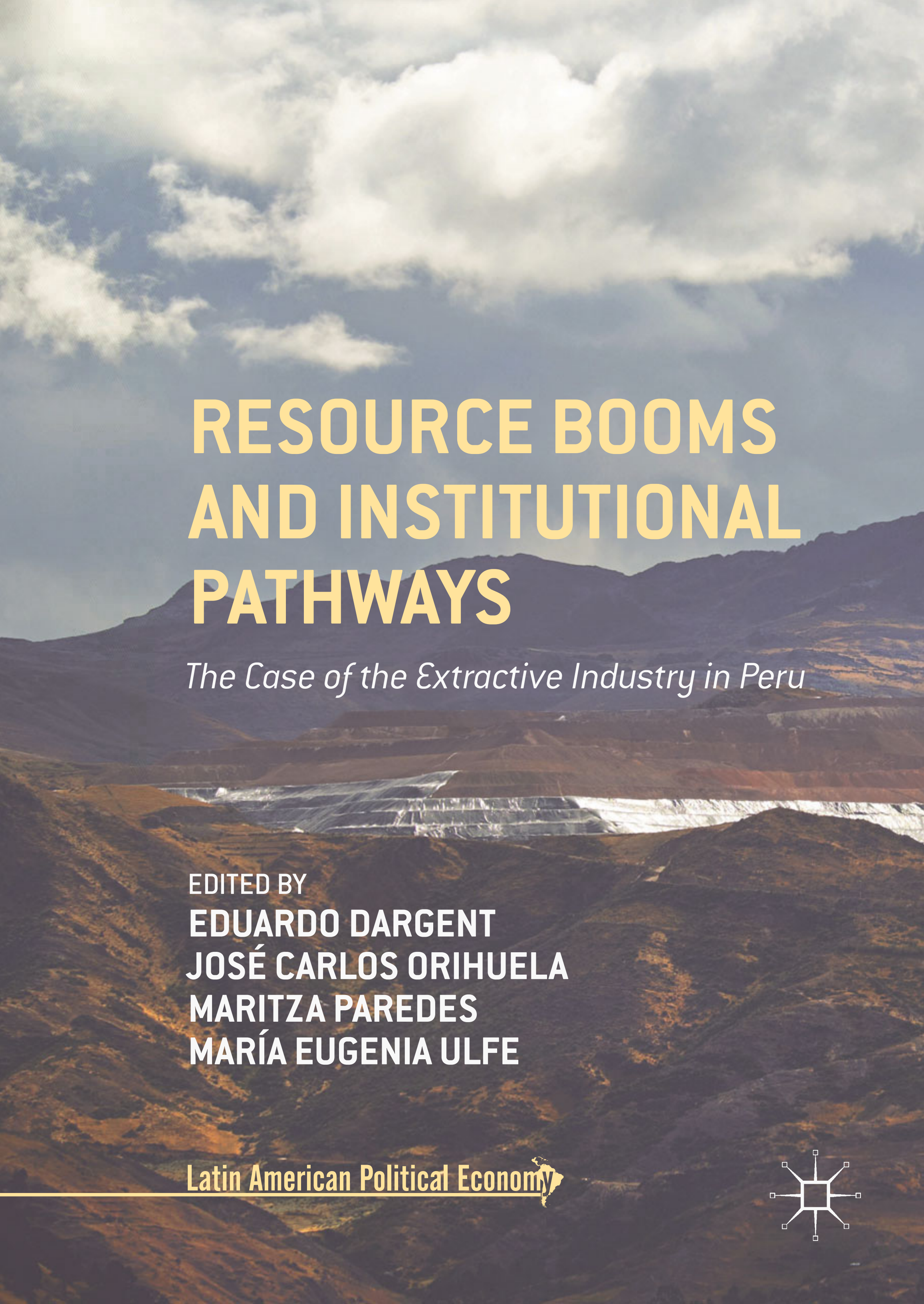

RESOURCE BOOMS AND INSTITUTIONAL PATHWAYS

The Case of the Extractive Industry in Peru

EDITED BY
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Latin American Political Economy

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Maritza Paredes · María Eugenia Ulfe
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CHAPTER 1

Cycle of Abundance and Institutional Pathways

Eduardo Dargent, José Carlos Orihuela, Maritza Paredes and María Eugenia Ulfe

From 2004 onward, Peru has experienced its most recent economic growth cycle based on a natural resources boom and, in particular, on minerals. With a new cycle of growth came a wave of conflict and social unrest that once again put "the paradox of plenty" into the debate (Karl 1997). The effects of natural resource abundance cycles on relationships between state and society have been largely debated in the social sciences.[1] From different disciplines, there is a vast literature that reveals the challenges of societies in constructing institutions for development during resource booms driven by a surge in commodity prices. Existing

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literature has been particularly eloquent about the challenges of growth based on non-renewable natural resources, such as minerals and hydrocarbons. Economic studies have argued that growth is "impoverishing," if not invested in new capital while sociology, political science, and anthropological studies have claimed that growth comes hand in hand with authoritarianism, corruption, and environmental and redistributive conflicts.[2] In this way, the recent rise in the international prices of these commodities revives the debate over institutional challenges that the new resource boom has originated in Latin American countries and beyond.[3] This book explains the unexpected institutional development that Peru has undergone in recent years to manage the benefits and cost of rapid extractive industry expansion due to a commodity boom.

Peru is an emblematic case of the so-called natural resource curse. From the early studies of Auty (1993) and Mahon (1992) that developed the idea of the resource curse in Latin American developing countries, to studies focused on the effects of recent commodity booms (Arellano-Yanguas 2008, 2011a, b; Bebbington et al. 2008), literature has studied the effects of these growth cycles, regarding both the initial formation of the Peruvian state (Paredes 2013) and its subsequent development (Paredes 2016; Orihuela 2014; Arce 2006; Bebbington 2013). Today, Peru is once again a relevant case for the study of resource abundance growth. It has been one of the countries with highest average growth in the region (over

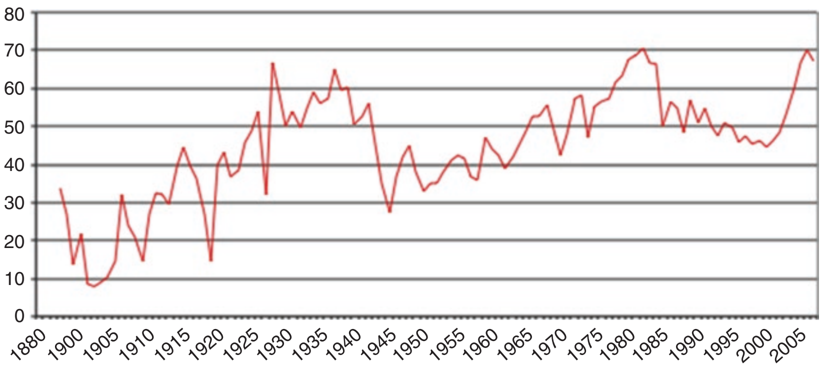

Fig. 1 History of mineral exports in Peru (1890–2010). *Source* Elaboration of Orihuela (2014) based on Thorp and Bertram (1978) and Central Bank of Peru data

Table 1 Type of institutional regimes and cases

Institutional regimes	
Benefits management	*Costs management*
Canon	Environmental regulation
Canon for research in state universities	Conflict management
Local consultations	Local consultations

6% annually), based on the exportation of minerals (gold and copper) and hydrocarbons (mainly gas). However, as Fig. 1 shows, this cycle has not been the only one. Mineral exports have constituted more than 50% of total exports during various moments in Peruvian history. Thus, without tracing back to the nineteenth-century guano era, the study of institutional transformation in Peru concerning this type of growth cannot ignore the legacies of previous cycles. The recent economic cycle and opportunities for state expansion are strongly permeated by previous cycles' legacies.

This book understands institutional development as the evolution of institutional regimes. The latter is broadly defined as the system of formal and informal rules of the game and the institutional organizations that enforce and give support to such rules. Thus, by "institution," we can be referring to either a rule of the game or an organization-shaping political-economic agency (Meyer and Rowan 1991).

The book addresses what we see as the most important state institutional developments associated with the governance of extractive industries. We group institutional change in two broad types: benefits-management and costs-management institutional development. Some institutions have emerged to manage the (distribution of the) benefits of resource extraction, beginning with the canon redistributive scheme (Chap. 2) and the earmarking of a percentage of the canon to finance state universities' investment in research (Chap. 3). In contrast, other institutions have emerged fundamentally to manage the (distribution of the) costs of resource development, such as formal rules of the game and state organizations for environmental regulation (Chap. 4), conflict management (Chap. 5), and formal and informal rules of participation and local consultation (Chap. 6)—thus, participation can also shape the management of benefits, by creating institutions to decide over the canon and non-canon mining transfers (Table 1).

The chapters in this book dialogue with literature about the natural resource curse and with other perspectives that help to explain the paradox of institutional development in the resource abundance context. Overall, the book posses the questions of what has happened with institutional state construction during the recent commodity boom in Peru (2004–2012); how more regulatory and mediation institutions developed in these years in spite of adverse conditions and powerful veto actors; and why some institutional developments occurred rapidly at the cycle's beginning while others took their time, emerging only toward the end. Why were some processes more contested than others? What type of actors has mobilized the activation and implementation of these different institutions? And, what are the challenges left by the commodity boom?

The theoretical framework developed in the fourth section of this introduction aims to answer these questions. As discussed in detail below, we propose that three dimensions explain the institutional development in resource-abundant Peru: (a) preceding power distribution of state and society actors, (b) historical repertoires of state and society action, and (c) the entrepreneurship of actors embedded in transnational networks. Our framework aims to provide a comparative road map for similar analysis in Latin American countries affected by the recent commodity boom.

This introductory chapter is organized into five sections. The first one explains the new cycle of economic development based on natural resources and the main conflicts/tensions that it has produced. The second section describes significant institutional state changes in Peru, which today have a relevant spot in the political scene that they did not have in the 1990s, thanks to the abundance cycle. The third section discusses literature that explain the relevance of resource abundance cycles for institutional state development. The fourth section, the main one of this chapter, presents the arguments developed in conjunction with our findings. The final section describes the book's methodology and organization.

1 Economic Abundance and Social Unrest

The increase in international prices of minerals, especially copper and gold, brought alongside a vertiginous increase of mineral exports, as shown in Fig. 2. Private investment in mining increased almost sixfold

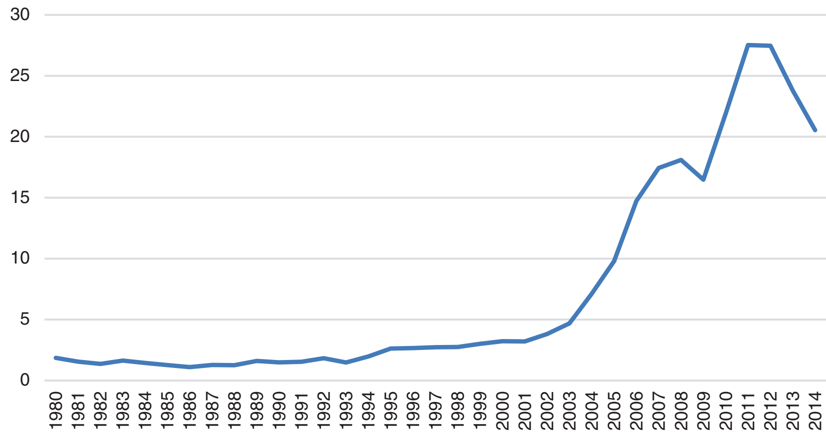

Fig. 2 FOB exports of mining producers, Peru. (FOB values in millions of US$). *Source* Self-elaboration, based on Central Reserve Bank of Peru data

between 2006 and 2015, taking over a quarter of foreign capital investment in this sector.[4] The growth of mining investment also partly responds to the policy adopted by the Peruvian state that helped the country take advantage of the resource boom cycle. Since the 1990s, Fujimori's government reduced state participation in the mining sector and promoted private investment through fiscal incentives and the simplification of providing concessions (Arellano-Yanguas 2011a, p. 21). As a consequence of these changes on the international and national level, mining has represented on average in the last 20 years 10% of GDP, reaching 15% in 2006. Peru, along with Chile and Bolivia, has become one of the countries where extractive industries represent the largest percentage of GDP in Latin America. The boom thus nourished already powerful private stakeholders and increased their presence in the territory.

Along with macroeconomic growth, the Peruvian state received greater earnings on all levels: national, regional, and local.[5] Figure 3 shows the growth of public budgets mainly as a result of income tax that extractive enterprises pay. This sum is also the base of subnational transfers: the canon. Regarding mining, income tax represents the bulk of tax earnings for this activity, which also pays mining royalties and concession rights.[6] During Alan Garcia's government (2006–2011), the Mining

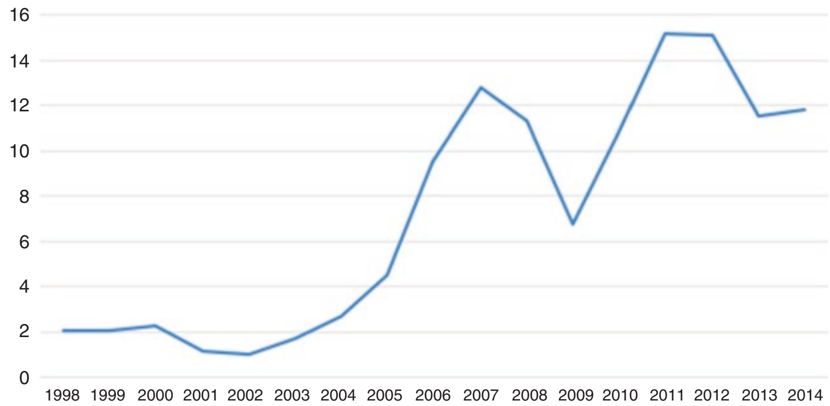

Fig. 3 Taxes collected by the National Tax Agency (SUNAT) in mining and hydrocarbons (millions of *Nuevos Soles*). *Source* Self-elaboration, based on SUNAT data

Voluntary Contribution was introduced in early 2007 and lasted until the change of government in 2011.[7] With this contribution, enterprises committed to allocating 2% of their net annual utilities to the "Local Mining Fund" and 1% to the "Regional Mining Fund." During Humala's government (2011-2016), the Special Tax on Mining (Law 29789) was created and applied to utilities with a tax rate of between 2% and 8% to enterprises that did not have a stable contract. For enterprises with a stable contract, a special levy was established (Law 29790), which manifested itself into a new tax burden contracted by a voluntary agreement between the state and enterprises with a new rate of between 4% and 13% of utilities. Finally, during the government of Humala, the Mining Royalty Law was amended to increase rates to between 1% and 12% of utilities (Sanborn and Dammert 2013, pp. 24–30).

Despite tax cuts and incentives for the extractive sector, the quantity of income collected by the La Superintendencia Nacional de Aduanas y de Administración Tributaria (SUNAT) in this sector went from 27,362 million Peruvian *Nuevos Soles* in 2004 to 15,152.7 million in 2011, approximately seven times more.

Figure 4 shows state rents also grew on subnational levels due to canon transfers. This growth, however, has created great territorial disparities. Given that canon beneficiaries were exclusively producers subnational areas

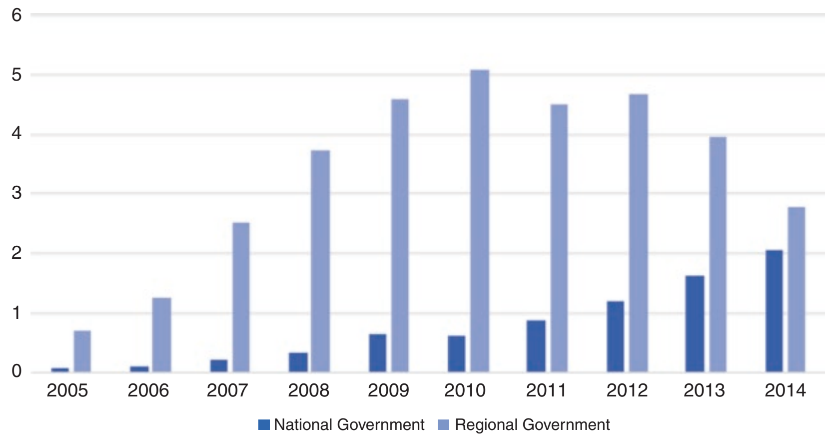

Fig. 4 Canon budget by government (includes SobreCanon, Royalties, and Participation) (in Thousand Millions of Nuevos Soles). *Source* Self-elaboration, based on Ministry of Economy and Finance of Peru data

at different levels (regions, provinces and districts), the canon contributed to increasing inequality of earnings between subnational áreas producing minerals and hydrocarbons and those not producing them. Thus, while in regions such as San Martin, Lambayeque, and Amazonas, subnational governments received on average earnings of less than one Peruvian *Nuevo Sol* per inhabitant. In regions, such as Cuzco and Moquegua, subnational governments received more than S/.1, 400 per inhabitant in 2013. This situation was repeated on the other subnational levels (provinces and districs), generating a large disparity of income between producing and non-producing subnational governments and causing small groups of regions (Ancash, Cajamarca, Tacna, Moquegua, and Arequipa) to concentrate more than 60% of the total canon (MEF 2013). The central government has tried to remedy this inequality with compensation mechanisms, such as the reduction of the canon percentage for the smallest subnational levels of government, the district, where the resource is located and an increase of the canon percentage for the largest subnational levels of government, the region. This was established to reduce disparities among subnational governments and increase capacity to invest in projects on the regional level. However, there is still a significant disparity among these subnational areas.

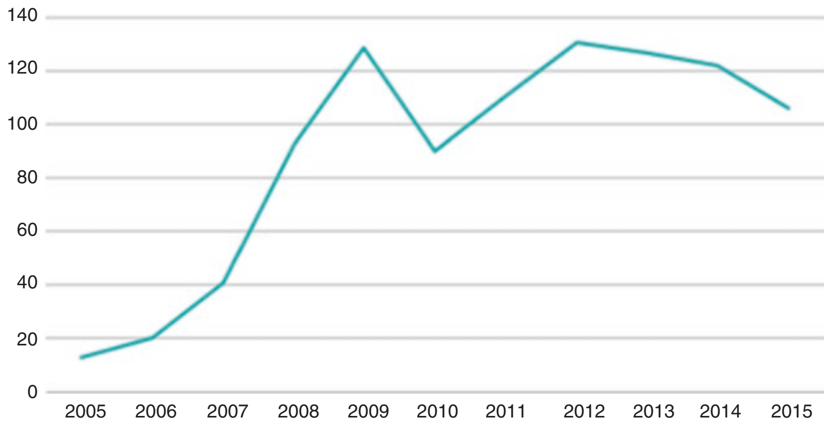

Fig. 5 Increase of socio-environmental conflicts in Peru (2004–2012) (in number of conflicts). *Source* Self-elaboration, based on Ombudsman Office-Peru data

The other face of economic growth based on natural resources has been civil unrest. The Ombudsman's Office (Defensoría del Pueblo, DP) registered a systematic increase of socio-environmental conflicts across the country since the extractive cycle's beginning in 2004. The number of these conflicts grew surprisingly in 2008 when the economic cycle reached its peak (Fig. 5), with mining as the economic activity with the strongest link to socio-environmental conflict (Orihuela et al. 2014).

Researchers coincide in identifying socio-environmental conflicts with the redistributive debate associated with the canon, and environmental problems associated with the extractive activity, like the quantity and quality of water, as main forms of conflict. Redistributive disagreement and environmental unrest feed one another in the generation and evolution of protest (Arellano-Yanguas 2011a; Bebbington 2013; De Echave et al. 2009; Paredes and De la Puente 2014). Orihuela and Paredes (2014) discuss one aspect of this unrest: land concessions. The authors document that concessions of hectares to mining have been increasing since 2004, reaching a peak of more than 4000 hectares in 2011. Added to this is the pressure of diverse concessions frequently falling to the same land area, due to a lack of coordination between state institutions. In the same hectare, there can be an overlap of mining, forest, and agricultural concessions, which generate greater rivalry for the use of territory (Orihuela and Paredes 2014,