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Viewpoint

Local procurement in mining: A central component of tackling the resource curse

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ABSTRACT

This thought piece will argue that a central issue that deserves far more attention in the cause of improved mineral resource management is local procurement. In most cases procurement by a mining operation is the single largest potential economic impact in a host country, more than payments in taxes, wages and community investment combined. However, technical assistance institutions, civil society organizations and overseas development assistance providers are not giving as much attention to this issue relative to other mineral extraction impacts. Mining companies themselves also have an economic interest in purchasing more goods and services closer to their sites of activity, in the form of improved relations with stakeholders and lower supply chain costs in the long run. In addition, bilateral and multilateral aid providers and development organizations have an important role to play to support economic development planning utilizing the procurement spending of mining companies. While local procurement is not a silver bullet to defeat the resource curse, the current slowdown in global mining activity provides a chance to "get it right" and drastically improve the development outcomes of mining.

1. Introduction

The recent decline in mineral prices that has mirrored the 2008 global financial crisis and the ensuing slowdown in Chinese growth has caused economic downturns across the vast majority of resource-driven developing countries. Only a few short years after many countries were experiencing booms and the slogan of "Africa rising" seemed to be omnipresent across the mineral-rich continent, there are now widespread concerns that "the resource curse is back". Economic crises, which have often been followed by political ones, have occurred across sub-Saharan Africa, as well as other mineral-resource countries such as Brazil, Russia and Mongolia. Although the concept of the "resource curse" has been qualified a great deal since Auty (1993) and Sachs and Warner (1995) popularized it two decades ago, there regrettably is little doubt the central argument remains quite in tact. The McKinsey Global Institute recently supplied figures that showed that "almost 80 percent of resource-driven countries have below-average levels of per capita income" (2013, p. 6). This current series of difficulties across the global system of mining serves as a reminder for those working to ensure mineral extraction creates meaningful economic development in host countries that there still remains a long way to go.

This paper will argue that a central issue that deserves far more attention in the debate on the resource curse is local procurement, a subject which has received a growing amount of attention in the *Extractive Industries and Society* (see e.g. Lange and Kinyondo, 2016; Melyoki, 2017; White, 2017; McHenry et al., 2017). Typically usedinterchangeably with "national procurement" by most mining companies and governments, local procurement refers to the purchase of goods and services used in the mining process from suppliers within the host-country of operation.[1] While other areas of focus for the global mining industry and its stakeholders, such as environmental performance, occupational safety, and transparency in tax payments have steadily improved over the past two decades

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[1] There has been guidance created by organizations including the International Finance Corporation on defining "local" based on factors including location, ownership, level of impact from mining activity and the presence of disadvantaged groups (see IFC, 2011). However, most government efforts to increase local procurement have generally meant in-country procurement regardless of proximity to a mine. In addition, most mining companies use the term "local" in corporate social responsibly reporting to refer to in-country spending, though some provide further breakdown within this definition (Mining Shared Value, 2014).

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Table 1
Breakdown of total global payments by Anglo American for 2015.

Spending type	Amount ($ millions)	Percentage of total spend
Payments to governments (includes both host and home country payments)	6749	30.2%
Procurement	11,446	51.2%
Wages and related costs	4037	18.1%
Corporate social investment	124	0.5%

with increasing attention, local procurement as an issue has not received a corresponding rise in consideration. For mining companies, standards and management systems have firmed up quite extensively when it comes to the other issues, but local procurement efforts remain relatively *ad hoc* in nature, with few standardized best practices or globally-accepted management systems. On the governance side, while there is some expertise to draw from for developing countries looking to institute local procurement regulations, efforts made by international government organizations, non-governmental organizations (NGOs) and donors to assist host countries maximize in-country spending remain scattered and under-resourced. This is despite the fact that in most cases procurement spending is *the single largest* economic payment type in host countries during the mining life cycle (see below).

This paper argues that this current slowdown in the global mining sector presents an opportunity to “get it right”. Recently, Frank Dixon Mugyenyi, a senior advisor for the Department of Trade and Industry at the African Union Commission, stated that Africa must improve governance of mineral extraction in time for the next upswing in commodity prices (Tumwebaze, 2016). If mining-dependent countries are to have any chance of achieving this, they must position themselves to make the most of the single largest economic impact during mining activity. Fortunately, there are some positive signs that this is being recognized by international institutions, including the African Union, the World Bank, and UNCTAD. Notably, the latter, in its recently released 2016 *Trade and Development Report*, emphasized the importance of structural adjustment and creating more links between foreign direct investment and host economies (UNCTAD, 2016). However, there is a real risk that a return to a period of high prices for mineral commodities and ensuing spikes in revenues may relieve the pressure to make the structural changes across mining-dependent economies that are needed. Actions need to be taken now by the global mining industry and those that influence its behavior to ensure success in the long-term in overcoming the resource curse.

2. Local procurement: the largest potential lever for impact

There are certainly reasons to be optimistic that the global mining industry can meaningfully improve its performance in the area of local procurement and create more benefits for host economies if the recent and ongoing experience of revenue-transparency continues. The last decade has witnessed a consistent and largely successful movement towards shining a light on the amount of revenue mining companies pay to governments in taxes, in order to both incentivize government accountability and help prevent problematic tax arrangements and contracts. The Extractive Industries Transparency Initiative (EITI) has slowly grown in membership to include most of the largest destinations for mining investment, and more recently laws in Europe, and Canada have forced companies listed on their respective stock exchanges to report their payments to foreign governments (Cameron and Stanley, 2017). These movements should be applauded and are now starting to serve as the foundation for a multitude of effective actions aimed at preventing corruption and tax avoidance, and bringing the problematic uses of tax havens to an end.

What is striking, however, is that in most cases, tax constitutes a relatively small portion of the payments that a mining operation will make in a host country. The available data show that the procurement of goods and services will typically constitute the largest single spend made by a mining company in the country where it operates. For 2012 and 2013, the World Gold Council, an industry body representing most of the world’s largest gold mining companies, found that procurement represented 68% and 71% of total in-country spend respectively (World Gold Council, 2013, 2014).[2] These totals were more than payments in taxes, payments to employees, and community investment *combined*. While industry-supplied figures should always be viewed with some trepidation, the trends of these aggregated figures from the World Gold Council are largely echoed across most public reporting provided by mining companies (Mining Shared Value, 2015).

This is not to say that there should be any less pressure on tax transparency and avoidance – only that making the most out of procurement is clearly as important if not more so in the quest to improve the impacts of mining in host countries. In looking at Table 1, which breaks down mining giant Anglo American’s payments by type across all of its operations, the scale of impact is very clear. Even when including taxes and wages paid at home corporate offices and non-operational locations, procurement still represents more than half of all total spending made by the company (Anglo American, 2016). This means that even a small percentage increase in what portion of procurement spending goes to local suppliers represents millions of dollars for host countries. With individual mine sites spending as much as hundreds of millions on procurement each year, increasing the level of goods and services produced and procured locally has the potential to make significant impacts on the balance of trade of host countries. This is especially relevant given there are many developing countries where a mine represents the single largest private sector investment.

In addition, the development impacts from mining companies purchasing goods and services extend far beyond jobs and revenue. The benefits of creating “backward linkages” from investing industries to supplying firms was first laid out most extensively by Hirschman (1958), who outlined the potential for harnessing such linkages for capacity-building and spillovers across the wider economy. Of course, the “Asian Tigers” – Japan, South Korea and Taiwan – all used regulations and incentives to pressure investing companies to purchase inputs locally, which proved instrumental in facilitating their explosive growth (Johnson, 1982; Wade, 1990;

[2] It is important to note that in this World Gold Council study as well as in virtually all cases where mining companies report on local procurement, supplied figures included imported goods resold by domestic businesses. While this does mean that the amount of revenue ultimately staying in the country from procurement is less than the provided percentages, it also means that shifting locally procured goods to locally *manufactured* goods will greatly increase economic benefits even if the total percentage of goods that are local procured remains the same.

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