

Natural Resources and Economic Growth: Theory and Evidence^{*}

Dustin Chambers[†] and Jang-Ting Guo[‡]

September 3, 2007

^{*} We are indebted to Shu-Hua Chen and Richard Suen for helpful discussions and comments. Part of this research was conducted while Guo was a visiting research fellow at the Institute of Economics, Academia Sinica, whose hospitality is greatly appreciated. Of course, all remaining errors are our own.

[†] Department of Economics and Finance, Salisbury University, 1101 Camden Ave., Salisbury, MD 21801, 1-410-543-6320, Fax: 1-410-546-6208, E-mail: DLChambers@salisbury.edu.

[‡] Corresponding Author. Department of Economics, 4128 Sproul Hall, University of California, Riverside, CA, 92521, 1-951-827-1588, Fax: 1-951-827-5685, E-mail: guojt@ucr.edu.

Abstract

This paper develops a one-sector endogenous growth model in which renewable natural resources are postulated as both a factor of production and as a measure of environmental quality. We show that sustained economic growth and a non-deteriorating environment can coexist along the economy's balanced growth path. Moreover, the output growth rate is positively related to the steady-state level of natural-resource utilization in production. Motivated by this theoretical prediction, we estimate a panel cross-country growth regression model that includes a broad measure of productive natural resources – the Ecological Footprint – as one of the conditioning variables, and find strong empirical support. Our estimation results also suggest that the costs of environmental conservation are fairly minimal, and that growth strategies based on greater physical capital formation and openness to international trade outperform those relying on more intensive utilization of the environment.

Keywords: Natural Resources; Endogenous Growth; Ecological Footprint.

JEL Classification: O41; Q21; Q56.

1. Introduction

In response to high energy prices and the OPEC oil embargo during the 1970's, economists began to systematically examine the growth effects of non-renewable natural resources within dynamic general equilibrium macroeconomic models. For example, using an exogenous-growth framework, Solow (1974) and Stiglitz (1974) show that sustained economic growth is possible so long as the reproducible factor of production (physical capital) can be substituted for exhaustible resources along the economy's balanced growth path.¹ This finding, while unquestionably essential, is somewhat restrictive in scope in that it ignores the impact of economic activities on the quality and state of the environment. As a result, economists began to broaden their focus to investigate the interrelations between economic growth and pollution emissions in the 1990's. Specifically, Stokey (1998) finds that continuing growth is possible despite ever tightening pollution restrictions that are met with costly abatement.² More recently, Brock and Taylor (2005) demonstrate the co-existence of sustained economic growth and zero net pollution emissions (dubbed the "Kindergarten Rule") in an endogenous growth model in which the abatement technology improves through learning-by-doing. Although this latter branch of the literature implicitly discusses the relationship between economic development and environmental quality through the narrow lens of pollution, it neglects the dual role that natural resources play in the production of GDP and hence long-run economic growth. Motivated by this gap, we develop a one-sector endogenous growth model that captures the environment's roles as (i) a provider of factors of production, and (ii) a stock of renewable natural resources that accumulates over time to preserve environmental quality as GDP continues to grow. Our main finding is that in the long run, the economy's output growth rate is positively related to the steady-state level of utilized natural resources. In addition, a panel cross-country growth regression, which includes a broad measure of productive natural resources, provides strong empirical support for this theoretical prediction.

¹ Suzuki (1976) finds that continuing output growth can arise within environmental endogenous growth models as well.

² See Lopez (1994) and Smulders and Gradus (1996) for other examples of growth models with pollution abatement.

The results of Solow (1974), Stiglitz (1974), and Stokey (1998), among others, together suggest that sustained economic growth is possible despite limitations on the productive availability of exhaustible natural resources, and that additional costs and restrictions associated with preserving environmental quality are not an insurmountable impediment to growth. By contrast, this paper focuses on the feasibility of a balanced-growth-path equilibrium with non-deteriorating environmental quality in a canonical one-sector endogenous growth model with renewable natural resources. In our model economy, households live forever, provide fixed labor supply and derive utility from consumption. A continuum of identical, competitive firms produce output using natural resources, which are assumed to regenerate at a constant rate over time, as a factor of production. The economy's aggregate production function displays increasing returns-to-scale because of the presence of productive externalities generated by capital inputs. We show that along the balanced growth path (BGP), output, consumption, and physical capital all grow at a common positive rate, whereas the stock of total natural resources and the level of natural resources allocated to the firms' production process maintain their respective steady-state values.³ It follows that the quantity of utilized natural resources per unit of GDP steadily declines in the economy's BGP equilibrium, a result that is also echoed in Solow (1974), Stiglitz (1974), and Stokey (1998) under non-renewable resources. Furthermore, we find that an increase of natural-resource utilization in production will raise the BGP's output growth rate.

Next, to empirically verify our main theoretical finding, we incorporate an inclusive measure of productive natural resources – the Ecological Footprint (EF) – into Barro's (1991) cross-country growth regression model. Formally, natural capital includes all the productive resources that can be extracted from the earth, as well as all the biological processes and services that facilitate life such as the absorption of waste or the conversion of carbon-dioxide into oxygen. The EF series is based on this broader concept of natural capital. As described in Rees (1992) and Wackernagel and Rees (1996), the EF variable systematically measures the quantity of renewable natural

³ See Smulders (1999) for a survey of other mechanisms that also demonstrate the compatibility of continuing output growth and environmental preservation within the context of endogenous growth models.

resources and life-facilitating services demanded by each nation.⁴ In order to overcome the inherent problem of aggregating over many disparate measures, the Ecological Footprint is constructed by first converting an exhaustive and comprehensive list of renewable natural resources and life-support services into standardized units of land area called *global hectares*. The resulting quantity, expressed in per-capita terms, offers a standardized measure of the land needed to support an average person's consumption expenditures (based on the country's current level of per-capita income), and facilitate ecologically necessary life-facilitating services. To our knowledge, the EF series is the best available proxy for natural-resource utilization in the economy's production process.

In addition to the Ecological Footprint, our dataset consists of a broad international panel that includes 5-year growth spells of output, together with some standard conditioning variables such as initial per-capita GDP, an educational attainment proxy for human capital, government and investment's shares of output, and trade openness. In order to obtain unbiased estimates from our dynamic panel regressions, Arellano and Bond's (1991) two-step GMM estimation procedure is employed. We first find that this empirical model passes the necessary specification tests whereby no second or higher-order serial correlations in the estimation residuals are present. We then show that the estimated coefficient on the Ecological Footprint is positive and statistically significant at the 1% level. This estimation result provides strong empirical support for the key prediction of our theoretical model, that is, more intensive utilization of natural resources in production leads to an increase in the economy's output growth rate. Moreover, the signs and statistical significance of the remaining regressors are generally in-line with neoclassical growth theory and previous empirical studies.

The remainder of this paper is organized as follows. Section 2 describes the theoretical model and analyzes the equilibrium conditions for the economy's balanced growth path. Section 3 employs an international panel dataset that includes the Ecological Footprint to empirically verify our main theoretical findings. Section 4 concludes.

⁴ The Ecological Footprint does not include measures of mineral deposits extracted in a given year.

2. The Theoretical Model

We develop a one-sector environmental endogenous growth model in which the representative household lives forever, provides fixed labor supply, and derives utility from consumption. The economy's social technology exhibits increasing returns-to-scale because of the presence of productive externalities generated by capital inputs. For analytical simplicity, and to maintain consistency with the subsequent empirical work that employs the Ecological Footprint to measure environmental utilization, we assume that *all* natural resources are renewable (such as a forest or fishery) in our theoretical model. Moreover, some of the natural resources are used in the firm's production function to capture the environment's productive value. Our analytical focus is to explore the interrelations between the output growth rate and environmental quality along the economy's balanced growth path (BGP).

2.1. Firms

There is a continuum of identical, competitive firms in the economy, with the total number normalized to one. Each firm produces output Y_t using a constant returns-to-scale Cobb-Douglas production function

$$(1) \quad Y_t = K_t^\alpha H_t^{1-\alpha} X_t, \quad 0 < \alpha < 1,$$

where K_t and H_t are physical capital and harvested/utilized natural resources (or natural capital), respectively, and X_t represents productive externalities that are taken as given by individual firms. In addition, X_t is postulated to take the form

$$(2) \quad X_t = A \bar{K}_t^{1-\alpha}, \quad A > 0,$$

where \bar{K}_t denotes the economy-wide average level of the capital stock. In a symmetric equilibrium, all firms take the same actions such that $K_t = \bar{K}_t$. Hence, (2) can be substituted into (1) to obtain the following social production function that displays increasing returns-to-scale:

$$(3) \quad Y_t = A K_t H_t^{1-\alpha}.$$

Under the assumption that factor markets are perfectly competitive, the first-order conditions for the firm's profit maximization problem are given by

$$(4) \quad r_t = \alpha \frac{Y_t}{K_t},$$

$$(5) \quad p_t = (1 - \alpha) \frac{Y_t}{H_t},$$

where r_t is the capital rental rate and p_t is the real price paid to utilized natural resources.

2.2. Households

The economy is populated by a unit measure of identical infinitely-lived households, each has perfect foresight and maximizes a discounted stream of utilities over its lifetime

$$(6) \quad \int_0^{\infty} \frac{C_t^{1-\sigma} - 1}{1-\sigma} e^{-\rho t} dt, \quad \sigma > 0, \quad \sigma \neq 1,$$

where C_t is the individual household's consumption, $\rho \in (0,1)$ is the subjective discount rate, and σ is the inverse of the intertemporal elasticity of substitution in consumption.

The budget constraint faced by the representative household is

$$(7) \quad C_t + \dot{K}_t + \delta K_t = r_t K_t + p_t H_t, \quad K_0 > 0 \text{ given},$$

where $\delta \in [0,1]$ is the capital depreciation rate. As is commonly specified in the environmental macroeconomics literature (see Smulders (1999) and references therein), the economy's ecological process or the law of motion for total renewable resources (as a proxy for environmental quality) N_t is given by

$$(8) \quad \dot{N}_t = f(N_t)N_t - H_t, \quad N_0 > 0 \text{ given},$$

where $f(N_t)$ is the regeneration function that is often assumed to be strictly increasing in N_t . Without loss of any generality, we postulate that the rate of natural regeneration is independent of the environmental state, specifically $f(N_t) = \theta > 0$.⁵

The first-order conditions for the representative household's dynamic optimization problem are

$$(9) \quad C_t^{-\sigma} = \lambda_{Kt},$$

$$(10) \quad \lambda_{Kt}(r_t - \delta) = -\dot{\lambda}_{Kt} + \rho \lambda_{Kt},$$

$$(11) \quad \theta \lambda_{Nt} = -\dot{\lambda}_{Nt} + \rho \lambda_{Nt},$$

⁵ We also consider the formulation in which only the non-utilized natural resources are allowed to regenerate. In this case, the accumulation equation (8) becomes $\dot{N}_t = \theta N_t - (1 + \theta)H_t$. It turns out that all our theoretical results are qualitatively robust to this modification.

$$(12) \quad \lambda_{K_t} p_t = \lambda_{N_t},$$

$$(13) \quad \lim_{t \rightarrow \infty} \lambda_{K_t} K_t e^{-\rho t} = 0,$$

$$(14) \quad \lim_{t \rightarrow \infty} \lambda_{N_t} N_t e^{-\rho t} = 0,$$

where λ_{K_t} and λ_{N_t} are shadow prices (or utility values) of capital and natural resources, respectively. Equation (9) states that the marginal benefit of consumption equals its marginal cost, which is the marginal utility of having an additional unit of physical capital. In addition, (10) and (11) are standard Euler equations that govern the evolution of K_t and N_t over time. Equation (12) shows that the firm utilizes natural resources to the point where the marginal value of more output is equal to the marginal cost of resource depletion. Finally, (13) and (14) are the transversality conditions (TVC).

2.3. Balanced Growth Path

In light of the household's CRRA utility formulation (6), together with the linearity of physical capital in the aggregate technology (3), the economy exhibits sustained endogenous growth whereby output, consumption, and physical capital all display a common, positive constant growth rate denoted by g . On the other hand, the regeneration/depletion equation (8) implies that in the long run, total and utilized natural resources will reach their respective steady-state levels, N^* and H^* . This in turn imposes a long-run environmental quality constraint, as in Solow (1974), Stiglitz (1974), and Stokey (1998) under exhaustible natural resources.

To derive a balanced-growth-path (BGP) equilibrium, we first make the variable transformation $X_t \equiv \frac{C_t}{K_t}$, which in turn allows the model's equilibrium conditions to be

re-expressed as autonomous differential equations

$$(15) \quad \frac{\dot{X}_t}{X_t} = \frac{\alpha A H_t^{1-\alpha} - \delta - \rho}{\sigma} - A H_t^{1-\alpha} + X_t + \delta,$$

$$(16) \quad \frac{\dot{H}_t}{H_t} = \frac{1}{\alpha} [A(1-\alpha)H_t^{1-\alpha} - X_t + \theta],$$

$$(17) \quad \dot{N}_t = \theta N_t - H_t.$$

Given the above dynamical system (15)-(17), the BGP equilibrium is characterized by a triplet of positive real numbers (X^*, H^*, N^*) that satisfy the condition $\dot{X}_t = \dot{H}_t = \dot{N}_t = 0$.

It is straightforward to show that our model economy exhibits a unique balanced growth path along which the utilized natural resource maintains its steady-state value

$$(18) \quad H^* = \left[\frac{\sigma\theta - [\rho - (\sigma - 1)\delta]}{\alpha A(\sigma - 1)} \right]^{1/(1-\alpha)},$$

which in turn leads to the expressions for X^* and N^* as follows:

$$(19) \quad X^* = A(1 - \alpha)(H^*)^{1-\alpha} + \theta \quad \text{and} \quad N^* = \frac{H^*}{\theta}.$$

With (18) and (19), it follows that the common (positive) rate of economic growth g is given by

$$(20) \quad g = \frac{\theta - \rho}{\sigma - 1} \quad \text{or} \quad g = \alpha A(H^*)^{1-\alpha} - \theta - \rho.$$

As a result, the BGP's growth rate *ceteris paribus* is positively related to the level of utilized natural resources.⁶ That is, a higher (lower) usage of services from the environment in production will raise (reduce) the economy's rate of growth in output, consumption, and physical capital. Moreover, the quantity of utilized natural resources per unit of GDP steadily declines along the economy's balanced growth path, a result that is also echoed in Solow (1974), Stiglitz (1974), and Stokey (1998), among many others.

3. The Empirical Model

There are two interesting implications that follow from the above theoretical model.

First, as mentioned earlier, the BGP's output growth rate rises with the productive

utilization of natural resources $\frac{\partial g}{\partial H^*} > 0$. Second, the economy's long-run rate of

economic growth increases with the reproduction rate of natural resources $\frac{\partial g}{\partial \theta} > 0$. The

latter implication is difficult to verify empirically because of the need to access data on

the *stock* of natural resources, whereas the former is more easily testable given that it

requires the *flow* of natural resources used in production. As a result, we restrict our

empirical analysis to the effects of natural-resource utilization on GDP. Since output is a

⁶ To ensure that the BGP's output growth rate g is positive, we impose the following parametric restriction: $\theta > (<) \rho$ when $\sigma > (<) 1$.

non-stationary variable, we cannot simply regress GDP on the aggregate factors of production in levels. Instead, we incorporate the natural-resource usage into Barro's (1991) specification and examine the following panel cross-country growth regression model:

$$(21) \quad \text{growth}_{it+1} = \beta_1 \text{income}_{it} + \beta_2 \text{education}_{it} + \beta_3 \text{gov}_{it} + \beta_4 \text{inv}_{it} + \beta_5 \text{trade}_{it} + \beta_6 \text{footprint}_{it} + \alpha_i + \eta_t + \varepsilon_{it+1},$$

where the dependent variable (growth_{it+1}) measures the average annual growth in real GDP per capita in country i over the period of 5 years (between t and $t+1$). To account for conditional convergence, our model includes income_{it} , which is the natural log of PPP-adjusted, chain-weighted per-capita GDP at period t . Human capital is controlled by way of the proxy education_{it} , which equals the average years of education for the entire population aged 15 and above. To account for differences in fiscal policies across countries, we include gov_{it} , which measures public expenditures on goods and services relative to GDP ($= G_{it}/Y_{it}$), as a conditioning variable. To control for the rate of capital formation, the investment share in output ($= I_{it}/Y_{it}$), denoted as inv_{it} , is also included. The openness of a nation is captured by trade_{it} , which is the ratio of total trade to GDP, that is $(\text{IM}_{it} + \text{EX}_{it})/Y_{it}$. To control for the natural-resource utilization in production, we include footprint_{it} , which equals the natural log of the per-capita quantity of renewable natural resources, in our panel estimation. Finally, α_i is a country-specific effect, η_t is a period-specific effect, and ε_{it+1} is an i.i.d. stochastic shock with zero mean and standard deviation σ_ε^2 .

3.1. The Data

Our international panel dataset is constructed from three sources. Output growth, income, government and investment's shares of GDP, and trade openness are taken from the Penn World Table v. 6.2 (Heston, Summers, and Aten, 2006). These variables are expressed as percentages with the exception of income, which is expressed (prior to taking the natural log) in constant (2000) international dollars (\$I). The education series comes from Barro and Lee (2000), and measures the average years of schooling for the

entire population aged 15 and above. Finally, the natural-resource series – the Ecological Footprint – is obtained from the Global Footprint Network (2005).⁷ This variable measures the quantity of renewable natural resources, in standardized global hectares (gha), needed to produce a nation’s current level of per-capita consumption.⁸ In sum, our dataset consists of an unbalanced panel of 93 countries over 9 five-year time periods (1961, 1966, ..., 2001), for a total of 794 observations. Table 1 lists the nations and periods covered in the dataset, and Table 2 presents summary statistics of the raw, untransformed data on the Ecological Footprint.

3.2. Estimation Method

It is well known in the empirical growth literature that using standard fixed or random effects methods to estimate a dynamic panel model such as (21) generates biased estimates. Typically, this problem is resolved by use of a Generalized Method of Moments (GMM) estimator along with suitable instruments. Within this family of estimation procedures, Arellano and Bond’s (1991) 2-step estimator is one of the most popular methods, and is also the estimator of choice for this paper. The first step of Arellano and Bond’s estimation procedure is to take the first difference of (21), which, after some algebraic manipulation, can be expressed as

$$(22) \quad \Delta \text{income}_{it+1} = (1 + \beta_1) \Delta \text{income}_{it} + \beta_2 \Delta \text{education}_{it} + \beta_3 \Delta \text{gov}_{it} + \beta_4 \Delta \text{inv}_{it} + \beta_5 \Delta \text{trade}_{it} + \beta_6 \Delta \text{footprint}_{it} + \Delta \eta_t + \Delta \varepsilon_{it+1},$$

thus the country-specific term α_i is removed. The next step is to construct an appropriate set of instruments. Generally speaking, the strictly exogenous variables in (22) can serve as their own instruments, as well as lagged observations of the remaining predetermined, untransformed endogenous variables. In the current context, we follow previous studies (see, for example, Barro (2000) and Forbes (2000), among others) and postulate both the series of income and investment’s share of output to be endogenous regressors.

⁷ See Haberl, Erb, and Krausmann (2001) for a good introduction on how ecological footprints are calculated.

⁸ Since this paper seeks to investigate how the rate of natural resource utilization affects economic growth, the total footprint series was adjusted by removing the per-capita quantity of developed land (*i.e.* urbanized space). The value of permanent improvements to land and the structures placed on land are generally included in a nation’s capital stock, thus including this area in a renewable resource (flow) measurement is inappropriate. The nuclear power component was removed from the footprint measure as well.

Moreover, since it is conceivable that a higher rate of economic growth boosts the productive usage of the environment, we make the cautious modeling decision and treat the natural-resource utilization as an endogenous conditioning variable as well. As a result, our instrument set consists of all lagged values of income, investment's share of output, and ecological footprints, expressed in levels

$\{\text{income}_{it-1}, \dots, \text{income}_{i1}, \text{inv}_{it-1}, \dots, \text{inv}_{i1}, \text{footprint}_{it-1}, \dots, \text{footprint}_{i1}\}$, together with the remaining (exogenous) regressors, expressed in differences $\{\Delta \text{education}_{it}, \Delta \text{gov}_{it}, \Delta \text{trade}_{it}\}$, serving as their own instruments.⁹

3.3. Specification Tests

Arellano and Bond (1991) state that the following two conditions must be satisfied for their two-step GMM estimator to be consistent and efficient: (i) all of the regressors (apart from the lagged dependent variable) must be predetermined by at least one period, *i.e.* $E(X'_{it}\varepsilon_{is}) = 0$ for all $s > t$, where $X_{it} \equiv \{\text{education}_{it}, \text{gov}_{it}, \text{inv}_{it}, \text{trade}_{it}, \text{footprint}_{it}\}$ in this paper; and (ii) the model's estimation errors cannot be autocorrelated, *i.e.*

$E(\varepsilon_{it}\varepsilon_{is}) = 0$, for all $s \neq t$. The first condition cannot be tested as a formal test does not exist. However, Arellano and Bond (1991) propose two serial-correlation tests: the m_2 test for second-order serial correlations, and the Sargan test for overidentifying restrictions.¹⁰ Before reporting estimation results in the next subsection, we first conduct these specification tests on our empirical model as in (22).

The m_2 test for second-order autocorrelations in the residuals of (22) is crucially important because lagged values of the right-hand side regressors are used as instruments in the estimation procedure. Under the null hypothesis that there is no second-order autocorrelation, the test statistic has an asymptotic standard normal distribution

$$(23) \quad m_2 = \frac{\Delta \varepsilon'_{-2} \Delta \varepsilon_*}{\sqrt{v}} \underset{a}{\sim} N(0,1),$$

⁹ The one exception is the time-period effects, which (as is customary) enter the instrument matrices in levels, not in differences.

¹⁰ As a third test, Arellano and Bond (1991) also suggest a Hausman specification test. However, using Monte Carlo experiments, these authors show that the Hausman test lacks power and is very susceptible to outliers. For this reason, Hausman specification tests are not commonly employed to test for serial correlation.

where $\Delta\varepsilon_{-2}$ is the vector of residuals from (22) lagged twice, $\Delta\varepsilon_*$ is the vector of residuals from the same model trimmed to match $\Delta\varepsilon_{-2}$, and v is a scalar that is defined as

$$(24) \quad v \equiv \sum_{i \in N} \Delta\hat{\varepsilon}'_{i(-2)} \Delta\hat{\varepsilon}_{i*} \Delta\hat{\varepsilon}'_{i*} \Delta\hat{\varepsilon}_{i(-2)} - 2\Delta\hat{\varepsilon}'_{-2} X_* (X'Z A_N Z'X)^{-1} X'Z A_N \\ \times \left(\sum_{i \in N} Z'_i \Delta\hat{\varepsilon}_i \Delta\hat{\varepsilon}'_{i*} \Delta\hat{\varepsilon}_{i(-2)} \right) + \Delta\hat{\varepsilon}'_{-2} X_* \text{avâr}(\hat{\delta}) X'_* \Delta\hat{\varepsilon}_{-2},$$

where X includes all the right-hand side conditioning variables, $\hat{\delta}$ includes all the estimated coefficients, Z is the matrix of instruments, and A_N is the weighting matrix used in the Arellano-Bond procedure. It turns out that for model (22), the m_2 test statistic is equal to 0.33, with a corresponding p-value of only 0.7415, yielding no evidence of second-order autocorrelation.

As another check of our model's estimation residuals, the Sargan test for overidentifying restrictions is employed to confirm the validity of the moment restrictions implied by the instruments. Under the null hypothesis that the moment restrictions are valid (which implies the absence of second or higher-order autocorrelations), the test statistic, denoted as s , is asymptotically chi-square distributed with $q - k$ degrees of freedom (*i.e.* χ^2_{q-k}):

$$(25) \quad s = \Delta\hat{\varepsilon}'Z \left(\sum_{i \in N} Z'_i \Delta\hat{\varepsilon}_i \Delta\hat{\varepsilon}'_i Z_i \right)^{-1} Z' \Delta\hat{\varepsilon} \underset{a}{\sim} \chi^2_{q-k},$$

where q is the number of moment restrictions, and k is the number of coefficients estimated in the model.

The Sargan test statistic for model (22) is equal to 82.86, with a corresponding p-value of 0.44, hence we cannot reject the null hypothesis that the overidentifying restrictions are valid. The above test results indicate that (22) lacks second or higher-order serial correlations in the estimation residuals. Therefore, the two-step GMM estimator that we report below is both consistent and efficient.

3.4. Estimation Results

Before discussing our estimation results, it is instructive to examine the coefficient estimates within a benchmark specification that excludes the footprint series from model (22). Table 3 shows that the coefficient estimates from this standard formulation are generally in-line with the existing empirical growth literature. In particular, the estimated

coefficient on initial income is negative and statistically significant at the 1% level, indicating the presence of growth convergence, *i.e.* more developed nations *ceteris paribus* grow more slowly than their less developed counterparts. The coefficients on education, investment's output share, and the degree of openness are all positive and statistically significant. These results conform to the neoclassical growth theory where increased accumulation in physical and human capital or higher volumes of international trade will raise a nation's output per worker. Finally, the estimated coefficient on government expenditures is positive but marginally insignificant, with a p-value of 0.156.

Turing to a full estimate of model (22) with the footprint variable included, Table 3 shows that the estimated coefficients are very similar to those in the benchmark specification.¹¹ However, the coefficient on government's share in GDP is now positive and statistically significant, which is at odds with the findings of other researchers (see, for example, Levine and Renelt (1992) and Barro (2000), among others). On the other hand, consistent with the key prediction of our theoretical model, the estimated natural-resource coefficient is positive and statistically significant at the 1% level. In other words, when more natural resources (as measured in standardized global hectares) are utilized in production within a nation, its subsequent 5-year growth rate in output will rise.

Since the footprint series has been transformed by taking the natural log, the estimated coefficient is interpreted as a growth elasticity measure. Specifically, a ten percent increase in natural-resource utilization leads to a 0.17% rise in the annual growth rate of GDP over the next 5-year period. Given the relatively small magnitude of this effect, it would be inadvisable for an underdeveloped nation to rely too heavily on natural resource extraction as a means of promoting economic growth. Instead, the estimation results in Table 3 suggest that promoting domestic capital accumulation produces a much larger quantitative impact on the economy's future growth. In particular, a ten percent increase in investment's GDP share would boost the rate of output growth by almost 1.1%. Moreover, we note that a ten percent expansion in trade openness would enhance

¹¹ Both the benchmark specification and model (22) include period dummies, whose estimated coefficients are not reported in Table 3. In addition, the Sargan test fails to reject the null hypothesis that the overidentifying restrictions are valid at any standard level of statistical significance in either formulation. See Table 3 for the respective test statistics and p-values.

economic growth by the same magnitude as the corresponding increase in natural-resource usage. Therefore, our analysis offers some empirical support for adopting mainstream growth strategies, such as promoting foreign direct investment and reaping the gains from international trade, that are more economically rewarding and less harmful to the environment. These results also suggest that developed nations should not be overly opposed to well-reasoned conservation programs designed to slow down the rate of natural-resource extraction because they appear to generate little drag on the economy. In addition, anti-globalization efforts, *i.e.* opposition to the free flow of capital and goods and services, will leave impoverished nations with few growth-promoting options. Environmental degradation, be it for internal consumption (*e.g.* deforestation for small homesteads) or external consumption (*e.g.* the export of raw commodities), is often the result. This implies that anti-globalization, anti-poverty, and pro-environmental goals are likely to be internally inconsistent.

4. Conclusion

In examining long-run economic growth within the context of dynamic environmental macroeconomic models, most of the existing literature has developed along the following two strands: (i) the environment is a source of non-renewable factors of production, and (ii) the state of the environment's quality is measured by pollution emissions. In this paper, we incorporate both of these environmental concerns, but from a different perspective, into an otherwise standard one-sector endogenous growth model. Specifically, the environment is postulated to be a storehouse of renewable natural resources, some of which are used in the firm's production process, that accumulate over time to maintain environmental quality while output continues to grow. We show that sustained economic growth and a non-deteriorating environment can be simultaneously present along the economy's balanced growth path. Moreover, we find that the BGP's output growth rate is positively related to the steady-state level of natural-resource utilization in production.

To verify the empirical veracity of our theoretical findings, we estimate a panel cross-country growth regression model that includes the Ecological Footprint, a broad measure of productive natural resources, as one of the conditioning variables. The

estimation results provide strong empirical support for the positive relationship between the utilization rate of natural resources in production and subsequent output growth. However, this finding needs to be interpreted carefully since our empirical results also suggest that the costs of environmental conservation are fairly minimal, and that growth strategies based on greater physical capital formation and openness to trade outperform those depending on more intensive use of the environment. In addition, it is important to underscore that the BGP's output growth rate is positively related to the stationary, long-run value of natural-resource utilization. Hence, higher usage of natural resources today may boost economic growth in the short run, but will likely decrease its steady-state level, thus permanently reducing the economy's long-run rate of output growth. In light of this short- vs. long-run growth tradeoff, and the fact that the short-run costs of environmental conservation are relatively low, it is advisable that nations not rely heavily on environmentally-intensive economic growth strategies.

References

- Arellano, M., and S. Bond (1991). "Some Tests of Specification for Panel Data: Monte Carlo Evidence and an Application to Employment Equations," *Review of Economic Studies* 58, 277-297.
- Barro, R. J. (1991). "Economic Growth in a Cross-Section of Countries," *Quarterly Journal of Economics* 106, 407-444.
- Barro, R. J. (2000). "Inequality and Growth in a Panel of Countries," *Journal of Economic Growth* 5, 5-32.
- Barro, R. J., and J. Lee (2000). "International Data on Educational Attainment: Updates and Implications," Center for International Development, Harvard University, Working Paper No. 42. URL: <http://www.cid.harvard.edu/ciddata/ciddata.html>
- Brock, W. A., and M. S. Taylor. (2005). "Economic Growth and the Environment: A Review of Theory and Empirics," in *Handbook of Economic Growth*, Vol. 1B, edited by P. Aghion and S. N. Durlauf, Elsevier: Amsterdam, 1749-1821.
- Forbes, K. (2000). "A Reassessment of the Relationship between Inequality and Growth," *American Economic Review* 90, 869-887.
- Global Footprint Network (2005). *National Footprint and Biocapacity Accounts*, Academic Edition. URL: <http://www.footprintnetwork.org>
- Haberl, H., K. Erb and F. Krausmann (2001). "How to Calculate and Interpret Ecological Footprints for Long Periods of Time: The Case of Austria 1926-1995," *Ecological Economics* 38, 25-45.
- Heston, A., R. Summers and B. Aten (2006). *Penn World Table Version 6.2*, Center for International Comparisons of Production, Income and Prices, University of Pennsylvania. URL: <http://pwt.econ.upenn.edu/>
- Levine, R., and D. Renelt (1992). "A Sensitivity Analysis of Cross-Country Growth Regressions," *American Economic Review* 82, 942-963.
- Lopez, R. (1994). "The Environment as a Factor of Production: The Effects of Economic Growth and Trade Liberalization," *Journal of Environmental Economics and Management* 27, 163-184.
- Rees, W. (1992). "Ecological Footprints and Appropriated Carrying Capacity: What Urban Economics Leaves Out," *Environment and Urbanization* 4, 121-130.
- Smulders, S., and R. Gradus. (1996). "Pollution Abatement and Long-Term Growth," *European Journal of Political Economy* 12, 505-532.

- Smulders, S. (1999). "Endogenous Growth Theory and the Environment," in *Handbook of Environmental and Resource Economics*, edited by Jeroen C.J.M. van den Bergh, Edward Elgar: Cheltenham, UK, 610-621.
- Solow, R. M. (1974). "Intergenerational Equity and Exhaustible Resources," *Review of Economic Studies* 41, 29-45.
- Stiglitz, J. (1974). "Growth with Exhaustible Natural Resources: Efficient and Optimal Growth Paths," *Review of Economic Studies* 41, 123-137.
- Stokey, N. L. (1998). "Are There Limits to Growth?" *International Economic Review* 39, 1-31.
- Suzuki, H. (1976). "On the Possibility of Steadily Growing Per Capita Consumption in an Economy with a Wasting and Non-Replenishable Resource," *Review of Economic Studies* 43, 527-535.
- Wackernagel, M., and W. Rees (1996). *Our Ecological Footprint, Reducing Human Impact on the Earth*, New Society Publishers: Philadelphia.

Table 1: Countries and Periods

Country	Observations	Range	Country	Observations	Range
Afghanistan	7	1971-2001	Lesotho	9	1961-2001
Algeria	9	1961-2001	Liberia	7	1971-2001
Argentina	9	1961-2001	Malawi	9	1961-2001
Australia	9	1961-2001	Malaysia	9	1961-2001
Austria	9	1961-2001	Mali	9	1961-2001
Bangladesh	6	1976-2001	Mauritius	9	1961-2001
Benin	9	1961-2001	Mexico	9	1961-2001
Bolivia	9	1961-2001	Mozambique	9	1961-2001
Botswana	7	1971-2001	Nepal	9	1961-2001
Brazil	9	1961-2001	Netherlands	9	1961-2001
Cameroon	9	1961-2001	New Zealand	9	1961-2001
Canada	9	1961-2001	Nicaragua	9	1961-2001
Central African Republic	7	1971-2001	Niger	9	1961-2001
Chile	9	1961-2001	Norway	9	1961-2001
China	6	1976-2001	Pakistan	9	1961-2001
Colombia	9	1961-2001	Panama	9	1961-2001
Congo, Republic of	4	1986-2001	Papua New Guinea	7	1971-2001
Costa Rica	9	1961-2001	Paraguay	9	1961-2001
Denmark	9	1961-2001	Peru	9	1961-2001
Dominican Republic	9	1961-2001	Philippines	9	1961-2001
Ecuador	9	1961-2001	Poland	7	1971-2001
Egypt	6	1976-2001	Portugal	9	1961-2001
El Salvador	9	1961-2001	Rwanda	9	1961-2001
Finland	9	1961-2001	Senegal	9	1961-2001
France	9	1961-2001	Sierra Leone	7	1971-2001
Gambia, The	9	1961-2001	South Africa	9	1961-2001
Germany	7	1971-2001	Spain	9	1961-2001
Ghana	9	1961-2001	Sri Lanka	9	1961-2001
Greece	9	1961-2001	Sudan	7	1971-2001
Guatemala	9	1961-2001	Swaziland	7	1971-2001
Guinea-Bissau	9	1961-2001	Sweden	9	1961-2001
Haiti	6	1971-1996	Switzerland	9	1961-2001
Honduras	9	1961-2001	Syria	9	1961-2001
Hungary	7	1971-2001	Tanzania	9	1961-2001
India	9	1961-2001	Thailand	9	1961-2001
Indonesia	9	1961-2001	Togo	9	1961-2001
Iran	9	1961-2001	Trinidad & Tobago	9	1961-2001
Iraq	7	1971-2001	Tunisia	9	1961-2001
Ireland	9	1961-2001	Turkey	9	1961-2001
Israel	9	1961-2001	Uganda	9	1961-2001
Italy	9	1961-2001	United Kingdom	9	1961-2001
Jamaica	9	1961-2001	United States	9	1961-2001
Japan	9	1961-2001	Uruguay	9	1961-2001
Jordan	9	1961-2001	Venezuela	9	1961-2001
Kenya	9	1961-2001	Zambia	9	1961-2001
Korea, Republic of	9	1961-2001	Zimbabwe	9	1961-2001
Kuwait	7	1971-2001			

Table 2: Summary Statistics of the Ecological Footprint

Country	Avg	Min	Max	Std. Dev.	Country	Avg	Min	Max	Std. Dev.
Afghanistan	0.22	0.14	0.31	0.06	Lesotho	0.96	0.75	1.23	0.15
Algeria	1.21	0.81	1.49	0.27	Liberia	0.80	0.58	0.9	0.11
Argentina	2.70	2.28	2.92	0.21	Malawi	0.69	0.46	0.91	0.19
Australia	6.60	5.34	8.24	1.06	Malaysia	1.58	1.08	2.61	0.51
Austria	3.77	2.56	4.67	0.70	Mali	0.94	0.78	1.2	0.14
Bangladesh	0.45	0.34	0.55	0.07	Mauritius	1.02	0.71	1.7	0.32
Benin	0.93	0.77	1.08	0.12	Mexico	1.94	1.4	2.38	0.35
Bolivia	1.14	0.99	1.25	0.09	Mozambique	0.66	0.55	0.72	0.06
Botswana	1.37	1.01	2.34	0.47	Nepal	0.64	0.56	0.75	0.06
Brazil	1.80	1.61	2.08	0.15	Netherlands	3.71	2.48	4.49	0.69
Cameroon	0.94	0.74	1.12	0.14	New Zealand	4.43	3.87	5.38	0.56
Canada	6.19	4.5	7.29	0.80	Nicaragua	1.30	0.94	1.49	0.21
Republic	0.89	0.82	0.98	0.07	Niger	1.32	1.09	1.49	0.15
Chile	1.50	1.17	1.71	0.21	Norway	4.40	2.9	5.92	1.01
China	1.23	0.91	1.54	0.25	Pakistan	0.58	0.53	0.64	0.04
Colombia	1.16	1.09	1.27	0.06	Panama	1.67	1.51	1.87	0.11
Congo, Republic of	0.67	0.52	0.86	0.16	Papua New Guinea	1.48	0.96	1.82	0.29
Costa Rica	1.84	1.53	3.07	0.48	Paraguay	1.89	1.72	1.99	0.09
Denmark	5.01	3.9	6.77	0.85	Peru	0.90	0.68	1.09	0.14
Dominican Republic	1.16	0.96	1.65	0.20	Philippines	0.92	0.83	1.05	0.07
Ecuador	1.18	0.87	1.44	0.16	Poland	4.16	3.3	4.78	0.61
Egypt	1.14	0.97	1.25	0.09	Portugal	2.87	2.19	4.17	0.69
El Salvador	0.91	0.79	1.22	0.13	Rwanda	0.81	0.64	0.97	0.11
Finland	4.68	3.96	5.52	0.50	Senegal	1.38	1.14	1.62	0.17
France	3.67	2.89	4.05	0.39	Sierra Leone	0.85	0.71	1.06	0.13
Gambia, The	1.08	0.84	1.28	0.12	South Africa	2.50	1.74	3	0.41
Germany	4.45	3.81	4.78	0.34	Spain	2.93	1.9	4.16	0.66
Ghana	0.87	0.7	1.06	0.12	Sri Lanka	0.76	0.69	0.85	0.05
Greece	3.09	1.86	5.06	1.03	Sudan	0.95	0.85	1.09	0.10
Guatemala	0.93	0.89	1.05	0.05	Swaziland	1.03	0.82	1.33	0.21
Guinea-Bissau	0.80	0.66	0.88	0.07	Sweden	4.29	3.59	5.18	0.56
Haiti	0.66	0.53	0.75	0.09	Switzerland	3.88	2.92	4.42	0.50
Honduras	1.26	0.97	1.75	0.26	Syria	1.36	1.02	1.65	0.24
Hungary	3.57	2.85	3.99	0.46	Tanzania	0.77	0.61	0.87	0.09
India	0.71	0.66	0.81	0.05	Thailand	1.00	0.78	1.54	0.25
Indonesia	0.90	0.83	1.05	0.07	Togo	0.94	0.73	1.22	0.17
Iran	1.53	1.15	2.02	0.29	Trinidad & Tobago	2.37	1.24	4.06	0.87
Iraq	0.85	0.62	1	0.14	Tunisia	1.26	1.11	1.45	0.12
Ireland	3.84	2.75	4.91	0.65	Turkey	1.88	1.73	2.05	0.11
Israel	4.05	2.34	8.5	1.83	Uganda	1.30	1.01	1.7	0.27
Italy	2.98	1.87	3.79	0.63	United Kingdom	4.29	3.23	4.93	0.50
Jamaica	1.56	1.09	2.04	0.33	United States	7.21	4.69	8.42	1.19
Japan	3.27	1.88	4.07	0.71	Uruguay	3.40	2.06	10.47	2.66
Jordan	1.40	1	1.79	0.26	Venezuela	2.34	1.72	2.88	0.33
Kenya	0.86	0.69	1.04	0.12	Zambia	0.77	0.53	1.03	0.19
Korea, Republic of	1.95	0.79	3.08	0.81	Zimbabwe	1.00	0.55	1.23	0.22
Kuwait	5.41	2.35	7.91	1.97					

Note: Ecological Footprints are measured in standardized global hectares (gha).

Table 3: Two-Step GMM Estimation Results

Variable	Benchmark	Model (22)
income	-0.0493 (0.0012)***	-0.064 (0.0010)***
education	0.0099 (0.0025)***	0.013 (0.0011)***
government	0.0241 (0.0170)	0.057 (0.0080)***
investment	0.1054 (0.0241)***	0.106 (0.0122)***
trade	0.0174 (0.0063)***	0.017 (0.0033)***
footprint		0.017 (0.0027)***
Sargan test	64.44	82.86
Sargan p-value	0.156	0.422
Observations	608	608

White robust (period) standard errors in parenthesis

***, **, * - statistically significant at the one, five, and ten percent levels respectively