Tony Addison

Macro-Financial Policies in Resource Based Economies

UNITED NATIONS UNIVERSITY
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Key Macro & Financial Challenges for Resource LICs & LMICs

- Dependence on export revenues from mining & oil & gas is increasing on average: Diversification remains the challenge!

- Covi-19 pandemic: oil prices slumped (then partial recovery). Few oil exporting LICs & MICs had fiscal buffers sufficient to ease fiscal adjustment (but oil price fall helped net oil importers).

- Oil: headwind from Net Zero transition (e.g. EVs). Global Gas demand is high, especially Asia (inc. China)

- Metals prices slumped with Covid but then recovered to above pre-pandemic level. Now a Boom (but low mining investment). Metals: tailwind from Net Zero (e.g. batteries, EVs) + global recovery (esp. China).

- Global food prices remain a concern. Net Food importers + weak currencies => food price shock ahead?

- Finance: Median public debt for SSA expected to be 75% of GDP in 2022, up from 56% in 2019 (Risks as Fed etc. eventually pull back on quantitative easing & raise rates). More debt defaults ahead.

- SDR $650bn increase: good news but modest help for average highly debt-vulnerable countries (= to about 5% of their public debt stock: UNDP). Avoid oil-backed loans: non-transparent & fiscal risk

China's Relevance for Resource Based Economies

- China is the biggest market for many metals (e.g copper) and is the biggest importer of coal, oil & natural gas.
- Therefore LICs and LMICs need to closely watch China's macro-economic trends and policies. In 2020, many expected a prolonged slump in metals prices, but China's short recession & fast recovery fed into high demand and a boom in metals prices
- China offers many useful lessons on economic diversification, not least in having a long term vision backed by private and public action to deliver the necessary investments to move up global value-chains (GVCs).
- For LICs and smaller LMICs, adding value to unprocessed commodities is essential to moving up global GVCs. For those with mining, there are local content possibilities. But mining is increasingly characterized by automation (& associated digital technologies). For oil & gas economies, there is a danger that local content investments (e.g. in refining & petrochemicals) may become 'stranded' along with the oil itself as the markets begin to soften with the global move to Net Zero. Smaller and high cost oil producers are vulnerable.
- Investing resource rents in agriculture has high returns for diversification, growth & poverty reduction. But climate change is increasing the frequency of floods, droughts & storms. Destroying renewable natural capital (forests, fisheries, biodiversity etc.) via mining & O&G production should be avoided as such natural capital is far more valuable, especially for livelihoods, in the long-term.
- GVCs in metals, O&G and manufacturing will increasingly focus on emissions content (see EU carbon border tax plans). Countries need to strip out fossil fuels from their energy systems & push carbon abatement, carbon capture & storage etc. Africa still has a very low percentage of renewables in its energy generation. More coal fired power is *not* the solution to energy poverty.
- Carbon pricing, including carbon taxes, is expanding (> 40 countries). China's carbon market is now the world's largest & this will increasingly influence the prospects for LIC and LMIC exports, not least in metals and O&G, but also in manufacturing.

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Helsinki, Finland