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**Mineral Resources and Economic Development**

by

**Gavin Wright**

**Jesse Czelusta**

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Stanford University  
John A. and Cynthia Fry Gunn Building  
366 Galvez Street | Stanford, CA | 94305-6015

**Abstract**

Recent studies assert that natural resource abundance (particularly minerals) has adverse consequences for economic growth. This paper subjects this “resource curse” hypothesis to critical scrutiny. Our central point is 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,” so-called “nonrenewable” resources have been progressively extended through exploration, technological progress, and advances in appropriate (often country-specific) knowledge. Indeed, minerals constitute a high-tech knowledge industry in many countries. Investment in such knowledge should be seen as a legitimate component of a forward-looking economic development program.

Many observers, including economists, believe that reliance on natural resources has adverse consequences for economic growth. A recent edited volume, in nineteen essays elaborate on this theme, opens with the firm statement: “In recent decades the resource-abundant developing countries have underperformed when compared with the resource-deficient developing countries...Moreover, the *mineral*-driven resource-abundant countries have been among the weakest performers” (Auty 2001, p. 3). Although concern over the efficacy of resource-based development is centuries old, the recent cycle begins with Sachs and Warner (1995, 1997), who presented evidence of an inverse statistical relationship between natural resource based exports (agriculture, minerals and fuels) and growth rates during the period 1970-1990. Summarizing and extending this research (to 1989) several years later, Sachs and 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, pp. 828, 837). This thesis has been widely disseminated and is now often encountered in the popular press (Surowiecki 2001).

Much of the profession has sufficient confidence in the resource-curse hypothesis that a second generation of studies sets out to explain the mechanisms through which the effect operates. Many candidates have to do with economic processes, from the Dutch disease (crowding out of other more promising sectors) to market volatility to nonsustainability (taken as axiomatic for nonrenewable resources such as minerals). But the most recent literature highlights the link between particular natural resources and poor governmental policies and institutions. For example, Sala-I-Martin and Subramanian (2003) find that “stunted institutional development – a catch-all for a range of related pathologies, including corruption, weak governance, rent-seeking, plunder, etc. – is a problem intrinsic to countries that own natural resources such as oil and minerals” (p. 5). Isham et al (2003) argue that the problem is specific

to what they call “point source” resources such as oil, minerals, and plantation crops, while natural resource exports that are “diffuse” do not seem to have these pathological consequences.

In this paper we subject this literature to critical scrutiny. We concentrate on minerals, in part for reasons of our own expertise but also because oil and other “point-source” minerals have been fingered as the primary culprits in this melodrama. 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.

Modern writers occasionally reflect some awareness that there are many historical examples of successful resource-based development, most notably the United States. It is seldom appreciated, however, that these historical cases were 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 as we have shown in earlier work, the country’s mineral endowment was not particularly favorable (David and Wright 1997, Wright and Czelusta 2002). Instead, the U.S. 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.

In this paper we argue that the minerals sector is if anything even more closely 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. Contrary to the language of “windfalls” and “booms,” we argue that mineral reserves are created and extended by *investments* of various kinds, including investment in new knowledge. Resource economists are well aware that fears of impending scarcity have been overwhelmed by technological progress over the past two centuries (Krautkraemer 1998 and Tilton 2003). 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.

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. The notion of a “curse” conveys the impression that countries have no choice in the matter, but in reality, development in the minerals sector is shaped by a host of government policies. Relevant policy issues include: (1) the infrastructure of public knowledge (e.g., geological surveys); (2) engineering education; (3) systems of exploration concessions and property rights for mineral resources; (4) export and import controls; (5) supporting infrastructure (such as transportation); (6) targeted taxes or royalties. In contrast to policy analysis, resource-curse proponents offer the diagnosis that their patient’s condition is hopeless, its problems resulting from an ill-fated factor endowment. Isham et al conclude: “Our results suggest how entrenched – and ‘environmentally determined’ – poor institutions can be...So these results, in a certain sense, further raise cautions about casual attempts at institutional reform. Poor institutions are deeply rooted” (p. 26).

Poor institutions may certainly be deeply rooted, but such diagnoses are dangerous because they confuse symptoms with the disease. 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? How else should policy-makers understand the implications of a thesis that seems to say that a country would be better off not knowing about its underground wealth potential? Recognizing the knowledge-based and policy-dependent character of minerals is a necessary first step in integrating this sector into a forward-looking economic development program.

## The Resource Curse Literature

Recent economic writings on natural resources and growth pay relatively little attention to the economic character of these resources nor to the concept of “resource abundance.” Theirs is indeed a black box approach. The standard approach is to relate growth rates in per capita income to measures of the importance of natural-resource exports to a country, such as the share of primary products in total exports, or the ratio of primary product exports to GDP (Sachs and Warner 1995, 1997, 2001; Auty 2001, pp. 3-6).<sup>1</sup> Robust negative correlations are reported, even in the presence of control variables, leading to the conclusion that “the tendency for resource-abundant countries to underperform is insensitive to the classification criteria” (Auty 2001, p. 4).

The first difficulty is that the relative size of resource exports is at best an indicator of *comparative* advantage in resource products, but this is not equivalent to “resource abundance.” The elementary theory of international trade teaches that every country has a comparative advantage in something. 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, the statistical bias inherent in the use of such variables is not removed by adding a host of additional variables to a cross-country regression.

Leamer (1984) argues that a more appropriate measure of resource abundance in terms of Heckscher-Ohlin trade theory is *net* exports of resources per *worker* in the economy. This variable has two conceptual virtues over Sachs and Warner’s: it aggregates resource flows in both directions (thus resolving the anomaly posed by the fact that one of the highest ratios of resource exports to GDP is found in Singapore); and it relates resource trade to the size of another basic national resource stock, namely the labor force. However, the Leamer index continues to conflate stocks and flows, by using a trade-based measure (influenced by productive performance) as a proxy for resource endowment. Nonetheless, Maloney (2002) and Lederer and Maloney (2003) report that even this partial conceptual improvement completely eliminates the purported adverse effects of natural resources on growth. They find that the coefficient on the Leamer index is insignificant in cross-section regressions, and strongly *positive* in panel estimation.

More consistent with the Heckscher-Ohlin framework would be a measure of natural resource *stocks*. Jean-Philippe (2003, Chapter 1) has conducted a thorough review of the evidence on mineral reserves by country, and finds no significant correlation these variables and GDP growth rates. It seems clear that the Sachs-Warner export ratios are not even rough proxies for resource *endowments*. When more conceptually appropriate measures are used, the resource-curse effect disappears.

Behind this econometric dispute is a deeper interpretive issue. The resource curse studies assume not only that patterns of resource exports are generated by factor abundance (and that relative factor abundance is all that matters), but that these resource “endowments” are fixed in size and given exogenously to the economy, by geology in the case of minerals. When revenues from these economic activities are described, terms such as “windfalls” and “booms” are generally not far behind, confirming the implicit assumption of geological determinism. Given this mindset, observers and analysts are quick to infer that mineral wealth is corrupting and invidious, because they view it as unearned “easy money,” inspiring biblical allusions on the consequences of ill-gotten gains. Yet even a casual look at the evidence from mineral industries demonstrates the falsity of such images.

Perhaps the most comprehensive indicators of national resource abundance are those developed by the World Bank’s program on sustainable wealth. The 1994 estimates of subsoil wealth per capita are displayed in Figure 1. The number one country, Saudi Arabia, has been omitted in order to improve the visibility of the rest. When we look at the rest of the top ten, it is notable that we do not see a string of corrupt kleptocracies. Instead, we find a number of developed, well-managed and generally successful economies like Norway, Australia, Canada, and Chile – along with a few others whose status is more debatable. Perhaps the biggest surprise is that the United States, a country whose minerals sector has long since slipped out of prominence, holds down the number ten slot. These elite countries are at the top of a resource-abundance pyramid whose range is awesome. Although the first page of the graph conveys the impression that mineral resources are marginal in countries like Indonesia and Bolivia, in fact the top twenty-five towers over the next tier in the same way that Saudi Arabia towers over the rest. Perusing this picture, it should hardly be surprising that studies using measures such as these do not find an inverse relationship between resource abundance and economic growth.

But the asset values in Figure 1 do not represent exogenous “endowments” of minerals any more than the Sachs-Warner export shares do. Advanced countries are resource-abundant largely because they have developed their geological potential over an extended period, through investments in knowledge as well as physical capital. Geologists and mineral economists understand very well that so-called “reserves” constitute no more than a working inventory at a point in time. Not only are reserve levels subject to change as mineral prices and transportation costs shift the margin of profitable extraction, but they have trended upward over time, not just because of fortunate new discoveries, but as the result of ongoing improvements in the scientific bases of new knowledge about mineral locations and properties.

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,” and the information gain that occurs from continued exploration within regions, the more it is evident that the expansion potential of the resource base – an economically meaningful concept of endowment – is vast if not unlimited. Our point is that opportunities for resource-extension occur in individual countries, not just in the world as a whole.

This perspective has many implications for the resource-curse discussion. Once it is accepted that mineral supplies are not exogenous and not fixed, but are influenced by economic choices, the subject area may be returned to the realm of development economics as contrasted with wistful speculation on historical inevitability. The presumptions that resource sectors are fated to decline, and that non-resource sectors have greater potential for learning and expansion, should be tested rather than assumed. To be sure, mineral production may sometimes have distinctive characteristics that should be taken into account in development planning: the danger of excessive concentration and market volatility; limited job creation; environmental effects; and the risk of political manipulation. None of these are unique to resource sectors, and accounting for them is a normal part of development policy. But the first essential step is to realize that resource development is a policy choice.

## Historical Background

In earlier work, we have shown that contrary to the intuition that natural resources decline in significance over time, manufacturing in the United States became *increasingly* mineral-intensive during the half-century of its ascendancy after 1880 (Wright 1990). By 1913, the country was the world's dominant producer of virtually every one of the major industrial minerals of that era. But this growing resource abundance should not be seen as merely a fortunate natural endowment. We argue that 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. Conversely, areas of the world that are now known to be richly endowed with minerals – Latin America, Russia, Canada, even Australia – failed to develop this potential and may be characterized as “resource-rich underachievers” (David and Wright 1997).

The case may be conveniently summarized in Tables 1-3. Table 1 shows that the 1913 U.S. share of world mineral production was far in excess of the U.S. share of world mineral reserves, as reported in modern sources for the year 1989. The third column extends the comparison further by adding cumulative 1913-1989 production to the 1989 reserves, generating in effect an estimate of the true 1913 reserves according to 1989 scientific knowledge. The fourth column reports the results of the same exercise, using the variant known as “reserve base,” which includes resources that are known but considered marginal or subeconomic. No matter which concept we use, US production in 1913 was disproportionate to what we now believe to be the country's share of world resources. For most minerals the gap was huge.

Contrast the U.S. picture with Table 2, which repeats the exercise for Latin America. If we except gold and silver, in 1913 these countries in the aggregate had barely made a beginning at exploiting their potential in zinc, lead, bauxite, iron ore, phosphate rock and petroleum. Even Chile's copper production was far below its proportionate share of world copper resources. Contemporaries and historians have found many rationalizations for slow Latin American mineral development, but the proximate impediment seems to have been a lack of accurate knowledge about the extent and distribution of that potential. A report by Orville A. Darby, published as part of an international geological survey in 1910, called attention to enormous

undeveloped iron ore resources in Brazil and attracted great interest in that country. Yet as late as the 1930s experts were cautioning that “a belief that South America is a vast reservoir of untouched mineral wealth is wholly illusory (Bain and Read 1934, p. 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 Table 63 shows that Australia was an under-achiever in virtually every other mineral, particularly coal, iron ore and bauxite. Although the country did develop something of an independent mining system by 1914, Australia lagged well behind other developed countries in engineers per capita (Edelstein 1988, p. 14). By the 1930s Australians had become pessimistic about the possibilities for further expansion of their mineral resources, and as a result enacted misguided conservationist policies. The policies were 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, p. 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 proved reserves of high-grade iron ore were already more than 40 times the level of 10 years earlier (Warren 1973, p. 215).

## **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 US, 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 a mineral for which the United States has enormous reserves (coal) in favor of a liquid mineral in which the domestic supply 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. The rotary drill was first applied to petroleum 1900, and was responsible for bringing in the Spindletop gusher of 1901. 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, p. 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 15 years most new crude discoveries were based on the surface mapping of anticlines. Prior to the 1920s, oil development outside of the US 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 (Owen 1975, p. 437).

It was not geology but this investment in geological knowledge that explains the long American domination of world oil production (Figure 2) ~~(Figure 4)~~. 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 towards globalization reflects the many years of depletion of the US 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 US 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*

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.

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 establish 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 US manufacturing from traditional mass production to science-based technologies. Prior to 1920, there was little contact between oil companies and the chemical industry. The rise of the US to world stature in chemicals was associated with a shift of the feedstock from coal tar to petroleum. Working in close partnership with M.I.T., 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 the 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, p. 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. 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, pp. 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, forecasts of impending depletion have been repeatedly overturned and reserve estimates adjusted upward (Anderson 1993, p. 159, Noreng 2002, pp. 213-214). Although a recent economic study bemoans the general public’s lack of appreciation for the nonsustainability of oil wealth (Hanneson 2001), production levels have continued to grow (Figure 3). 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

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

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, “the complete antithesis of Venezuela” according to Karl (1997, p. 217). Oil-rich Venezuela, on the other hand, is one of the world’s “most tremendous development failures” (Rodriguez and Sachs 1999, p, 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?

Rodriguez and Sachs (1999) believe that 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. Production fell precipitously between 1973 and 1985, but by the late 1990s it had recovered to the levels of the early 1970s (Figure 4). 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.

According to Ascher, the fall in production during 1970-75 was attributable to a slowdown in new Venezuelan investments by multinational companies, in turn the result of major new discoveries elsewhere in the world and the forbidding character of Venezuela’s heavy crude and tar sands (1999, p. 211). The nationalization of 1975 was motivated not just by rent-seeking, but by the desire to restore the priority of oil development. In principle, even a rent-seeking government has an interest in maximizing the present value of the long-term flow of oil revenues. In Venezuela, however, an internal power struggle led to a massive scale-back of exploration projects in the 1980s, as the state-owned oil development agency (PDVSA) invested its funds abroad to keep out of the hands of the government (ibid., p. 219).

Since then, PDVSA has had considerable success in developing technologies appropriate for the unusual concentration of heavy oil in the Orinoco Belt. 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 (Brossard 1993, pp. 170-177).

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, p. 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” (264).

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 (exposing underlying weaknesses in its political institutions).

But ill-considered extrapolation of oil and other mineral revenues during the 1970s was a pathology by no means unique to Venezuela. Manzano and 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), 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 1970-1990.

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 does it 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 in Latin America

Venezuela shows that there are risks of policy failure associated with resource-based growth, but this does not justify a conclusion that resource development itself is mistaken as national policy. Indeed, the essence of the policy failures described by Ascher (1999) 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.

Having neglected ~~their~~ resources for generations, and having stifled incipient expansion in more recent decades through misguided state policies, ~~many the countries of~~ Latin American countries turned the corner in the 1990s. The turnaround was fostered by reforms encouraging foreign investment in mining and increasing the security of mining investments – sometimes including privatization of mining companies, but also with strong roles for state geological agencies (World Bank 1996). Latin America is now the world’s fastest growing mining region, well ahead of Australia, Canada, Africa and the US in its share of spending on exploration (*Engineering and Mining Journal*, January 2002, p. 29). The business press regularly reports new discoveries, new investment projects to develop existing deposits, and new technological developments that extend the mining potential of particular areas. The leaders in this burgeoning new minerals growth are Chile, Peru and Brazil. Argentina has yet to experience major minerals success, but maintains a high level of exploration activity, knowing that “the country as a whole is underexplored compared to its neighbors” (*Mining Journal*, April 20, 2001).

### *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, p. 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 mis-steps, 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” (*Economist*, December 1, 2001), growing at an average annual rate around eight 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 (January 2002, pp. 29-30). As the *Mining Journal* comments: “Without successful exploration, many such projects would not have come to fruition.” The state mineral development company (Codelco) has been very active in exploration activity. Typical reported projects include: \$7 million “to continue delineating the Gaby Sur porphyry copper deposit located in Region II;” “Codelco plans to spend US\$20 million during 2001 quantifying reserves at the Mina project in the north;” “Codelco was also active in a number of exploration joint ventures;” “Codelco is in talks to form a partnership with Ventanas, the copper smelter and refinery complex owned by another state body, Enami” (*Mining Journal* May 1, 2001). 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” (*ibid.*). 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, Couer 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” (*Skillings Mining Review*, February 2, 2002, p. 15).

### *Peru*

Peruvian mining is considered the region’s “greatest success story.” 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* reports: “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” (May 1, 2001). The president of Codelco, Juan Villarzu, “liken(s) the country to Chile in the early 1990s” (*Mining Magazine*, January 2002, p. 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 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 1.38Mt for copper, 1.16 Mt for zinc, and 146 Mt for gold" (*Mining Magazine* January 2002, p. 6; 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 lbs. of copper over the first ten years (*Mining Engineering* December 2002, p. 21). 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.*, p. 21). In May of 2002, Barrick Gold Corp. announced the discovery of an estimated 3.5 million ounces of gold at its Alta Chicama property in southern Peru (*Skillings Mining Review* May 4, 2002, p. 8). Substantial investments in mineral processing facilities are also underway (*Mining Engineering* December 2001, p. 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 (CVRD) was privatized in 1997 (US 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 60 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" (*Mining Journal* April 20, 2001). 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 \$200US million expansion by the end of 2002 (*Mining Engineering*, March 2002, p. 10).

## The Development Potential of Minerals

Economists have known for some time that the theoretical prediction derived from Hotelling (1931), 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 ~~n~~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, pp. 2066, 2091).

Hotelling's model is not wrong; rather, its premise of a known, fixed resource stock has been falsified by new discoveries, as well as by ongoing advances in the technologies of search, extraction and utilization that have effectively extended the world's mineral supply.

But Krautkraemer's analysis, like virtually all economic writing on this subject (cf. 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 may be appropriate for testing the Hotelling prediction, 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 continuing renewal of nonrenewable resources has operated within individual countries as well as across continents.

Table 4 displays average annual growth rates of mine production for eight major minerals in six relatively well-managed mineral-producing nations. The strong positive growth rates for the world as a whole in the reinforce —Krautkraemer's point. — But equally striking is the ~~preponderance of~~ vigorous production growth ~~for~~of nearly every mineral in nearly every country. The one notable exception (among the minerals displayed in Table 4) 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, ~~in~~ 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 nonrenewable resources” (Krautkraemer 1998, p. 2103, emphasis added). But if examples of successful country-specific mineral development are so numerous, the question arises whether common underlying processes ~~that are common to~~ 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 recent 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, p. 1035).

In the important case of copper, an example of a geophysical relationship that would underlie open-ended progress is the proposition that there is an inverse relationship between the average grade of deposits and the mineral tonnage available at that grade. Harris and Skinner report that a belief in such a relationship is strongly held among specialists (1982, pp. 312-313). Although Harris (1993) suggests that the available statistical evidence may suffer from sampling and truncation biases (i.e., the contamination of geologic data by economics), it nonetheless seems that the long-term decline in the average yield of copper ore (depicted in Table 2-) has continued through the twentieth century, supporting an ongoing increase in copper production, even while the real price of the mineral has fallen. If similar relationships are common, it is not difficult to imagine a future in which extension of the minerals frontier can continue indefinitely.

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. 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.

Perhaps the clearest recent example of the importance of country-specific knowledge comes from the United States, a country that has extracted more minerals for a longer time period than any other nation on earth, and yet is still among the world's mining leaders. Tilton and Landsberg (1999) recount the technological breakthroughs that revived American copper mining in the 1980s and 1990s, after it had been pronounced dead by observers in the mid 1980s. The primary vehicle was not new discoveries and newly opened mines, but development and application of the solvent extraction-electrowinning (SX-EW) process, which separates the mineral from the ore more effectively and is especially useful for the leaching of mine dumps from past operations. Although this technology will ultimately become global, its near-term impact has been most significant in countries like the US, which have substantial accumulated waste piles of oxide copper minerals, and where copper deposits are located largely in arid regions. The SX-EW process is also best suited for countries with stringent environmental regulations, which require recovery of sulfur emissions from smelting operations, thus providing a low-cost source of sulfuric acid for the SX-EW process. Thus there is a symbiotic relationship between the new SX-EW process and traditional technology (*ibid.*, p. 131).

## Conclusion

Contrary to long-entrenched intuition, so-called “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 policy makers and businesses *view* minerals that determines the outcome. If minerals are conceived as fixed stocks, and mineral abundance as a “windfall” unconnected to past investment, then the problem becomes one of divvying up the bounty rather creating more bounty. Minerals are not a curse at all in the sense of inevitability; the curse, where it exists, is self-fulfilling. Studies have shown that insecure ownership has adverse effects on production and exploration in minerals as it does in other industries (Bohn and Deacon 2000).

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Table 1: U.S. Share of World Totals (%)

	1913 output	1989 reserves	1989 reserves plus cumulative production	1989 reserve base plus cumulative production
Petroleum	65	3.0	19.8	
Copper	56	16.4	19.9	18.5
Phosphate	43	9.8	36.3	15.4
Coal	39	23.0	23.3	
Bauxite	37	0.2	0.5	0.5
Zinc	37	13.9	14.0	15.6
Iron ore	36	10.5	11.6	7.4
Lead	34	15.7	18.1	18.8
Gold	20	11.5	8.6	8.4
Silver	30	11.7	16.3	17.6

Sources: David and Wright (1997), using data from: *Minerals Yearbook; The Mineral Industry--Its Statistics, Technology and Trade* (supplement to *Engineering and Mining Journal*); American Petroleum Institute, *Basic Petroleum Data Book*, Vol. X (September 1990); National Coal Association, *International Coal*; COE/EIA, *Annual Prospects for World Coal Trade* (1991).

Table 2: Latin American<sup>1</sup> Share of World Totals (%)

	1913 output	1989 reserves	1989 reserves plus cumulative production	1989 reserve base plus cumulative production
Petroleum	7.4	13.4	21.8	
Copper	12.6	32.1	26.5	28.9
Phosphate	0.0	5.2		
Coal	0.2	1.1	1.0	
Bauxite	0.0	27.2	29.4	30.0
Zinc	0.6	11.1	12.1	10.2
Iron ore	0.02	12.5	12.0	9.7
Lead	4.8	10.7	13.2	11.8
Gold	5.6	4.4	4.4	4.3
Silver	38.6	30.3	30.3	27.8

<sup>1</sup>South America plus Mexico and Caribbean.

Sources: David and Wright (1997), using data from: *Minerals Yearbook; The Mineral Industry--Its Statistics, Technology and Trade* (supplement to *Engineering and Mining Journal*); American Petroleum Institute, *Basic Petroleum Data Book*, Vol. X (September 1990); National Coal Association, *International Coal*; COE/EIA, *Annual Prospects for World Coal Trade* (1991); C. J. Schmitz (1979), *World Non-Ferrous Metal Production and Prices 1700-1976*, London: Frank Cass; B. R. Mitchell (1983), *International Historical Statistics: The Americas and Australia*, Detroit, MI: Gale Research Co.

Table 3: Australian Share of World Totals (%)

	1913 output	1989 reserves	1989 reserves plus cumulative production	1989 reserve base plus cumulative production
Copper	4.7	5.1	3.8	5.5
Coal	0.9	8.6	8.9	
Bauxite	0.0	20.2	20.5	20.5
Zinc	21.8	13.2	11.1	13.5
Iron ore	0.06	9.9	9.1	14.5
Lead	21.8	20.0	15.3	16.8
Gold	9.9	4.3	3.4	3.6
Silver	7.5	10.0	7.5	7.8

Sources: David and Wright (1997), using data from: *Minerals Yearbook*; *The Mineral Industry--Its Statistics, Technology and Trade* (supplement to *Engineering and Mining Journal*); American Petroleum Institute, *Basic Petroleum Data Book*, Vol. X (September 1990); National Coal Association, *International Coal*; COE/EIA, *Annual Prospects for World Coal Trade* (1991); C. J. Schmitz (1979), *World Non-Ferrous Metal Production and Prices 1700-1976*, London: Frank Cass; B. R. Mitchell (1983), *International Historical Statistics: The Americas and Australia*, Detroit, MI: Gale Research Co.

Table 4: Average Annual Growth Rates of Mine Production for Selected Mineral/Country Pairs, 1978-2001

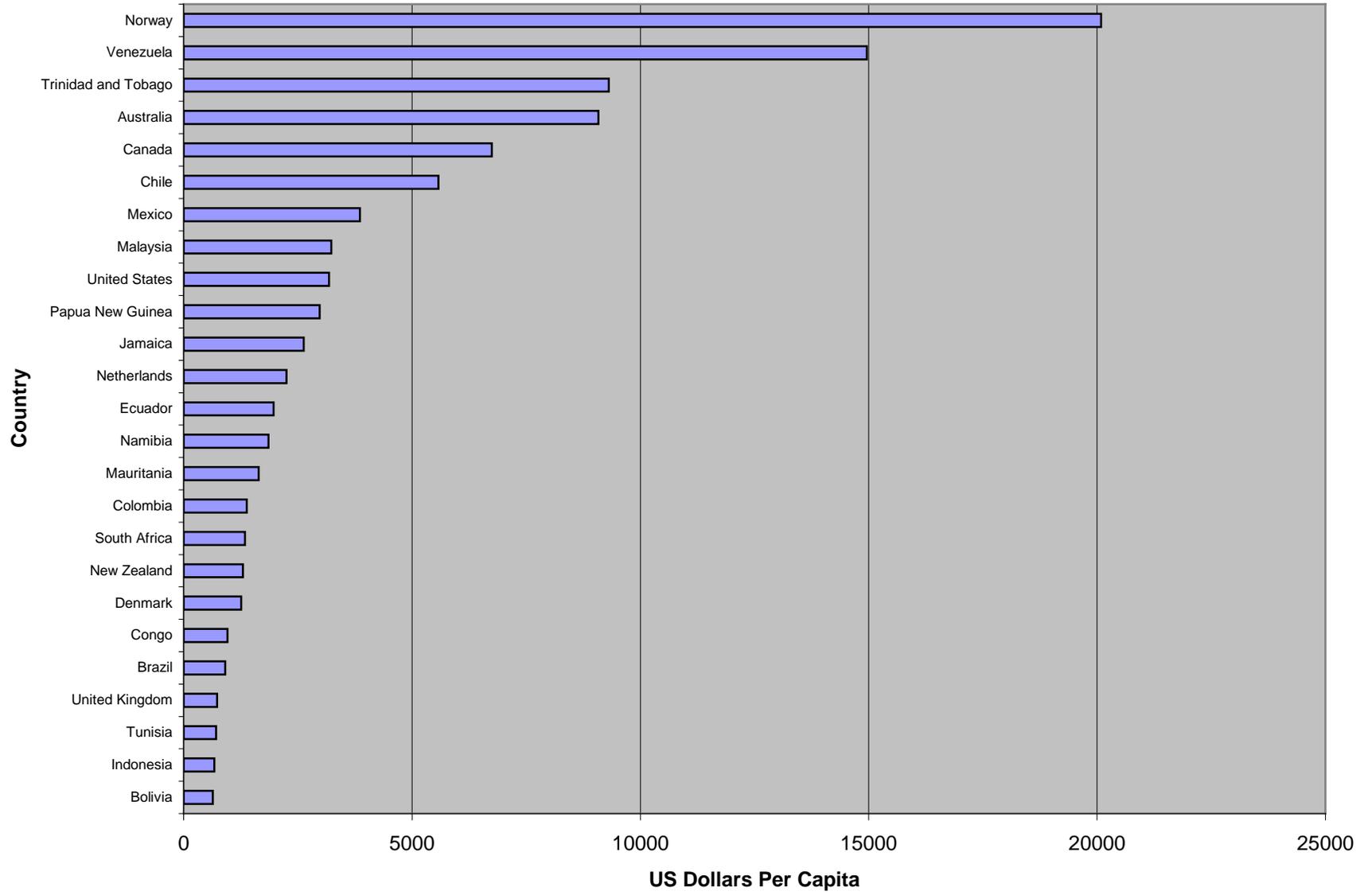
	Australia	Brazil	Canada	Chile	Peru	Mexico	WORLD*
Bauxite	3.41	7.72					2.15
Cobalt	5.30		6.43				-0.17
Copper	5.77	16.89	-0.22	6.93	1.96	4.81	2.80
Gold	14.04	4.45	5.14	9.49	16.39	9.02	2.43
Lead	2.08	-6.32	-3.54	-0.67	1.83	-0.63	-1.20
Nickel	3.03	8.93	1.69				2.56
Silver	3.73	5.47	1.03	8.12	2.90	2.61	2.60
Zinc	4.17	2.98	-0.62	13.17	2.96	2.63	1.07

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

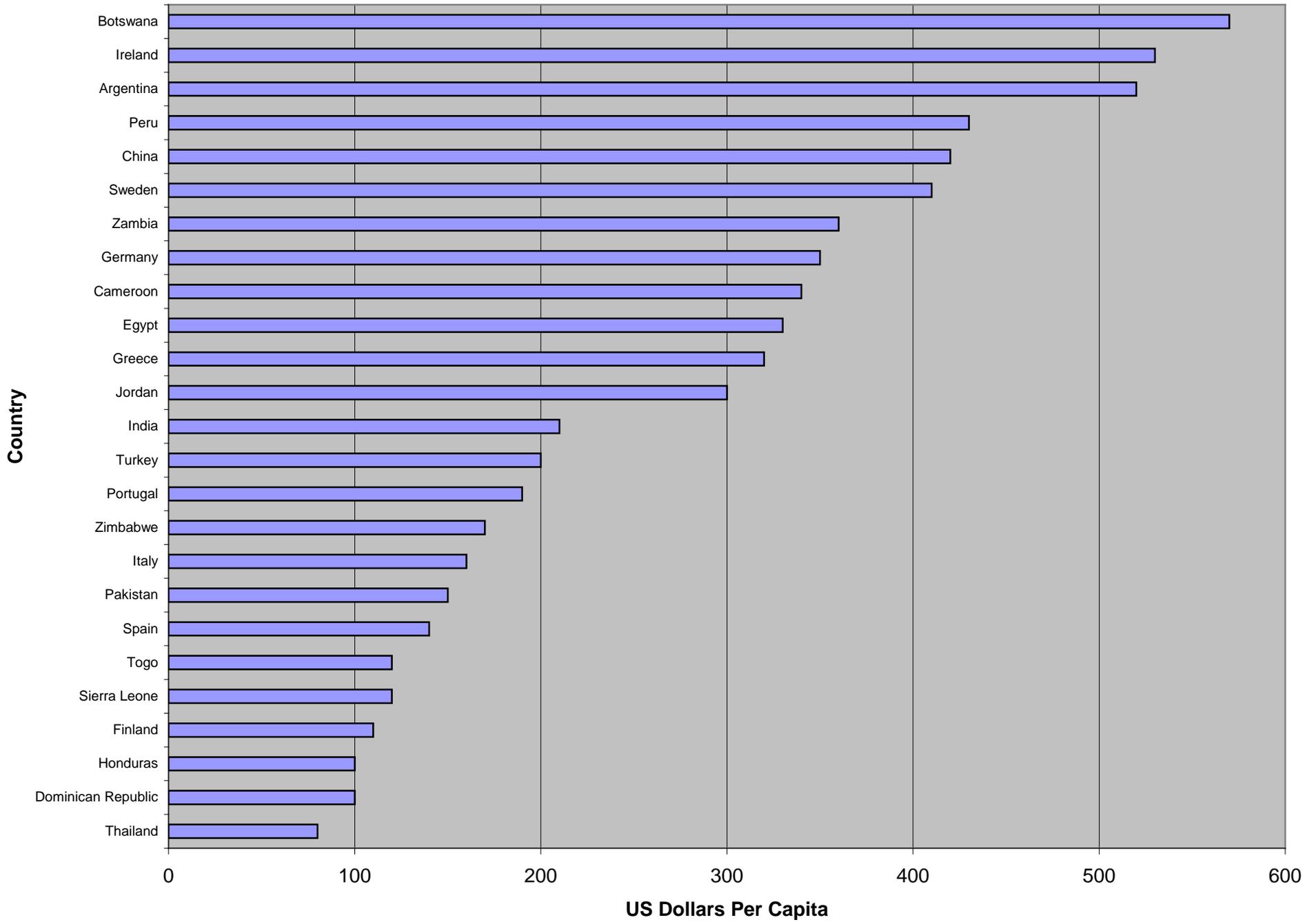
\*1978-2000

Sources: *Non-Ferrous Metals Yearbooks* (selected years from 1978 to 1998) and *Minerals Yearbook* (2001).

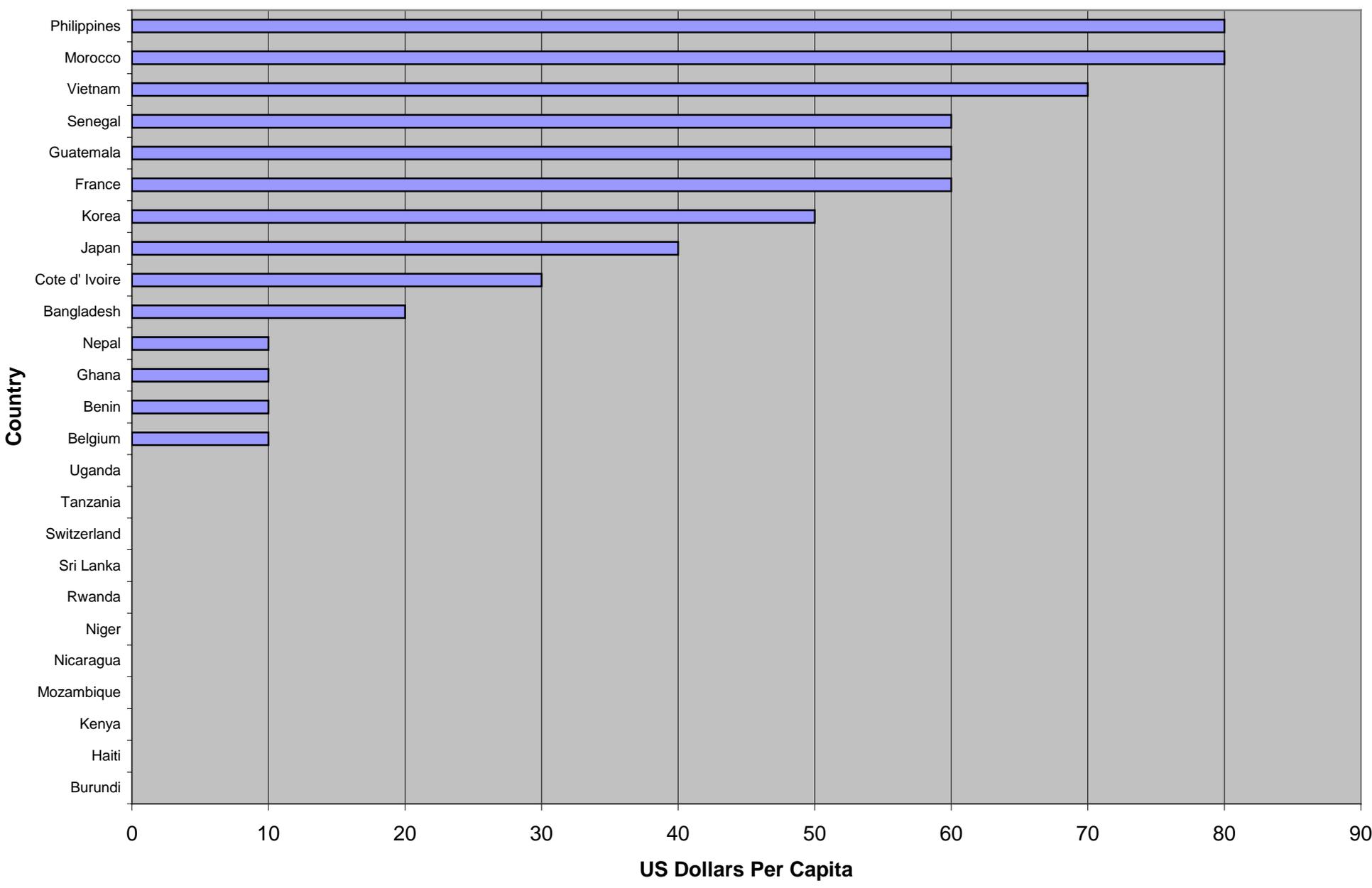
### Subsoil Assets, 1994



### Subsoil Assets, 1994 (Continued)

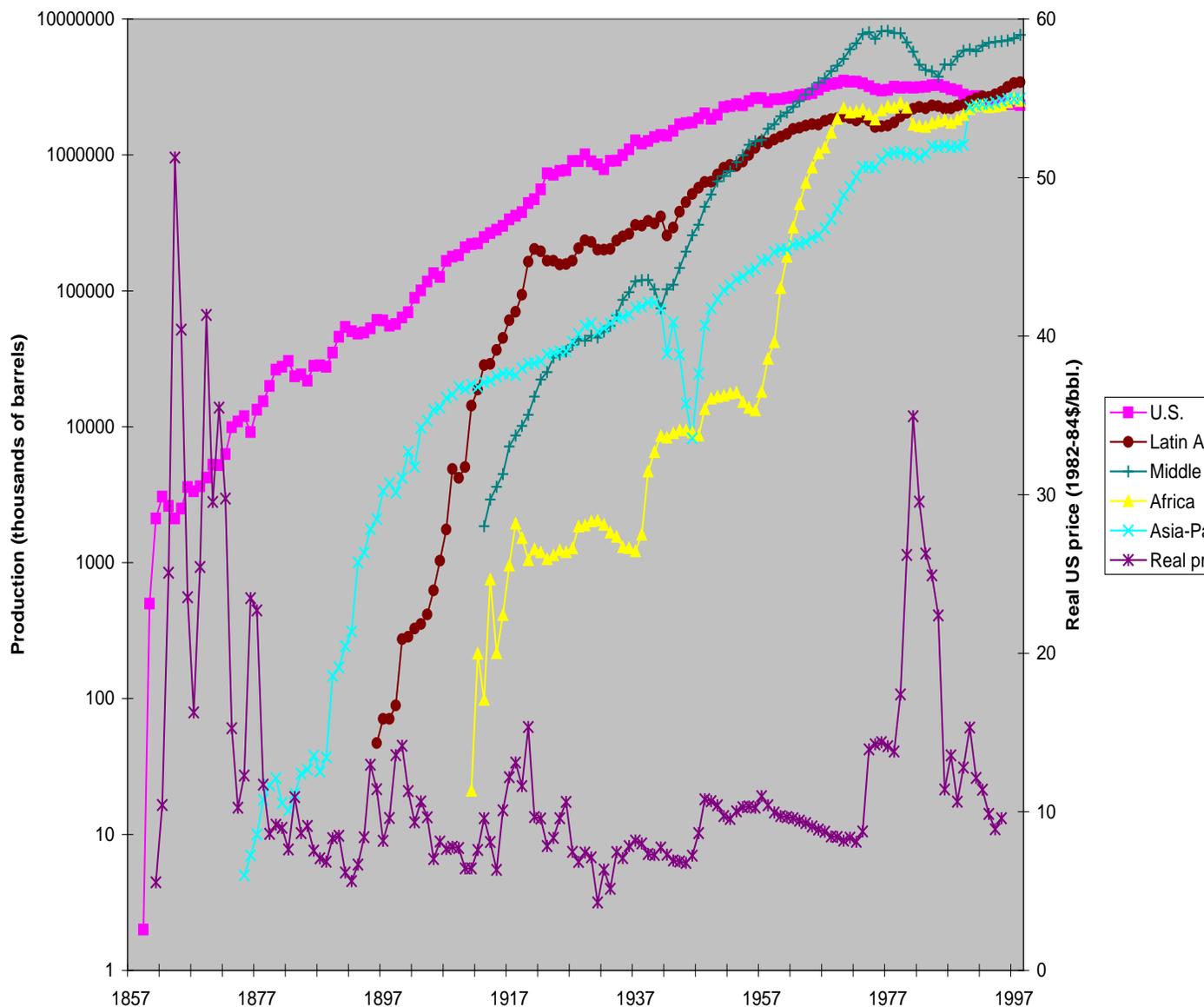


### Subsoil Assets, 1994 (Continued)



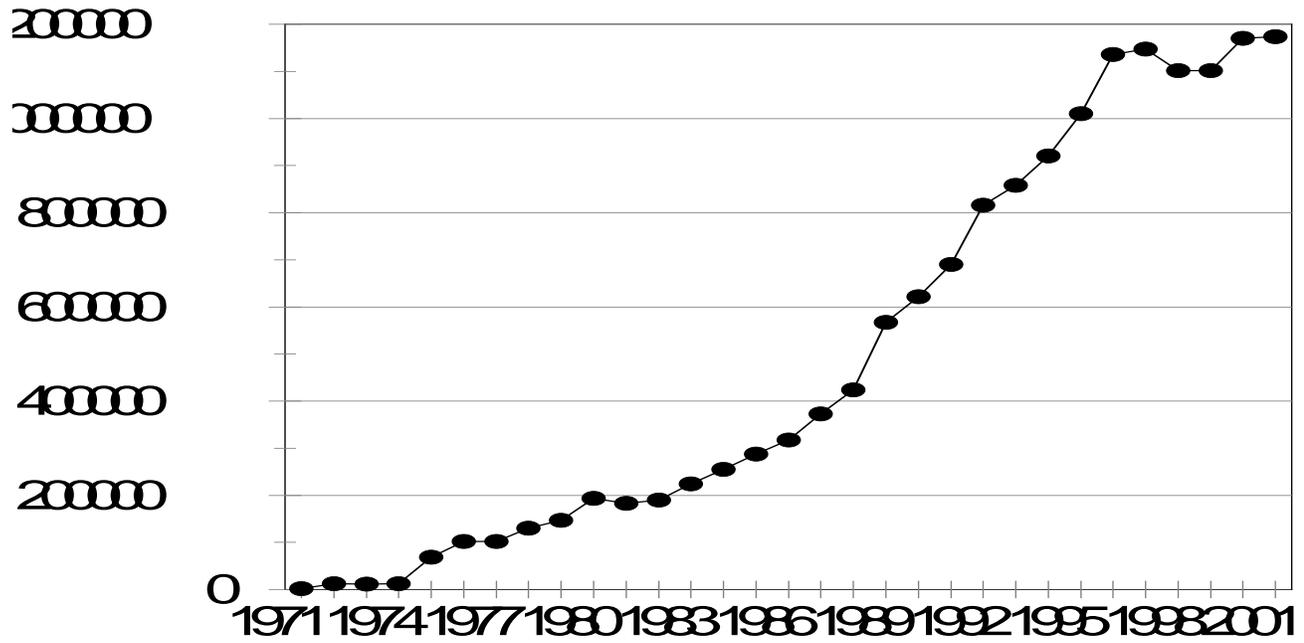
Source: The World Bank (1997). "Expanding the Measure of Wealth: Indicators of Environmental Sustainability," *Environmentally Sustainable Development Studies and Monographs Series No. 17*, Washington, D.C.

**Figure 2: Crude oil production by area and real US price of oil, 1857-1998**

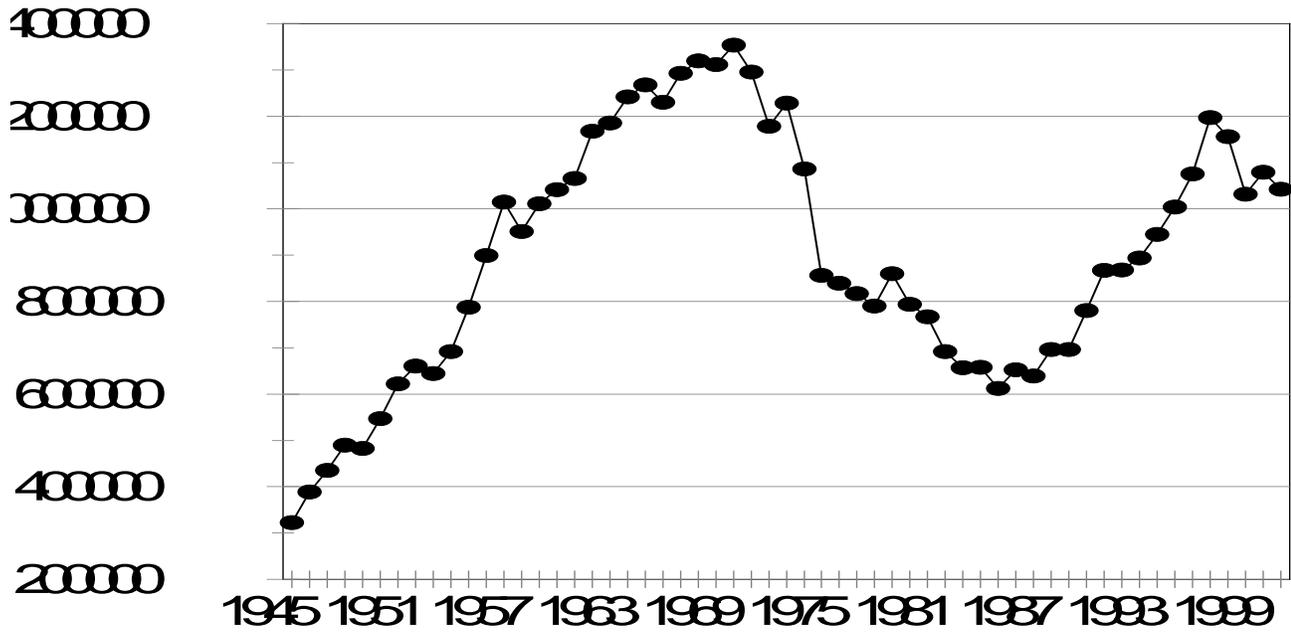


Sources: Production: American Petroleum Institute, *Basic Petroleum Data Book* (1999), Section VI, Table 1: “World Crude Oil Production by Area (Thousands of Barrels);” and Section VI, Table 10: “Historical World Crude Oil Production by Area: 1857-1946 (Thousands of Barrels).” Prices: 1859-1931: U.S. Bureau of Mines, *Mineral Resources of the United States*; 1932-1976: *Minerals Yearbooks*; 1977-1995: U.S. Energy Information Administration, *Monthly Energy Review*. Price deflators: Bureau of Labor Statistics and Paul David and Peter Solar, “A Bicentenary Contribution to the History of the Cost of Living in America,” *Research in Economic History*, vol. 2 (1977), pp. 1-80, Table 1, pp. 16-17.

**Fig 3 Norwegian Crude Oil Production**  
(Thousands of Barrels)



### Fig 4 Venezuelan Crude Oil Production (thousands of barrels)



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<sup>1</sup> Auty also groups countries according to hectares of cropland per capita in 1970 (2001, p. 4), which at least has the virtue of being a resource stock rather than a production flow. Mineral categories, however, come from the share of minerals in total exports. Sachs and Warner assert that variation in mineral exports accounts for a large fraction of the overall variation in their natural resource variable (2001, p. 83). Auty reports that “the *mineral*-driven resource–abundant countries have been among the weakest performers” (2001, p. 3).