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# The peril and promise of resource nationalism: A case analysis of Mongolia's mining development

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ABSTRACT

Resource nationalism is often cited as the most serious risk to foreign mining investment in developing countries. Mongolia provides an important case study of studying this phenomenon and its impacts, especially during the global mining boom years from the late 1990s to 2010. This phenomenon has been exposed mainly through the ever increasing role of state ownership in major mineral deposits, mostly by direct equity participation. The rationale behind these nationalist policies is to maximize the economic and political benefits from extractive industries. However, in reality, the Mongolian government lacks financial and human resources as well as practical knowledge to engage directly in mega projects which pose substantial risks, if carried out improperly. The aim of this paper is to examine the underlying nature of the state-centric resource development model in Mongolia. Using an institutionalist approach, the study provides a systematic understanding of the root causes for the growing state involvements in mineral resource development, and its implications for and implementation upon the Mongolian mining sector, including major challenges encountered as a result of the dominant ownership structures shaping the industry.

## 1. Introduction

Extractive industries have often been defined as national assets in legal and social terms whereby they command ascendancy in political discourse on nationalism. Such “resource nationalism” can certainly have many favourable impacts in terms of its potential for wealth distribution across society. Often such nationalism can be manifest in the form of some state-ownership preference for extractive industry projects that can lead to relative success stories, such as diamonds in Botswana and copper in Chile. While such “positive” resource nationalism deserves to be recognized for its potential, it is usually successful when coupled with some level of foreign engagement.

Due to endogenous factors within rapidly urbanizing and industrializing societies, there are also emerging forms of resource nationalism which are largely premised on suspicion of all foreign investment. We term this exclusionary and conspiratorial form as “negative resource nationalism”. Such negative resource nationalism is also a major cause of internal political conflict within countries and can also fuel violent secessionist movement (Bannon and Collier, 2003). Although self-determination of communities based on consensus should be a fundamental right, the argumentation and rationalization of such assertions should be premised on positive forces of national identity and governance efficiency rather than visceral fear of foreigners or suspicion.

No doubt there are many communities in resource rich areas which are often not realizing the full benefits of foreign corporate investment and have legitimate grievances around resource rents not fulfilling their objective. Such dashed expectations are further fuelling a form of xenophobic nationalism in developing and developed countries alike that deserves attention (Bremmer and Johnston, 2009; Stevens, 2008). In this paper we explore both positive and negative forms of resource nationalism and consider how best to modulate their impact in the case of Mongolia, a country that has experienced a massive growth in foreign mining interests over the past two decades.

We seek to address the research question of how resource nationalism could be more effectively configured between public, private,

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local and foreign investment to ensure most economically and socially efficient outcomes in a developing country, particularly with a small population relative to its very large resource endowments. One would hypothesize that smaller, more ethnically homogenous countries, such as Mongolia, would have less regional resource nationalism. However, the rise of resource nationalism in such a country provides an important test case to study the phenomenon at its core level. The Mongolian case thus suggests the urgency of addressing the challenge of effective resource governance in the wake of nationalist impulses, which could lead to even more complex and intractable conflicts in larger more heterogeneous countries.

## 2. Shifting approaches to resource nationalism

The governance structures of mineral industries have been experiencing a dramatic shift over the past two decades due to cyclical price volatility of the mineral commodities (Wilson, 2015). Along with the surging values of minerals and metals in the mid-1970s, resource-rich nations tend to take both regulatory and non-regulatory approaches to intervene in the activities of the mining sector, in order to maximize the social, political, as well as economic benefits that could be generated from the extractive industries. The incentives for taking such arrangements can be explained by several reasons-from narrowly defined political interests to national development requirements. These incentives could also be implemented through different ways, such as increasing resource rent taxes, controlling prices, restricting outputs, deferring and breaching contractual agreements with investors, and even expropriating all privately-owned mines (Auty and Mikesell, 1998; Webb, 2008). As a result of this new wave of state-driven resource sector reforms, "resource nationalism" has emerged as a potent force in determining investment risk.

The fundamental idea of nationalizing mineral resources is established under the assumption that 'laissez-faire' market principles cannot create sufficient benefits for the local economy where mining activities occur and thus states should take rather interventionist actions to receive higher levels of pay-offs (Moran, 1971). This ideology together with individual state's sovereign rights on exercising its mineral endowments within the territory has paved the way of state participation in exploring and exploiting mineral resources, financing and developing mining projects, either directly or through SOEs (Southalan, 2012). In practice however, majority of those enterprises are shaped by common features: lower productivity, lack of accountability, high corruption, and poor governance practice compared to their private counterparts (Perotti, 2004). Hence, there have been massive shifts from the state-centered bureaucratic model to private sector-led development policy during the last 20 years (World Bank, 2011a, 2011b). This is largely due to intensifying competition over the global non-renewable resources supply, and more importantly, the mineral industries' strategic importance to national economic and political stability. As a result, state participation in the mining sector remains relatively high and the ownership model is often dominated by natural resource companies (NRCs) or other government appointed organizations. This is especially the case in developing countries (Ramamurti and Vernon, 1991) where economies are heavily reliant on mining industries.

Regarding the ways of operationalizing resource nationalism, Gilpin (1987) identified two different policy options: either state-based or market-based governance mechanisms that resource countries face for the management of resources in ground. Wilson (2011) defined the ways in which these two types of management systems are employed in natural resource sectors: resource nationalism and resource liberalism. According to him, resource nationalism is a state-driven approach to the management of mineral resources.

Similarly, Joffé et al. (2009, p. 4) describe resource nationalism as "the expression, by states, of their determination to gain the maximum national advantages from the exploitation of national resource". They investigated the cyclical nature of resource nationalism and pointed out the relationship between state and international oil companies, in terms of exploiting crude oil during the boom and bust periods. Stevens (2008) stresses two basic characteristics of resource nationalism: limiting the operations of private firms and demanding greater government control over resource development. The author further argues that resource nationalism is not only a growing concern in developing regions, but it has become a major issue in several resource-rich developed countries such as Canada and Australia, where it may be manifest through domestic private ownership, rather than state-ownership or assets.

Domjan and Stone (2010, p. 38) define resource nationalism as "a wide range of strategies that domestic elites employ in order to increase their control of natural resource". They explain resource nationalism from practical perspectives and assert that it encompasses reasserting state control over natural resources before or after most investment has been sunk in mining project and the full exclusion of foreign participation. Building on this notion, in his research on resource nationalism in Latin American countries, Mares (2010) states that natural resources are a 'national patrimony' and, consequently, should not be used for private gain.

Bridge (2014) refers the term "resource-state nexus" (p. 1) to examine the spatiotemporal characteristics of individual states sovereign right over the governance of common resources such as water, land, and minerals. Conceptualizing that binding nature of the territorial dominances of the state to explore and develop mineral wealth in such a way is particularly important as it shed lights on the fundamental relationship between 'state-resources' from critical geographical perspectives.

Having said that, he further illustrates the constitutive relationship between volume of minerals and state sovereignty taking into account of vertical as well as horizontal dimensions of the resource exploitations (Bridge, 2013). The state being a legitimate owner of the mineral wealth within its territory, it can tend to transfer such tenure rights to private entities through grants and contracts. As a result, the static form of resources where they are considered underground (subsurface both literally and figuratively) must also be coupled with their horizontal nexus in terms of the state being co-opted by various neoliberal clients (Bridge, 2014). Thus human geographers offer an important critique of the conventional linear, and often binary notion, of resource nationalism between public and private spheres that political scientists and international relations scholars have espoused (Childs, 2016).

Bremmer and Johnston, (2009 pp. 150–152) categorize resource nationalism into four distinct types depending on their root causes, impact on mining industries, and on investment in resource industries. They first introduce a so called "revolutionary resource nationalism" and take Russia and Venezuela as an example of this category. The aim of the revolutionary resource nationalism is not only to increase government control over the mineral sector but also to achieve certain political goals. This form is often expressed as public unrest that demands the transfer for natural resources from private owners to public coffers. Secondly, "economic resource nationalism" is a more common variant of resource nationalism and it aims to support economic diversification through receiving larger share of resource revenues from international mining companies. Compared to revolutionary resource nationalism, this type of resource nationalism is separate from a political agenda and is focused more on revenue maximization from its minerals. Kazakhstan has been considered as typical example in this category.

"Legacy resource nationalism" is a third form that is featured in persistent historical episodes where nationalist ideology has attached to the political and cultural identity (Bremmer and Johnston, 2009). Mexico and Nigeria's long-established value on the national oil industry and subsequent changes during the 1938s and 1970s are clear cases.