

The Effects of Resources on Economic Growth

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Abstract: *This paper delves into the intricate dynamics surrounding the 'Resource Curse,' a paradoxical scenario where nations possessing substantial natural resources find themselves unable to leverage these riches for sustained economic growth. Primarily concentrated in regions such as Africa, South America, Asia, and the Caribbean, these countries grapple with an alarming inability to escape the clutches of poverty despite their abundant resource endowments. Through a comprehensive analysis, this study identifies key contributing factors to this phenomenon, emphasizing the critical role of institutional deficiencies, political instability, corruption, and a lack of visionary leadership. The exploration of these facets aims to shed light on the intricate interplay between resource abundance and economic development, unraveling the complex web of challenges that hinder nations from translating their natural wealth into tangible prosperity. By pinpointing these impediments, the paper not only aims to contribute to a deeper understanding of the Resource Curse but also seeks to provide valuable insights for policymakers and stakeholders striving to break free from this paradox and foster sustainable economic growth in resource-rich nations. As the global community grapples with issues of economic disparity and resource management, this research offers a timely examination of the multifaceted nature of the Resource Curse, encouraging a nuanced approach to address the underlying factors that thwart the transformative potential of abundant resources in certain regions.*

Keywords: *Poverty, Economic Growth, Institutions, Political instability*

INTRODUCTION

Economic growth is a multifaceted concept encompassing the enhancement or augmentation of the inflation-adjusted market value of goods and services produced within an economy during a specific financial period (Mankiw and Taylor, 2014). Analysts and economists typically gauge this growth through the percentage rate of increase in both real and nominal Gross Domestic Product (GDP). Real GDP, adjusted for inflation, serves as a more accurate measure by mitigating the distorting effects of inflation on the prices of goods produced. This approach provides a nuanced understanding of the actual expansion in the economy, accounting for changes in prices and allowing for more precise comparisons across different time periods. National income accounting serves as the primary method for quantifying economic growth, emphasizing the importance of accurately capturing the value of all goods and services produced within a country's borders.

The metric of economic growth, defined by the annual percentage change in GDP, is not without its limitations and merits. On one hand, it offers a comprehensive snapshot of a nation's economic health, revealing trends and patterns in production and consumption. However, this method is not without drawbacks, as it may oversimplify complex economic dynamics. One such limitation lies in its failure to account for the equitable distribution of wealth and resources among the population. As countries strive for progress, the ratio of GDP to population, commonly known as per-capita income, becomes a pivotal benchmark for cross-country comparisons. Evaluating economic growth through per-capita income facilitates a more nuanced understanding of how the benefits of growth are distributed among the populace, shedding light on issues of income inequality and social welfare. Thus, a holistic examination of economic growth requires consideration not only of aggregate figures but also of their impact on individual citizens and societal well-being (Mankiw and Taylor, 2014).

The concept of the "rate of economic growth" is fundamental to understanding a nation's overall economic performance over time. This metric, expressed as the geometric annual rate of growth in Gross Domestic Product (GDP) between the first and last years within a specified period, provides a comprehensive view of the economy's trajectory. The growth rate encapsulates the trend in the average GDP level over the analyzed timeframe, smoothing out any short-term fluctuations. Economic growth can be categorized into two types: intensive and extensive. Intensive growth results from more efficient utilization of inputs, such as increased productivity in labor, physical capital, energy, or materials. On the other hand, extensive growth is driven solely by an expansion in the quantity of inputs, exemplified by factors like population growth or territorial expansion.

One significant driver of economic growth is the continuous development of new goods and services. In the United States, for instance, approximately 60% of consumer spending in 2013 was allocated to products and services that did not exist in 1869. This innovation-driven growth underscores the dynamic nature of economies and their capacity to evolve through technological advancements and changing consumer preferences. Calculating the economic growth rate relies on accurate data, primarily derived from GDP estimates provided by countries' statistical agencies. This data-driven approach ensures that the growth rate is grounded in empirical evidence, facilitating a nuanced understanding of economic trends.

Turning our attention to the phenomenon of the "resource curse," a critical survey of pertinent literature sheds light on key questions surrounding resource endowments and their impact on development. This exploration includes an examination of whether resource endowments are inherently beneficial for development, the origins of the resource curse, and strategies to avoid its detrimental effects. Addressing these inquiries necessitates careful consideration of several observations. Firstly, while resource curse is often linked to various policy strategies, conclusive evidence remains elusive. Secondly, existing explanations for the resource curse inadequately account for the role of externalities in the social and political landscape. Lastly, noteworthy exceptions, such as resource-rich countries like Malaysia, Canada, Chile, Norway, Botswana, and Indonesia, challenge the notion that resource abundance inevitably leads to economic

underperformance (Stevens, 2003). These countries serve as examples of effective resource management and strategic development, providing valuable insights for policymakers grappling with the complexities of resource-driven economies.

In the discourse surrounding the resource curse and its impact on development, it is imperative to reassess the questions posed by scholars. Rather than solely focusing on why resource endowments often lead to negative setbacks and hinder development, a more insightful inquiry would be to discern the political and social forces that enable some resource-rich nations to harness their potential for positive development while others falter. The nuanced examination of this issue is underscored by Syndar and Bhavnani (2005) and Shrank (2004). As evidenced by the multidimensional nature of the resource curse, it is crucial to explore the factors that contribute to successful resource utilization for development, thereby illuminating the intricate interplay between political, social, and economic forces in resource-rich nations.

The literature on the resource curse and resource endowment can be broadly categorized into three themes: (i) Economic performance and rural resource endowment, (ii) the Relationship between resource endowments and armed conflicts, and (iii) the relationship between political regimes and resource endowment. Ross (1999) significantly contributes to the understanding of the first theme, emphasizing the intricate dynamics of economic performance in resource-rich nations. The conceptual evolution of the resource curse has been enriched by the works of Collier and Hoeffler (1998), Wantchekon (1999), and Ross (2001a), transforming it into a multidimensional phenomenon. It is noteworthy that the definition of the resource curse is not universally homogenous, varying across perspectives. Some scholars define it in terms of specific commodities, such as oil or minerals, while others consider it in relation to the size of the primary sector. This diversity in perspectives underscores the complexity of the resource curse and necessitates a comprehensive understanding of its manifestations across different contexts (Syndar & Bhavnani, 2005; Shrank, 2004; Ross, 1999; Collier & Hoeffler, 1998; Wantchekon, 1999; Ross, 2001a). Additionally, considering the impact on GDP per capita growth, it is crucial to adopt a multidimensional analytical framework that captures the intricate relationships between resource endowment, political forces, and development outcomes (Syndar & Bhavnani, 2005; Shrank, 2004; Collier & Hoeffler, 1998; Ross, 2001a).

Economic growth is a complex phenomenon influenced by a myriad of factors, with the availability and utilization of resources playing a key role in shaping the trajectory of a nation's economy. This review explores the intricate relationship between resources and economic growth, delving into both the positive and negative aspects of resource abundance or scarcity. Scholars have extensively debated the "resource curse" phenomenon, where nations rich in natural resources, particularly oil and minerals, experience slower economic growth and development. A seminal work by Sachs and Warner (1995) argued that resource-rich countries often face challenges such as Dutch Disease, where a surge in resource exports leads to an appreciation of the national currency, negatively impacting other sectors. Additionally, political instability and

corruption, commonly associated with resource-dependent economies, further exacerbate the resource curse (Ross, 1999).

However, it is crucial to recognize that the relationship between resources and economic growth is nuanced and context-dependent. While resource abundance may pose challenges, proper resource management and institutional frameworks can transform resources into drivers of sustainable economic growth. For instance, Norway and Canada have effectively navigated the challenges of resource abundance, leveraging strong institutions and prudent fiscal policies to ensure long-term economic prosperity (Auty, 1993). The literature suggests that prudent resource management, transparent governance, and strategic investments in human capital are pivotal for converting resource endowments into catalysts for economic development (Collier & Hoeffler, 2004). Moreover, technological advancements and innovation play a crucial role in mitigating the negative effects of resource dependence, enabling countries to diversify their economies and foster resilience in the face of volatile commodity markets (Arezki & van der Ploeg, 2011).

Resource scarcity, on the other hand, poses a distinct set of challenges to economic growth. As global populations continue to grow, the demand for essential resources, such as water and energy, intensifies. The depletion of these resources can hinder economic development and exacerbate social inequalities. Water scarcity, in particular, has been identified as a critical factor affecting agricultural productivity and industrial activities in various regions (World Bank, 2016). This underscores the need for sustainable resource management strategies and the development of innovative technologies to address resource constraints. The importance of resource efficiency is highlighted in studies that emphasize the potential economic gains from adopting sustainable practices, such as circular economy principles (European Commission, 2020).

LITERATURE REVIEW

Is Natural Resource Abundance Necessary for Economic Development?

Available evidence from existing literatures suggests that natural resource endowments are generally bad for development. Here we analyse the evidence accordingly:

Economic prosperity: Wheeler (1984) opines that natural resources endowment reduces economic growth, especially within Sub-Saharan Africa; mineral-rich countries grew rather less than those without during the 1970s. Gelb et al (1988) argues that resource-rich countries experience terrible deterioration in their ability to raise investible capital domestically during the oil-boom era of 1971- 1983, unlike non-mineral endowed countries, which led to declining growth rates in hard mineral economies such as DR Congo, and stagnant growth rates in oil-exporting economies such as Nigeria (Auty,1993). Experiences of resource-dependent economies were examined by Sachs and Warner (1995), in which a large collection of data was analysed between 1970 and 1989. The outcome was that natural resources endowment was negatively correlated with economic growth. Those scholars who concurred with Sachs and Warner (1995) includes Gylfason et al (1999), Leite and Weidmann (1999) by producing similar results. Also examining large set of data, Auty (2001a) in his contribution on the subject, discovered that per capita GDP of resource-poor economies grew

at rates far better than those of resource-rich economies between 1960 and 1990. Also, Neumayer (2004) came up with studies which confirm whether natural resources endowment had adverse effect on economic growth, that is, if growth is measured in terms of GDP less depreciation on capital to determine real income; his findings were affirmative.

Nankani (1979) argues that in terms of primary agricultural economies, negative growth rates were noticeable. Other setbacks include inflation, high unemployment rates, wages dualism and high external indebtedness. Export of manufactured goods is unlikely in resource-rich countries due to lack of adequate technology (Wood and Barge, 1997). Corruption has been identified as a major challenge in almost all resource endowed countries (Leite and Weildmann, 1999).

Armed Conflicts: Collier and Hoeffler (1998) conclude that natural resource abundance and armed conflicts are positively correlated, especially going by the experiences of 98 countries and about 27 wars. The authors observed that resource abundance increases the risk of secessionism and other forms of agitations for the control of the rents from natural resources. Available records suggest that issues of secessionism and civil wars are most likely in most resource-rich states (Collier and Hoeffler, 2002).

Other scholars argue that resource abundance tend to lengthen the duration of civil wars (Collier and Hoeffler, 1998) and with a curvilinear relationship. Doyle and Sambanis (2000) argue that income from natural resource is negatively correlated with resolution of armed conflicts. Fearon (2004) and Ross (2004a) also concurred with this assessment.

Caution is sought with regards to the notion of resource curse. Researchers have supported that the findings of such issues as cited earlier are prone to variation in measurement of the extent of natural resources endowment. The parameters are either in terms of ratio of countries' natural resources exports to GDP or the ratio of countries' primary exports to total exports. Whenever different yardsticks are employed, the results tend to yield minimum support to the notion of resource curse. In the works of Stijens (2001), it was observed that when endowments were measured in terms of levels of production and reserves instead of exports, it does not comply with the negative correlation between endowment and democracy.

Auty (2001a) observed that certain studies have used non-export based parameters of resource endowments such as Gylfason et al (1999) and Auty (2001), implying that such findings are richer than what critics of resource curse theory would like to believe. It is not clear whether those findings are robust to larger changes in the parameters of natural endowment. Also, it remains unclear that the percentage of primary export to GDP or the percentage of primary export to total exports is appropriate measures of natural resource endowments. Thus far, the consensus among scholars is that the major problem with resource endowment is that it leads to economic dependence or a biased export structure of the economy due to easy rents that accrues to the economy.

Isham *et al* (2002) suggests that the major development challenges in resource abundant countries is not the abundance per se, rather, the major challenge is the reliance on a particular type of resource. Sala-i- Martin and Subramanian (2003) opined that point source resources are well correlated with poor economic development but an endowment of diffuse natural resources was not. Leite and Weldman (1999) observed that iron ores and fuels are negatively related with weak economic growth on primary production in agriculture. Summary

By and large, though there is significant evidence in support of the idea of resource curse, it is not entirely conclusive. There are numerous reasons on the issue of the measurement of key variables which casts suspicion on the findings of studies that are in support of the resource curse hypothesis, especially civil war outcomes and resource endowments. Secondly, it is not clear whether the curse in resource endowments applies to all resource-rich countries or just some of them. Thirdly, some researchers report findings contrary to the dictates of resource curse hypothesis, even when same parameters of relevant variables were used. There is no conclusive link that causation emanates from natural resource endowment to poor economic results rather than the other way round.

What Is the Genesis of Resource Curse?

Though the evidence on resource curse is inconclusive, many scholars have accepted the notion that wealth from natural resources endowments leads to negative economic results and have attempted to explain why such is the case, regionally or globally.

Here perspectives vary according to cause and the emphasis attached, but may be broadly categorized into seven (7) classes:

Radical perspective that emphasizes the role of foreign actors: this group of scholars aligned with Marxist ideology that colonial exploitation of the periphery by the Centre, unequal terms of trade at international markets and connivance of local elites with multinational corporations are the major issues impeding progress in the resource rich countries and not resource abundance per se. Structuralist perspective that emphasizes the role of social groups or socio-economic structure: the opinion here shows that resource curse syndrome emanates mainly because of its effect on the relative influence of the various social groups or classes. This category of scholars view that resource abundance enriches powerful business elites, which tend to exert pressure on government to perform effectively (Broad 1995; Urrutia 1988). Some scholars argue that the main reason why East Asia develops more than Latin America in terms of economic growth and poverty reduction in recent years is the effect of resource endowments in the two regions on their respective industrial policies. It is argued that in Latin America resource endowments led to political and social dominance of the business and landed elites with interest in Import-Substitution Industrialization (ISI), thus impeding the emergence of externally competitive industrial sector. While in East Asia, resource poverty implies that such elites did not exist, or are not as influential in the government, which makes it easier for adoption of export-oriented industrialization and the formulation of an externally competitive economy (Auty 1995; Mahun 1992).

Social Capital perspective that emphasizes the extent of social integration: this group views that the problem with resource abundance is that it hinders social unity and also restricts the ability of governments to absorb economic instability. Point-resource ownership, it argues is normally in the grips of few powerful individuals or groups, which tends to create friction in the society. Certain frictions may be masked during prosperity and may eventually surface during crisis. The outcome, arguably, consensus among members becomes difficult around reform strategy for dealing with the crisis. Thus, in such instance, elites win out and tangible reform is frustrated (Isham et al 2002).

The State-Centred perspective, which underscores the significance of the state in shaping economic development, contends that resource abundance adversely impacts economic progress by influencing the state's capacity to foster development. Scholars have scrutinized the drawbacks associated with 'rentier-states,' characterized by substantial unearned income through royalties, taxes, and rents. State-owned enterprises play a prominent role in these states, leading to a lack of necessity for comprehensive economic policies, as highlighted by Luciani (1987:74). Karl (1997:16) identifies the emergence of 'petro-states,' reliant solely on the political distribution of rents, hindering economic growth and private investment. Auty and Gelb (2001) argue that resource abundance tends to foster hostile oligarchic states, rather than developmental ones, due to factors such as land surplus, tolerance for income inequality, protective trade policies, support for inefficient sectors, and susceptibility to policy errors.

In contrast, the Rational-Actor perspective focuses on the interests of political parties and groups, positing that rational political elites can effectively utilize resource windfalls for positive outcomes. Ross (2001b) argues that during resource booms, rational political elites are crucial for optimizing rent windfalls. Ascher (1999) observes that resource abuse occurs when political elites divert resources meant for overall economic development to parochial rent-seizing programs. Robinson *et al.* (2002) emphasize that rent-seizing tends to impede economic progress. This perspective challenges the notion of irrational behavior, asserting that the crux of the problem lies in the rational allocation of resources by political actors.

The Behavioralist perspective contends that resource abundance fosters irrational and emotional behavior among the political class, resulting in inefficient decisions and policies. This viewpoint draws on the works of Machiavelli, Montesquieu, Mill, Levin (1960), Nurske (1958), and Wallace (1960). It posits that resource abundance leads to short-sightedness, laziness, and excessive exuberance among political actors, undermining the long-term economic interests of a nation. Lastly, the Econometric perspective stresses the role of economic mechanisms, providing a quantitative lens to analyze the impact of resource abundance on economic development. This multifaceted analysis reveals the complexities inherent in understanding the relationship between resource abundance and economic progress, highlighting the need for comprehensive perspectives that encompass political, rational, behavioral, and econometric dimensions.

3.1 Economic Mechanism

Earlier studies of performance of resource endowed economies shows that causal relationship between abundance and performance were basically economic in principle. Prebisch (1950) and

Singer (1950), for instance, opined that declining terms of trade suffered by resource-rich economies is the reason for their poor economic growth and development. Other researchers such as Levin (1960) and Nurske (1958) argued that instability in international commodity prices were the causes of poor economic growth in resource-rich economies. Hirschman (1958) argued that the issue was the 'enclave' nature of resource activities and multinational corporations in these sectors basically repatriate gains and not reinvesting them in the resource economy. This capital flight made the process of development very challenging. Also, the issue of 'Dutch Disease' has been attributed to be responsible for this woes – a situation in which a resource boom leads to appreciation of the real exchange rate which in turn harms manufacturing and industry in the resource-rich economies, (Bruno and Sachs, 1982) and (Corden and Neary, 1982).

Much of such views cannot be taken for granted. Recent studies on commodity prices show that though overall market prices nosedived during the twentieth century, this was attributed exclusively to fall in prices of goods exported by the rich countries. Some studies show that instability in export prices could be useful to exporters so long as it can encourage private investment because investors tend to shield self against future price volatility.

Other scholars argue that instability in export prices does not harm exporters, though is not clearly shown that exporters of primary goods get harmed as well. For instance, Hirschman (1958), views the economic linkages of the resource curse and the 'Dutch Disease' hypothesis. However, Hirschman (1958) also shows that government could take full control of the situation if there exist a political will. Interestingly, this issue points that these negative effect prevails more through political than economic processes.

Thus, most studies on nexus between natural resource abundance and economic performance (poverty) has given more consideration to political manipulation in handling the scenario. In certain instance, resource curse studies incorporate ideas from political scientists, especially neoclassical political economy and the new institutionalism (Auty 2001c, 2001d; Torvik, 2002). Also, debate on resource curse incorporates issues such as behavioralism, Marxism, Public Choice Theory, Structuralism/Dependency Theory and Fiscal Social Systems, most of which appreciates the power of political factors in moulding economic outcomes.

By and large, the consensus among scholars is that poor economic management and not resource abundance is the genesis of underdevelopment in most resource-rich economies (Mitra 1994, Karl 1997, Ascher 1999, Usui 1997).

These viewpoints shows that resource-abundant countries eventually got compelled into the global capitalist system, a phenomenon in which the interests of the less developed countries are relegated to the background and those of the rich countries are promoted, which in turn hinders real economic prosperity and genuine development in the poor countries.

Perelman (2003) argues that resource abundance turns a poor country into a prey and a target for the rich nations. The outcome, according to dependency theorists, is that governments in resource-rich countries are allowed to perpetrate fraud and economic sabotage to their states so long as they give respect and obedience to the dominant nations, (Bellamy, 2004; Amin, 2001).

Panacea to the Paradox of Resource Curse

Most literature on the paradox of resource curse contains varieties of recommendations aimed at helping affected countries get out of the woods. For instance, Sarraf and Jiwandi (2001) emphasize adoption of sensible macroeconomic policies, minimum external and domestic debts, maximum budget surpluses, minimum inflation and competitive exchange rates. Also, Ussui (1997) and Mikesell (1997) argue that competitive exchange rate and cogent macroeconomic policies could help resource-rich countries in stemming the tide of the 'Dutch Disease'. However, Auty (1994) and Collier (2000) emphasize the need for diversifying the economy in order to minimize dependence on primary resources by setting up industries and adding value to their natural resource thereby creating employment for the population.

A second category of scholars emphasized the importance of political and social changes to overcome the menace of resource curse. Here it is argued that economic policies become functional only if and when social and political environments are transformed. For instance, Mitra (1994) argues in line with the Behavioralist view that governments in resource-rich countries deliberately perpetuate resource curse and such could only bend when there is a change in policies and ideas of elites in these countries. That is, elites need to view booms and prosperities as temporary phenomena and the rents thereof as unreliable event so as to halt the excitement and euphoria that normally accompanies boom. Karl (1997), Auty (2001b) and Pearce (2005) view from rational-actor and state-centred opinion and argued that in order to end resource curse, countries need to build state capacity and functional institutions which could then accelerate policy reforms across the system.

A third category of scholars argue that the state needs to be ignored. Instead of efforts to boost the state, rents and royalties should be distributed across board directly to citizens (Sala-i-Martin and Subramanian, 2000). Such system could reduce tension and eliminate opportunities for corruption and mismanagement. However, Ross (2001b) countered that if rents and royalties are transferred to the population, the state may use taxation to retrieve a significant share of it even though it is feasible.

A fourth category of scholars suggested the use of privatization strategy in resource abundant countries. For instance, Ross (2001b) argues that privatization could end the issue of 'rent-seizing'. Weinthal and Jones Luang (2001) suggested that privatizing natural resource sector to domestic private interests tend to be more viable than selling off to foreign interests, especially in the absence of effective tax policies in most resource-rich countries. This strategy has the ability of curbing the menace of capital flight to foreign countries.

A fifth category of scholars argue that the international multinational organizations have the power to come up with strategy that could end resource curse. Though, efforts to regulate international commodity prices have consistently failed, and few see this idea as a good one (Ross, 2001b).

Poverty In Nigeria

The incidence of poverty in Nigeria is estimated at about 40% of the population of about 200 million people. According to the *Nigeria Economic Report* as released by the World Bank in 2014, the growth rate of the economy is put at 7.4% of GDP. Lack of data on the informal sector of the economy (about 60%) makes it difficult to comprehend the extent of poverty in the system. Ethnic conflicts, income inequality and political tension tend to intensify abject poverty among the population.

Nigeria has been an unfortunate development story (Sala-i-Martin, 2003). In terms of every parameter, Nigeria's performance since independence has been a failure. By 1970, Nigeria's per capita GDP stood at US\$1.113 and estimated to remain at US\$1.084 by the year 2000. This data puts Nigeria among the 15 poorest nations in the world for which data are available.

In terms of poverty and income distribution, the situation is even worse. Between 1970 and 2000, the percentage of the population living on less than US\$1.00 per day increased from about 36% to almost 70% of the population.

Also, income distribution crashed sharply during the 30 year period between 1970 and 2000. Data for 1970, 1980, 1990 and 2000 shows the two tails of the Gini Diagram got flattened, indicating an increase in inequality between the rich and the poor.

These patterns coincided with the advent of oil revenues in the Nigerian economy. In a period of about 35 years, Nigeria's cumulative oil revenues (net) stood at US\$350 billion at 1995 prices. In 1965, when oil revenue was US\$33 billion, GDP per capita stood at US\$245. By the year 2000, when revenues hit US\$325 billion, GDP per capita remained at 1965 levels. Literally, all the revenues from oil – about US\$350 billion, did not have any meaningful impact on poverty and raising the living standards in Nigeria. Rather, it tended to negate the living standards of the people.

Conclusion

On the balance, natural resource endowments such as oil, minerals and gas deposits may not necessarily be a curse to a nation. The culture of waste and Dutch Disease, especially in the Third World where functional institutions are non-existent, tends to add weight to the issue of the resource curse. Corruption and parochialism especially among the political elites have been the major force which perpetuates abject poverty in resource-rich countries and Nigeria in particular. Remedies for the problem include sound macroeconomic policies, trade liberalization, privatization, an effective financial sector and a vibrant foreign policy to attract foreign direct investments. Strengthening of institutions within the system could minimize waste and corruption which in turn could make revenues from natural resource endowment beneficial to the generality of the people.

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