The Extractive Industries and Society 2 (2015) 46–55

Contents lists available at ScienceDirect

The Extractive Industries and Society

journal homepage: www.elsevier.com/locate/exis

Original Article

Will Uganda succumb to the resource curse? Critical reflections

David Ross Olanya

Gulu University, Public Administration and Management, Awich Road, Gulu, Uganda

ARTICLE INFO

Article history:
Received 10 November 2013
Received in revised form 30 September 2014
Available online 7 November 2014

Keywords:
Accountability
Development
Institutions
Governance
Oil

ABSTRACT

Few resource-rich countries in sub-Saharan Africa have experienced significant growth and social transformation. In Uganda, one of the region's newest petro-states, the government favors using revenue to improve infrastructure and generate industrial development. However, there is growing skepticism surrounding this approach. As is highlighted in this paper, concerns about prudent management of oil revenue in Uganda are very real because of the country's degree of vulnerability to a 'resource curse', specifically its weak institutions and governance, social fragmentation, lack of political inclusiveness, and the opacity of Production Sharing Agreements (PSAs) signed by politicians and oil companies.

1. Introduction

The conventional view on natural resource wealth is that it is a catalyst for development. The revenues derived once the wealth is extracted can easily be converted to schools, infrastructure, and other capital stocks that directly contribute to national wellbeing. Recent studies, however, have shown precisely the opposite phenomenon, with disappointing performances in many resource-rich countries (Davis and Tilton, 2005; Ross, 2001). This wealth, therefore, is often associated with a natural 'resource curse', situations characterized by abnormally slow economic growth (Sachs and Warner, 1997) as well as corruption and at times, armed conflict (Collier and Hoeffler, 2004). Economic and fiscal reliance on resource wealth can perpetuate authoritarianism in developing countries (Haber and Menaldo, 2010) and provide a steady stream of revenue to corrupt regimes that marginalize their populations (Mahdavy, 1970). Natural resource wealth increases the power of the state bureaucracies of such countries and reduces the need for taxation (Huntington, 1991). In most cases, weak institutions precede the discovery of oil and/or other minerals (Haber et al., 2003), which explains why these policymakers tend to increase spending when commodity prices are high and why they are unable to reduce expenditures when the prices decline (Pegg, 2010).

In Uganda, there are an estimated 3.5 billion barrels of recoverable oil. Commercial production is expected to start by 2017, and Uganda's net oil revenue will be approximately US$84 billion. The royalty rate is 12.5 percent, the government's share is 67.5 percent, the company's share is 32.5 percent, and the corporate tax is 30 percent. The government will retain 93 percent of the revenue from royalties, and the remaining 7 percent will be shared among the districts in exploration and production areas. Uganda's reserves compare favorably to several countries in sub-Saharan Africa, including Chad (1.5 billion barrels), Republic of Congo (1.9 billion), Equatorial Guinea (1.7 billion), Gabon (3.7 billion), Ghana (5 billion) and South Sudan (6.7 billion) (Twinoburyo, 2013). The British company Tullow Oil has been granted an exploration license that covers an area of150 square kilometers adjacent to the Murchison Falls National Park, and the French company Total and Chinese National Offshore Oil Corporation have each acquired one third of Tullow's oilfield (Gelb and Majerowicz, 2011).

This article critically reflects on the Hirschman's (1981) Staple Thesis in an attempt to broaden understanding of the potential resource curse emerging in Uganda. After reviewing Staple Thesis, the article reviews the literature on the resource curse, drawing on key elements to frame the Uganda case. In addition, this article critically assesses Uganda's oil regimes in relation to practices in other countries.

Referring to growth in the early stage of production that relies mostly on a sequence of staple activities, Hirschman (1981) wondered about the circumstances in which one thing would lead to another, which was a way of describing how growth experience in a country is concretely shaped by specific primary products that are successively linked to export markets. In this regard, certain

E-mail address: davidolanya@yahoo.co.uk.

http://dx.doi.org/10.1016/j.exis.2014.09.002
2214-790X/

characteristics of leading activities are conducive for providing stimuli. The effects of interactions between the leading sector and other sectors are divided into production, consumption, and fiscal linkages. The efficiency of fiscal linkages is the most important determinant of ultimate benefits, and such efficiency can only be accomplished through taxation and productive investment.

Considering forward and backward linkages, Hirschman (1981) argued that fiscal linkages are outside linkages by definition and associated with direct participation of the state in the income stream generated by the staple export. Forward linkages have potential significance in staple-based economic development. Inside linkages occur when a state has developed the entrepreneurship initiatives of the old agents and attempts to disrupt the existing status quo. Outside linkages have the advantage of mobilizing new agents and preventing a concentration of economic power and wealth. According to Hirschman's analysis, outside linkages lead to the provision of public goods by the state; however, a state that only knows how to tax a staple may be very far from making effective contributions to development. Hirschman argued that promoting irrigation, transportation and education is good for the staple product.

Fiscal linkages have a better chance of emerging if enclave resources are owned by foreigners because the enclave will be taxed more readily than when the resource extraction in question is in the form of an activity with dense networks. Taxing a foreign company is easier than assessing nationals, who in addition to owning the resources, may run or control the government and may resist paying taxes (Hirschman, 1981). Thus, the possibility of politicians-turned-businesspersons owning a share of oil companies increases the degree of tax resistance. As such, the ability of the state to tax a new staple and invest in a productive manner determines the possibility of fiscal linkages, which raises the following question: what conditions are favorable for fiscal linkages? The ability to tax must develop before the ability to invest. According to 'staple thesis,' development hinges on the establishment of successive activities rather than a single focus, which was aptly demonstrated by the experiences a series of high income countries, notably the United States, Canada, and Australia (Reynolds, 1979).

According to staple thesis, 'backward areas' commonly form with initial stimuli contributed by primary product exports that attract capital and labor and induce a diversified production structure (Innis, 1930; Watkins, 1963). This process is explained by the resource curse literature, which is reviewed briefly below.

2. A critical review of resource curse literature

The conventional view considers mineral wealth to be a profitable asset that can increase a country's natural stock of capital because it helps in the conversion process and brings in new technologies which improve technical efficiency (de Ferranti et al., 2002; Wright and Czelusta, 2004). This has been witnessed in the historical development of the United Kingdom, United States, and Germany. More recently, mineral wealth has provided a platform for economic growth in Australia, Canada, Chile, Malaysia, Peru, Netherlands and Botswana (UNCTAD, 2002).

Proponents of the 'alternative view' of the resource curse point to how economic growth in many mineral-rich countries has been negligible over extended periods; growth has in some cases even been negative (Auty, 1990,1993). A greater dependence on minerals, it is argued, is associated with slower economic growth after the usual determinants of growth are controlled for (Sachs and Warner, 1999, 2001), the implication being that minerals are negatively associated with economic development. Mineral-rich countries, it is further contested, experience inadequate investment in education (Gylfason, 2001), increased risk of civil war (Collier and Hoeffler, 2000; Ross, 2004), difficulty in establishing and/or consolidating democratic forms of governance (Ross, 2001), and increased corruption that negatively affects the quality of institutions (Sachs and Warner, 1995, 2001).

The argument can also be extended to the type of governance that is required and not limited to whether mineral-rich countries can achieve the desired governance (Davis and Tilton, 2005). Whether minerals should be exploited is a matter of policy choice for a host country. Mineral wealth does; however, appear to have impeded long-term economic development in the Central African Republic, Democratic Republic of Congo, Guinea, Liberia, Niger and Sierra Leone (UNCTAD, 2002). The means by which mineral wealth impedes economic development include declining terms of trade, volatile markets, the Dutch disease, nature of mining, and use of rents. In the case of the former, the prices of primary commodities tend to fall relative to those of manufactured goods over time, implying that there is need to increase the amount of exports for a given basket of manufactured imports, which was the central argument raised by Presbisch (1950) and Singer (1950) in the 1950s. This situation makes it difficult to rely on revenues from the mineral sector when pursuing effective planning for economic development. The Dutch Disease remains a popular explanation for the poor performance of many resource-rich countries (Pegg, 2010), and it occurs because of resource movement and spending effects (Corden and Neary, 1982:827). The resource movement effect occurs when a booming extractive sector draws capital and labor away from other sectors (Davis and Tilton, 2005), which requires costly adjustments in agriculture and manufacturing (Gary and Karl, 2003). The spending effect occurs when the extra income derived from the booming resource rents is spent on domestic goods and services, which raises their prices (Corden and Neary, 1982:827). However, the Dutch Disease does not provide an adequate explanation for the numerous economic problems in resource-rich countries (Sala-i-Martin and Subramanian, 2003), and by encouraging resource mobility, the disease actually benefits a country (Davis and Tilton, 2005).

The nature of mining affects surrounding communities in terms of environmental impacts and other social costs. The revenues may allow governments to mollify dissent and avoid accountability (Isham et al., 2003) because revenue flows into domestic economies are not restricted (Ross, 1999; World Bank, 2002) and enrich a number of contractors and politicians (Gelb, 1988; Martin, 2008). Those who rule often assume that they 'own' the natural resources, and therefore assign themselves property rights over the natural resources (Karl, 1997). The absence of incentives to tax weakens the administrative reach of the state (CGD, 2004), and political accountability is minimized (Le Billion, 2005; Ross, 1999). Although there is more evidence from the poorest countries portraying mining as a curse, such evidence can also be challenged as irrelevant, such as when the revenues (taxation and royalties) from mining are used to support education, public health, infrastructure development and investments are made that stimulate development (Davis and Tilton, 2005)

Collier and Hoeffler (2002) have shown that a country that has natural resources that contribute approximately 26 percent of the GDP faces a probability of civil conflict of 26 percent, whereas a country that has no natural resources faces a probability of civil conflict of 0.5 percent. Similarly, high expectations and subsequent disappointments from poor performance lead to political instability as small groups become richer while the rest of the population descends into poverty (Collier, 1999). However, within the conflict dimension, the relationships between natural resources and conflict remain poorly understood and controversial (Ross, 2004). Mehlum et al. (2006) argued that the main reason for conflict is found in the quality of institutions, which is defined as the human-devised constraints that structure political, economic