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Learning Brief:

Promoting Impact of Natural Resource Investments

This learning brief is designed for policymakers working on economic development programmes in low-income countries rich in natural resources. It draws upon lessons from the recent evaluation of the Employment and Skills for Eastern Africa (E4D/SOGA) programme.

What's the issue?

The exploitation of natural resources can be powerful in driving domestic growth and improving living standards. Their extraction and exportation boosts national income, creates jobs and generates business opportunities for local suppliers. Employment opportunities directly generated by 'extractive' industries have the potential to increase the incomes of local people and reduce poverty (Addison and Roe, 2018).

Investments not only create jobs in transport, refining, mining and other activities directly associated with the extraction and exportation of natural resources, they also generate wider economic opportunities through creating positive linkages between multinational and local firms. Multinational investing firms form links with local businesses in their supply chains by buying locally manufactured parts or by contracting locally supplied services. For more on the benefits of these linkages for firm growth, see brief on industry partnerships.

Despite such potential, there are many cases of sizeable natural resource investments failing to lead to tangible and sustainable economic benefits for local peoples and their communities. In fact, over the last few decades, resource-poor countries have outperformed resource-rich ones (Sachs & Warner 1995). Concerns that the benefits of resource booms in developing countries are not shared stem from the theory that foreign resource investments do not **automatically** create sufficient linkages with host economies (Gallagher & Zarsky, 2012).

Enclave is the term used to describe these kinds of investments (Gallagher & Zarsky, 2007). They bring in the majority of their workforce from overseas, import the majority of their raw materials and re-export the majority of their final products, rather than hiring local workers, buying from local suppliers and selling to local buyers.

Helping local actors gain a foothold in this process is essential for capturing the economic impacts of natural resource investments. As such, avoiding **enclave development** and promoting **linkage development** is a vital policy concern for developing countries, especially the many that are heavily reliant on natural resources (see figure below). More than half the countries in Africa depend on the export of some major mineral commodity and for several, mining accounts for over half their export revenues.

Global Post, Simran Khosla, Data from 2013 and CIA factbook. link

Best practice from the literature on design

Evidence shows that, despite the widespread use of local content requirements, wage subsidies, and other policies designed to artificially encourage linkages between multinational firms and local economies, the most efficient long-term approach is to directly address the skills deficiencies of local workers and enterprises.

Local Content Requirements

One approach to encourage linkage development has been to embed 'forced localisation' into domestic legislation. Local content requirements (LCRs) are requirements that commonly stipulate that investing firms employ a minimum number of local people, purchase a minimum number of inputs locally or contract a minimum number of local firms further up the supply chain. The use of these policies has become increasingly common in developing countries. **In the last decade over 145 new LCRs have been put in place** by governments with the aim of promoting domestic economic development (OECD 2019). However, the concern is that they discourage investments and, since they also fail to address the underlying skills deficiencies causing multinational firms to overlook local workers and suppliers, they are generally considered to undermine long-term competitiveness (Hufbauer & Cimino-Isaacs, 2013).

Employment subsidies

Another policy has been to subsidise local employment through offering wage subsidies, payroll tax cuts or direct payments to employers. These kinds of active labour market policies do encourage linkages between multinationals and local workers, but are costly and heavily targeted towards particular industries, risking displacement and the crowding out of workers in industries without subsidy (McKenzie, 2017). Like LCRs, they do not tackle underlying skills deficiencies, meaning their long-term impacts are equally concerning.

Skills development interventions

There is far more optimism regarding interventions that promote linkage development by addressing skills gaps and improving the competitive characteristics of the domestic economy. Low-income countries tend to suffer from weaker infrastructure, less competitive firms, less profitable domestic markets, and lower existing levels of the technical and vocational educational skills needed in the natural resource sector. As a consequence, these countries seem to suffer more from enclave development than high-income countries (Lahn & Stevens, 2018) Deficiencies in low-income economies mean that, in unregulated markets free of LCRs and subsidies, investing firms often hire overseas workers to work in jobs for which they struggle to hire locally, and buy from overseas suppliers to supply goods for which they struggle to procure locally (Ostensson, 2018). Extractive industry investments are often located in remote and rural areas where education access and attainment figures are lower than national averages, which points to the long-term value of interventions that develop the skills of local workers and firms. For lessons regarding best practice and success factors relating specifically to these types of interventions, see **learning brief on skills programmes**.

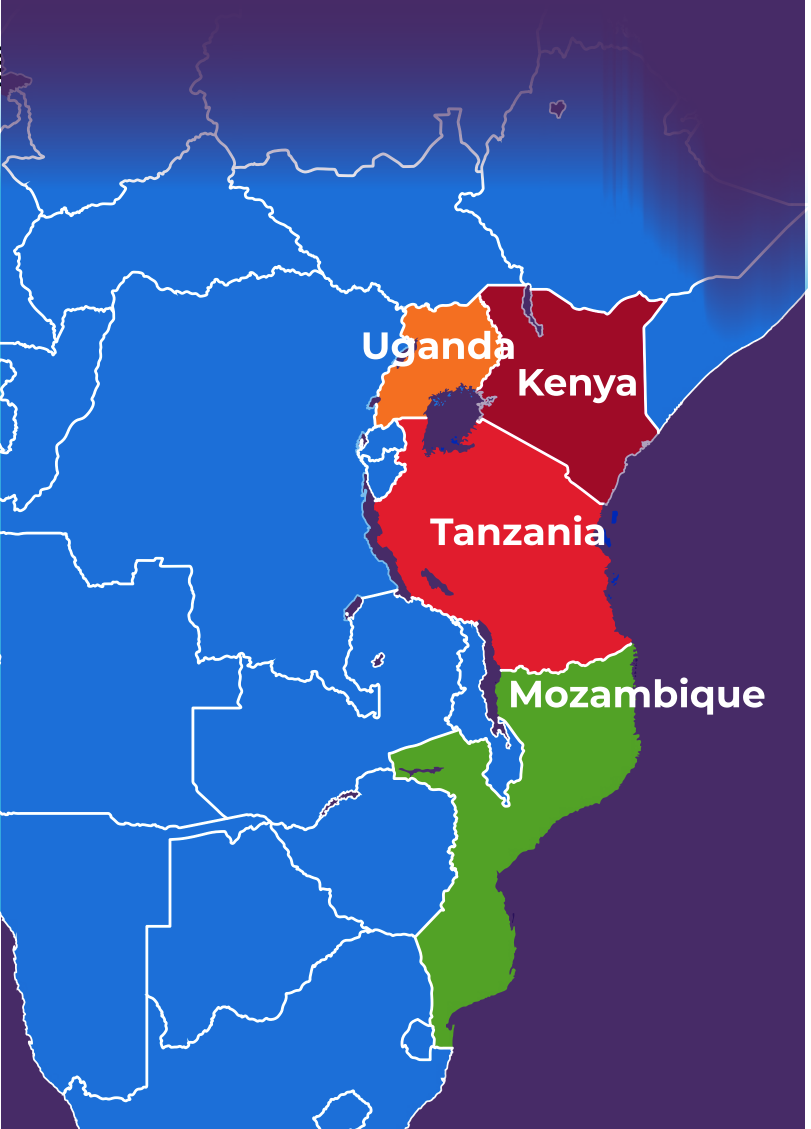
However, it should be noted that skills interventions alone fail to consider the structural challenges, specific to the extractive sector, that makes the incorporation of local actors difficult. The physical execution of oil and gas investment projects requires International Oil Companies (IOCs) to secure a wide range of technical and commercial contracts and permits. Since these agreements are not always straightforward to secure, there is often a disconnect between strategic investments and actual engineering, procurement and construction (EPC) work taking place. Addressing these structural challenges by improving institutional arrangements is therefore another important component for linkage development programmes to consider (Dietsche, 2018).

Programme Approach

The E4D/SOGA employment and skills programme was an extensive five-year programme of local employment promotion, targeted skills training, enterprise development and job-matching services in four East African countries (Kenya, Tanzania, Mozambique, Uganda).

In each of the selected countries, there was a need to capitalise on expected imminent oil and gas investments by large multi-national firms and international oil companies.

Due to low existing levels of technical and vocational educational skills that were needed in the oil and gas sector and a lack of cohesion in labour market architecture, there was a risk that, without intervention, local people would not access the employment opportunities generated by these investments.



Programme Design

Across the four countries, the programme delivered 30 individual projects, with 20 focused on skills development for individuals and 10 focused on enterprise development for local businesses. Three incorporated components of both.

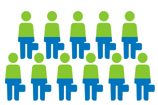
The content of the skills development projects varied and included training in vocational skills specific to the oil and gas sector (welding and machine operation) basic skills (literacy and numeracy) and work-readiness skills (time management and body language).

The original enterprise development projects offered support to local small and medium sized enterprises (SMEs), but evolved to also include small and micro-sized agricultural enterprises and support for individuals to develop their own businesses. Through a combination of technical skills training, business skills training and coaching, the programme aimed to help individuals gain a foothold in the informal sector.

The projects also incorporated services to match trained individuals to jobs, and enterprises to supply chain opportunities. This was done through developing and implementing partnerships with industry and through providing careers fairs, job centres and other matching platforms.

Programme Results[1]

As of February 2019:



▶ **11, 248 people moved into jobs** (48% of original target of 23,000

▶ **84.5% average income increase** (versus original target of 10%)

▶ **50% of graduates obtain and maintain a job** (versus original target of 70%)

1 Note that there is likely to be some lag time between implementation and results. The number of people moved into jobs nearly doubled in the last year of the programme, which indicates that the long-term impact is ultimately likely to be greater than the evaluation figures suggest.

Our findings

Despite some programme level success in promoting linkage development, the effectiveness of individual interventions was highly variable. Based on those that were most effective, the evaluation identified a number of important findings to be considered by policymakers designing interventions to help developing countries capture the impacts of natural resource investments.

A focus on meeting international standards can help promote linkage development

Some interventions were designed to train local people and businesses specifically to meet international standards and these incorporated internationally recognised certifications into their offerings. Large, multinational lead operators typically dominate natural resource industries and, in order to link effectively with them and be incorporated into global value chains, local firms need to possess the capabilities to meet their requirements.

Training courses that were designed to upskill graduates to a level closer to those required of international companies can be effective in their capacity to move graduates into sustainable jobs.

The most effective programmes reflect the needs of multinational investments

For optimal results, interventions need to be designed to fit the labour and skills needs of the industries receiving the largest investments. The evaluation found support for the consistent evidence that skills interventions are most effective when focused on vocation-specific training to place graduates into sectors with strong actual demand for skilled workers. Training should be delivered to a certain standard, focused and targeted to the needs of sectors with high demand in order to lead to decent and sustainable employment.

An effective demand-driven approach requires strong partnerships with the private sector

In order to match patterns of actual demand as accurately as possible, programmes need to engage effectively with the private sector. Publically available information on labour demand at a national level is difficult to obtain, especially in natural resource industries, meaning that partnerships and positive relationships with the private sector are necessary to obtain sufficient information to produce an effective analysis of future labour and skills demand. Stronger partnerships produced more successful employment outcomes.

Continuous analysis is required to build necessary flexibility

Anticipated demand can often fail to materialise and local political economy circumstances are often unstable. Despite high-level initial analysis, actual patterns of labour and skills demand diverged hugely from those predicted at the start of the programme. This forced the programme to broaden its sectoral scope and to focus on wider enterprise development (rather than concentrating only on medium sized firms supplying the oil and gas sector specifically). This highlights the importance of designing interventions that are adaptable to changing circumstances and, therefore, a continuous process of industry mapping should be implemented by future programmes as a sensible practice to help identify actual, rather than expected demand.

Further Reading

- Final Report: Independent Evaluation of the E4D/SOGA Programme
- **Learning Brief: Skills Programmes & E4D/SOGA**
- **Learning Brief: Industry Partnerships for Local Development & the E4D/SOGA Programme**
- *No miracle drug: Foreign direct investment and sustainable development*, Gallagher & Zarsky, 2012, **link**
- *Natural Resource Abundance and Economic Growth*, Sachs & Warner, 1995, link
- *The Enclave Economy: Foreign Investment and Sustainable Development in Mexico's Silicon Valley*, Gallagher & Zarsky, 2007, **link**
- *Sustainable and Responsible Mining in Africa, International Finance Corporation*, 2013, **link**
- *Local content requirements impact the global economy*, OECD, 2019, **link**
- *Local Content Requirements: A Global Problem*, Hufbauer, Schott, & Cimino-Isaacs, 2013, **link**
- Extractive Industries: The management of resources as a driver of sustainable development, Addison and Roe, 2018, **link**
- *How Effective Are Active Labor Market Policies in Developing Countries?*, McKenzie, 2017, **link**
- The Curse of One size fits all – Re-evaluating what we know about extractives and economic development, (Chapter 5), Lahn &and Stevens, 2017, **link**
- Chapter 5 The Curse of One size fits all – Re-evaluating what we know about extractives and economic development, Lahn and Stevens, 2017, **link**
- Political Economy and Governance (Chapter 6), Evelyn Dietsche, 2017, **link**
- Local Content, Supply Chains, and Shared Infrastructure (Chapter 24), Olle Ostensson, 2018, **link**

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