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NATURAL RESOURCE WATCH

REPORT ON:

SUB-SAHARAN AFRICA

JULY 2015

INTRODUCTION

Many developing countries are endowed with abundant natural resources, such as oil, gas and minerals. While extraction of these non-renewable resources presents an opportunity for rapid economic growth and poverty reduction, few countries have actually managed to convert the endowment of natural resources into sustained and inclusive growth.

The Natural Resource Watch series examines the policy and economic trends of the extractive sectors in a number of natural resource-rich developing countries. The purpose is to make data from the extractive sector more accessible and understandable for all citizens, which is a precondition for an open dialogue on how the extraction of natural resources can lead to a path of equitable development. This volume sheds lights on the Sub-Saharan African region.

SUB-SAHARAN AFRICA – OVERVIEW

Sub-Saharan Africa's economy has grown significantly in the last decade, in spite of the global financial crisis, and is expected to continue to do so in years to come[1]. Nevertheless, it remains the world's least developed region[2], where more than 400 million people live in extreme poverty[3].

The economic growth in many Sub-Saharan African countries has to a large extent been driven by the extraction and export of non-renewable natural resources[4]. This sector continues to create huge value, and is likely do so in the years ahead, as massive deposits of exploitable natural resources remain underground, most of them still undiscovered[5]. According to recent estimates, Sub-Saharan Africa contains 30% of the world's minerals[6], and more than 20% of the world's undiscovered crude oil – which is more than the Middle East and North Africa put together[7].

Sub-Saharan Africa's wealth of non-renewable natural resources could contribute to poverty alleviation and socially inclusive growth. However, avoiding the so-called 'resource curse' will require strong policies, transparency, good governance and an active civil society.

SUB-SAHARAN AFRICA AT A GLANCE

TOTAL VALUE OF NATURAL RESOURCE EXPORTS IN 2012

US$ 300 BILLION

EXPORTS OF NATURAL RESOURCES AS A SHARE OF TOTAL EXPORTS FROM SUB-SAHARAN AFRICA

2002: 56%

2012: 75%

NATURAL RESOURCE RENTS AS % OF TOTAL SUB-SAHARAN AFRICA GDP FROM 2005 TO 2012:

20.4 %

Source:
World Bank World Development Indicators, and World Bank 2015: "Africa's Pulse" vol. 8 and 11.

Note:
According to the World Bank definition, natural resource rents are the difference between production costs and world market price of a commodity.

WHICH COUNTRIES EXPORT NATURAL RESOURCES?

Today, 28 countries in Sub-Saharan Africa can be classified as resource-rich (see map on page 8), which means that more than 25% of their exports are made up of non-renewable natural resources such as minerals, oil and gas[8]. The number of resource-rich countries has increased from 20 in 2010[9], and will probably rise further in the future, due to much of the underground is still to be explored.

1 MAIN EXPORTS FROM RESOURCE-RICH COUNTRIES IN SUB-SAHARAN AFRICA

- ANGOLA
- BOTSWANA
- BURKINA FASO
- CAMEROON
- CENTRAL AFRICAN REPUBLIC
- CHAD
- CONGO, DR (COBALT, COPPER)
- CONGO, R
- EQUATORIAL GUINEA
- GABON
- GHANA
- GUINEA (BAUXITE)
- IVORY COAST
- LIBERIA
- MADAGASCAR (TITANIUM)
- MALI
- MAURITANIA
- MOZAMBIQUE (ALUMINIUM)
- NAMIBIA (VARIOUS METALS AND MINERALS)
- NIGER (URANIUM)
- NIGERIA
- SIERRA LEONE
- SOUTH SUDAN
- SOUTH AFRICA
- SUDAN
- TANZANIA
- ZAMBIA (COBALT, COPPER)
- ZIMBABWE

Sources: EITI, World Bank, IMF, UN Comtrade. Data from 2013 or 2012.

GOVERNMENT REVENUE FROM THE EXTRACTIVE INDUSTRIES

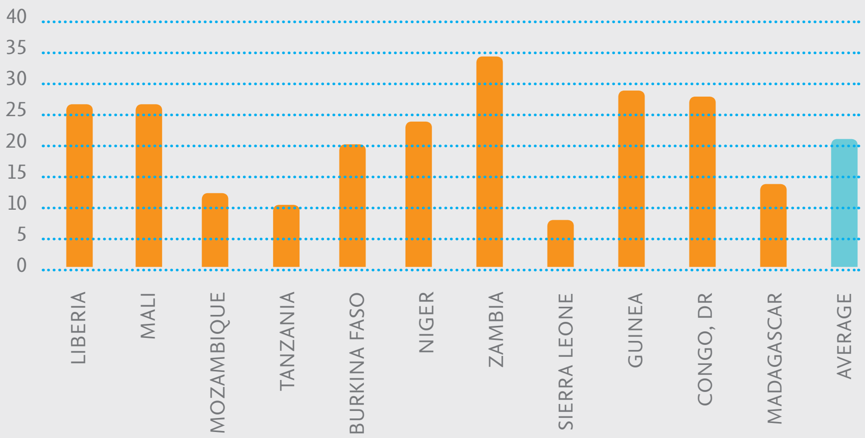
It is difficult to find good and reliable data on how much revenue governments in Sub-Saharan Africa obtain from natural resources[10], although better data on oil, gas and minerals are being delivered by countries compliant with the Extractive Industries Transparency Initiative (EITI). Keeping this in mind, close examination of the data available does reveal some overall trends.

First of all, oil-exporting countries are in a different league from countries exporting minerals and metals. Oil is the single most important commodity exported from Sub-Saharan Africa[11], and governments usually derive much higher revenues from export of oil than for other minerals[12]. Even for countries exporting small amounts of oil, revenues can be significant. Niger only exports around 20,000 barrels of crude oil per day, but this translated into government revenues of US$ 164 million in 2012[13], which is more than government spending on healthcare[14].

By using data from the EITI, it is possible to assess the amount of revenues paid to governments by companies in the extractive industries. These transfers include both recurring payments (e.g. corporate taxes and royalties) and one-off payments (e.g. sign-on bonuses), but reporting methodology vary from country to country, which makes direct comparisons and aggregate data less precise.

With this in mind, graph 2 shows that payments made by companies in eleven EITI-compliant mineral-exporting countries in Sub-Saharan Africa corresponded to around 20% of total government revenue in these countries. However, there is significant variation in the group of countries. While payments in Zambia corresponded to more than 30% of government revenue, the figure for Sierra Leone was less than 10%. The government take depends on countries' ability to establish efficient taxation regimes, but also on other factors, such as the maturity of the mining industry.

2 PAYMENTS FROM THE MINING SECTOR AS % OF GOVERNMENT REVENUE



Sources: EITI, World Bank World Development Indicators. Data from 2012 or 2011.

NIGERIA

– THE BIGGEST OIL EXPORTER IN SUB-SAHARAN AFRICA

PRODUCTION PER DAY IN 2011:

2.2 MILLION BARRELS

GOVERNMENT OIL REVENUE IN 2011:

US$ 50 BILLION
- 70% OF TOTAL GOVERNMENT REVENUE

SOUTH SUDAN

– THE MOST OIL-DEPENDENT COUNTRY IN THE WORLD

PRODUCTION PER DAY IN 2011:

500.000 BARRELS

GOVERNMENT OIL REVENUE IN 2011:

US$ 3.39 BILLION
– 98%

OF TOTAL GOVERNMENT REVENUE

Sources: Natural Resource Governance Institute and IMF 2014: Article IV report for South Sudan

NATURAL RESOURCE PRICE FLUCTUATIONS

A central issue when looking at government revenues from extractive industries is the volatile world market prices of non-renewable natural resources. As shown in graph 3, commodity prices reached astounding heights in recent years, but have dropped significantly since June 2014. The boom-bust cycles and the unpredictability of commodity prices can have serious consequences for governments reliant on income from natural resources, as revenues lower than expected can create large financing gaps in government budgets.

COMMODITY PRICE DROPS FROM JUNE 2014 TO APRIL 2015

OIL: 54 %

IRON ORE: 70 %

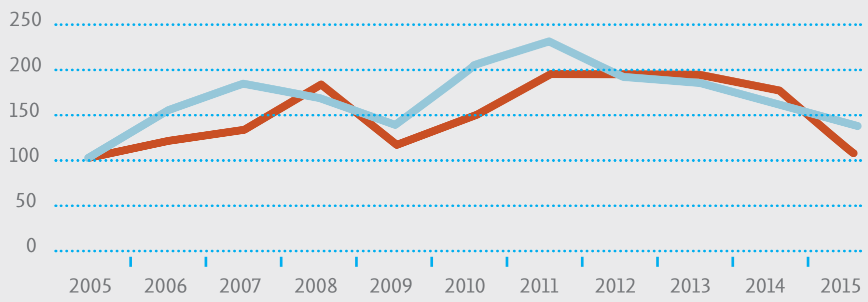
COPPER: 40 %

COAL: 54 %

Source: Columbia Center for Sustainable Investment 2015: "Resource resilience: How to break the commodities cycle" and World Bank 2015: Africa's Pulse vol. 11

3 INDEX OF AVERAGE WORLD MARKET PRICE OF METALS AND ENERGY FROM 2005 TO 2015

2005 = 100



METALS (COPPER, ALUMINUM, IRON ORE, TIN, NICKEL, ZINC, LEAD AND URANIUM)

ENERGY (OIL, GAS AND COAL)

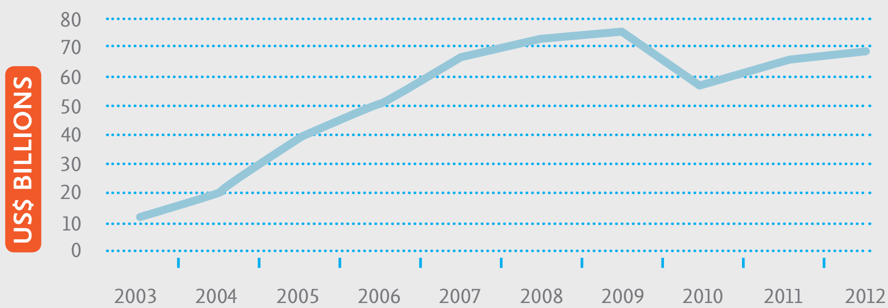
Source: IMF monthly primary commodity price indices

ILLICIT FINANCIAL FLOWS FROM THE EXTRACTIVE INDUSTRIES

Extraction of natural resources is often isolated from the rest of the economy in resource-rich countries. As a result, tax becomes the main contribution from extractive industries to social development[15]. This is why massive illicit financial flows from Sub-Saharan Africa pose a huge challenge, which often is, in economic terms, more severe than corruption[16], and undermines the potential benefits of natural resource extraction.

According to Global Financial Integrity, illicit financial flows from Sub-Saharan Africa amounted to more than US$ 500 billion in the last decade[17]. Relative to the size of the regional economy, this makes Sub-Saharan Africa the region in the world that suffers most from illicit financial flows[18].

4 ILLICIT FINANCIAL FLOWS FROM SUB-SAHARAN AFRICA



Source: Global Financial Integrity 2014

More than half of the illicit financial flows are estimated to derive from trade in oil, precious metals and minerals, iron ore, steel, and copper[19]. Companies within the extractive industries often use complex company structures, including establishing company subsidiaries in tax havens[20]. This enables companies to transfer part of their profits from a given resource-rich country to a tax haven, where they pay little or no taxes.

A common way of using complex company structures for tax dodging is trade mispricing, whereby companies deliberately overstate the price of imports and/or understate the price of exports between subsidiaries of the same company, in order to avoid paying taxes in the countries where they operate[21]. In South Africa, such practices in the extractive industries cost US$ 359 million in lost tax revenue in 2012[22], and for all of Africa, lost tax revenue due to trade mispricing (in all sectors) amounted to approximately US$ 11 billion in 2010[23].

A concrete example of trade mispricing in the extractive industries is the case of the Mopani copper mine in Zambia, owned by the English mining giant Glencore. In 2010, an audit revealed that one of Glencore's subsidiaries, which operated the mine in Zambia, had sold extracted copper to a subsidiary in Switzerland (a known tax haven) at artificially low prices. Combined with an overstatement of the costs of operating the mine, the result was that the subsidiary in Zambia was left without any profit, and thus without any corporate tax obligations in Zambia[24].

AVERAGE ANNUAL TAX LOSSES FROM TRADE MISPRICING, FROM 2002 TO 2011

GHANA:
US$ 386 MILLION

MOZAMBIQUE:
US$ 187 MILLION

KENYA:
US$ 435 MILLION

TANZANIA:
US$ 248 MILLION

UGANDA:
US$ 243 MILLION

Source: Global Financial Integrity 2014: "Hiding in plain sight"

TAX INCENTIVES: A RACE TO THE BOTTOM

In order to attract investments in the extractive industries, many governments grant private companies additional tax incentives. These can take multiple forms, such as lower corporate income tax rate, tax holidays, and exemptions from customs duties and value-added tax. The net result of granting these tax incentives is often substantial lost government revenue, and further potential for corruptive behaviour. The 'Give us a Break' report by ActionAid International estimates that Sub-Saharan African governments lose around US$ 7.6 billion each year from lower corporate income tax rates alone (in all sectors)[25]. Optimizing taxation of the extractive industries is not straightforward[26], but there is compelling evidence that these are especially undertaxed[27].

Several reports from civil society, IMF and the World Bank have also demonstrated that tax incentives can work against the economic interests of the government granting them[28]. Tax incentives may not even be such an important factor in the investment decisions of private companies. Rather, they tend to value other factors, such as political and economic stability, good governance, an educated workforce and well-functioning infrastructure (electricity, transports and communications) – all of which require tax revenues to be financed in a stable and sustainable manner[29].

LOST REVENUE FROM TAX INCENTIVES IN THE EXTRACTIVE INDUSTRIES

SIERRA LEONE (2012):
US$ 224 MILLION

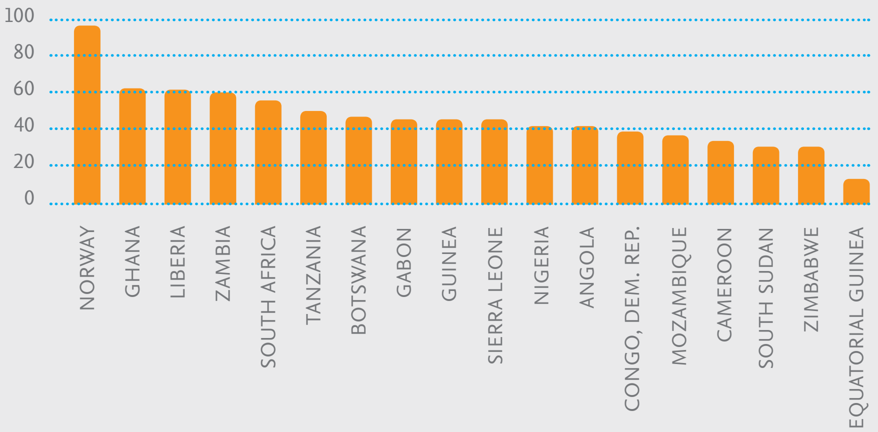
MALAWI (2008-2012):
US$ 300 MILLION

Source: Budget Advocacy Network 2014: Losing out and ActionAid 2013: Give us a break

LOW LEVELS OF TRANSPARENCY

Most resource-rich countries in Sub-Saharan Africa have low levels of transparency in their management of public revenues[30], and particularly when it comes to tax revenues from natural resources[31]. Graph 5 shows the score of 17 selected resource-rich countries in Sub-Saharan Africa from the 2013 Resource Governance Index; and includes Norway, the highest-ranking country in the worldwide index, for the purpose of comparison. The graph illustrates that some countries in Sub-Saharan Africa, such as Ghana, Zambia, Liberia and South Africa, perform moderately well by receiving a score above 50, whereas most other countries receive scores below 50, which indicate weak or failing management of natural resource revenues.

5 SELECTED RESOURCE-RICH COUNTRIES' SCORES ON THE RESOURCE GOVERNANCE INDEX



RECOMMENDATIONS

GOVERNMENTS OF RESOURCE-RICH COUNTRIES IN SUB-SAHARAN AFRICA SHOULD:

- **Develop robust tax policies and avoid granting tax incentives.** Tax exemptions cost resource-rich countries billions in lost revenues every year. Rather than granting tax incentives to attract investment, countries should focus on building an attractive long-term investment climate and robust fiscal regime.

- **Promote a new global tax system.** This is crucial to reduce illicit financial flows and tax dodging by multinational corporations. Establishing a new intergovernmental tax body with all countries around the table should be complemented with an international action plan to combat abusive tax planning, including a strong focus on extractive industries and opaque company structures.

- **Strengthen transparent and accountable management of resources and contracts.** All resource-rich countries in Sub-Saharan Africa should become EITI compliant, which, in combination with other regional and global standards and regulations, can strengthen transparency in extractive industries. Transparency is not an end in its own right, but is crucial to hold companies and governments accountable.

- **Focus more on redistribution and spending of revenues from extractives industries.** Generating sustained and pro-poor development in resource-rich countries is not only about collecting fair tax revenues from natural resources, but also about spending efficiently for the intended development purposes, and redistributing fairly to fight poverty and inequality.

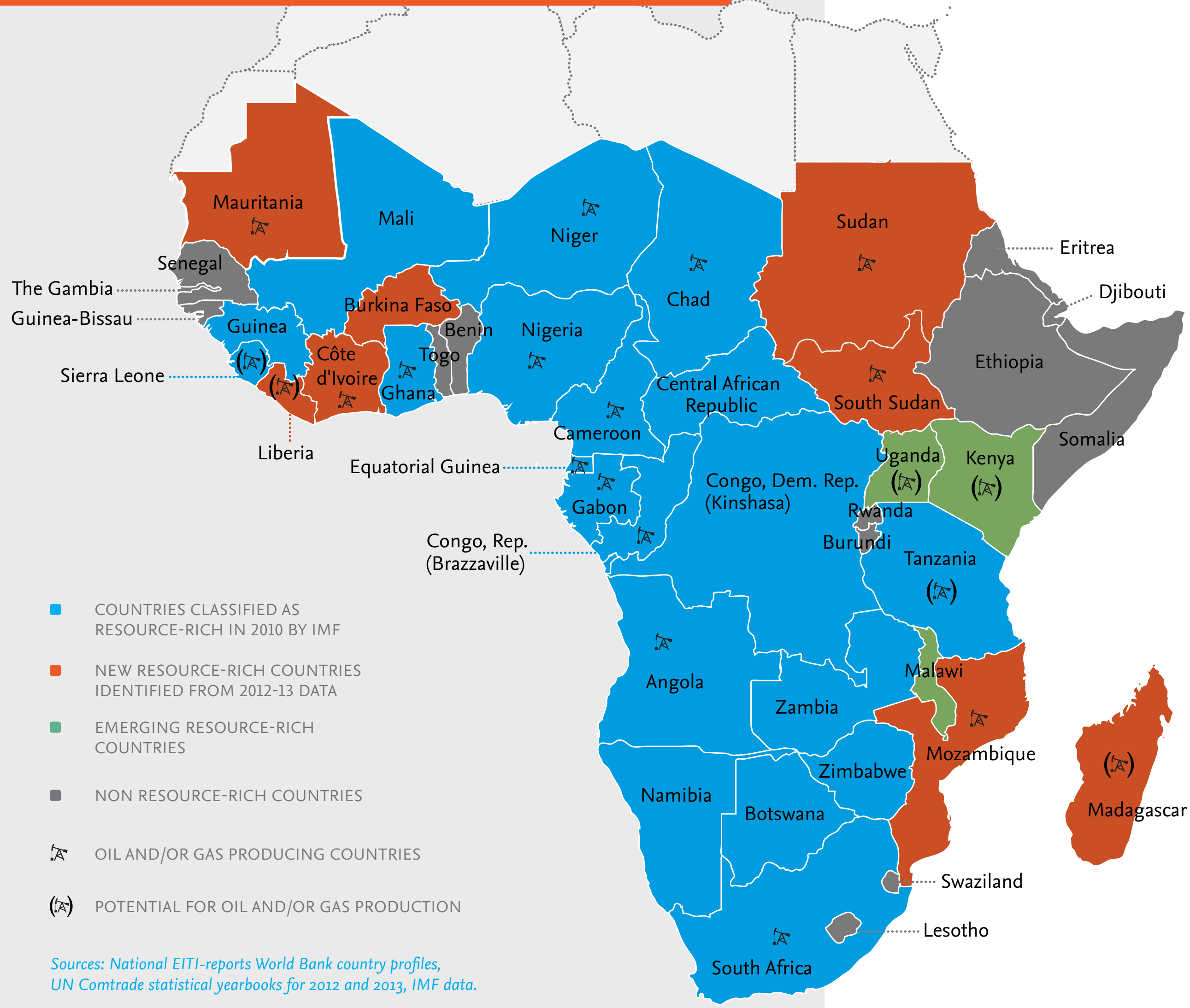
- **Install frameworks to mitigate fluctuating revenue streams resulting from natural resource boom-bust cycles.** Sovereign wealth funds can alleviate some of the adverse impacts of commodity price fluctuations by stabilising government expenditures and saving for future generations. It is important that such funds have clear objectives, are managed within a solid fiscal framework, and are subject to public audits and oversight.

- **Integrate extractive industries into long term development planning at the national and local level.** Resource-rich countries need to diversify their economies to be less dependent on the export of natural resources, and to promote, and to promote backward/forward linkages from extractives industries to the national and local private sector.

ENDNOTES

1 World Bank 2015: “Global Economic prospects” p 106
2 United Nations Development Programme: Human Development Report 2014
3 World Bank: http://povertydata.worldbank.org/poverty/region/SSA
4 World Bank 2015: “Africa’s Pulse” vol. 11, p 18
5 IMF 2013: “Boom, bust or prosperity? Managing Sub-Saharan Africa’s natural resource wealth” p. 7
6 Africa Progress Panel 2013: “Equity in extractives” p 44
7 United States Geological Survey 2012: “An estimate of undiscovered conventional oil and gas reserves of the world” p 3
8 Which is the IMF definition of a resource-rich country – see IMF 2013: “Boom, bust or prosperity? Managing Sub-Saharan Africa’s natural resource wealth”
9 IMF 2013: “Boom, bust or prosperity? Managing Sub-Saharan Africa’s natural resource wealth”
10 IMF 2014: http://www.imf.org/external/np/sec/pr/2014/pr1454.htm
11 World Bank 2015: Africa’s Pulse vol. 11, p 26
12 Ross, Michael 2012: ”The Oil Curse”
13 Reuters Africa and Sahel Blog: https://sahelblog.wordpress.com/2011/12/06/nigers-oil-boom/ http://af.reuters.com/article/investingNews/idAFJOE7B404B20111205?feedType=RSS&feedName=investingNews
14 World Bank: World Development Indicators
15 Africa Progress Panel 2013: “Equity in extractives” p 63
16 Oxfam International 2015: “Africa: Rising for the few”
17 Global Financial Integrity 2014: “Illicit Financial Flows from Developing Countries 2003-2012” p vii
18 Global Financial Integrity 2014: “Illicit Financial Flows from Developing Countries 2003-2012” p 11
19 High Level Panel on Illicit Financial Flows from Africa 2014: “Track it! Stop it! Get it!” p 97
20 Tax Justice Network-Africa and Christian Aid 2014: “Africa Rising” p 52. For tangible examples, see i.e. Danwatch 2011: “Not sharing the loot” and CIP & Eurodad 2013: “Mining without Development”
21 Africa Progress Panel 2013: “Equity in extractives” p 49
22 Oxfam International 2015: “Africa: Rising for the few” p 5
23 Oxfam International 2015: “Africa: Rising for the few”
24 http://www.actionaid.org.uk/tax-justice/glencore-tax-dodging-in-zambia
25 ActionAid international 2013: “Give us a break”
26 IMF 2010: “The taxation of petroleum and minerals: principles, problems and practice” p 104
27 Africa Progress Panel 2013: “Equity in extractives” p 63
28 See for example World Bank 2013: “How to improve mining tax administration and collection frameworks – a sourcebook”; IMF 2014: “Administering fiscal regimes for extractive industries – a handbook” and ActionAid 2013: “Give us a break: how big companies are getting tax-free deals”
29 Oxfam 2014: “Business among friends” p 9
30 Transparency International 2014: ”Sub-Saharan Africa: Corruption still hurts daily lives”.
31 Revenue Watch Institute 2013: Resource Governance Index for Sub Saharan Africa

MAP OF RESOURCE-RICH COUNTRIES IN SUB-SAHARAN AFRICA



Sources: National EITI-reports World Bank country profiles, UN Comtrade statistical yearbooks for 2012 and 2013, IMF data.

ABOUT IBIS AND THE AFRICA AGAINST POVERTY (AAP) PROGRAMME

IBIS is a Danish member-based development organisation working at the global, national and local levels to create equal access to education, influence and resources for poor and marginalised peoples in Africa and Latin America.

Africa Against Poverty (AAP) is a regional advocacy programme focusing on extractive industries, taxation and other emerging development challenges in Sub-Saharan Africa.

NATURAL RESOURCE WATCH

THIS REPORT HAS BEEN WRITTEN BY:
NIKOLAJ THORBORG AND MORTEN BLOMQVIST

FOTO:
WILLIAM VEST-LILLESØE

DESIGN:
SARA H. MORTENSEN // EGGS LIBRIS

IBIS
VESTERBROGADE 2B
1620 COPENHAGEN V

IBIS@IBIS.DK
WWW.IBIS-GLOBAL.ORG
WWW.IBIS.DK

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Education for development