

Natural Resource Rents, Good Governance, and Entrepreneurship

PRELIMINARY DRAFT*

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Abstract

This study makes a central contribution to empirical explanations of the resource curse by investigating whether rents from natural resources have a crowding-in effect on entrepreneurship in a sample of 116 countries. Using data for the period 2004-2012, the paper finds that good governance plays a significant role in facilitating the positive effects from natural resource wealth which stimulate entrepreneurial activity of new local firms. The significance of overall governance is driven by control of corruption, government effectiveness and regulatory quality dimensions. In addition, the results also show that there is a threshold level of governance quality above which resource rents crowd-in new local firms. For all the sample countries in Sub-Saharan Africa, Latin America & Caribbean, Middle East & North Africa, and South Asia, the quality of governance is below the estimated threshold value that would let natural resource rents crowd-in entrepreneurship. The only regions where some countries have a domestic governance system that is sufficiently developed so that natural resource rents have a crowding-in effect on entrepreneurship are East Asia & Pacific, Europe & Central Asia, and North America. The policy conclusions of the empirical analysis are quite clear. Natural resource rents by themselves may be a curse on entrepreneurship. The development of a good governance system is an important precondition for ensuring that natural resource rents have a crowding-in effect on entrepreneurship, thus turning the curse into a blessing. Developing countries seeking to use their natural resource wealth as an instrument of development should therefore implement reforms that would raise the quality of the domestic governance system to a level that is sufficient for natural resources to facilitate entrepreneurship. Reforms targeting the control of corruption, government effectiveness, and regulatory quality dimensions of governance are the most important. In light of the findings in this paper, countries can also adopt measures to accomplish good governance in the natural resource sector that are championed by the Extractive Industries Transparency Initiative.

Keywords: natural resource rents, governance, entrepreneurship, crowding-in, rent-seeking

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