

The **Charlie Rose Show**
May 4, 2005 Wednesday

CHARLIE ROSE: Joining me now, **Nancy Birdsall** and **Arvind Subramanian**. This summer, they wrote an article in "Foreign Affairs" magazine, which was entitled "Iraq: Escaping the Oil Curse." **Nancy Birdsall** is the president of the Center for Global Development; **Arvind Subramanian** is the division chief at the IMF. I am pleased to have them here to talk about exactly what they mean by escaping the oil curse. I'll start with you.

ARVIND SUBRAMANIAN: Oh, well, you know, there is this finding based on the post-war experience that countries that have oil and other minerals, not just that the oil does not just have -- does not have a positive impact, in fact it has a negative impact. So that countries that have oil gross lower than countries that don't have oil, and that countries that have oil generally have much weaker political institutions for their people.

So that's the curse of oil. So the question is, how do you get out of a situation where oil does not exert this dampening effect on your growth prospects, on your developing prospects, and for developing your political and economic institutions. So that's the escaping the curse.

CHARLIE ROSE: OK, and the answer, I mean, the first question you have to address is why is it that those countries that have oil don't have the kind of economic growth and the political structure that those countries that don't have oil in some cases do?

ARVIND SUBRAMANIAN: Right. There are many reasons, but the most important reason is that what oil does is it actually impedes the development of institutions in the following way. Think of what the supply-siders say. They say if tax are low, you do brilliantly. But with oil, it is the ultimate supply-sider's paradise, because you have all these governments with all this oil revenue, you don't need to tax.

CHARLIE ROSE: Right.

ARVIND SUBRAMANIAN: But that paradox is what prevents them from developing the institutions, because having to tax creates a connection between the state and its citizens.

CHARLIE ROSE: Right.

ARVIND SUBRAMANIAN: So that on the one hand, the state has an incentive to promote institutions for growing the economy, and on the other hand, citizens, because they're taxed, have this incentive to hold governments accountable.

When you have oil, that link's severed, and over the long run, that has a very damaging effect on institutional development.

CHARLIE ROSE: Is there an exception to this?

NANCY BIRDSALL: Sure, there are exceptions. In fact, well, I suppose it's not an exception, but it's worth making the point that a country like Norway discovered oil late in the game, late in the development of its democratic institutions, late in the development of its economic institutions -- the rule of law, property rights, political institutions that ensure there are checks and balances, that you can't have abuse of power, that people participate in their democratic system.

So when a country like Norway acquires this great asset, it is great for Norway, and it already is a functioning democracy, then it doesn't have the same problems.

CHARLIE ROSE: Does oil encourage radical fundamentalism?

ARVIND SUBRAMANIAN: Oh, well, I mean, the manifestations of the curse are many. One is, of course, is that even before you get into radicalism, you have the situation where actually struggling -- there are fights over these natural resources that give rise to civil wars, for example. In Africa, in Angola, in Nigeria, this is a great example of where these natural resources led to civil war and civil strife and internal conflict. Yes, sometimes.

CHARLIE ROSE: Led to civil war because they -- various political parties wanted their hands on the revenue.

ARVIND SUBRAMANIAN: Yeah. Not just political parties, various groups in society, you know. Because many of these countries do not even have political parties, but you know, there is a fight for the spoils, because this is the biggest spoil out there. And so that's one manifestation.

Yes, and indirectly, yes, oil can give rise to a more extreme manifestations, you know. The fact that oil impedes political developments, stifles people's rights, for example, in terms of political participation, then that sense of being disenfranchised that oil indirectly leads to can have extreme forms.

CHARLIE ROSE: Some people will argue that the United States should become energy-independent. And that's a whole other story, and we've had people say it is impossible to do in a short span of time, and you can't have a man on the moon kind of project in 10 years and make the country energy-independent. But if suppose that there was not this huge demand by the United States and by the Western -- and by the industrialized world on the oil in the Middle East, what would happen, for example, in Saudi Arabia? What would it cause to happen?

NANCY BIRDSALL: Wow, that's a great question. I think in the short run, what it would mean is that a government that has come to rely on what you might call easy money, would run into great difficulties, because the government would be unable -- in the absence of that revenue, would be unable to sustain what services do exist -- schooling,

health services and so on. So there would probably be the beginnings of the kind of breakdown in society as a whole that exists now. So you would have a problem.

It's not to say that with the oil there are not problems also, in a place like Saudi Arabia. It's an example of a country where there has been economic development, in part because of that asset, but not political development.

CHARLIE ROSE: Would it promote political development if they had no place to sell their oil to, and therefore the dominion of people who have used oil to stay in power.

NANCY BIRDSALL: I mean, I think it would be difficult to imagine what the transition would be. But in the medium term, I think it would, because a country like Saudi Arabia would then need to institute a tax system. And imagine that it starts at the local level. Then you have people who understand that the taxes that they're paying make their mayor and their school superintendent accountable to them. And then you can have the beginning of the development of political parties. Then you have property rights become much more important than they are in the absence of a tax system, since a tax system ultimately has to be based on some combination of your rights and your property and the work that you do.

CHARLIE ROSE: Do you think the world has the political will to be weaned off of oil?

NANCY BIRDSALL: I certainly think that we have, in the West, the political will to work with countries in the developing world to minimize the risks that oil poses for them. It's a different question of whether in the long run we will be weaned off of oil. I'm an economist, and there is no question that if the price keeps going up, we will eventually find our way to other technologies. And there are ways that governments can have that price go up artificially in the short run, to help push along that technological change.

But I think the issue really is so much broader in terms of how oil and other natural resources hurt developing countries that have weak institutions. That, in turn, creates global problems for all of us. So there are a lot of global issues like oil and failing states.

CHARLIE ROSE: It would seem to me that there ought to be societies in which they could escape the oil curse. I mean, that there ought to be countries that had enough creativity so that they could use the revenue from oil and not be dependent on it and not be.

(CROSSTALK)

NANCY BIRDSALL: Well, Mexico has. Colombia is working on it.

CHARLIE ROSE: So they have escaped the oil course then.

ARVIND SUBRAMANIAN: I think the two good examples are.

NANCY BIRDSALL: Or are escaping. Sorry.

ARVIND SUBRAMANIAN: Chile was an example that was reliant on copper, you know, again, easy money, yeah? And then the combination of, you know, good leadership, you know, building good institutions certainly providing a great atmosphere for the private sector to invest. Through these policies, Chile was able to kind of escape the curse. Malaysia is another example, which was heavily reliant on rubber, but gradually weaned itself off rubber.

Indonesia is a very interesting case as well, though. For a long time, we thought that it had escaped the curse, because it did very, very well in the '70s and '80s, until the mid-'90s, but then in the '90s they had this crisis, and some people argue that, you know, what we saw in the aftermath was a crisis was in fact some lagged effect of in fact the effect of oil, because.

NANCY BIRDSALL: The corruption.

ARVIND SUBRAMANIAN: . the corrupt -- the political institutions hadn't developed. So the curse is not inevitable. There are countries that can escape the curse, but the requirements are pretty steep in terms of what it takes for a developing country with weak institutions to escape that.

NANCY BIRDSALL: What's actually.

CHARLIE ROSE: What it takes is leadership, in part, doesn't it?

ARVIND SUBRAMANIAN: In part, yeah. I think Chile was an example of that, strong leadership.

NANCY BIRDSALL: And then it can also -- the process can be helped along greatly by the rich countries.

CHARLIE ROSE: Doing what?

NANCY BIRDSALL: By taking steps, for example, pushing for public disclosure of the resources, the money that sometimes comes from those who are benefiting from this corruption into Western banks, by encouraging the kind of legislation that would make multinationals culpable legally if they participate in a process which involves corruption.

So I think there are steps that can be taken in the rich world, and it is important to do that. I was thinking when Arvind was talking about Indonesia, that people can understand very easily the big difference between a place like Nigeria with its problems with oil, and the history of places like Korea, Hong Kong, Taiwan.

CHARLIE ROSE: That have no oil.

NANCY BIRDSALL: That had not -- they didn't have the curse.

CHARLIE ROSE: They relied on technology.

NANCY BIRDSALL: You know, even though some countries can manage their way out of the curse, it's interesting that those who didn't start with this asset actually developed a different asset.

CHARLIE ROSE: Japan is another example.

NANCY BIRDSALL: Japan is another example. The human capital of their people. We should give the example of Chad, where Chad has recently discovered oil, and along with Cameroon, borrowed from the World Bank and private creditors to do a pipeline. And as part of that process, the World Bank worked with the government of Chad to set up a special fund, which kind of segregates this money, and there is external monitoring, to be sure it's used for social services and for investment.

This is another kind of step where -- whether you can sustain that, in the absence of enlightened leadership, is hard to say.

CHARLIE ROSE: And enlightened leadership is easier to.

ARVIND SUBRAMANIAN: Exactly.

CHARLIE ROSE: . is easier to describe than to have.

ARVIND SUBRAMANIAN: Exactly. To have, yeah. You know, if you look around the world, the million-dollar question is, you know, how do you get -- how do you build public -- good public institutions, you know? In some cases, you get good leaders, but often you don't. So you know, if it were as easy as getting a good leader, then you know, we would be -- you know, large parts of the world wouldn't be where they are.

CHARLIE ROSE: Thank you for coming. Thank you very much.

NANCY BIRDSALL: Thank you very much.

CHARLIE ROSE: Thank you for joining us. We'll see you next time.

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