PEA in the mining/extractives sector

Claire Mcloughlin

26.11.2013

Question

What is the relevance of political economy analysis (PEA) to mining/extractives interventions? How and why has political economy analysis (PEA) been applied in this sector? What tools or guidance are available for conducting PEA in this sector?

Contents

1. Overview
2. Relevance of PEA to the mining/extractives sector
3. Examples of PEA applied to mining programmes
4. Tools and guidance
5. References

1. Overview

Political economy analysis (PEA) is a form of analysis concerned with understanding the prevailing political and economic processes governing behavior in society – specifically, how these processes affect the incentives of different actors, and the distribution and contestation of power between them (GSDRC, 2009). It is intended to support more effective and politically feasible development interventions by setting realistic expectations of what can be achieved, over what timescale, and the risks involved (ibid). There are, however, ongoing debates about how to realise this potential of PEA to improve development programming.

1 The GSDRC’s topic guide on political economy analysis gives a fuller explanation: http://www.gsdrc.org/go/topic-guides/political-economy-analysis
2 For example, a recent workshop held at the University of Birmingham on 15 November, 2013 entitled ‘Making Politics Practical II’ highlighted some of the ongoing challenges development agencies face in ‘thinking and working politically’. Podcasts of presentations will be made available on http://www.dlprog.org. See:
There is limited literature on the relevance and applicability of PEA to the mining sector. Many PEA studies are not released into the public domain due to their political sensitivity. According to experts contacted for this rapid report, PEA has not been widely applied to development interventions in this area. However, the World Bank has been somewhat active, funding 11 studies in over the past 5 years, under the rubric of its Governance Partnership Facility.\(^3\)

The limited available literature suggests that the particular relevance of PEA to mining is that it can help development agencies to understand:

- **The (potential) impacts of mining on development**: specifically, to understand the obstacles to allocating resource rents for developmental purposes.
- **Relationships between actors**: including between different levels of the state.
- **Elite incentives and the potential for ‘resource curse’**: in particular, understanding elite incentives to generate rents, and the complex range of factors that affect their capacity to do so.
- **Rent distribution**: understanding why and how elites use rents to re-enforce their power, and why they select certain public policies.
- **The feasibility of reform**: much of the literature emphasises the role of PEA in highlighting ‘best fit’ (as opposed to best practice) solutions.

The case-study examples included in this report further highlight the range of practical purposes for which PEA has been commissioned in the mining sector, how it has been undertaken in practice (i.e. methodologies), and its subsequent implications for programming. In these examples, PEA has been commissioned to better anticipate elite responses to a resource boom (Mongolia), to identify project funding likely to gain most traction (Malawi), and to understand why mineral wealth hasn’t translated into economic development (Ghana). These studies have helped identify windows of opportunity (Mongolia), the gender dynamics of decision-making (Ghana), and coalitions likely to support or stand in opposition (i.e. be ‘winners and losers’) to various reform options (Malawi; Burkina Faso). Practical outcomes have included increased capacity for sector analysis, both within the donor agency and in civil society (Mongolia), and more effective systems for monitoring and oversight (Burkina Faso).

No specific guidance was found on conducting or commissioning political economy analysis in the mining sector. The majority of PEA tools available are not specific to any sector or area of intervention.\(^4\) Rather, they tend to give generic advice on how to analyse the core, common elements of most PEA analyses: actors, institutions and incentives. However, Barma et al. (2012) provide some tailored guidance on how to adapt value chain analysis to the mining/extractives sector. They also present a typology for classifying the political economy of the country, based on whether the state can make credible commitments over time, and the degree to which the political regime is inclusive. This is intended to help development agencies to identify the types of mining reform likely to be feasible.

---

\(^3\) These studies were in Angola, Ghana, Nigeria, Niger, Mongolia, Timor Leste, the Democratic Republic of Congo, Tajikistan, Uganda, Zambia, and Burkina Faso. Those available online are referenced in this report.

\(^4\) Though no tools for PEA in mining were found, guidance on conducting governance assessments in the sector has recently been produced by The Policy Practice. See: [http://www.thepolicypractice.com/papersdetails.asp?code=21](http://www.thepolicypractice.com/papersdetails.asp?code=21)
2. Relevance of PEA to mining/extractives sector

Understanding the (potential) impacts of mining on development

According to a forthcoming stock take of World Bank experience (due for publication in 2014), PEA can enhance aid effectiveness in mining by highlighting the incentives of the main stakeholders and decision-makers operating in the sector (Fritz, forthcoming). Its basic premise is that a better appreciation of these incentives enables development agencies to better anticipate the potential constraints to and opportunities for reform (ibid). Specifically in the extractives sector, PEA often seeks to understand whether and how incentives can be aligned towards the spending of natural resource revenue to improve citizen welfare. As expressed by Barma et al. (2012: 25), greater recognition of the political economy dynamics prevalent in extractives can enable development partners to ‘better understand and address the institutional and political obstacles to extracting and allocating resource rents for developmental purposes’.

Writing for the World Bank, Barma et al. (2012) put forward a widely-used typology for predicting whether resource-rich states are likely to be capable and willing to reform their extractives sectors for developmental purposes. Based on a comprehensive set of case studies, they argue that natural resource rents are most likely to be transformed into positive development outcomes, rather than wasted, when:

- **Government can make credible, inter-temporal commitments (i.e. commitments over time):** meaning there is a degree of stability in the policy environment over time, making it easier for bargains to be enforced between extractive companies, governments and citizens, and for deviations from those agreements to be sanctioned.

- **The political regime is inclusive:** meaning that diverse social, economic, and political interest groups are incorporated into decision-making processes, and a sense of either collective welfare is privileged over personal elite interests.

Understanding relationships between actors

A recent study of the Lao People’s Democratic Republic (Lao PDR) emphasises that politics, governance and institutions are among the key variables that determine whether or not mining is likely to support economic development and poverty reduction (Mining Partnerships for Development, 2011). It argues that in particular, PEA can illuminate the decision-making processes and power relationships among different actors, or groups of actors in this regard (including citizens, government and the private sector). For example, it can help explain why a regulatory framework operates as it does, or why a fiscal regime for extractive industries penalises or favours certain types of activities. In this particular case, a combined economic and social assessment of the sector identified competing and conflicting jurisdictions between different levels of government, both over the granting of concessions and the raising of taxes. It also illustrated that in implementing community development funds, mine operators were having to balance discrepancies between the demands and needs expressed by local communities, and those set out under district development plans (ibid).
Understanding elite incentives and the potential for ‘resource curse’

Barma et al. (2012) note that resource-dependent developing countries often pursue short-sighted policies for extracting resource rents, and that elites subsequently allocate those rents in ways that privilege their own private consumption rather than promote collective social welfare. They argue this leads to the so-called resource-curse, whereby resource-rich countries experience limited economic growth, weak accountability, and can be at greater risk of conflict. Understanding how rents from resource extraction are generated and distributed are therefore core elements of a political economy approach to the extractive sectors. However, this is complicated by a number of distinctive characteristics of extractive industries:

- **The finite nature of hydrocarbons and minerals**: what constitutes ‘ore’ at any given time is a function of commodity price, technology, extraction costs, and government policy.

- **The ‘super-normal’ profits yielded by resource extraction, and the state’s sovereign right to some portion of those rents**: Rents depend on geological conditions and the prevailing business climate. Because extraction often occurs in remote areas, there is frequently a lack of transparency to the public or to government entities. The wealth generated by the extractive industries can in turn generate incentives to avoid and discourage transparent oversight and investments in institutional capacity.

- **The volatility of commodity prices**: Mineral price cycles are characterised by volatility and uncertainty. The political economy of extractives may be different in the ‘boom years’ (high prices), during which time stakeholders are likely to be focused on short-term rent-seeking, than it is during the ‘bust years’ (low prices), during which time the political economy is likely to be dominated by competition over spending and avoiding cutbacks.

- **The long timeframe of the extraction or production cycle**: Sound management of the sector requires planning the national resource extraction portfolio over the long-term. This may be a core challenge facing new producers (e.g. Lao PDR).

- **Ownership structures in the resource sectors**: Ownership in the sector is often highly concentrated, partly because mining is typically associated with very high upfront investments (ibid).

Understanding rent distribution

Empirical research has demonstrated that natural resource rents (the siphoning of resources by individuals) alters the behaviour of political elites (Mildner & Lauster, 2011). Specifically, it increases the value of being in power, creating strong incentives to spend more on power-preserving activities (ibid). The World Bank acknowledges the importance of using PEA to understand this dynamic: specifically, how elites use their discretionary control over public resources to increase their chances of maintaining power or being re-elected (Fritz, forthcoming). In resource-rich countries, the electoral cycle may play an important role in the nature and timing of mining contracts with major investors, as recently demonstrated in the case of Mongolia (Fritz, forthcoming: 5).

Assessing the feasibility of reform

PEA sometimes aims to explore why technical fixes, such as regulations, guidelines and manuals, in practice often do not in practice produce the intended effects (Cabello, 2011). Although the literature is limited, much of it concurs that PEA can assist in identifying ‘best fit’ as opposed to best practice reforms,
meaning reforms that are adequately adapted to an appreciation of context (Tilitonse, 2013; Cabello, 2011: Barma et al., 2012). For example, Tilitonse (2013: 3) argues PEA in mining has the potential to 'inject greater realism into practice' by promoting a more open discussion of the forms of power, politics, corruption and incentives that enable or constrain reform in the sector. Others have similarly argued that the success of development initiatives in resource-rich environments depends on the degree to which donors can 'find mechanisms to work within the constraints of, resonate with, and eventually transform, the underlying political and institutional dynamics associated with resource dependence' (Cabello, 2011).

3. Examples of PEA applied to mining programmes

Responding to a mining boom in Mongolia


This PEA, commissioned by the World Bank, aimed to enable the Bank's country team to adapt their programming in the face of an imminent mining sector boom in Mongolia. It was prompted both by a general concern about the profits of mining booms being widely wasted in developing countries, and also by immediate concerns about certain policy choices and trends, volatility in decision making, and unregulated licensing practices in the Mongolian context. The methodology entailed analysing fiscal and commodity price dynamics, historical legacies of reform, electoral dynamics and resulting political incentives, and process tracing of key policy decisions.

The study analysed the incentives and challenges facing the country’s elites in responding to the resource boom, including how they were likely to react to public and political pressure to spend and distribute mining revenues. It also sought to identify how newly accrued resources were being spent, and why certain public investments (for example, a new social transfer system) were being chosen. The context consisted of weak institutions that were unable to ensure accountability and transparency, patronage networks, lack of regulation of potential conflicts of interest in the public sector, concerns over protecting sovereignty and the national interest, and limited awareness of the costs and benefits of policy options for managing a mineral-based economy.

Although the challenges of the resource boom remained substantial, the study reportedly had three significant practical impacts on country programming: First, it helped the World Bank country team to seize a window of opportunity (during the financial crisis of 2008-2009) to promote the adoption of legal constraints on fiscal management. Second, it contributed to a mining sector specialist being based in the country office (the first time the Bank had ever done so anywhere) who could help analyse key trends and stakeholder interests on an ongoing basis. Finally, it laid the foundation for greater engagement with nongovernmental stakeholders, and in particular the development of a local think tank dedicated to policy engagement and monitoring procurement in the sector.

Overall, the study is considered to have encouraged the Bank to shift from a first-best approach to a more feasible set of interventions. Moreover, it reportedly ‘contributed crucially to ensuring that the World Bank’s engagement is relevant and significant for counterparts and stakeholders and that it is a knowledgeable and strategic partner for country stakeholders rather than just a technically competent external source of advice’ (ibid: 62).
Identifying opportunities and constraints to reform in Burkina Faso  


This PEA, undertaken for the World Bank by Oxford Policy Management (OPM), sought to analyse the prevailing institutions or ‘rules of the game’ operating in the mining sector in Burkina Faso (Cabello, 2011). It was commissioned to inform the design of a mineral support project, and specifically aimed to understand how different groups of stakeholders would likely position themselves with respect to different reform initiatives. The aim was to highlight the obstacles and risks that could be encountered by the Bank when pursuing reform.

The methodology entailed a stakeholder analysis – a mapping of key actors’ motivations and their relationships, both to each other and to the project. This included the ruling party and elite networks, the bureaucracy, Parliament, the military, civil society and the media. Each stakeholder was given an assessment rating based on a) their propensity to promote reform and b) their relative capacity to either promote or thwart reform. The researchers also conducted an institutional analysis, which assessed the framework of both formal (laws, regulations, institutional mandates) and informal institutions (social norms, de facto practices). The emphasis was on how these shape the behaviour, interactions, incentives and power of the stakeholders. A number of areas of mining activity were identified as being of particular concern, including:

- **Access to resources**: Competition for licences was creating space for rent-seeking.
- **Monitoring of operations**: Monitoring of the environmental and social performance of mines was virtually non-existent.
- **Collection of taxes and royalties**: The analysis uncovered conflicts between different government ministries on whether mining taxes should be set to maximise public revenue or attract investment were evident.

The PEA identified a number of potential ways in which space for progressive reform might open up. These included the population’s frustration with the lack of development, the potential entry of major companies, and the professionalisation of employees of the mining company (Burkinabe). It also made a number of specific suggestions for reform aimed at enhancing the contribution of the mining sector to development, mainly aimed at increasing the inclusiveness of the policy making and implementation process (ibid).

Understanding the impact of mining on development in Ghana  


This PEA, commissioned by the World Bank, examined why Ghana has failed to translate its mineral wealth into economic development (Ayee et al., 2011). To this end, the researchers analysed the institutions and political incentives underlying the value chain of extraction, taxation and spending of resource wealth. The methodology involved literature review and interviews with representatives of public institutions, politicians, civil society groups, the private sector, and academics.

The analysis found that an excessively centralised policy-making process, a powerful executive, strong party loyalty, a system of political patronage, lack of transparency, and weak institutional capacity at the political and regulatory levels were all contributing to the problems identified in the sector. Furthermore,
a weak system of checks and balances, poor institutional recordkeeping and access to information, power imbalance between the government, mining companies, and communities, and an investor-friendly regime created vested interests and increased the risk of corruption.

In response to the prevailing political economy conditions, the report recommended that the checks and balances provided for in the constitution be reinforced. The analysis also identified a number of opportunities for addressing the various incentive problems in the sector. These included the recent election of a new political party, the willingness of some mining companies to renew the terms of their investment agreements, and the prospects of dialogue being created by national coalition groups (ibid).

**Identifying mining projects to fund in Malawi**


This PEA commissioned by a multi-donor pooled fund, Tilitonse\(^5\), helped identify which types of projects should be funded under an open call for project proposals (Tilitonse, 2013). The methodology involved interviews in two districts, with government, international NGOs, donors, civil society organisations and mining companies. The analytical framework focused on identifying the key stakeholders, and the degree to which they might be potential winners and losers in any reform of institutions or governance arrangements.

The analysis identified the following problems related to the political economy environment: (a) weak and outdated legislative, policy and institutional frameworks; (b) weak and fragmented role of civil society organisations; (c) lack of a framework for stakeholder engagement at community level; and (d) absence of robust revenue management and transparency mechanisms. At the local level, it identified the issue that massive tracts of land were being alienated from communities in order to accommodate mining, and also highlighted how women’s voices were often stifled in the context of patriarchal norms.

The report set out a number of potential programmatic areas for intervention, including measures for improving transparency and accountability in revenue collection and management, and for setting up a framework for stakeholder engagement at community level. For each of these, it identified key stakeholders who could form an informal coalition in support of the reform, as well as those that might stand in opposition to it (ibid).

**Analysing environmental assessment and approval processes (EAAPs)**


The international mining for Development Centre (IM4DC) has recently developed a methodology for analysing the political and institutional factors that influence environmental assessment and approval processes (EAAPs) for mining projects (IM4DC, 2013). A case study in Peru found that poor proponent-community relations, a weak regulatory framework, and an absence of civil society trust hindered constructive dialogue. The aim of the analysis was to devise better ways to take account of, and respond to these factors. It proposed a number of solutions including an early start to dialogue with local communities and civil society?, end encouraging the involvement of elected decision-makers in that dialogue.

\(^5\) See: http://tilitonsefund.org/
4. Tools and guidance

General approaches

Methodologies for conducting PEA can variably include household surveys (to ascertain citizen’s perceptions), the use of process tracing to track how policy decisions were arrived at, interviews with key stakeholders, historical analysis of trajectories of reform in a particular sector and/or the history of state-society relations in general, statistical analysis of budget allocations, and analysis of electoral outcomes (Fritz, forthcoming). Several development agencies have designed their own approaches to PEA, though according to researchers at The Policy Practice (Duncan and Williams, 2010), most of these approaches have the following features in common:

- **Emphasising the centrality of politics**: Examining how political power is secured, exercised and contested.
- **Downplaying the normative**: Understanding country realities and seeking to ground development strategies in these.
- **Identifying underlying factors that shape the political process**: Understanding current realities in the context of a country’s history, society and geography.
- **Focusing on institutions**: Institutions are seen to determine the incentives that govern patterns of behaviour.
- **Recognising that development agencies are political actors**: Development agencies are explicitly analysed as having their own geostrategic, commercial and developmental objectives.

General guidance is provided in a comprehensive sourcebook of tools for institutional, political and social analysis of policy reform published by the World Bank in 2007 (see Holland, 2007). This gives detailed narrative on methods for analysing meso-, macro- and micro-level institutions.

More recently, EC DEVCO have published their own guidance on conducting PEA, including a discussion of the practical aspects of timing, resource requirements, sources and advice on managing the process (EC DEVO, 2011). Their approach to PEA focuses on understanding collective action, state-society bargaining, institutions, elite incentives, and the role of leadership.

Value chain analysis

Writing for the World Bank, Barma et al. (2012) set out an analytical framework for assessing how a country’s political economy and institutional environment affects its likelihood of translating natural resource wealth into development outcomes. Applying a ‘value chain approach’, this analysis traces the political and institutional arrangements across five key dimensions of the natural resource management (NRM) value chain:

1. Sector organisation and the award of contracts and licenses
2. Regulation and monitoring of operations

---

6 These include: DFID’s Drivers of Change studies; the Netherland’s Power and Change Analysis (part of the Strategic Governance and Corruption Analysis); SIDA’s power analysis; and the World Bank’s problem focussed analysis. For a fuller description, see: http://www.gsdrc.org/go/topic-guides/political-economy-analysis/tools-for-political-economy-analysis
3. Collection of taxes and royalties
4. Revenue distribution and public investment management
5. Implementation of sustainable development policies

The aim of the above analysis is to articulate ‘good-fit’ (i.e. feasible in the given context), sustainable interventions. The approach has been applied in several country cases, including the following in the Asia Pacific: Lao People’s Democratic Republic, Mongolia, and Timor-Leste (ibid).

Typologies of reform-readiness

Applying Barma et al.’s (2012) typology, analysing whether government can make credible inter-temporal commitments and whether the political regime is inclusive can help development agencies identify good-fit interventions that are likely to be ‘incentive-compatible’, and therefore effective. Based on the findings of the analysis, interventions may be targeted towards three main areas:

- **Extend time horizons**: for example by granting concessions that minimise investor uncertainty and enhance predictability.
- **Facilitate stakeholder cooperation**: for example by easing information asymmetries by using model contracts or by disclosing contract terms to enable third-party oversight.
- **Enclave institutions and capacity in the sector**: so that it is able to function even when the wider political economy dynamics are not conducive to developmental outcomes.

Problem-driven approaches

The World Bank’s problem-driven approach to PEA focuses on identifying intractable problems that have been resistant to technical solutions, and in so doing aims to produce specific, actionable findings on how to address the problem (See: Fritz et al., 2009). Researchers work through three stages of the analysis:

- **Step 1: Identify a specific challenge**. This could be narrowly conceived as a problem in a particular sector function (e.g. teacher absenteeism), or absence of progressive reform in a sector as a whole.
- **Step 2: Analyse the specific political economy drivers of the problem**. These include structural factors influencing stakeholder positions (e.g. geography, resource endowment, demographics), existing institutions (formal and informal) and ongoing processes of institutional change and stakeholder interests.
- **Step 3: Identify ways to initiate change**. This must be clear about the risks and potential unintended consequences associated with different entry points. Response can either entail accepting institutions and incentives and carving out feasible reform paths within those constraints, or trying to alter existing relationships between stakeholders to create new space for reform.
5. References


Duncan, A., & Williams, G. (2010). Making development assistance more effective by using political economy analysis: what has been done and what have we learned? London: The Policy Practice.


Expert contributors
Shilpa Banerji, World Bank
Naazneen H. Barma, Naval Postgraduate School
Aoife Mccullough, The IDL Group
Rachel Ort, World Bank
Vlado Vivoda, Griffith Asia Institute

Suggested citation

About this report
This report is based on three days of desk-based research. It was prepared for the Australian Government, © Australian Government 2013. The views expressed in this report are those of the author, and do not necessarily reflect the opinions of GSDRC, its partner agencies or the Australian Government.

The GSDRC Research Helpdesk provides rapid syntheses of key literature and of expert thinking in response to specific questions on governance, social development, humanitarian and conflict issues. Its concise reports draw on a selection of the best recent literature available and on input from international experts. Each GSDRC Helpdesk Research Report is peer-reviewed by a member of the GSDRC team. Search over 300 reports at www.gsdrc.org/go/research-helpdesk. Contact: helpdesk@gsdrc.org.