics 1951)

However, when the policy regime changed in the 1960s, lifting the embargo and offering state encouragement to exploration and construction of new ore terminals, a rapid series of new discoveries opened up previously unknown deposits, not only of iron ore but of copper, nickel, bauxite, uranium, phosphate rock, and petroleum. By 1967, proven reserves of high-grade iron ore were already more than forty times the level of ten years earlier (Warren 1973, 215).

Before the 1960s, Australians accepted any number of unscientific rationalizations for the absence of important minerals such as petroleum: oil could not be found south of the equator; Australia's rocks were too old to contain oil; the country had been so thoroughly scoured by prospectors that surely nothing valuable could remain to be found. But this very attitude could lead to lethargic and therefore self-confirming search behaviors. Geologist Harry Evans recalled his own classic "rational expectations" reaction when a search party from the Weipa mission on the Cape York Peninsula found extensive outcrops of bauxite in 1955: "As the journey down the coast revealed miles of bauxite cliffs, I kept thinking that, if all this is bauxite, then there must be something the matter with it; otherwise it would have been discovered and appreciated long ago." Indeed there was nothing wrong with it: By 1964 Weipa held about one-quarter of the known potential bauxite in the world (Blainey 1993, 332).

Thus, it seems that Australia's problem was not one of excessive

reliance on minerals, but instead a failure to exploit its vast minerals potential early enough. Once Australia began to develop this potential in the 1950s and 1960s, growth of minerals production accelerated, as did growth of gross domestic product (GDP).

## **The Rise of Petroleum: Causes and Implications**

The leading global mineral story of the twentieth century has been petroleum. In its origins and growth as an American specialty, petroleum illustrates the themes of this essay very well: mineral development as a knowledge industry; evolving institutional relationships among government agencies, academic institutions, and private corporations; and national economic strength emerging from a resource base. The usefulness of the liquid mineral originally known as “rock oil” was first recognized in the United States, which dominated world production for more than a century. New discoveries led to an ever-widening range of uses in the twentieth century. It would seem to be a classic example of a nation building comparative advantage around its resource base. Yet we now know that from a world perspective, the United States was not particularly well endowed with petroleum. Paradoxically, American technology launched a worldwide, century-long movement away from a mineral for which the United States has enormous reserves (coal) in favor of a liquid mineral, the domestic supply of which is drying up and for which geographic linkages between resources and industry have been substantially weakened.

Before petroleum, the role of applied science in industry was negligible. When the first oil well was put down at Titusville, Pennsylvania, in 1859, the techniques used were well known from centuries of drilling deep wells for brine and water. As discoveries moved on to more difficult terrain, drilling was facilitated by technological improvements, such as the replacement of the cable drill by the rotary drill. In addition to advances in machinery, the application of petroleum geology was critical. At the Columbia School of Mines, the curriculum included instruction in the drilling of artesian, brine, and oil wells, while Charles F. Chandler, its dean and professor of applied

chemistry, devised the flash-point test for kerosene and was the foremost chemical consultant for the industry at the time. During the 1880s and 1890s, several pioneer American geologists were employed as consultants by oil operators to help locate deposits in the Appalachian fields (Williamson et al. 1963, 441).

The major breakthroughs for petroleum geology came in the two decades after the turn of the century. At least forty professional geologists and geological engineers were employed in California between 1900 and 1911, probably more than in any other oil region of the world at the time. Working with reliable field data published by the U.S. Geological Survey, these early graduates of the University of California and Stanford were influential in popularizing the anticlinal theory of the structure of oil-bearing strata. While the major elements of the theory had been worked out before 1900, the discovery in 1911 of the rich Cushing pool in Oklahoma dramatically demonstrated that anticlines were favorable places to find oil. In 1914 the Oklahoma Geological Survey published a structure-contour map of the Cushing field clearly indicating that the line separating oil from water was parallel to the surface structure contours. For the next fifteen years, most new crude discoveries were based on the surface mapping of anticlines. Prior to the 1920s, oil development outside of the United States and Canada was almost entirely based on surface seepage. Because of the absence of detailed structural maps, major potential fields in other parts of the world had been passed over.

It is not geology but this investment in geological knowledge that explains the long American domination of world oil production. Other producing centers eventually emerged, most notably in the Middle East, which collectively passed the United States in 1960. The rich oil potential of the Middle East had long been suspected, but its exploitation was delayed by political turmoil and international rivalries. As late as 1948, estimated reserves in North America and the Middle East were closely matched. By the 1980s, total world reserves surpassed anything dreamed of in 1948. The Middle East held by far the largest share, but oil reserves in virtually every other continent have come to surpass those of North America. To some extent this trend toward

globalization reflects the many years of depletion of the U.S. stock. But the more important influence has been the spread of exploration around the world, using advanced science-based techniques and with drilling capabilities that make even deep offshore wells commercially viable. If all the oil extracted in the United States since 1859 were put back in the ground, North America would still be a minor player in the world oil production picture today.

### ***Oil and Economic Development in the United States***

The historical American specialization in petroleum was thus not primarily a matter of endowment but of learning. One might well question, however, just what contribution this historical path has made to American economic development in general. Many modern analysts believe that the advent of petroleum has led to economic deterioration, if not ruin, for “petro-states” such as Venezuela (e.g., Karl 1997). Does the extended American love affair with oil have any lessons to offer on this score?

The discoveries of oil in the San Joaquin Valley, at Signal Hill, Santa Fe Springs, and Huntington Beach, did not bring economic ruin to southern California (Rhode 1997). Before 1900, California was a remote, peripheral economy. Between 1900 and 1930, California (not Texas) became the leading oil state in the nation, and the result was a “sudden awakening” of the regional economy. Spurred not just by jobs in oil but also by the dramatic fall in the cost of energy, California’s share of national income nearly doubled. Contrary to Dutch disease models, the size of the state’s manufacturing sector quadrupled. One clear lesson from California: Do not restrict the indicators of progress to per capita income. With the rush of population, California’s per capita income continued its slow downward convergence toward the national average. But the state was launched on its modern course of leadership in technology and innovation.

The transition from coal to oil entailed learning of many kinds, as California became the world’s first oil-fueled economy. Potential users had to “learn to burn” the new fuel, convert burners, and estab-



lish fuel supply networks. The Southern Pacific Railroad began using fuel oil on a permanent basis after 1895 and switched over completely after 1900. The state's electric utilities and sugar refining led the way, as virtually all of the large fuel consumers switched. With oil came a commitment to the gasoline-powered automobile, as California came to symbolize the high-mobility American lifestyle of the twentieth century. Although opinions are undoubtedly divided about the value of this lifestyle for humanity, one cannot deny that the institutions of higher learning that petroleum geology helped to put on the map—Berkeley and Stanford, to name two—have evolved into world-class research universities.

The developmental contribution of oil was not limited to California. With the rise of petrochemicals in the 1920s, petroleum was instrumental in the transition of U.S. manufacturing from traditional mass production to science-based technologies. Before 1920, there was little contact between oil companies and the chemical industry. The rise of the United States to world stature in chemicals was associated with a shift of the feedstock from coal tar to petroleum. Working in close partnership with Massachusetts Institute of Technology, New Jersey Standard's research organization in Baton Rouge, Louisiana, produced such important process innovations as hydroforming, fluid flex coking, and fluid catalytic cracking. As chemical engineer Peter Spitz has written: "regardless of the fact that Europe's chemical industry was for a long time more advanced than that in the United States, the future of organic chemicals was going to be related to petroleum, not coal, as soon as the companies such as Union Carbide, Standard Oil (New Jersey), Shell, and Dow turned their attention to the production of petrochemicals" (Spitz 1988, xiii). Progress in petrochemicals is an example of new technology built on a resource-based heritage.

### ***The Case of Norway***

The reader may accept this analysis as history and yet protest that it has little relevance for the newer oil-producing nations of the world.<sup>3</sup>

How could such newcomers expect to contribute to what is now an extremely advanced science-based world petroleum technology? In rebuttal, consider the example of Norway, in which the first commercial discoveries of oil occurred only in 1969. In many ways the Norwegian experience parallels that of California. Though not poor by world standards, Norway in the 1960s was remote and structurally underdeveloped. Yet in fairly short order, the country was able to reorient its traditional engineering skills from shipbuilding to become a full partner in the adaptation of oil exploration and drilling technologies to Norwegian conditions. Virtually from the start, negotiations with international oil companies emphasized the transfer of competence and control to Norway (Anderson 1993, 98–100). With the establishment of a state-owned company (Statoil) in 1973 and investment in the training of petroleum engineers at the Norwegian Technical University and Rogaland Regional College, “recipient competence” was transformed into “participant competence,” making it possible to speak of an independent Norwegian oil industry.

The Norwegian industry became expert at producing deepwater drilling platforms. Initially designed to overcome immediate production bottlenecks, the platforms came to be export goods, as they proved useful for offshore drilling in other parts of the world. A distinctive approach to exploration developed at the University of Oslo’s Department of Geology, focusing on the properties of different types of sandstone as reservoir rock and the flow of water and oil in sediment basins, has come to be known as the “Norwegian school of thought” regarding oil exploration. As a result of this approach, forecasts of impending depletion have been repeatedly overturned and reserve estimates adjusted. In effect, these advances in technology and in the infrastructure of knowledge have extended the quantity of Norway’s petroleum reserves, and they have allowed Norwegians to participate in the process as well-paid professionals, not just as passive recipients of windfall economic rents.

### ***The Case of Venezuela***

Granted, Norway sets a high standard for national administrative competence and responsible democratic government, but it is “the complete antithesis of Venezuela,” according to Terry Lynn Karl (1997, 217). Oil-rich Venezuela is one of the world’s “most tremendous development failures” (Rodriguez and Sachs 1999, 277). After a strong performance from the 1920s to the 1970s, overall economic growth in Venezuela has been negative for twenty years or more. This dismal performance certainly shows that a favorable mineral endowment is no guarantee of sustained economic progress. But what exactly went wrong in Venezuela?

Francisco Rodriguez and Jeffrey Sachs (1999) believe the problem is that natural resource industries “which rely on exhaustible factors of production, cannot expand at the same rate as other industries” (p. 278). They characterize the decline in Venezuelan oil exports per capita as a “simple depletion of a natural resource” (p. 284). But this interpretation is untenable. Despite the intragovernmental conflict described by Karl (1997), Venezuela’s state-owned oil development agency (Pétroleos de Venezuela, S.A., or PDVSA) has had considerable success in developing technologies appropriate for the unusual concentration of heavy oil in the Orinoco Belt. Country-specific advances in heavy-oil technology led to a significant upward jump in reported Venezuelan reserves beginning in the 1980s, and the level of reserves has been rising since then. Aided by collaborative research agreements with BO Petroleum (a company with Canadian experience in heavy oil), PDVSA developed a new fuel, orimulsion, for use by power utilities and heavy industry. Orimulsion has favorable market prospects, because it has a potential for gasification, can be used in a combined fuel cycle, and is environmentally friendly.

Nor can the growth implosion be traced to Dutch-disease distortions or unfavorable externalities associated with oil. As Ricardo Hausman points out in a persuasive critique:

Venezuela's growth collapse took place after 60 years of expansion, fueled by oil. If oil explains slow growth, what explains the previous fast growth? Moreover, the growth collapse occurred when oil revenues were declining, so that the Dutch disease should have operated in reverse, facilitating the growth of output in nonoil tradables: it did not happen. (2003, 246)

Hausman shows that the decline in the nonoil Venezuelan economy is traceable to a massive rise in real interest rates, dating from the country's loss of bond rating in the wake of its 1983 default. He attributes the subsequent continuation of low bond ratings to "distributive conflict surrounding the allocation of the decline in oil revenues" (ibid.).

Unquestionably, this diagnosis of Venezuela's growth implosion draws upon and perhaps thereby confirms some of the components of some of the critiques of resource-based development. Excessive reliance on a single commodity for export earnings is unwise, especially if the market in question is volatile and if it provides the major source of government revenues. As economists have long advised, it is imprudent for governments to make major spending commitments during periods of rapid revenue growth, as though this growth could be extrapolated into the indefinite future. In such a situation, adverse shocks are extremely stressful for any society, and in the case of Venezuela, it may have been more than the society could withstand.<sup>4</sup>

However one may assign responsibility for these events, the central point is that they should be understood as elements of a specific historical episode, not as recurring or inherent features of resource development. Still less do they constitute evidence for the transience of oil wealth. Much of the resource-curse literature simply assumes nonsustainability, making no distinction between demand-side fluctuations and the determinants of long-run supply.

### **Minerals and Economic Development: Modern Success Stories**

Venezuela shows that there are risks of policy failure associated with resource-based growth, but this finding does not justify a conclusion that resource development itself is mistaken as national policy. In-

deed, the essence of the policy failures described by Ascher (1999, chap. 6) is not an excessive expansion of resource-based activity but political interference with incentives to develop these resources more fully. At times of fiscal crisis, cash-poor governments in Mexico and Venezuela chose to raid the investment budgets of state-owned oil companies, weakening their research and development programs. Such knowledge and human capital expenditures should properly be seen as a positive part of infrastructure investment. The successes of well-managed resource-based regimes illustrate some of the possibilities.

### **Chile**

The resurgence of Chilean copper production in the first half of the twentieth century took place in the absence of strong domestic technical capacity. According to Patricio Meller, “in the 1950s, one could have learned more about Chilean copper in foreign libraries than in Chilean ones. . . . [Nor] was there training of Chilean engineers and technicians specializing in copper” (1991, 44). It took thirty years (1925–1955) for the government to recognize the need to build such a capacity and about ten years to train Chilean specialists (p. 45). The enhancement of technical expertise did not prevent disastrous policy missteps, culminating in the nationalizations of 1971. But the new mining code of 1983 strengthened private rights in mining concessions, though the state-owned copper mining company (Codelco) retained more than half of the country’s copper production.

Since 1990, Chile has been “Latin America’s star economy” (“In Search of New Tricks; Chile’s Economy,” *Economist*, December 1, 2001, 37) growing at an average annual rate of around 8 percent. The mining industry has been central to this growth, accounting for 8.5 percent of GDP and 47 percent of all exports during the decade. Copper is still Chile’s most important mineral, but its expansion has not deterred diversification within the sector or within the economy more broadly. Chile now also exports substantial quantities of potassium nitrate, sodium nitrate, lithium, iodine, and molybdenum.

The *Engineering and Mining Journal* notes that “investment plans

are . . . coming into the pipeline at a higher-than-average rate in Chile"; planned mine projects rose to US\$10.7 billion in 2001 ("Latin America Still on Top," January 2002, 29–30). As the article comments: "Without successful exploration, many such projects would not have come to fruition." Codelco, the state mineral development company, remains very active in exploration activity in a number of locations throughout the country.

The relationship between ore grade and reserve quantity is illustrated by reports such as the one stating that "estimated resources at Escondida, which include resources used to define ore reserves, have increased significantly due to the release for the first time of low grade ore which is below the current concentrator cut-off grade but above the *economic* cut-off grade" ("Andean Action," *Mining Magazine*, May 1, 2001, 234). Investments in exploration and processing continue to expand for an array of other minerals, even as production of almost every Chilean mineral continues to rise. In early 2002, Coeur d'Alene Mines Corp. announced the discovery of high-grade gold and silver deposits on its Cerro Bayo property in southern Chile but noted that "only a small portion of the Cerro Bayo property has been explored" ("Coeur Discovers More Gold/Silver at Cerro Bayo," *Skilling's Mining Review*, February 2, 2002, 15).

## **Peru**

Peru is considered the region's newest success story by the mining press. After the privatization program started in 1992, mining exports doubled to \$3.01 billion by 1999. As of the end of 2001, Peru ranked second in the world in production of silver and tin, fourth in zinc and lead, seventh in copper, and eighth in gold. *Mining Magazine* reported:

There is a determination that the mining sector should play an even larger role in the economy and a number of legal instruments are now in place aimed at promoting foreign investment . . . As mining regimes go, Peru's can be fairly described as possessing an enabling environment. ("Andean Action," 240)

The president of Codelco, Juan Villarzu, “liken(s) the country to Chile in the early 1990s” (“Peru’s Comeback,” *Mining Magazine*, January 2002, 12). That present development is far below potential is confirmed by such reports as: “Iscaycruz is one of the world’s highest-grade zinc mines, but at present operates on only 1,000 ha [hectares] of the 52,000 ha it holds in concessions” (ibid.).

Yet Peru appears to be on its way to reaching this potential. For instance, “Roque Benavides, chief executive of Compania de Minas Buenaventura, is forecasting that by 2008, output will have climbed to 1.38 Mt [Million tons] for copper, 1.16 Mt for zinc, and 146 for gold” (ibid., 6; these figures represent increases relative to 2000 of 145, 28, and 11 percent, respectively). A US\$3.2 billion project began production at Antamina in 2001 and is expected to yield 675 million pounds of copper over the first ten years (“Peruvian Mining Convention Highlights Mining Development and Importance,” *Mining Engineering*, December 2001). In Yanacocha, “exploration efforts [by Minera Yanacocha, Latin America’s largest gold producer] indicated major copper sulfide deposits under the gold deposits . . . Yanacocha may someday become a major copper producer in addition to gold” (ibid., 21). In May 2002, Barrick Gold Corp. announced the discovery of an estimated 3.5 million ounces of gold at its Alta Chicama property in southern Peru (“Barrick Makes New Gold Discovery in Peru,” *Skilling’s Mining Review*, May 4, 2002, 8). Substantial investments in mineral processing facilities are also under way (“Peruvian Mining Convention,” 21).

### **Brazil**

Brazil is the leading industrial nation of the region, though the share of the mining sector is low relative to its neighbors. Following an intensive government investment program in prospecting, exploration, and basic geologic research (highlighted by the Radar Survey of the Amazon Region Project), mineral production grew at more than 10 percent per year in the 1980s. Exploration was interrupted between 1988 and 1994 because of restrictions imposed by the constitution of



1988 on foreign participation in mining. These restrictions were lifted in 1995, and the government mining company was privatized in 1997 (U.S. Geological Survey 1999). Mineral exploration activities expanded significantly in the 1990s, increasing both production and Brazil's reserves of most minerals. Currently Brazil produces more than sixty mineral commodities and is the world's largest exporter of iron ore.

At present, Brazil has only one copper mine and imports substantial amounts of copper. Because of a number of major discoveries in the Carajas region in Para State, however, Brazil expects "to occupy a prominent position in world copper production beginning in the period 2003–2005" ("Explorations in South America," *Mining Journal*, April 20, 2001, 289). Production capacity for bauxite, which has already risen dramatically over the past two decades, is expected to increase further, with Brazil's largest bauxite producer planning to finish a \$200 million expansion by the end of 2002 ("Brazilian Bauxite Producer Expands Capacity," *Mining Engineering*, March 2002, 10).

### **Australia**

The most striking success story is Australia. Beginning in the 1960s, Australia witnessed a simultaneous resurgence of successful minerals search and economic growth. Across the board and almost without exception, production of minerals has increased rapidly. Figure 1 showcases a few of the dramatic surges in production of Australian minerals. Contrary to earlier fears, increased production has not diminished mineral reserves. From 1989 to 1999, Australian mineral reserves expanded alongside production for almost all minerals. As the *Mining Journal* reports:

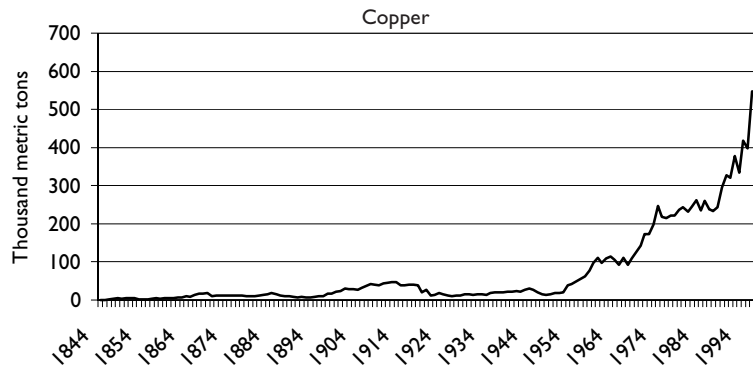
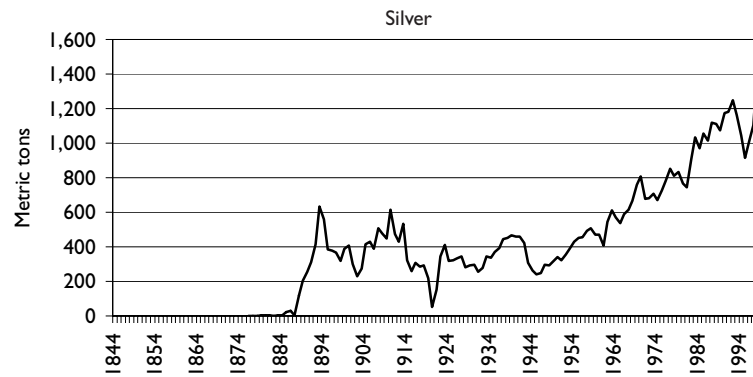
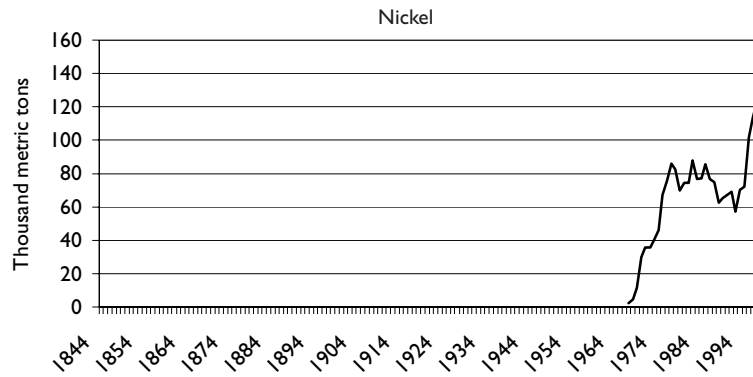
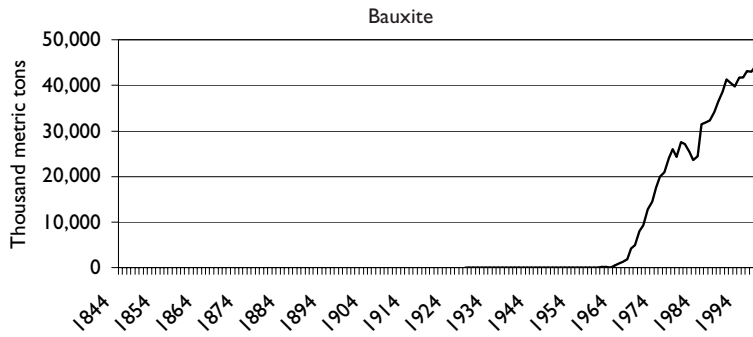
There have been 136 gold discoveries since 1970. . . . In other mineral sectors and against a background of difficult commodity prices, (more) recent Australian successes include an entirely new mineral sands province, the Murray Basin; the development of lateritic nickel deposits such as Murrin Murrin, Cawse and Bulong, and sulphide nickel deposits such as Black Swan, Cosmos and RAV 8; and major zinc and copper discoveries such as Century, Cannington and Ernst Henry. ("Exploration: The View from Down Under," April 5, 2002, 244)

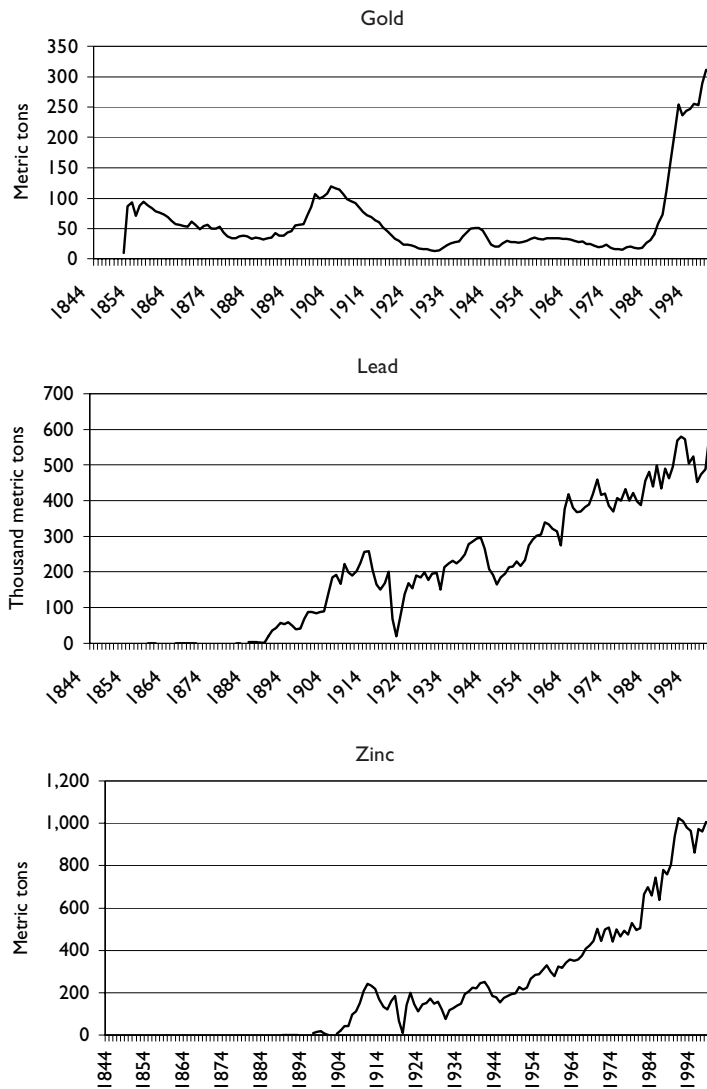
The Australian minerals sector has created much more wealth than it has depleted. The real value of Australia's subsoil assets increased by almost 150 percent from 1990 to 1998, while the real value of the mining sector's capital stock increased by 40 percent over the same period, almost twice the rate for all other industries (Stoeckel 1999, 18–19).

The case of Australia demonstrates that expansion of a country's minerals base can go hand in hand with economic growth *and* technological progress. The Australian minerals sector's share of GDP expanded through the mid-1980s as Australia reversed more than a century of relatively slow GDP growth. New and old Australian industries also benefited. Manufacturing industries with important connections to minerals include: metal and steel products, autos, industrial equipment, petroleum products, ships, and chemicals.

The Australian minerals sector is knowledge intensive. In the past ten years, income from Australian intellectual property in mining has grown from \$40 million a year to \$1.9 billion a year. R&D expenditures by the mining sector accounted for almost 20 percent of R&D expenditure by all industries in 1995–96 (Stoeckel 1999, 17), a disproportionate contribution relative to the sector's share of GDP. The mining sector's contributions to Australia's human capital are also relatively large. From July to September of 1996, the mining sector spent an average of \$896 per employee on training, while the average for all industries was \$185; over the same period, the proportion of payroll spent on training was 5.8 percent for mining and 2.5 percent for all industries (*ibid.*, 18).

As Australia's mineral production has flourished since the abandonment of the passive conservation policies of the 1930s, the country has emerged as one of the world's leaders in mineral exploration and development technology. "Australia leads the world in mining software and now supplies 60 to 70 per cent of mining software worldwide" (*ibid.*, 25). Australia's unique geology calls for unique science; for example, World Geoscience, an Australian company, is a leader in the development of airborne geophysical survey techniques. Industry leaders have put forward an ambitious technological vision known as the "glass Earth project," a complex of six new technologies that





**Figure 1. Australian Mine Production, Selected Minerals, 1844–1998**

Sources: Christopher J. Schmitz, *World Non-Ferrous Metal Production and Prices, 1700–1976* (Totowa, NJ: Biblio Distribution Centre, 1979); and American Bureau of Metal Statistics, *Non-Ferrous Metal Yearbook*, various years.

would allow analysts to peer into the top kilometer of the Earth’s crust to locate valuable mineral deposits. One executive stated: “The discovery of another Mt. Isa or Broken Hill—and we think they are out there—would lift us to fifth [place in the world]” (Cave 2001, 7). Yet many of the technologies coming out of Australia’s particular

geological conditions find applications in other parts of the world and “Australian mining companies search the world for minerals, (with) the bigger Australian companies now spending 30–40 per cent of their exploration budgets offshore” (Stoeckel 1999, 31).

## **The Development Potential of Minerals**

Economists have known for some time that Harold Hotelling’s theoretical prediction, that the scarcity and relative prices of nonrenewable resources would rise inexorably over time, has not been borne out by the facts of history. Jeffrey Krautkraemer’s recent comprehensive survey of the evidence reaches the following conclusions:

For the most part, the implications of this basic Hotelling model have not been consistent with empirical studies of nonrenewable resource prices and *in situ* values. There has not been a persistent increase in nonrenewable resource prices over the past 125 years. . . . Economic indicators of nonrenewable resource scarcity do not provide evidence that nonrenewable resources are becoming significantly more scarce. Instead, they suggest that other factors of nonrenewable resource supply, particularly the discovery of new deposits, technological progress in extraction technology, and the development of resource substitutes, have mitigated the scarcity effect of depleting existing deposits. (1998, 2066, 2091)

But Krautkraemer’s analysis, like virtually all economic writing on this subject (see Tilton 2003), is conducted at the level of the entire market supply for a commodity, which is to say the world as a whole. Although this approach may be appropriate for testing the Hotelling thesis, these conclusions leave open the possibility that the specter of depletion has only been staved off at the global level—i.e., in large part through the opening up of new or previously underexplored territories. What has not been appreciated is that the process of ongoing renewal of nonrenewable resources has operated within individual countries as well as across continents.

Table 1 displays average annual growth rates of mine production for eight major minerals in six relatively well-managed mineral-pro-

Table 1

**Average Annual Growth Rates of Mine Production for Selected Mineral-Country Pairs, 1978–2001 (percent)**

	Australia	Brazil	Canada	Chile	Peru	Mexico	World*
Bauxite	3.41	7.72					2.15
Cobalt	5.30		6.43				-0.17
Copper	5.77	16.89	-0.22	6.93	1.96	4.81	2.80
Gold	14.04	4.45	5.14	9.49	16.39	9.02	2.43
Lead	2.08	-6.32	-3.54	-0.67	1.83	-0.63	-1.20
Nickel	3.03	8.93	1.69				2.56
Silver	3.73	5.47	1.03	8.12	2.90	-7.85	2.60
Zinc	4.17	2.98	-0.62	13.17	2.96	2.63	1.07

Sources: *Non-Ferrous Metals Yearbooks* (selected years from 1978 to 1998) and *Minerals Yearbook* (Washington, DC: U.S. Bureau of Mines, 2001).

\*1978–2000.

Note: Growth rates are coefficients from a log-linear trend regression Brazilian copper production in 1979 set equal to that of 1978 (100 metric tons).

ducing nations. The strong positive growth rates for the world as a whole reinforce Krautkraemer’s point. But equally striking is the vigorous production growth of nearly every mineral in nearly every country. The one notable exception (among the minerals displayed in Table 1) is lead mining, for which production has declined in the world as a whole. This decline is presumably related to lead’s unique position as a recyclable; two-thirds of consumption consists of scrap recovery, thus reducing demand for the newly mined mineral. For a true mineral economic success story like Australia, however, production growth has continued for every one of the minerals on the list, lead included. For the group taken as a whole, it is remarkable that production has expanded country by country across a twenty-year period during which real minerals prices have drifted downward.

Many economists are aware of the global historical evidence but remain in the grip of the intuition that because minerals are nonrenewable, eventually they must grow scarcer—these forms of advance serve only to “mitigate” the Hotelling forecast, so that “finite availability . . . has not yet led to increasing economic scarcity of nonre-

newable resources" (Krautkraemer 1998, 2103, emphasis added). But if examples of successful country-specific mineral development are so numerous, the question arises whether common underlying processes in such countries may exist, and this possibility in turn leads to reconsideration of the sustainability of nonrenewable resources as a base for economic development.

Certainly we are not qualified to make pronouncements about the geographical distribution of minerals in the earth's crust, much less within particular countries. But a cursory reading of the geological literature on mineral stocks convinces us that most geologists would not be surprised by the patterns we have described. DeVerle P. Harris, for example, notes in a survey article that

ore deposits of a specific kind, e.g., massive sulfide copper, are created from common crustal material by earth processes that are characteristic of that deposit type. Consequently, such deposits exhibit some common characteristics irrespective of where they occur, e.g., in the African or North American continents. (1993, 1035)

Among these characteristics are deposit size, average grade, intradeposit grade variation, and depth to deposit. Mapping the statistical properties of these distributions is now the object of sophisticated, large-scale computer modeling, such as the Minerals Availability System (MAS) of the U.S. Bureau of Mines. The broad picture that emerges from such investigations is that the underlying elasticities of mineral supply are very high with respect to any number of physical and economic margins. The more that is learned about the effects of deposit features on "discoverability," with the information gain that occurs from continued exploration within regions, the more it is evident that the potential for expansion of the resource base—the economically meaningful concept of mineral resource endowment—is vast if not unlimited.

From the standpoint of development policy, a crucial aspect of the process is the role of country-specific knowledge. Although the deep scientific bases for progress in minerals are undoubtedly global, it is in the nature of geology that location-specific knowledge continues to be



important. Sometimes this has to do with unique features of the terrain, affecting the challenge of extraction. At other times, heterogeneity in the mineral itself calls for country-specific investments in the technologies of manufacture and consumption. The petroleum industries of Norway and Venezuela, respectively, provide examples of these two possibilities. The development of the solvent extraction–electrowinning (SX-EW) process in the United States serves as another example of the potential benefits of country-specific knowledge. This technique revived American copper mining in the 1980s and 1990s, after it had been pronounced dead by observers in the mid-1980s, and is particularly suited to countries with substantial accumulated waste piles of oxide copper minerals and stringent environmental regulations. More generally, in virtually all the countries we have examined, the public-good aspects of the infrastructure of geologic knowledge have justified state-sponsored or subsidized exploration activities, often with significant payoffs to provincial or national economies.

## **Conclusion**

Contrary to long-entrenched intuition, “nonrenewables” can be progressively extended through exploration, technological progress, and investments in appropriate knowledge. We suggest that such processes operate within countries as well as for the world as a whole. The countries we have reviewed are by no means representative, but they are far from homogeneous, and together they refute the allegation that resource-based development is “cursed.”

The resource-price escalation of the 1970s did indeed constitute an exogenous unanticipated windfall boom from the perspective of many minerals-based economies. It is obvious in retrospect that those boom times were destined to end, and perhaps one can argue that even then, countries (and lenders) should have been more aware of the ephemeral character of the boom and planned accordingly. Without doubt, many countries made poor use of these one-time gains. Nothing in this paper offers any guarantees against corruption, rent-seeking, and mismanagement of mineral and other natural resources. But

the experience of the 1970s stands in marked contrast to the 1990s, when mineral production steadily expanded through purposeful exploration and ongoing advances in the technologies of search, extraction, refining, and utilization; in other words, by a process of learning. It would be a major error to take the decade of the 1970s as the prototype for minerals-based development.

What is at stake in this debate? The resource-curse hypothesis seems anomalous as development economics, since on the surface it has no clear policy implication but stands as a wistful prophecy: Countries afflicted with the “original sin” of resource endowments have poor growth prospects. The danger of such ostensibly neutral ruminations, however, is that in practice they may influence sectoral policies. Minerals themselves are not to blame for problems of rent-seeking and corruption. Instead, it is largely the manner in which policymakers and businesses *view* minerals that determines the outcome. If minerals are conceived as fixed stocks, and mineral abundance as a “wind-fall” unconnected to past investment, then the problem becomes one of divvying up the bounty rather than creating more bounty. Minerals are not a curse at all in the sense of inevitability; the curse, where it exists, is self-fulfilling.

## Notes

1. Problems of agricultural development belong in a very different policy category, involving as they often do the employment of large portions of the population. In that case, human resource issues are at least as pressing as the natural resource content of their economic activity. Renewable resources such as forests also raise distinct policy questions, though much of what we argue may apply to these sectors as well.

2. In the eighteenth century, “mine” referred to an outcropping or deposit of a mineral.

3. This section draws upon unpublished research by Ole Andreas Engen, Odd Einar Olsen, and Martin Gjelsvik of the Rogaland Research Institute in Stavanger, Norway.

4. Ill-considered extrapolation of oil and other mineral revenues during the 1970s was a pathology by no means unique to Venezuela. Osmel Manzano and Roberto Rigobon (2001) show that the Sachs-Warner natural resource variable (primary exports divided by GDP, which they refer to as “resource abundance”) is highly correlated with the growth of debt in the 1970s. Manzano and Rigobon argue that

high resource prices led countries to borrow internationally, using their resource reserves as collateral (perhaps implicitly) and leaving a debt overhang when this asset bubble burst in the 1980s. They show that the debt-to-GDP ratio for 1981 fully accounts for the apparent adverse effect of natural resources on growth rates during 1970–90.

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