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Oil resource abundance, institutions and growth: Evidence from oil producing African countries

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Abstract

The study interacted different measures of institutional quality and oil-resource abundance to determine if good institutions can reverse resource curse or enhance resource blessing in African oil rich countries. Result showed that institutional quality insignificantly enhanced per-capita income growth, thereby questioning institutional quality in these countries, but surprisingly, the interaction variables were negative and significant alluding to the fact that the quality of institutions in these countries would not be able to reverse the resource curse in these countries. It is therefore expedient to strengthen the quality of the institutions to sustain growth and enhance proper resource management in these countries.

JEL classification: O11; O13; Q0

Keywords: Oil resource abundance; Institutions; Panel data; Per capita GDP growth

1. Introduction

Natural resources have been recognized as crucial to economic development of many resource rich countries by the assessment of international financial institutions in the past decades and

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until the 1980s, natural resource abundance was considered an advantage by economists. However, theoretical and empirical studies starting in the 1980s and subsequent years up till date reached conclusions that are contrary, revealing that natural resources have posed more economic problems, chaos, and crises to its host economies, and consequently, might be an economic curse rather than a blessing (Sachs & Warner, 1995a; Sala-i-Martin, Xavier, & Subramanian, 2003). For instance, Africa has provided many instances where natural resource greediness such as that of minerals or crude oil has led to political instability, corruption and even civil war. Instead of serving as development agent, natural resources have served as propellants of internal conflicts in Africa as it is seen in the prolonged internal conflicts in Sierra Leone, Liberia, and the Democratic Republic of Congo who are all endowed with natural resources (Park & Lee, 2005). This is why studies like Letiche (2010) suggested that the entire sub-Saharan Africa needs a total economic transformation.

Mehlum, Karl, and Ragnar (2006a), Mehlum, Karl, and Ragnar (2006b), Brunnschweiler and Bulte (2008) and Wizarat (2013) suggest that on the average, resource dependent countries have a lower long-run growth rates than countries with a more diversified export structure. Consequently, it is possible that resource dependence may impact institutional development, which can determine a country's growth potential following resource booms. Similarly, there is a budding consensus in the literature that institutional weakness is central to the explanation of the negative effects of resource booms (Collier & Hoeffler, 2009; Kronenberg, 2004; Sachs & Warner, 1995b).

All nations have what it takes to benefit from both abundant natural-resource endowments in general by deepening the quality of their institutions. Bulte, Richard, and Robert (2005), Mehlum et al. (2006a), Beland and Tiagi (2009), Perry and Olivera (2009) and Nathan and Okon (2013) opined that strong institutions have the capacity to make resource-rich countries turn a resource curse into a resource blessing as natural resources and growth have some spillovers and interactions between them. However, rent seeking and poor governance is likely to prevail in countries where institutions have not been well developed and if this is the case, conflict is more imminent (Wizarat, 2013). This indicates that natural resource endowments coupled with very strong institutional framework will not only serve as a catalyst for growth and development, but will also eradicate the curse associated with resource wealth. Though improving the quality of institutions when institutions are weak can be very sluggish and uncertain (Addison & Baliamoune-Lutz, 2006), hence, leaders in oil abundant countries should focus more on developing strong institutions in order to promote economic prosperity resulting from oil abundance (Beland & Tiagi, 2009). This is prevalent on the fact that if institutions are weak, oil wealth may not translate to economic prosperity (Arezki & Ploeg, 2007; Auty, 2007; Bulte et al., 2005; Knack & Keefer, 1995; Mehlum et al., 2006a, 2006b; Perry & Olivera, 2009).

Knack and Keefer (1995), Mauro (1995), Sachs and Warner (1995a), Gylfason (1999), Hall and Jones (1999), La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1999), Acemoglu, Johnson, and Robinson (2001), Sala-i-Martin et al. (2003) have focused on the important role of institutional quality in promoting economic growth, however, empirical work on the resource curse hypothesis, especially on institutional channel as a potential important cause of resource curse has rarely been verified with much success especially in the case of African where institutions are weak. Hence, this present study seeks to bridge this gap by contributing to the literature with a view to answering three major questions. Have oil resource abundant countries of Africa benefitted from the rents generated by these resources? Is the effect witnessed in the economies depending on the quality of institutions? What impact has oil resource abundance had on the institutions-growth link in oil resource-rich African countries? To answer these questions, the study focuses on estimating the effect of oil resource abundance on per capita GDP growth in oil producing countries of