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## Oil and Arab economic development

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In Robert Mabro's extensive contribution to the analysis of oil and Arab economic development, three themes are consistently present: concern over sustainability; emphasis on the central importance of developing human capital; and rejection of the concept of 'resource curse'.

### Sustainability

Reflecting on oil markets in 2006 in his

introduction to the book *Oil in the Twenty-First Century: Issues, Challenges, and Opportunities*<sup>1</sup> (quotations from which appear in this article) Mabro argues that the 'of any oil country is to establish the basis of sustainable economic growth in the long run'. The underlying logic of this view is that irrespective of the future evolution of oil prices and export volumes, 'it is likely that the level or growth of revenues will not be

*continually sufficient to cope with demographic pressures and increasing development needs*'.

This view can be derived from two separate concepts. The first being the fact that oil is a depletable resource, while the second is the classic paradigm of economics involving ever-increasing wants in a world of constrained resources.

Oil is depletable in the sense of it being



an exhaustible resource (in geological terms, it is no longer being created). However, it is also potentially 'depletable' in value terms in a technological sense as energy alternatives and improved efficiency of oil use emerge. Thus 'peak oil' will happen because of a lack of demand not supply. An alternative way of expressing this is that oil revenues are NOT income in the conventional economic sense of a continuous flow of money derived from a reproducible factor of production. Thus a country has a national portfolio of assets, which includes oil below ground. Producing the oil and selling it simply switches a component of the portfolio from 'oil below ground' to another component, 'dollars above ground'. To be 'sustainable', this revenue needs to be invested in order to generate a future source of income. Once the barrel is produced it is gone forever. Only in this way can oil production be 'sustainable' over time and form the basis of continuing economic progress.

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At the same time, acutely aware of the high levels of poverty in much of the Arab World, Mabro realized that expectations were developing for improved standards of living and all the other paraphernalia of economic and social development. Thus oil can be seen as a window of opportunity to promote development; this development involves the diversification of economies to create reproducible income-earning assets over the long run. This however, is easier said than done. The challenges of diversification were the obstacles faced, which Mabro saw very specifically as: a limited resource base outside the oil sector, and an insufficient endowment of human capital.

**Developing human capital**

Mabro saw the development of human capital as key to the process of economic development and progress, but at the same time he realized that this was a process that *'takes a long time to yield its fruit'*. There is, however, an additional problem involved, apart from time lags. Developing human capital inevitably involves educating the population – in the broadest sense of the term. However, once you begin to 'educate' people, they are less likely to accept political systems in which they have little or no involvement. An educated population is one that will demand a political say in some shape or form. Thus in many of the Arab countries, as the twentieth century unfolded, the ruling elites were reluctant to allow the genie of education out of the proverbial bottle. Education to produce skills – such as those of doctors and engineers – was fine but not if it began to breed political unrest which challenged the position of the ruling elites.

At the same time, these same ruling elites were in the business of capturing as much economic rent as they could. In many cases they created what were in effect kleptocracies ('government by thieves'). A key consequence of this was that much of the private sector in the Arab World was effectively stifled and excluded from economic activity. There can be little doubt that economic development in any country depends upon an active and vibrant private sector. In the Arab World, with a few notable exceptions, this has for the most part been missing; political reform will be required if an effective private sector is to emerge in the future. In the language of the debate in the Soviet Union in the late 1980s: economic liberalization (perestroika) in the Arab World will not be possible without political liberalization (glasnost). This

creates a fundamental contradiction for oil and development in the Arab World. On the one hand, economic progress requires political reform; but at the same time, oil revenues accruing to the state reinforce the elite captured economy and therefore the status quo.

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**'MABRO SAW THE DEVELOPMENT OF HUMAN CAPITAL AS KEY TO THE PROCESS OF ECONOMIC DEVELOPMENT ...'**  
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The Arab Uprisings, which began in Tunisia at the start of 2011, offered a brief glimmer of hope. Sadly, for the most part, these glimmers have been extinguished, at least for the time being. However, if we are moving into a lower oil price world – where government spending on jobs and subsidies will have to decrease – the ability of the current status quo to survive may well be restricted. This is especially true given the growing demographic pressures of a young population. For example, the IMF in 2011 pointed out that in Saudi Arabia nearly half the population was under 15 years of age (compared to 20 per cent in Norway, Singapore, and the USA). This is a typical pattern in the Arab World more generally. Whatever the outcome of the Arab Uprisings, Mabro was right. The future of economic progress in the region will depend upon the ability of the ruling elites to invest in and promote human capital development; this in turn will require political reform.

**Rejection of the concept of 'resource curse'**

A third common theme in Mabro's writing on oil and development has been his rejection of the presence of 'resource curse'. The term 'resource curse' argues that large windfall revenues from oil are a 'bad thing'

since they somehow damage the existing economy, ultimately leaving the nation worse off. The transmission mechanism from oil revenue to economic damage is complex but contains a mixture of Dutch Disease; crowding out by the oil sector; and various sociopolitical issues revolving around rentier societies and rent capturing elites. Mabro argued that: *'All oil-exporting countries although in different ways and degrees would be worse off today if they never had oil.'* The result of the revenues has been: *'improved health, nutrition, education, housing, public utilities and more generally the standard of living of at least part of the population'*. For the producers of the Gulf Cooperation Council (GCC) countries this has certainly been the case. Given the state of the GCC members before oil – dire poverty based upon subsistence economies with a little entrepôt trade – the simple 'resource curse' argument simply has no validity. Without oil revenues the GCC countries would probably not even exist as sovereign entities. However, with a more nuanced approach it is possible to turn the resource curse argument on its head to accommodate Mabro's point, while at the same time raising important questions relevant not only to the GCC but to other oil producers. Thus: rather than asking if the oil sector and its revenues caused damage to the rest of the economy (and why), instead ask why the oil sector failed to have a 'better' impact on the countries concerned (and why)?

Note

<sup>1</sup> *Oil in the Twenty-First Century: Issues, Challenges, and Opportunities*, Robert Mabro (ed.), Oxford: OUP/OPEC, July 2006.

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In other words this approach treats the issue of a 'resource curse' in terms of an opportunity cost, although it begs the question: how to define a 'better' impact? This brings the analysis back to the first of Mabro's themes: sustainability. Sustainability for an oil producer can only mean successful diversification of the economy away from dependence on oil revenue and the creation of an economy not dependent upon the export of crude oil. While this has been a major (and oft-stated) aim of Arab oil producers since the first oil shock of 1973, their record for the most part has been abysmal. In 2011 the IMF claimed that the GCC's non-hydrocarbon sector had formed 61 per cent of its GDP in 1990, but that by 2010 the figure had fallen to 51 per cent. As for the non-hydrocarbon primary fiscal deficit – an excellent proxy measure for oil dependence – for Saudi Arabia this rose steadily from a figure of (on average) below 50 per cent in the 1990s, to 140 per cent by 2010. In effect, attempts at diversification are not only failing in the region, they are actually going backwards. Apart from anything else, this means that the oil sector has failed to fulfil the role of a leading development sector (along the lines of textiles in Great Britain in the eighteenth century or railroads in the USA in the nineteenth century).

Mabro claims that part of the explanation for this failure to diversify and promote economic development

is due to the fact that *'oil reduces the incentive to introduce painful policy reform'*. In other words, oil revenues have simply helped governments to paper over the cracks of a failing economy. Arguably this view undermines his own argument about the absence of resource curse, since the idea of oil revenues inhibiting economic and political reform is central to much of the 'resource curse' literature. However, whatever the reasons for previous failures, the diversification of Arab oil producers' economies is now moving to the top of the policy agenda. Growing concerns about climate change and unburnable carbon mean that the future of oil revenues must be viewed as being extremely uncertain. Such uncertainties are reinforced if we really are moving towards a period of lower oil prices. Thus the ability of any government in the Arab World to maintain an oil-dominated economy beyond the short term must be in question. The challenge is: how to diversify these economies and rebuild the income-earning portfolio of national assets to meet the needs and expectations of future generations? Mabro argues that, in the absence of alternative resources, the answer lies in developing human capital. This is undoubtedly true but, as argued above, a necessary condition for this to happen is political reform. Such reform would have the additional benefit of unleashing the enormous talents, abilities, and imaginations of the Arab private sector, releasing it from the shackles of the kleptocracies that have dominated the region for centuries.

