Post-conflict economics

Learning the ropes

What are the best ways of creating sustainable economic development in post-conflict states? Gerd Junne and Vidya Marapin review five books in search of viable strategies.

Violent conflicts do not always aggravate poverty. Contrary to widespread belief, communities in Indonesia, the Philippines, Colombia and Sri Lanka that have experienced large-scale violent conflict had a higher chance of escaping poverty than communities that have lived in a relatively peaceful environment. This is the challenging conclusion of *Rising from the Ashes of Conflict*, the fourth volume of *Moving Out of Poverty*, a large-scale World Bank study published in 2010 on economic development in post-conflict countries, mainly in Asia, and it is not a conclusion supported by all case studies in the volume. This and several other recent publications underline that we still know relatively little about economic development after violent conflict.

Many studies in the past decade have shown how important economic motives are in explaining why wars break out and why their average duration is so much longer than in the past. In striking contrast to this, Graciana Del Castillo observes in her 2008 book, *Rebuilding War-Torn States*, that 'post-conflict economic reconstruction has been a much-neglected aspect of the extensive and fast-growing literature on war-to-peace transitions'. There are two main reasons for this:

- Much of the literature still builds on the 'liberal peace' theory, which takes market-led economic development for granted, once the rule of law is re-established.
- Post-conflict discourse has largely been dominated by a 'fragile states' rhetoric during the past decade. It concentrates on state structures and governance, and largely neglects the economic aspects of post-conflict development.

The rediscovered state

The policy of international financial institutions in the 1990s was to curtail the role of the state in the economy of developing countries as part of 'structural adjustment' policies.

By **Gerd Junne**, professor of international relations at the University of Amsterdam, the Netherlands, and **Vidya Marapin**, PhD researcher on the development of identities in post-conflict countries.

- *Moving Out of Poverty. Volume 4: Rising from the Ashes of Conflict*, ed. by Deepa Narayan and Patti Petesch, Palgrave Macmillan and World Bank, 2010, 548 pp.
- *Business, Conflict Resolution and Peacebuilding: Contributions from the Private Sector to Address Violent Conflict*, by Derek Sweetman, Routledge, 2009, 151 pp.
- *The Political Economy of Transitions to Peace*, by Galia Press-Barnathan, University of Pittsburgh Press, 2009, 257 pp.
- *Rebuilding War-Torn States: The Challenge of Post-Conflict Economic Reconstruction*, by Graciana Del Castillo, Oxford University Press, 2008, 436 pp.
- *Peace and the Public Purse: Economic Policies for Postwar Statebuilding*, ed. by James K. Boyce and Madalene O'Donnell, Lynne Rienner Publishers, 2007, 343 pp.

The rediscovery of the state in the present century is based on the acknowledgment that the state does play an important role not only in guaranteeing security and law and order, but also in stabilizing the economy. To fulfil this role, the state needs to be able to collect and manage resources. But many post-conflict states do not. As James K. Boyce and Madalene O'Donnell argue in their introduction to *Peace and the Public Purse*, published in 2007, 'a tax/GDP ratio of less than 15%' is regarded as 'an indicator of "state fragility"'.

Much has been written on public finance in developing countries, but little on how to tailor these policies to the circumstances of post-conflict countries. *Peace and the Public Purse* tries to close this gap. The authors in this volume counter the general advice that institutions such as the IMF and the WTO give to developing countries, namely to switch from tariffs on imports and exports to value added tax. Countries with a nascent bureaucracy (as is the case in most post-conflict countries) are probably better off sticking to tariffs, Boyce and O'Donnell point out in their introductory chapter, because 'a relatively small number of border crossing points are attractive from an administrative standpoint'. The book does not mention that tariffs encourage smuggling, which is often a main source of income for criminal organizations. The extensive role of

In times of economic turmoil across the world, Albania, once the most isolated and desperately poor country in Europe, is showing robust growth and attracting the attention of foreign investors. Construction of a new road linking Albania's port of Durres and Kosovo, May 2009

criminal activities in post-conflict economies receives hardly any attention in the books reviewed here.

Another reason why switching to taxes is not the best idea, according to the editors, is that in most post-conflict countries there is a dramatic 'mismatch between fiscal capacities and needs as well as ongoing societal tensions that could precipitate the renewal of violent conflict'. The massive needs created by the destructive force of war need to be met – and met as soon as possible – in order to redress inequalities that contributed to the violence in the first place. Raising taxes is not an option, because there is little to tax. Taxation at an early stage would also reduce attractiveness for foreign and local companies. The reader's conclusion, then, is that the gap during the early stages of post-conflict situations can only be closed by aid.

A cynical attraction

Aid has to be massive, according to Deepa Narayan and Patti Petesch, editors of *Rising from the Ashes of Conflict*. They argue that effective development assistance in conflict-torn countries is not about giving small amounts of credit to the selected few. 'Chickens and miserly handouts,' as they argue, will not reduce poverty. The results of the numerous microcredit programmes which they found in post-conflict communities in seven countries, from Indonesia to Afghanistan to Colombia, were thin. Therefore instead, Narayan and Petesch argue, the solution is substantial grants to large numbers of people over a long period of time.

This will prevent people from letting their sons be recruited by armed groups. It will help get the production process underway and create local and national markets. Conflict-affected communities in Aceh, Indonesia, where the government provided cash to individuals and groups, saw the share of people classified as poor decrease by 11 percentage points. This is in contrast to a decline of less than one percentage point throughout Indonesia between 1996 and 2004.

Jobs for millions can only be generated through market-led recovery, Narayan and Petesch say – 'but with a new twist' (good market information and organizational advice). Credit only becomes transformational when borrowers are supported (by government agencies or non-governmental organizations) so they 'enhance the quality of their product, connect to markets, and aggregate their goods for marketing in order to achieve scale and bargaining power'.

Rising from the Ashes of Conflict is remarkable for its focus on the community level (most other studies focus on the national level). The authors are impressed by large-scale programmes that manage to reach thousands of post-conflict communities. One example they cite is the National Solidarity Programme in Afghanistan, devised by Scott Guggenheim of the World Bank, the same person who set up the Kecamatan Development Program in Indonesia. The latter had US$1.6 billion at its disposal, making it the world's largest community-driven development programme.

These programmes offer a broad choice between different projects at the community level and a transparent participatory process, in the hope that a culture of accountability will grow bottom-up and ultimately also lead to changes at government level. The question is whether this is not somewhat over-optimistic.

What it ultimately comes down to, according to *Rising from the Ashes of Conflict*, is that conflict-affected communities fare better than other communities because they seem to attract

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more aid. The analysis in this book seems to corroborate the somewhat cynical belief of many rebel movements that violence helps to attract the attention of donors.

Is foreign investment the answer?

International financial institutions and some governments (Kosovo's, for example) put tremendous hope in foreign direct investment. The latter is meant to flow in once fighting stops. Derek Sweetman also sees a major role for foreign companies in post-war reconstruction. They could make a direct contribution to mediation and reconciliation. In his 2009 book, *Business, Conflict Resolution and Peacebuilding*, he points out that foreign direct investment remains concentrated in a few sectors, mostly the extractive industries, bottled drinks, mobile phones, tourism – to a lesser extent – and in the processing of agricultural products. It is remarkable that mobile telecom companies prosper most in countries with high levels of violence. Governments rarely succeed in attracting foreign investment to other sectors, which makes diversification difficult.

Sweetman argues that foreign companies can do more than serve purely as economic catalysts. They can also be decisive in creating more peaceful relations between (formerly) conflicting groups. There are more foreign than local private companies explicitly trying to combine business (which provides employment) with an attempt to contribute to reconciliation. Extractive industries that are sensitive to unrest in their operational areas often use tri-sector partnerships, in which business, government and non-governmental organizations work together.

Derek Sweetman gives several more examples of conscious efforts by companies to bring people from different factions together in common projects. But the overriding message that stays with the reader is the tremendous gap between the potential contribution private businesses could make and the actual contributions made by the private sector to address violent conflict and the challenges of post-conflict development. The author is highly optimistic that this gap will diminish in the future.

He fails to analyze the highly disputed role foreign capital will play in all this, however. There will often be an internationalist faction advocating, along with the warring factions, open markets. Opposing them will be a statist coalition advocating the use of local capital and arguing in favour of the protective role of the state. This can easily be observed in the new Balkan countries. That there are always domestic economic winners and losers from the transition to peace is well described in Galia Press-Barnathan's 2009 book *The Political Economy of Transitions to Peace*, which is not about post-conflict development after civil strife, but about peace after war between states. She analyzes the post-war relations between Israel and Egypt and Jordan, between Japan, the Philippines and Indonesia, between Japan and South Korea, and between Germany and France and Poland.

A great deal can be learned from these situations about post-war reconstruction in countries torn apart by civil war. Political gains (in terms of reconciliation) from economic cooperation between former warring parties (such as the gas deal between Egypt and Israel) usually do not materialize, and it is very difficult to formulate broadly accepted economic policies in countries with wide disparities of economic power.

Foreign investment can only be attracted in post-conflict countries, which are typically at the bottom of business climate rankings, when special conditions are created and concessions are made to win over foreign companies. These conditions have to be directly negotiated with government authorities. Unfortunately, this provides ample opportunity for shady under-the-table private deals. The need to attract foreign investment may well be associated with a strong incentive to put the house in order and stamp out corruption, but history shows that the opposite is often true. The political elite tends to cooperate with a handful of foreign companies, while most other firms stay away because the business climate is not attractive enough.

There is often a tension between measures used to improve the business climate (by increasing productivity) and the need to create employment. *Rebuilding War-Torn States*, the most comprehensive of the five books, identifies a five-pronged employment promotion strategy, which would not be at loggerheads with a better business climate:

- Subsidize domestic enterprises, financed through aid
- Hire and train targeted groups
- Support agricultural production
- Create special 'reconstruction zones' for exports and encourage investment by micro- and small-sized enterprises
- Invest in infrastructure.

These measures alone, however, probably will not provide enough jobs, which should be the most important objective of post-war economic development. Some bold national projects are needed to create employment and a common vision of a better future.

A need for bold national projects

Governments would do well to choose a strategic, specialized niche. *Rebuilding War-Torn States* cites the example of Rwanda, where fibre-optic cable has been laid throughout the country, which could make it a regional hub for internet-based services and communication. This is amazingly ambitious for a country with scarcely any skilled labour and energy supply shortages, where only 5% of the population at the time the book was written was connected to electricity, which was the most expensive in the region to boot.

None of the books reviewed makes this point, but these kinds of projects have a dual benefit. First, they create jobs and income. But they are also alluring projects that appeal to a large part of the young population, instil new national pride and help overcome historic cleavages. Such ambitious, large-scale projects could go in different directions. They could, for example, focus on large-scale environmental ventures, or on initiatives to create a regional hub for higher education. They could encourage innovation in health care, introduce intensive forms of agriculture or set up alternative energy initiatives. But these kinds of projects have little historical precedent. They may just be the pipe dreams of this review's authors. ■