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# Post-Conflict Private Sector Development: Promoting Durable Peace

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What are the characteristics and short comings of economic development in post-independent, sub-Saharan Africa: examples from Mozambique?

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**Indicative Abstract:** In times of war the private sector adapts, often to function informally, and can serve to either perpetuate conflict or to incentivize peace. Accordingly, the private sector is a powerful tool that can be utilized during post-conflict reconstruction to enable sustainable peace and economic development. After a conflict, in an effort to establish a means of survival outside of the war economy, there is a pressing need for the population to have a means by which to provide a livelihood and productively contribute to society. Establishing sustainable economic exchange and developing social capital between various members of society is one mechanism by which to achieve restorative justice and dis-incentivize conflict.

Building upon an evaluation of the literature and practice of post-conflict economic development, this paper argues for a hybrid approach to private sector development that includes both the investment climate and interventionist methods to dis-incentivize a return to conflict. Defining private sector development as the set of activities undertaken to promote growth and reduce poverty by developing a market-oriented private sector, this addresses “the twin goals of economic growth and peace ... to strengthen conditions for the growth of a stable, accessible, and competitive private sector and to contribute to a lasting and durable peace”.<sup>1</sup>

Analysis of the war economy and the costs of conflict build a foundation for an exploration of economic reconstruction and the need to provide economic incentives for peace. Conflict is not irrational and participants, whether civilian or combatants, must balance incentives, opportunities, and feasibility calculations to determine their participation in and reaction to conflict. Economic activity can incentivize, drive, prolong, or bring an end to violence; accordingly, it is imperative that those engaged in private sector development in post-conflict countries understand and acknowledge the importance of conflict-sensitive economic development to promote durable peace. To demonstrate these principles, this paper conducts a review of the evolution of international paradigms of economic development. Highlighting the failure of previous policies in addressing underlying causes of war, this paper heavily emphasizes the importance of governance and coordination among actors to prevent a relapse in violence. Citing examples from sub-Saharan Africa, this paper analyzes the paradigm shifts in approach to economic development and the implications of their respective implementation in post-conflict developing countries.

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<sup>1</sup> Bagwitz, Daniel; Becker, Sabine; Elges, Reinhold; Goretzky, Wulf; Hofmann, Armin; Hilal, Tarig; Krech, Robert; Kruk, Gabriele (2008): *Economic Development in Conflict- Affected Countries: A Practitioner's Note*. Eschborn, Ger: FIAS. Washington DC: GTZ. [www.enterprise-development.org/download.aspx?id=1283](http://www.enterprise-development.org/download.aspx?id=1283).

## Table of Contents

Introduction.....	4
<i>Overview</i> .....	4
<i>Analytical Approach</i> .....	6
<i>Limitations</i> .....	8
Chapter One: Economics and Conflict .....	9
<i>Economic Drivers of Conflict</i> .....	10
<i>War Economies</i> .....	14
<i>Cost of Conflict</i> .....	18
<i>Conclusion</i> .....	22
Chapter Two: Paradigms of Economic Reconstruction.....	23
<i>1960s – 1973: Post – Independence Economics</i> .....	25
<i>1973 – 1980s: Attempted Industrialization and Crisis</i> .....	26
<i>Mid-1990s – 2000s: Cautious Resurgence</i> .....	30
<i>Present Day Post-Conflict, Context Specific Economic Development</i> .....	30
<i>Structural Adjustment and Poverty Reduction Examples</i> .....	34
Chapter Three: Private Sector Development Framework.....	35
<i>Investment Climate: Macroeconomic Stabilization</i> .....	36
<i>Interventionist Approach</i> .....	41
<i>Governance and Growth Examples</i> .....	44
Chapter Four: Challenges in Implementation of Private Sector Development.....	45
<i>Aid Dependency and Distributive Issues</i> .....	45
<i>Sequencing of Activities</i> .....	49
<i>Coordination of Actors</i> .....	52
Conclusion .....	57

## Introduction

### Overview

In 2000, the World Bank released “Can Africa Claim the 21<sup>st</sup> Century?” in which it outlined four steps for sub-Saharan African countries to realize their potential: (1) invest in people (education, health, skill training, gender equality); (2) improve governance and resolve conflict (address poverty-conflict cycle of underdevelopment, marginalization, and lack of economic diversification); (3) increase competitiveness (encourage investment by mitigating risk and uncertainty, integration and diversification of the economy); and (4) reduce dependency on aid.<sup>2</sup> These generic, four steps are necessary for growth in most developing countries; however, in sub-Saharan Africa the highlighted role of conflict in hindering the growth process is notable. It is apparent that “economic, social, and institutional change is possible” in the African context, but many countries “still face substantial governance and economic constraints to growth” heavily influenced by their post-conflict contextual realities.<sup>3</sup>

Ending conflict, achieving political stability, and improving governance are foundational requirements for improved macroeconomic policies enabling economic growth. African countries must continue to re-energize markets by improving the investment climate (decreasing inflation, foreign debt, and budget deficit; stabilizing exchange rates; reducing trade barriers; cutting corporate taxes; and privatizing enterprise) to encourage business. Furthermore, enhancing regional and international, as well as public, private, and local integration and investment, will enable more African countries to reach economies of scale and become competitive leading to sustainable economic growth in the future. Increasing demand and prices for natural resources, while providing much needed growth, will not sustain Africa without good governance, investment in human capital, and continued diversification into other sectors as seen in the last decade.

If war is a continuation of economics by other means,<sup>4</sup> this thesis argues that proper development of post-conflict economies, specifically the private sector, may assist mitigation of incentives for war and enable durable peace while promoting economic growth. Post- conflict

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<sup>2</sup> Gelb, Alan; Ali, Ali AG; Dinka, Tesfaye; Elbadawi, Ibrahim; Fosu, Augustin; Mlambo, Kupukile (2000): *Can Africa Claim the 21<sup>st</sup> Century?*. Washington, DC: The World Bank.

<sup>3</sup> Kaufmann, Daniel (2011): *On Africa's New Dawn: From Premature Exuberance to Tempered Optimism*. Washington DC: Brookings Institute. [http://www.brookings.edu/opinions/2011/0607\\_africa\\_new\\_dawn\\_kaufmann.aspx](http://www.brookings.edu/opinions/2011/0607_africa_new_dawn_kaufmann.aspx)

<sup>4</sup> Keen, David (1998): *The Economic Functions of Violence in Civil Wars*. Oxford: Oxford University Press for the International Institute for Strategic Studies.

reconstruction literature and practice widely acknowledge the importance of economics during times of both peace and war. An emphasis on negative economic aspects of conflict includes the greed vs. grievance debate, the power of war economies, and the role of a predatory private sector. In light of this, recent research and practice highlight economic incentives for peace and the positive impact of private sector development on transitioning societies.

Post-conflict ‘private sector development’ (PSD) is defined as the set of activities undertaken to promote growth and reduce poverty by developing a “productive, sustainable, and market-oriented private sector.”<sup>5</sup> This strategy addresses “the twin goals of economic growth and peace, in other words, to strengthen conditions for the growth of a stable, accessible, and competitive private sector and to contribute to a lasting and durable peace.”<sup>6</sup> In times of war, the private sector adapts, often to function informally, and can serve to either perpetuate conflict or to incentivize peace. Accordingly, the private sector should be utilized during post-conflict reconstruction to enable sustainable peace and development.

This paper seeks to explore the paradigm shifts<sup>7</sup> in approach to economic development and the implications of their implementation in post-conflict developing countries. By critically evaluating the literature and practice of economic development in post-independent sub-Saharan Africa, this paper argues in support of the private sector development framework’s hybrid approach of investment climate reform and interventionist strategies, as outlined by the Donor Committee for Enterprise Development (DCED). During the restoration phase of post-conflict reconstruction there is a “need to balance demands for greater economic growth with those for greater social justice and human welfare. A series of changes and promises to deal with grievances are likely to have been agreed to and underpin any peace deal; to ignore these and to impose generic policies for economic growth... may have high short run costs [and] may well simply lead to a reigniting of hostilities.”<sup>8</sup>

Fortunately, the PSD approach is conflict-sensitive, allowing for simultaneous pursuit of short and long-term goals, engagement of the public sector promoting governance and stability, and allowing integration with other post-conflict recovery work including humanitarian relief,

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<sup>5</sup> Sweeney, Naoise Mac (2008): *Private Sector Development in Post-Conflict Countries: A Review of Current Literature and Practice*. Cambridge: Donor Committee for Enterprise Development (DCED).

<sup>6</sup> Bagwitz, Daniel; Becker, Sabine; Elges, Reinhold; Goretzky, Wulf; Hofmann, Armin; Hilal, Tarig; Krech, Robert; Kruk, Gabriele (2008): *Economic Development in Conflict-Affected Countries: A Practitioner’s Note*. Eschborn, Ger: FIAS. Washington DC: GTZ. [www.enterprise-development.org/download.aspx?id=1283](http://www.enterprise-development.org/download.aspx?id=1283).

<sup>7</sup> The paradigm shifts in the Bretton Woods Institutions’ approach refers to structural adjustment under the Washington Consensus, poverty reduction strategies, and the current private sector development framework.

<sup>8</sup> Dunne, John Paul (1996): Post-conflict Mozambique and Rwanda compared. *The Economics of Peace and Security Journal*, 1(2):39-46.

security sector reform, and socio-economic development. However, in spite of economic growth and a sustained peace, examples from Mozambique highlight two major failures of the paradigm: (1) aid dependency and (2) distributive issues. The final chapter of this paper will address implementation challenges and the importance of appropriately sequencing PSD and coordinating actors to address socio-economic challenges.

### **Analytical Approach**

This paper is a qualitative survey of both the literature and practice of post-conflict private sector development (PSD). Accordingly, the relevant research will utilize both primary and secondary sources, building on knowledge of economists, academics, and development practitioners concerning general trends and the evolution of post-conflict economic reconstruction to develop the private sector. After providing a descriptive, fundamental understanding of the economic impact of conflict on a society, this paper will analyze the evolution of economic development paradigms in sub-Saharan countries with an emphasis on post-conflict states.

Post-conflict private sector development, and broader economic reconstruction, must be distinguished from general best practices for development. The objectives of post-conflict private sector development include sustainable peace and economic growth; in this context, traditional indicators and practices for economic development must be adjusted accordingly. Historically, the international paradigms have focused on “technical solutions to private sector development such as better roads, more power generation, and reduction of the regulatory burden”; but this does not adequately address grievances and incentives for conflict or government capacity to prevent relapse to violence.<sup>9</sup>

In the 1990s, the Bretton Woods Institutions, donor countries, and development organizations failed to acknowledge the significance of conflict-context-specific policies “as if war-torn countries could isolate their economic programs from the political and security realities of the aftermath of war.”<sup>10</sup> Fortunately, the failure of isolated macroeconomic stabilization programming led to a paradigm shift that incorporated human security and good governance into poverty reduction economic development and reconstruction strategies. While these policies

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<sup>9</sup> Eifert, Benn; Gelb, Alan; Ramachandran, Vijaya (2005): *Business Environment and Comparative Advantage in Africa: Evidence from the Investment Climate Data*. ICA Paper. World Bank.

<sup>10</sup> del Castillo, Graciana (2011): *The Economics of Peace: 5 Rules for Effective Reconstruction*. Washington, DC: United States Institute of Peace, Special Report 286.

have been met with some success, recent literature calls for greater public sector engagement in the development of the private sector for sustained growth and peace in post-conflict countries.

The PSD paradigm of the early 2000s was one in which “the poor relied on [small enterprises] for their livelihoods” and because “these businesses were disadvantaged...that justified subsidizing their access to knowledge and finance” leading to aid dependency and a lack of incentives for institutional and policy change.<sup>11</sup> While focusing on facilitating a better livelihood for the poor, such approaches are still insufficient for private sector development promotion of peace in post-conflict countries. Accordingly, while the current private sector development framework successfully addresses many of the flawed policies of the 1960s - 1990s, it still falls short of effectively establishing a mature private sector; instead, countries face high aid dependency and distributive issues. These problems have negative implications for the development of public sector capacity and legitimacy, entrepreneur activity, and private sector production of goods and services.

Utilizing brief, illustrative examples from Mozambique, this paper will first assess the International Financial Institutions’ private sector ‘solutions’ to growth from the 1960s - early 1990s and the reality of their failure to acknowledge the implications of on-going conflict across sub-Saharan Africa. This period will be contrasted with the late 1990s post-structural adjustment policies of poverty reduction that acknowledged the importance of governance and building capacity of the post-conflict public sector. The later begins to address the causes of conflict and escalating factors that incentivized violence. A shift in focus to supporting economic actors in crisis prevention, conflict transformation, and peace building represents strategic lines of intervention for the private sector.<sup>12</sup> While rapid growth during this period has received praise, the significance of impact is misleading as illustrated by two different perspectives of Mozambique:

One is of rapid GDP growth and growing exports and of transparent and clear management of donor money. The other is of worsening poverty in rural areas and of state capture, with predatory elite that robs banks and non-donor resources, smuggles and kills, and maintains a corrupt justice system. A symbiotic relationship has grown up between the Mozambican predatory elite and the donors to maintain the myth of the Mozambican success story.<sup>13</sup>

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<sup>11</sup> OECD (2004): *Accelerating Pro-Poor Growth Through Support for Private Sector Development*, 57.

<sup>12</sup> Bagwitz et al. (2008)

<sup>13</sup> Hanlon (2004: 760) as quoted in Bertelsen, Bjorn Enge (2005): *War, Peace, and Development in Mozambique: A Critical Assessment*. (Presented Workshop Paper). Bergen: Chr. Michelsen Institute, 66.

For the purposes of this paper, conflict—the antithesis of development—will include both intra and interstate conflict with Mozambique serving as a clear example of the devastation of intrastate conflict in sub-Saharan Africa.<sup>14</sup> Post-conflict reconstruction and recovery will be used interchangeably to signify “the long-term rebuilding of a society in the aftermath of violent conflict” including “political, socioeconomic, and physical aspects such as disarming and reintegrating combatants, resettling internally displaced persons, reforming governmental institutions, promoting trauma work and reconciliation, delivering justice, restarting the economy, and rebuilding damaged infrastructure,” among other activities.<sup>15</sup> It is not only the physical violence or “more obvious destruction of capital that [comes] out of the conflict but [also] the less visible damage to institutions, markets, and confidence, [as well as] the persistence of subsistence agriculture for the majority of the population” that plagues a country for years to come as demonstrated by the civil war in Mozambique.<sup>16</sup>

Building upon an evaluation of the contextual realities of post-conflict countries and the international paradigms for economic development, this paper argues for: (1) a hybrid approach to PSD that includes both the investment climate and interventionist frameworks to disincentive a return to conflict; (2) private sector development that facilitates the building of public sector capacity and legitimacy; and (3) a discussion of aid dependency and the importance of an integrated reconstruction strategy that enables capacity building and greater coordination of stakeholders.

### **Limitations**

In explaining social, political, and economic consequences of conflict, this paper will highlight general trends with the understanding that each case is different and that private sector development must be conflict sensitive and situation specific. Furthermore, it is beyond the scope of this paper to adequately address the wealth of literature concerning all causes of conflict and post-conflict reconstruction; therefore, this analysis will focus on the field of private sector development while acknowledging the importance of its integration with humanitarian relief, rule of law, security sector reform, human development, and transitional justice for sustainable peacebuilding and development. As it concerns examples from Mozambique, this paper will reference, but not significantly analyze, the implications of environmental or health factors and

<sup>14</sup>Collier, Paul (2003): *Breaking the Conflict Trap: Civil War and Development Policy*. Oxford: Oxford University Press & Washington, DC: The World Bank.

<sup>15</sup> USIP Glossary of Terms. “Post-Conflict Recovery.” (2012) <http://glossary.usip.org/resource/post-conflict-recovery>

<sup>16</sup> Dunne, Paul (2006): After the Slaughter: Reconstructing Mozambique and Rwanda. *Economics of Peace and Security Journal* 1(2):39-46.

their contributions to the Mozambican economy; this includes the droughts and famines of the 1990s as well as the HIV / AIDs crisis. Lastly, it should be noted that this paper addresses the high level paradigm of economic development and their implementations; it will not extrapolate to including monitoring and evaluating of specific programming.

This paper will not address the dynamics of conflict intervention, negotiation / mediation, and resolution; neither is the argument differentiating peacekeeping, peacemaking, and peacebuilding relevant. For the purposes of this paper, peacebuilding is one critical aspect of post-conflict reconstruction. Economic development plays a significant role in disincentivizing a return to violence and therefore assists in facilitation of this endeavor. Academics and development practitioners often differentiate between the stages of conflict and reconstruction in regards to which interventions are appropriate at given time periods; the author of this paper acknowledges the importance of this consideration without recommending one best practice approach.

## **Chapter One: Economics and Conflict**

The study of conflict and conflict prevention is interdisciplinary in nature. Today's prevalence of intrastate conflict has numerous social, political, and economic triggers (i.e. "the attainment of political independence or statehood, regime change, and military coups; elections; neighboring conflicts; and other dramatic events") as well as various risk factors (i.e. "presence of natural resources; low income; low economic growth; ethnic [or religious] antagonisms; neighborhood effects and external instigation of armed conflict; geography and large populations; a youth bulge, especially proportionally very large numbers of men between 15 to 29 years of age; political repression and corruption; competition for scarce resources; inequality; religious extremism; flawed or incomplete transition to democracy; high military expenditure and large armies; diasporas; colonialism and superpower rivalries; and the existence of previous conflicts)."<sup>17</sup> Although this study will not focus on social and political drivers, it is important to acknowledge that economic factors do not operation in isolation; for example, economy activity requires state provision of security, governance, and legal frameworks for protection of economic exchange or property rights.<sup>18</sup>

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<sup>17</sup>Brauer, Jurgen and Dunne, Paul (2010): *Chapter 13: Macroeconomics and Violence*, in: Braddon, D. and Hartley, K. (eds.), Handbook on the Economics of Conflict. Cheltenham, UK: Edward Elgar Publishing.

<sup>18</sup> This author acknowledges the limitations of a sole focus on economic drivers of war and the potential of flaw use of proxies and data limitations in the quantitative studies discussed in this chapter.

Economics play three different roles as it concerns conflict: (1) grievances before war, (2) funding / provision of resources during war, and (3) production and exchange mechanisms after war and during reconstruction.<sup>19</sup> In addressing the economic drivers and effects of conflict, this chapter will discuss the evolution in understanding the role of economics and conflict through the greed versus grievance debates, resource competition, war economies, the rise of the informal sector, distortions of capital and labor, and both immediate and legacy cost of conflict. This analysis will dispel the myth that markets and the private sector fail to operate during times of conflict; instead, they adapt but face heavy costs and risks in an insecure environment. An understanding of the economic drivers and effects of conflict highlights opportunities for public sector policies and private sector solutions as “economic policies implemented during a war will determine the size and nature of the country’s long-term peace dividend”.<sup>20</sup> By deconstructing the cost of conflict, this chapter will lay the foundation for a discussion of the economic incentives for peace and post-conflict reconstruction in ensuing chapters.

### **Economic Drivers of Conflict**

In both World Wars, and even during the Cold War, the major actors in violent conflict were States with set rules of engagement and specific agendas. Governments had complete sovereignty with little international pressure concerning what took place within a country’s borders, and warring parties acknowledged the distinction between civilians and soldiers. Furthermore, wars were fought to win; they ended in clear victory with agreements to dictate a return to peace. In the post-Cold War era, developing countries lost significant foreign aid, which negatively impacted their ability to use resources for service provision, patronage, or even to pay militaries. For some, war became a profession, an opportunity for looting, and a form of enterprise creating conditions of durable conflict allowing fighting in perpetuity. Accordingly, the 1990s witnessed the rise of civil wars and armed conflicts that brought about complex emergencies, loss of distinction between civilians and insurgents, increased arms, horrific atrocities including genocide, and a political war economy. These new wars have three major cyclical indicators: (1) the greatest predictor of this type of war is a previous war as 50% of civil wars will revert back to armed conflict within 5 years; (2) while conflict is development in

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<sup>19</sup> Brauer, Jurgen and Dunne, Paul (2010)

<sup>20</sup> Brück, Tilman (1997): *Macroeconomic Effects of the War in Mozambique*. (Working paper number 11.) Oxford: Queen Elizabeth House, University of Oxford.

reverse, poverty and underdevelopment increase a country's propensity to wage war; and (3) insecurity breeds violence, and negotiated peace arrangements that fail to bring security to citizens create a state of "not war, not peace".<sup>21</sup>

The rise in the number of civil wars has numerous context-specific political, social, and economic drivers that can be divided into four categories: (1) causes that fuel incentives or motives for participating in violence; (2) causes that facilitate the mobilization and expansion of violence; (3) causes found at the level of state capacity to manage and respond to violence; and (4) causes of a regional or international nature.<sup>22</sup> While drivers of conflict are not direct causal mechanisms, the presence of various factors within a country increases the likelihood and risk of conflict requiring that public, private, and civil society actors appropriately address such incentives and means by which others seize opportunities for conflict.

In analyzing economic causes of civil wars, Collier & Hoeffler conducted a quantitative study to explore the impact of per capita income and natural resources (proxies for taxable base), population size, and ethno-linguistic fractionalization on the occurrence and duration of conflict. They found that conflict occurs when incentives outweigh cost, making it a rational decision.<sup>23</sup> These conclusions are supported by the finding that high per capita income decreases the duration and probability of conflict, supporting the idea that poorly developed and low-income countries are more likely to engage in intrastate conflict. In making the decision to undertake conflict, rebel groups must consider numerous opportunity cost including the disruption of existing economic activity and the cost of fighting labor; accordingly, expected duration of conflict and the probability of conflict decreases for those countries with higher incomes per capita (i.e. higher opportunity cost). Additionally, the probability of rebellion decreases as the taxable base increases—the rationale being that increases in government revenue allow for an increase in military spending and the provision of security by the government, making the cost of conflict higher for rebels.

Collier & Hoeffler corrected their 1994 theory that rebel movements incur net costs during conflict, and instead they juxtaposed the opportunities for rebellion against the constraints, generating the infamous greed and grievance theory.<sup>24</sup> In analyzing greed (financing

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<sup>21</sup> Collier, Paul (2003)

<sup>22</sup> USAID (2004): *Conducting a Conflict Assessment: A Framework for Strategy and Program Development*. Washington, DC: USAID, 3.

<sup>23</sup> Grossman (1995) and Hirschleifer (1995) are economic theories that consider war a rationale choice; Grossman, H. I. (1995): *Chapter 8: Insurrections*, in: Hartley, K. and Sandler, T. (eds.), *Handbook of Defense Economics*, 1(1):191-212. Amsterdam: Elsevier.

<sup>24</sup> Collier, Paul; Hoeffler, Anke (2004): Greed and Grievance in Civil War. *Oxford Economic Papers*, 56(4): 563-595.

of a rebellion) and grievance (ethnic and religious divisions), the authors found that the economic drivers of greed theory have more explanatory power of incidence of civil war. Rebellion financing includes (1) extortion of primary commodity exports / natural resources, (2) diasporas' donations, and (3) subvention from other governments.<sup>25, 26</sup> In understanding causes of conflict as functions of preference, opportunities, and perceptions,<sup>27</sup> Collier & Hoeffler use per capita GDP, growth, social fractionalization, the ratio of primary commodity exports / GDP, and population size as proxies for opportunity.

Research shows that the incidence and opportunity for conflict is influenced by availability of finance (discussed previously), cost of rebellion (education, per capita income, growth rate, etc.), and military advantage. The ability of rebels or governments to finance conflict may also be related to availability of natural resources.<sup>28</sup> The impact of natural resources on conflict incidence and duration is non-monotonic; at high levels, the presence of natural resources can increase the financial capacity of the government to increase military expenditures and provide security, preventing conflict.<sup>29</sup> On the contrary, the initial presence of resources may increase the incidence and duration of conflict serving as both an incentive and means for waging war. To unpack this further, primary commodity exports increase the risk of conflict in two ways: (1) if extorted, they help fund rebellion and (2) resource dependence may negatively impact governance, enhancing grievances among the population and incentivizing rebellion.<sup>30</sup> Additionally, provision of finance for rebellion by the diaspora increases the risk of conflict. Opportunity costs for violence are defined as “proxying earnings foregone in rebellion.”<sup>31</sup> In concluding that greed motivates conflict, as explained with opportunity indicators, Collier & Hoeffler qualify that rebels are not “necessarily criminals, but the grievances that motivate rebels may be substantially disconnected from the larger social concerns of inequality, political rights, and ethnic or religious identity”.<sup>32</sup>

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<sup>25</sup> There is a wealth of literature on hostile governments funding rebel groups as well as the role of external military intervention and its impact on the duration of conflict (see Elbadawi and Sambanis 2000).

<sup>26</sup> Collier, Paul; Hoeffler, Anke (2004)

<sup>27</sup> Hirschleifer, J (1995): Chapter 7: Theorizing about conflict, in: Hartley, K. and Sandler, T. (eds.), *Handbook of Defense Economics*, 1(1):165-192. Amsterdam: Elsevier.

<sup>28</sup> Exploitation and confiscation of the population's economic assets whether through taxation or looting also finance conflict as depicted in Kalyvas, Stathis N (2001): New and old civil wars: a valid distinction? *World Politics*, 54(1):99-118. Cambridge: Cambridge University Press. This explores the control of civilians by insurgents and governments and the impact on conflict duration; this is related to civilian victimization, waging of war, and rebel recruitment.

<sup>29</sup> Collier, Paul; Hoeffler, Anke (1998): On Economic Causes of Civil War. *Oxford Economic Papers*, 50(4): 563-573.

<sup>30</sup> Collier, Paul; Hoeffler, Anke (2004)

<sup>31</sup> Collier, Paul; Hoeffler, Anke (2004)

<sup>32</sup> Collier, Paul; Hoeffler, Anke (2004)

In the 2009 study, “Beyond Greed and Grievance: Feasibility and Civil War,” Collier & Hoeffler<sup>33</sup> address the financial and strategic feasibility of rebel groups engaging government forces in a civil war. While their previous work focused on motivation for rebellion, this paper highlights basic feasibility. Building upon the Machiavelli Theorem that no profitable opportunities for violence will go unused, the authors suggest a feasibility hypothesis “that where a rebellion is financially and militarily feasible it will occur.”<sup>34</sup> In confirming results from their 1998 and 2004 studies, the authors find that the level, growth, and structure of income are significant. In 2009, Collier & Hoeffler put forth three channels through which the ‘structure’ of income, inclusive of primary commodities, relates to increased risk of conflict. The three channels of financing rebellion include: (1) preying on the population, (2) capturing commodity rents, and (3) capitalizing on the fact that resource-rich countries are less accountable to their populations, allowing exposure of the people’s grievances.<sup>35</sup>

There is much consensus on the role of per capita income in influencing the risk of conflict, but this indicator has been utilized differently by political scientists Fearon and Laitin and economists Collier & Hoeffler. As opposed to viewing per capita income as a measure of opportunity cost for rebellion like the economists, Fearon and Laitin use income as a proxy for effectiveness of the state and ability of government to deter rebellions. This leads them to conclude that a financially, bureaucratically, and militarily weak government increases the risk of civil war.<sup>36</sup> In support of Collier and Hoeffler’s research, Fearon and Laitin find poverty, political instability, rough terrain, and large populations to best explain countries at risk for civil war. While they support the idea that financial potential for rebels is a driver of conflict, Fearon and Laitin critique Collier and Hoeffler’s idea that primary commodity exports are an accurate proxy of financing potential for rebels; they believe that this variable encompasses oil, agricultural products, metals, and minerals which may be hard to exploit without robust infrastructure and distribution systems. They argue that a better measure would be that of “presence of minerals or contraband that can reward control of a small enclave with huge profits.”<sup>37</sup> In summary, Fearon and Laitin find that “state weakness marked by poverty, a large

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<sup>33</sup> In this study the authors identify three non-economic indicators that are statistically significant and support the feasibility hypothesis: the French security umbrella, the proportion of young men in the population, and the proportion of the terrain which is mountainous.

Collier, Paul; Hoeffler, Anke; Rohner, Dominic (2009): Beyond Greed and Grievance: Feasibility and Civil War. *Oxford Economic Papers*, 61(1):21-22

<sup>34</sup> Collier, Paul; Hoeffler, Anke; Rohner, Dominic (2009)

<sup>35</sup> Collier, Paul; Hoeffler, Anke; Rohner, Dominic (2009)

<sup>36</sup> Fearon, James; Laitin, David (2003): Ethnicity, Insurgency, and Civil War. *The American Political Science Review*, 97(1):88.

<sup>37</sup> Fearon, James; Laitin, David (2003)

population, and instability – are better predictors of countries at risk for civil war than indicators of ethnic and religious diversity or measures of grievance such as economic inequality, lack of democracy or civil liberties, or state discrimination against minority religions or languages.”<sup>38, 39</sup>

Sambanis reviews the quantitative literature on civil war utilizing economic theory, political rational choice theory, international relations theory, and constructivist theory. In addressing the discrepancies concerning the coding of civil wars and the limitations of current literature, there are four major points of consensus: “first, poverty exacerbates the risk of civil violence; second, ethnic diversity need not increase the risk of civil violence and may actually decrease it; third, excessive dependence on easily lootable natural resources increases the risk of conflict; [and] fourth, mountainous or heavily forested terrain facilitates insurgency.”<sup>40</sup> Blatman and Manuel summarizes that “civil war is more likely to occur in countries that are poor, are subject to negative income shocks, have weak state institutions, have sparsely populated peripheral regions, and possess mountainous terrain.”<sup>41</sup> However, they acknowledge that research still fails to distinguish between which drivers cause war and which are symptomatic of other systemic problems. The aforementioned quantitative studies have been complimented by qualitative, case study literature focused on the linkages between drivers and conflict incidence. It is important to remain mindful that some indicators contribute to both incidence and duration. An understanding of economic variables that influence either or both the onset and duration of war is important for prevention and monitoring mechanisms; additionally, it is also relevant to analysis and critical engagement of the functioning of war economies to identify ways to incentivize an end to conflict.

### **War Economies**

The ability to sustain conflict requires financial resources; accordingly, the continual struggle for income to sustain fighting has often lead to the exploitation of resources, whether commodities or human capital. While countries in conflict face significant economic costs and

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<sup>38</sup> Fearon, James; Laitin, David (2003)

<sup>39</sup> It must be noted that the economic explanations of civil war onset are not without their critics. Other scholars critique the flawed use of proxies and the conclusion that motives for violent behavior can all be categorized as greed. For example, economic inequality and power struggles (grievances) may also motivate violent action (Herbst 2000 and Kalyvas 2001).

Herbst, J (2000): *Economic, political, and social incentives in the organization of rebellion in Africa*. Paper prepared for the World Bank conference on “The Economics of Political Violence.” Princeton, NJ: Princeton University, 18–19 March 2000.

Kalyvas, Stathis N (2002)

<sup>40</sup> Sambanis, Nicholas (2010): A Review of Recent Advances and Future Directions in the Quantitative Literature on Civil War. *Defense and Peace Economics*, 13(3):215-243.

<sup>41</sup> Blatman, Christopher; Miguel, Edward (2010): Civil War. *Journal of Economic Literature*, 48(1):22.

distortions to market operations, economic exchange continues to occur. War economies are “the cluster of economic activities that feed into and flow out of conflict, requir[ing] an extremely high level of instability to function and hav[ing] a corrosive effect on state institutions.”<sup>42</sup> The previous section addressed the variables that increase the risk of conflict, many of which also impact the duration of conflict and the persistence of the war economy as illustrated by the incentives for war.

During war, there are three economies in operation: exchange, grants, and appropriations. The first addresses the trade of goods and services that may be interrupted during conflict due to insecurity and destruction of trade relations and infrastructure. Grants include transfer of resources such as foreign aid that may be exploited by either side of the conflict as seen with food aid to Somalia in the 1990s. In this manner, aid can be detrimental and utilized by warlords to exploit the population, or aid can negatively impact market structures leading to anomalies. Appropriations concerns the involuntary taking of economic resources, inclusive of both taxation and robbery; “the salience of appropriates economies lies in the need to establish a credible and enforceable social contract within, between, and among communities and societies.”<sup>43</sup> This last type of ‘war economy’ alludes to the role of crime resulting from insecurity during periods of war.

The presence of resources may impact the onset and duration of conflict by financing violence (i.e. the presence of oil and diamonds in Angola); however, resources controlled by the state can also dis-incentivize conflict by generating revenue for military spending and security provision.<sup>44</sup> Le Billion discusses the ‘resource defense dilemma’ where separate groups increase their defense capacity in an effort to secure resources as seen with various actors operating in the Democratic Republic of Congo. Similar to the security dilemma, these actions are viewed as threats to other actors and raise the stakes for conflict. In the presence of state collapse, combatants resort to violence as “the prim[ary] means of political action, economic accumulation, or simply survival” which may be provided from resource rents.<sup>45</sup> In addition to resources financing conflict, commodities or natural resources upon which a state is heavily

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<sup>42</sup> USAID (2004)

<sup>43</sup> Brauer, Jurgen and Dunne, Paul (2010)

<sup>44</sup> Collier, Paul and Hoeffler, Anke (2001): Data Issues in the Study of Conflict. Paper prepared for the conference on “Data Collection on Armed Conflict.” Uppsala, Sweden, 8-9 June 2001.

<sup>45</sup> Le Billion, Phillipe (2001)

dependent may initially impact the incidence of state failure, as exemplified by the decline in coffee exports in Rwanda prior to the 1994 genocide.<sup>46</sup>

In conflict, the state may control core areas and key economic zones but not the hinterland due to economic rationalization; in these environments, there is little incentive and great cost to consolidate power and provide security. This insecurity coupled with declining production and the need for resources influences a loss in assets and human resources “due to the importance of force and coercion during conflict, which often means that economic assets are forcibly taken control of by conflict actors, and some economic sectors are ‘captured’ by factions or interest groups. Informality of the economy is both favorable to, and partly created by, the predatory private sector.”<sup>47</sup> Accordingly, businesses and individuals must develop ‘coping strategies’ given the distortion of normal commercial patterns and the decline in both production and consumption.<sup>48</sup> The rise of the informal economy in regards to black markets, trafficking (humans, drugs, or arms), resource exploitation, entrepreneurial activity that promotes horizontal inequalities, and sanctions-busting activities is widespread and may often be necessary for survival.

Duffield<sup>49</sup> acknowledges the importance of recognizing the operations of the informal sector during and after conflict; this provides both a means of livelihood for many and can foster criminal and destructive behavior for others. Given a lack of regulations and standardized systems of procedure during conflict, private sector activities may be irregular and opportunistic with decreases in the scale of economic activity being partially responsible for informality.<sup>50</sup> The informal economy is characterized by underreported employment, tax evasion, and significant lack of regulations. Informality is on the rise in many countries, especially those that are labor-intensive, as a result of higher tax burdens and cuts in government enforcement budgets. The decision for economic actors to engage informality is dependent upon (1) limited enforcement of legal obligations, (2) cost of operating formally, and (3) social norms.<sup>51</sup> Government corruption and inability to devote resources to regulate the economy, in both conflict and post-conflict environments, may incentivize the rise of this means of economics. The short-term benefits of

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<sup>46</sup> Le Billion, Phillipe (2001)

<sup>47</sup> Sweeney, Naoise Mac (2008): 21.

<sup>48</sup> Bray, John (2007): *The Role of Private Sector Development in Post-Conflict Economic Recovery*. UNDP Report.

<sup>49</sup> Duffield, Mark (1998): Post Modern Conflict: Warlords, Post-Adjustment States and Private Protection. *Journal of Civil Wars*, 1(1):65-102. Duffield, Mark. *Global Governance and the New Wars: The Merging of Development and Security*. London, Zed Books, 2001.

<sup>50</sup> Sweeney, Naoise Mac (2008) 21.

<sup>51</sup> Farrell, Diana (2004): Hidden Dangers of the Informal Economy. McKinsey Quarterly, McKinsey and Company. [https://www.mckinseyquarterly.com/The\\_hidden\\_dangers\\_of\\_the\\_informal\\_economy\\_1448](https://www.mckinseyquarterly.com/The_hidden_dangers_of_the_informal_economy_1448)

informality include a rise in economic productivity, growth, and employment as well as potential alleviation of socio-economic unemployment issues that are not addressed during conflict. However, long-term implications include distortion of competition, limited productivity, and overall economic inefficiency. The damaging effects on productivity and economic growth are witnessed as the informal economy takes market shares from bigger, formal companies as others avoid taxes and regulations promoting grievances and dis-incentivizing compliance with legal policy. These actions undercut more productive companies that would normally take a larger share of the market. Accordingly, the rise of informality discourages investments, new technology, and best practices operating methods.<sup>52</sup>

Poor regulation and insecurity enable looting during war; however, Menkhaus discusses the interest of non-state actor during protracted conflict in which ‘warlords’ may become ‘landlords.’ Building upon Charles Tilly’s work in Europe, Menkhaus states that “warlords accumulat[e] wealth by plunder to a point where their interests shift towards systems of protecting rather than looting property” even “at the lowest ranks of gunmen as well as the wealthiest merchants,” thus impacting the functionality of the war economy.<sup>53</sup> The actual waging of war has economic considerations specifically as it concerns the decision to participate in violence and to engage in civilian victimization.<sup>54</sup> Downes explains that governments fighting guerilla insurgencies use civilian victimization for two reasons: (1) to dis-incentivize the people from supporting the rebellion and / or (2) to remove the population, making it impossible for them to help insurgents.<sup>55</sup> Accordingly, the type of resistance or violence employed then factors into “the cost and difficulty of achieving military victory.”<sup>56</sup> In this manner, violence alters the cost-benefit calculations of civilians as well as that of combatants. The challenging balance for combatants is that “a group’s abusiveness may destroy the human and physical base of the local economy on which armed groups often depend”; however, “too much violence might lead civilians to flee, undermining a group’s ability to obtain the support it needs to survive.”<sup>57</sup> The case study of Sierra Leone illustrates that individuals have the agency to rationally assess their

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<sup>52</sup> Farrell, Diana (2004)

<sup>53</sup> Menkhaus, Kenneth (2003): *From Warlord to Landlords: Non-State Actors and Humanitarian Norms in Somalia*. Draft as provided by author, 3.

<sup>54</sup> Kalyvas, Stathis N (2001)

<sup>55</sup> Downes, Alexander (2008): *Targeting Civilians in War*. Cornell, NY: Cornell University Press. As provided by the UCT Course Reader, 176.

<sup>56</sup> Downes, Alexander (2008):

<sup>57</sup> Humphreys, Macartan and Weinstein, Jeremy (2006): Handling and Manhandling Civilians in a Civil War. *American Political Science Review*, 100(3):429-447.

socio-economic position (wealth) and the opportunity cost (i.e. education) of joining the rebel group RUF.<sup>58</sup> These and other<sup>59</sup> micro-economic foundations of an individual’s behavior in war further support Collier and Hoeffler’s macroeconomic conclusions of the relevance of greed and feasibility to the onset and duration of conflict.

**Cost of Conflict**

The most apparent negative effect of war is the human cost in loss of life; however, post-WWII intrastate wars are relatively small and have less than 1,000 battle deaths. Nonetheless, they face heavy economic cost.<sup>60</sup> Collier estimates that countries experience a 2.2% annual loss of GDP per year of conflict.<sup>61</sup> While some costs of conflict may be measured in the short term using accounting methods, it is understood that there are long-term effects as seen with a counterfactual measurement approach (Figure 1.1<sup>62</sup>).

Figure 1.1 Counterfactual Cost of Conflict

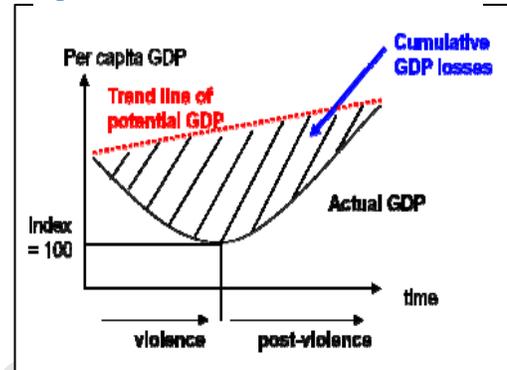
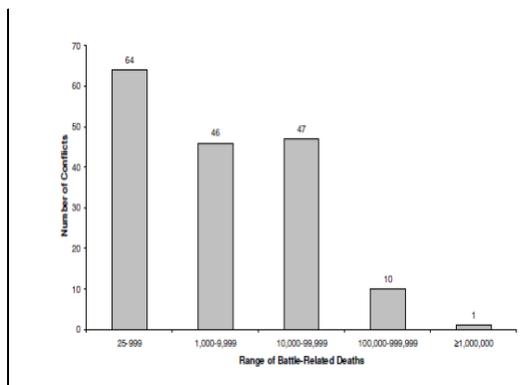


Figure 1.2 Range of Battle-Related Deaths



estimates include human cost (in regards to deaths and casualties), displacement (refugees or IDPs), military expenditures (of governments and rebel groups), loss of assets (capital destruction), production loss (of GDP and income), reduction in trade, and indirect costs encompassing inequality, human capital effects, and spill-over.

Before discussing the negative cost of conflict, it is important to acknowledge the

‘positives’ as illustrated by the theory of primitive accumulation<sup>63</sup> in which war is simply a part of the economic development process. This is similar to the idea of creative destruction and

<sup>58</sup> This paper acknowledges that societal pressures and vulnerability to coercion also influence an individual’s decision to join the RUF. Humphreys, Macartan and Weinstein, Jeremy (2008): Who Fights? The Determinants of Participation in Civil War. *American Journal of Political Science*, 52(2):436–455.

<sup>59</sup> Gates, S (2002): The Microfoundations of Rebellion. *Journal of Conflict Resolution*. 46(1):111-130. Oslo: PRIO & Michigan State University.

<sup>60</sup> Cost due to health, environment, displacement, or legacy cost are higher

<sup>61</sup> Collier, Paul (1999): On the Economic Consequences of War. *Oxford Economic Paper*. 51(1):168-183.

<sup>62</sup> Figures 1.1 and 1.2 cited from Dunne Lecture 6: UCT Course, Economics of Conflict, War, and Peace.

<sup>63</sup> Not cited but for more information see Giustozzi, Antonio (2011). *The Art of Coercion: The Primitive Accumulation and Management of Coercive Power*. New York: Columbia UP, 2011

modernization theory that war may be necessary in order to achieve the right conditions for future progress. Accordingly, wars establish new systems of power and profit in addition to new opportunities. While war itself may have negative implications, military spending has a multiplier effect and it can increase demand, enhance production, and stimulate an economy as seen with the United States and World War II following the Great Depression.<sup>64</sup>

The cost of conflict can be divided into four categories accordingly to Paul Dunne: short and medium term effects, long term-intergeneration effects, trans-boundary effects, and environmental effects (these can be further distinguished as destruction and deferred accumulation versus legacy cost). Short and medium term costs are more apparent and include the direct cost mentioned previously. Various models<sup>65</sup> measure the economic growth framework including both direct and indirect impact of conflict on physical capital, human capital, and intuitions. War can devastate the economy in regards to land, labor, and capital; the loss of assets (land, livestock, means of income, etc.) leads to smaller economies of scale and less purchasing power resulting in further market distortion.<sup>66</sup> Human capital, in the form of labor, represents a vital asset for any functioning economy. Implicit human capital costs include the loss of life and permanent injuries that reduce the long-term availability of labor in a society. For many, conflict interrupts educational opportunities, reducing the availability of skilled labor. Building upon this, high levels of refugees and internally displaced persons cause significant swings in the labor force in a given geographical region during and after the presence of conflict.

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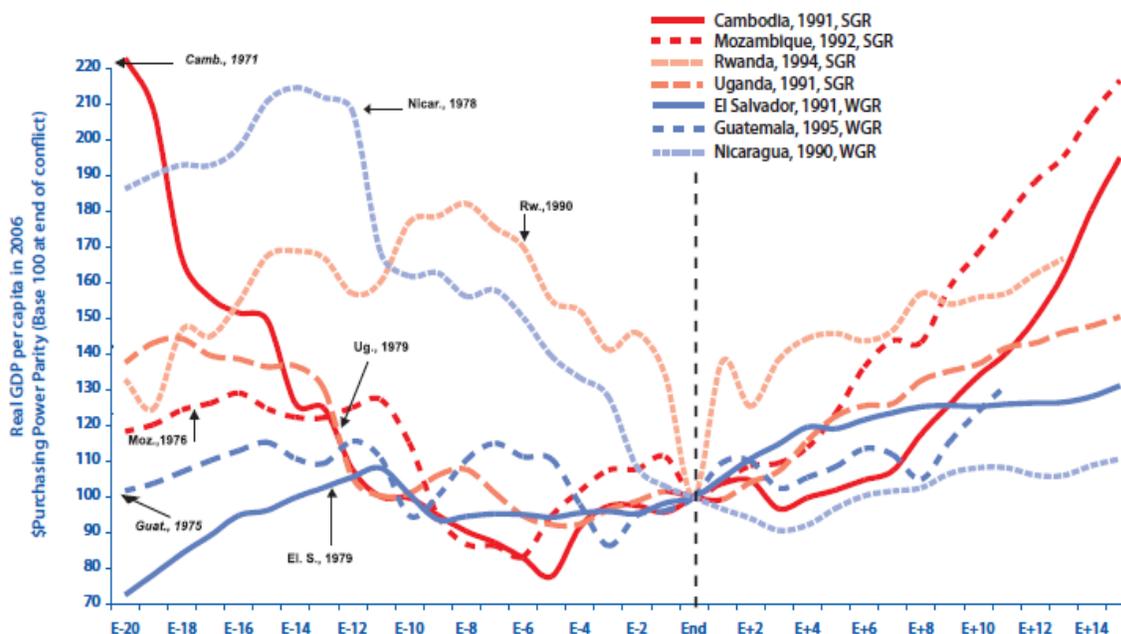
<sup>64</sup> For further reference review Keynesian effective demand / multiplier effect

<sup>65</sup> For example, the neo-classical economic approach, Keynesian economics, disequilibrium effects, the role of technology in production advancements, modernization, etc.

<sup>66</sup> MacDonald, M.H. (2006). *Private Sector Development in Reintegration and Reconstruction Programmes*. Berlin: Deutsche Gesellschaft für Technische Zusammenarbeit (GTZ).

### Figure 1.3 GDP per capita in Post-Conflict Countries<sup>67</sup>

Figure 4.2 GDP per capita in selected SGR and WGR countries (year conflict ended, group)



Note: Arrows point to starting year of conflict, unless where conflict is ongoing over the entire period covered (Cambodia, Guatemala), in which case the arrow points to the first year of the series.

There are numerous approaches to measuring the cost of conflict; the following depicts both the accounting and counterfactual approach. Dunne, as influenced by Lindgen – de Groote et al, provides Figures 1.1 to summarize the counterfactual analysis and the accounting method, depicted above with Figure 1.3, which illustrates the legacy cost of a conflict in displaying potential growth lost by comparison with a GDP trajectory. Research suggests that the “cost lies somewhere between 1.7 and 3.3 percent of GDP per country per conflict year prior to 1990 and averaging 12.3 percent of GDP post-1990”<sup>68</sup> with three main types of cost: current, legacy, and spill-over.<sup>69</sup> Current accounting cost calculations reference both the direct and indirect impact of violence in a set time and place while legacy costs are those that continue beyond the course of conflict including human capital cost due to injury and inability to work, and environmental devastation that reduce productivity. Spill-over, an indirect cost, refers to those imposed on bystanders to conflict as illustrated by the presence of refugees or internal displaced persons impacting both the labor market and the need for social service provision.

<sup>67</sup> Ohiorhenuan, John; Stewart, Frances (2008): *Post-Conflict Economic Recovery: Enabling Local Ingenuity*. UNDP Crisis Prevention and Recovery Report, Figure 4.2.

<sup>68</sup> Ohiorhenuan, John; Stewart, Frances (2008): 35.

<sup>69</sup> Brauer, Jurgen and Dunne, Paul (2010): 4.

To analyze how ‘collective violence perturbs the economic system,’<sup>70</sup> it is helpful to take a basic look at the supply and demand side of the economy. On the supply, the spikes in input prices from rising cost of production and decline in employment depend on intensity, duration, and spatial reach of the violence.<sup>71</sup> Regarding demand, consumption, investment, and exports fall while an increase in imports increases to substitute for domestic reduction in production that may further depress living standards. The continual decrease in government taxable revenue requires the state to “try to borrow, increase its debt load, and inject spending, especially military-related spending, into the economy to prop it up. But replacement of private by public economic activity is not a viable long-run economy strategy” for stability.<sup>72</sup> The “main economic purpose of trading currency is to facilitate the exchange of trade and services across currency boundaries” but conflict significantly impacts exchange rates and the potential for trade.<sup>73</sup> The appreciation of currency diminishes exports, due to the price increase for foreigners, and encourages imports. This leads to a decrease in surplus and potential increase in government deficit causing a decline in aggregate demand, reducing both economic growth and employment. While appreciation of demand is not favorable for the aforementioned reasons, it can decrease the price of imports allowing consumers and producers to operate with low inflation costs while appreciation also incentivizes domestic producers to be more efficient in order to compete in the marketplace.

The prevalence of violence and insecurity results in a “loss of business opportunities, increased country credit risk, and macroeconomic instability reflected in a devalued currency and inflation” with serious consequences for economic activity.<sup>74</sup> This phenomenon leads to lower returns on investment and discourages private sector investment impacting the low or negative growth rate resulting in decreased capacity to absorb labor and therefore a loss of jobs, incomes, and livelihood.<sup>75</sup> As addressed previously, this influences the growth of the informal economy decreasing government revenue and consequently the provision of social services to address indirect human capital cost of declining health and education. This relates to the guns verse butter<sup>76</sup> theory that the decision to spend money on militarization in an effort to provide the

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<sup>70</sup> Brauer, Jorgen and Dunne, Paul (2010)

<sup>71</sup> Brauer, Jorgen and Dunne, Paul (2010): 18.

<sup>72</sup> Brauer, Jorgen and Dunne, Paul (2010): 18.

<sup>73</sup> Brauer, Jorgen and Dunne, Paul (2010): 37.

<sup>74</sup> Bagwitz, Daniel; Becker, Sabine; Elges, Reinhold; Goretzky, Wulf; Hofmann, Armin; Hilal, Tarig; Krech, Robert; Kruk, Gabriele (2008): 5.

<sup>75</sup> Mills, Rob; Fan, Qimiao (2006): *The Investment Climate in Post-Conflict Situations*. Washington, DC: The World Bank.

<sup>76</sup> Dunne, John Paul; Smith, Ron; Willenbockel, Dirk (2004): *Models of Military Expenditure and Growth: A Critical Review*. Bristol, UK: University of West of England

public good of security, may result in the opportunity cost of not providing social services for the public and shifting production away for other non-military goods. While military expenditures can stimulate growth and government revenue (as seen with the Military Industrial Complex in America), it must be acknowledged that all military expenditure represents a trade-off and potential shift away from another socio-economic preferred good or service.

Lastly, any discussion of economic cost of conflict must acknowledge the erosion of social capital. Putnam defines the concept of social capital as features of “social organization such as networks, norms, and social trust that facilitate coordination and cooperation for mutual benefit”.<sup>77</sup> These bonds between individuals result in civic engagement that can have positive benefits in regards to “education, urban poverty, unemployment, the control of crime and drug abuse, and even health.”<sup>78</sup> Furthermore, the “networks of civic engagement foster sturdy norms of generalized reciprocity and encourage the emergence of social trust. Such networks facilitate coordination and communication, amplify reputations, and thus allow dilemmas of collective action to be resolved.”<sup>79</sup> Economically, social capital allows for a reduction in transaction costs such as monitoring, negotiating, litigating, and enforcing formal agreements that go along with contracts and formalized exchanges<sup>80</sup> while contributing to poverty alleviation, inequality reduction, and economic growth.<sup>81</sup> The destruction of these mechanisms increases transaction costs and stimulates informality and subsistence sectors, thus preventing the realization of full economic potential.

### **Conclusion**

In a seminal World Bank report, Collier’s described the ‘conflict trap’ illustrating that conflict weakens the economy and leaves a legacy of atrocities. It also creates leaders and organizations that have invested in skills and equipment that are only useful for violence. Disturbingly, while the overwhelming majority of the population in a country affected by civil war suffers from it, the leaders of military organizations that are actually perpetrating the violence often do well out of it. The prospect of financial gain is seldom the primary motivation for rebellion, but for some it can become a satisfactory way of life.<sup>82</sup>

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<sup>77</sup> Putnam, Robert (1995): Bowling Alone: America’s Declining Social Capital. An Interview with Robert Putnam. *Journal of Democracy*, 6(1):65-78. <http://xroads.virginia.edu/~HYPER/DETOC/assoc/bowling.html#FOOT4>

<sup>78</sup> Putnam, Robert (1995)

<sup>79</sup> Putnam, Robert (1995)

<sup>80</sup> Fukuyama, Francis (2001): Social capital, civil society, and development. *Third World Quarterly*, 22(1):10.

<sup>81</sup> Krishna, Anirudh; Shrader, Elizabeth (1999): *Social Capital Assessment Tool*. Prepared for the Conference on Social Capital and Poverty Reduction, June 22-24 1999. Washington, DC: The World Bank.

<sup>82</sup> Collier, Paul (2003)

Accordingly, the duration of war has increased, in part, due to both the ease of access in financing rebellions and acquiring arms as well as the profits to be gained from the war economy. In general, conflict decreases domestic productivity and exports, reduces tax revenue, increases government expenditures, increases government deficit, decreases private sector activity, declines per capita income and increases unemployment, appreciates the exchange rate, and disincentivizes investment; all of these factors significantly impact the livelihoods and future survival of households, businesses, and the state. An understanding of the functioning of war economies and the cost of conflict described in this chapter build the foundation for an exploration of economic reconstruction and the need to provide economic incentives for peace. Conflict is not irrational, and actors whether civilians or combatants (government or rebels), must balance incentives, opportunities, and feasibility calculations to determine their participation in and reaction to conflict. Analyzing the control of resources (whether property, human capital, or natural resource, etc.) and acknowledging competition for power is vital for an understanding of conflict that cannot occur without adequate financing. Accordingly, the literature alludes to the fact “that economic development is critical for reducing the incidence of civil war”<sup>83</sup> and “if the incidence of civil war is to be reduced ... it will need to be made more difficult.”<sup>84</sup> Economic activity does not end during the course of a conflict; on the contrary, “economic aspects related to labor, capital, trade, and finance can motivate, drive, prolong, and terminate violence.”<sup>85</sup>

## Chapter Two: Paradigms of Economic Reconstruction

Chapter One established a foundational understanding of the economic triggers and costs of conflict; it is important to comprehend that “economics co-determine the prospects for the success or failure of peace” and “the design and execution of postwar economic policies help determine the success or failure of peace. Not merely preventing relapse into war, the proper design and implementation of economic policies can be among the primary instruments for preventing armed violence in the first place”.<sup>86</sup> In analyzing post-1960 economic development paradigms, this chapter will illustrate the characteristics of standard economic development verses economic reconstruction / recovery, “the process of rebuilding degraded, damaged, or

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<sup>83</sup> Collier, Paul; Hoeffler, Anke; Rohner, Dominic (2009)

<sup>84</sup> Collier, Paul; Hoeffler, Anke; Rohner, Dominic (2009)

<sup>85</sup> Brauer, Jorgen and Dunne, Paul (2010)

<sup>86</sup> Brauer, Jorgen and Dunne, Paul (2010)

destroyed political, socioeconomic, and physical infrastructure of a country or territory to create the foundation for long-term development”.<sup>87</sup> This chapter will illustrate the evolution in economic development paradigms and articulate that ill-conceived economic development policies implemented in sub-Saharan African countries post-independence failed to enable the creation of an environment devoid of violent conflict. As aforementioned, the concept of conflicts economies is circular regarding which is the cause and which is the byproduct. It is not argued that the policies of donor countries, international financial institutions, and the newly formed democracies caused conflict, but there is evidence to the fact that the environment created by these policies failed to promote sustainable peace.

Economic development is a dynamic concept with complex definitions that incorporate the building of economic capability to support competition as well as the creation of jobs, wealth, and improved quality of life. Broadly defined, it is a process and set of activities over a sustained period of time that impact economics of a community. According to the International Economic Development Council (IECD), economic development includes:

- Policies that the government undertakes to meet broad economic objectives including inflation control, high employment and sustainable growth
- Policies and programs to provide services including building highways, managing parks and providing medical access to the disadvantaged
- Policies and programs explicitly directed at improving the business climate through specific efforts, business finance, marketing, neighborhood development, business retention and expansion, technology transfer, real estate development and other<sup>88</sup>

While, the Marshall Plan (1947 – 48) serves as a reference point for post-conflict economic development, the post-Cold War era is characterized by less of a need for **re**building formalized political structures and economies. More recent post-conflict environments are plagued with low-levels of development after intrastate war; there is a need to both rebuild basic infrastructure and service in addition to “the establishment of an adequate basic economic framework necessary for effective policymaking in a market-based economy, productive utilization of large volumes of aid, and creation of national reconciliation programs”.<sup>89</sup>

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<sup>87</sup> USIP Glossary of Terms (2012): “Reconstruction.” <http://glossary.usip.org/resource/reconstruction>.

<sup>88</sup> Community and Regional Development Institute: “Definitions of Economic Development.” Cornell University. <http://www.cals.cornell.edu/cals/devsoc/outreach/cardi/calendarevents/upload/DefinitionsEconomicDevelopment.pdf>

<sup>89</sup> del Castillo, Graciana (2011): “The Economics of Peace: 5 Rules for Effective Reconstruction”. Washington, DC: United States Institute of Peace, Special Report 286.

It is important to acknowledge that “economic reconstruction amid the complex transition to peace is fundamentally different from long-term development”.<sup>90</sup> An immediate, integrated strategy must be implemented in the aftermath of conflict to address the various transitions required to enable durable peace;

crime and violence must surrender to public security (the security transition). Lawlessness and political exclusion must give way to the rule of law, political participation, good governance, and respect for human and property rights (the political transition). Ethnic, religious, class, or other confrontation must be addressed (the social transition). War-ravaged or chaos-affected countries must become functioning economies that enable crises-affected groups and other ordinary people to make a decent and honest living (the economic transition).<sup>91</sup>

Accordingly, a focus on sequencing and prioritization of activities and transitions is paramount. For example, reconstruction aid for (re)-activation of vital industries, building infrastructure, and service provision must occur in the first stages while emphasis on “elections, institutions, policies, governance, security, and human capacity may have to follow” these first steps.<sup>92</sup> These trade-offs and accompanying inputs and outputs will be further discussed. The evolution in paradigms of economic development to be discussed encompass: (1) 1960s control regimes and post-independence economics; (2) 1970s attempted industrialization and crisis; (3) 1980s Washington Consensus; and (4) 1990s poverty reduction strategies.<sup>93</sup>

### **1960s – 1973: Post – Independence Economics**

The social, political, and economic development of the post-independence sub-Saharan African countries in the 1960s and 1970s were influenced by the economic, colonial history of the region. While there are significant impacts on socio-economic growth from the colonial era that are beyond the scope of this paper, of note are the extractive methods of the colonial state, the former methods of control and bureaucratic governance, the division of ethnic groups, contestation over resources, and the method of gaining independence. All of these factors and others had varying effects on conflict and economic development in post-colonial countries.

In the 1960s, a period of developmentalism and state intervention characterized young countries across the developing world. This post-independence era in sub-Saharan Africa

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<sup>90</sup> del Castillo 2011: 2

<sup>91</sup> del Castillo 2011: 2

<sup>92</sup> del Castillo 2011: 3

<sup>93</sup> Zoellick, Robert (2011): *A Timeline of Development Economics at the World Bank*. Adapted from “Democratizing Development Economics,” a speech by World Bank President Robert Zoellick at Georgetown University, September 29, 2011. <http://wbi.worldbank.org/wbi/devoutreach/article/1327/timeline-development-economics-world-bank>

witnessed high initial growth and optimism for the region. For example, Ghana's per capita income and export levels exceeded those of South Korea at the time.<sup>94</sup> The prevailing economic theory of the time was that of capital infusion to solve poverty and underdevelopment with major interventionist projects. The dominance of control regimes highlighted the power of the state and the emphasis on social engineering and self-sustained growth. Public policy supported "inward industrialization based on high tariffs and state subsidies" with the hope that "with time these policies would lead to the emergence of viable industries".<sup>95</sup> Unfortunately, these flawed policies led to pervasive market failures and economic stagnation.

### **1973 – 1980s: Attempted Industrialization and Crisis**

By the mid-1970s and 1980s, many countries experienced agricultural crisis with decline in per capita production. Africa's share in world commodity trade declined significantly as did its rise in food aid dependence with food grain imports over two decades. To illustrate the decline in production, 15 out of the 39 sub-Saharan African countries witnessed negative growth per capita in the 1970s. The 1973 Oil Crisis "signified the end of [the] African honeymoon" of rapid growth in the 1960s and the brief post-independence era of growth.<sup>96</sup> During this time, "governments combine[d] efforts to win legitimacy by highlighting the competence of their rule, on the one hand, with a continuing wariness of greater political participation and accountability, on the other".<sup>97</sup> The control regime paradigm of the 1960s had presumed the presence of a robust, capable nation state and that those in power would institute policies to increase the livelihood of the populous.<sup>98</sup> Instead, similar to the colonial state before it, newly independent African states were often ruled by a new 'political elite.' States were weak in the periphery and struggled to obtain legitimacy of rule across their borders. This was further complicated by competition for resources, often along ethnic lines, which lead to patronage politics to consolidate power. The political interest of the state lead to poor economic decisions with a focus on short-term revenue growth; destructive policies included the overvaluation of currency and

<sup>94</sup> Schrire, Robert (2005): *Economic Policy Since 1960 – Progress and Retrogression*. Printed version provided by University of Cape Town, 4.

<sup>95</sup> Schrire, Robert (2005): 6

<sup>96</sup> Schrire, Robert (2005): 4.

<sup>97</sup> Levy, Brian; Fukuyama, Francis (2010): *Development Strategies: Integrating Governance and Growth*. Policy Research Working Paper 5196, The World Bank. [http://www.wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2010/01/28/000158349\\_20100128134131/Rendered/PDF/WPS5196.pdf](http://www.wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2010/01/28/000158349_20100128134131/Rendered/PDF/WPS5196.pdf)

<sup>98</sup> For future reference see Ekeh, Peter P (1975): Colonialism and the Two Publics in Africa: A Theoretical Statement. *Comparative Studies in Society and History*, 17(1):91-112.

negative interest rates to encourage consumption. Accordingly, the state interventionist and control regimes paradigm contributed to a downward spiral of “economic mismanagement – economic decline – foreign borrowing – effective bankruptcy” in the 1970s.<sup>99</sup> African states were seen as parasitic in their reliance on development assistance leading to limited private sector investment growth opportunities and failing to address economic grievances of the population.

The 1980s exhibited a sharp turn away from the strong role of the state after the economic decline in the 1960s and 1970s and resulting market failures. Guiding paradigms for economic development from international financial institutions called for corrective behavior to state-lead growth. The shifting economic development paradigm prescribed: (1) reduction in the role for the state, (2) emphasis on exports / agriculture, (3) creation of economic incentives, and (4) significant increases in foreign assistance as highlighted by the structural adjustment programs of the Bretton Woods institutions.

The Berg Report, “Accelerated Development in Sub-Saharan Africa: An Agenda for Action,” emphasized the importance of structural (history, politics, and geography) and external factors (price shocks) when analyzing the significance of increases in economic growth; for example, countries emerging from conflict scenarios experience a large, relative growth rate because their past progress was minimal. Economic development paradigms should understand that growth is influenced by numerous factors including whether or not a country has experienced (or is experiencing) conflict, is landlocked, has natural resources, is democratic or autocratic, etc. Accordingly, there are many systems by which researchers have classified African states; for example -- diversified economies, oil exporters, transition economies, and pre-transition economies as illustrated by the McKinsey Global Institute.<sup>100</sup> Regardless of method of categorization, the 1980s economic paradigms codifications represent attempts to acknowledge the importance of context-specific development efforts.

International financial institutions’ imposition of an emphasis on exports, increased aid, and reduction in the role of the state in the 1980s led to further economic deficiencies as the paradigm did not account for external factors such as terms of trade and the need to integrate Africa into the world economy in a manner in which it would not be dependent on primary

<sup>99</sup> Schrire, Robert (2005): 8.

<sup>100</sup> Roxburgh, Charles; Dörr, Norbert; Leke, Acha; Tazi-Riffi, Amine; van Wamelen, Arend; Lund, Susan; Chironga, Mutsa; Alatovik, Tarik; Atkins, Charles; Terfous, Nadia; Zeino-Mahmalat, Till (2012): *Lions on the Move: The Progress and Potential of African Economies*. McKinsey Global Institute. [http://www.mckinsey.com/insights/mgi/research/productivity\\_competitiveness\\_and\\_growth/lions\\_on\\_the\\_move](http://www.mckinsey.com/insights/mgi/research/productivity_competitiveness_and_growth/lions_on_the_move)

commodities. Instead, the conditional incentives and prices created market failures on the supply side. Weak States were further undermined by financial constraints with limited social services for the poor and exacerbating inequality and grievances.

To make matters worse, countries in Africa that participated in the IMF's Enhanced Structural Adjustment Facility (ESAF) saw a decline in income that would take years to overcome. They experienced negative implications from a lack of government spending on health, education, and sanitation vital to development for the poor. Moreover, attempts to reduce debt burdens with IMF mandated macroeconomic policies and Heavily Indebted Poor Countries (HIPC) failed; instead, the debt burdens increased as a share of both GNP and GDP from 1985 – 1995. Poor, developing countries continued to spend resources on external debt relief instead of being able to fund health care and education; this realization was cause for a movement away from import substitution industrialization (ISI) policies.<sup>101</sup>

In understanding that the success of economic development is influenced by structural factors including history, politics, geography, and climate as well as external factors including oil price shocks, food price shocks, and falling mineral prices or declining terms of trade,; government responses to these factors may have long term implications for economic livelihood. For example, overvalued exchanges rates in former Zaire, Tanzania, Ghana, and Nigeria negatively impacted the countries' respective agricultural sectors by incentivizing cheap food imports and decreases in the price of exports. Poor agricultural policies not only countered pro-poor growth but resulted in a lack of resources, inefficient price structures, over-investment in large schemes, and inequality. Furthermore, such tactics led to market inefficiencies including misguided import substituting industrialization with excessive protection, overburdening of the public sector, and even corruption regarding access to import licenses.

### **1990s: Striking a Balance**

The economic development strategy of the 1980s was based on assumptions about agriculture being a source of cheap labor for industrialization in a world that was skeptical about the ability of developing countries to access international markets. Developing countries experienced falling exports, rising debt (in which only 15 out of 44 SSA countries were able to service their debts from 1980 – 1985), and fiscal problems including budget constraints that

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<sup>101</sup> Naiman, Robert; Watkins, Neil (1999): A Survey of the Impacts of IMF Structural Adjustment in Africa: Growth, Social Spending, and Debt Relief. Washington, DC: Center for Economic and Policy Research. [http://www.cepr.net/documents/publications/debt\\_1999\\_04.htm](http://www.cepr.net/documents/publications/debt_1999_04.htm)

limited the performance of basic government functions. These and other factors dis-incentivized investment as illustrated by a significant decline (over 5%) in the investment rate from by the mid-1980s in sub-Saharan Africa.

In the 1990s, the international financial institutions and governments began to realize that structural and market-oriented reforms were extremely slow in producing the desired results. The Washington Consensus, built on the foundational principles of the Berg Report, established a set of 10 policies for economic growth implemented through conditionality by the US and international financial (Bretton Woods) institutions. This framework crafted the economic paradigm of structural and macroeconomic adjustment in response to the economic challenges of the 1960s – 1980s. The 1980s and 1990s was characterized by stabilization and structural adjustment policies implemented by the IMF and World Bank. The IMF's imposition of stabilization consisted of demand restraint and devaluation of currency for developing countries, coupled with policy instruments including mobilization of domestic resources (fiscal policies and improved financial performance of public enterprises), improved efficiency of resource use (public sector reform and privatization, price decontrol, reduced subsidies, import liberalization, credit reform), and institutional reforms (strengthening capacity of public sector).

Although broadly defined, the Washington Consensus development paradigm of fiscal discipline has been criticized for a 'neo-colonial' approach. Despite 'good intentions' and the revelations of the 1980s Berg Report, agricultural trade continued to deteriorate during this time period and there was an over-reliance on price incentives, resulting in neglect of structural constraints and a reduction in rural infrastructure investment. In contrast to ISI<sup>102</sup> of the early time periods, the Washington Consensus triggered widespread de-industrialization, resulting in a reduction in labor productivity, limited export diversification due to dependence on primary exports, and a decreased share of GDP from manufacturing. Consequences of the new paradigm were two-fold, constituting both success and failure. For example, promotion of exports not only benefitted large corporations, but also brought about a challenge for subsistence farmers to meet domestic needs. Encouragement of privatization was seen as negatively impacting unemployment as business ownership and jobs shifted to foreigners instead of improving the livelihood of citizens. Once again, employment challenges and the decrease in government socio-economic spending negatively impacted social service provisions. These factors can be

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<sup>102</sup> This paper acknowledges that ISI policies and their negative impacts were felt most strongly in the Latin American region and not sub-Saharan Africa

linked to economic grievances that may have influenced incentives for violent conflict as explained in Chapter One and exemplified by countries in war during the 1990s.

### **Mid-1990s – 2000s: Cautious Resurgence**

The pattern of growth in Africa began to experience resurgence in the last decade. According to the McKinsey Global Institute, Africa's collective GDP is predicted to reach \$2.6 trillion in 2020 and real GDP witnessed a 4.9% increase per year from 2000 to 2008, which is in stark contrast to the declines in the previous decade.<sup>103</sup> Although significant growth is apparent, it is important to contextualize the optimism: collective GDP of \$1.6 trillion in 2008 for the entire region is compared to the singular countries of Brazil or Russia. However, Africa has 60% of the world's total amount of uncultivated, arable land. Although aggregate growth statistics provide a case for optimism, the question remains as to whether such growth is sustainable and what underlying causes enhance achievement of sustainability. Context specific economic development, coupled with continued good governance and improved macroeconomic policies, will enhance the investment climate and allow sustainable growth. In understanding the various paradigms of the 1960 – 2000 time period, this overview acknowledges the shifting view of the role of the State in fostering economic growth. Accordingly, structural change in both the private and public sectors in addition to economic factors such as increases in commodity prices are responsible for economic growth in the past decade and moving forward.<sup>104</sup>

### **Present Day Post-Conflict, Context Specific Economic Development**

Post-conflict economic reconstruction is distinguished from broader economic development as “economic programs, especially when conflict-sensitive, can minimize the detrimental effects of conflicts while maximizing the potential benefits to specific target groups”.<sup>105</sup> Conflict-sensitive and context-specific policies and interventions are best crafted after needs assessments to gather information about political, social, and economic contextual realities as “development interventions with the objective of promoting economic growth need a profound assessment of both the conflict and peace dynamics, as well as the political economy of

<sup>103</sup> Roxburgh, Charles et al. (2012)

<sup>104</sup> This paper does not address the shocks of the economic recession in 2008 but according to the World Bank, growth has rebounded in 2010 as a result of “prudent macroeconomic policies and financial support from multilateral agencies.”

The World Bank Africa Region (2011): *Africa's Future and the World Bank's Support to It*. The World Bank.

<sup>105</sup> Bagwitz, Daniel; Grossmann, Helmut; Elges, Reinhold; Kruk, Gabriele; Lange, Ralf (2009): *Sustainable Economic Development in Conflict-Affected Environments*. Eschborn: Deutsche Gesellschaft für Technische Zusammenarbeit (GTZ) GmbH, 4.

the respective country”.<sup>106</sup> Purely economic focused policies and programs will not prevent, mitigate, or help end conflict in developing countries leading to sustainable growth and peace. In addition to needing economists, this context requires development specialists, socio-political scientists, technical specialists, and country experts to adequately evaluate a post-conflict setting for both political landscape<sup>107</sup> and economic perspectives<sup>108</sup> from all levels of society (household, firm, and national).

The international financial institutions, donor countries, and NGOs have continually evaluated and adapted their approaches to economic development. While the lessons learned and best practices have evolved, it is vital to acknowledge the specific context of a post-conflict economic environment as discussed in Chapter One. For example, one of the most critical tasks in post-conflict reconstruction efforts is (re)-building trust, “highlighting the importance of social capital development”.<sup>109</sup> This task can manifest itself in various programs across all sectors of society; emphasis is often placed on reconciliation among perpetrators and victims. However, as it concerns a need for justice for victims in the immediate / short term, a balance must be struck with long term goals of sustainable peace. Oslen et al cites the justice-development trade-off which acknowledges the opportunity costs of spending economic resources on justice mechanisms that could be utilized for other purposes including social service provision, job growth stimulation, skills training, etc. Furthermore, while justice mechanisms deliver various forms of justice or truth to address emotional well-being, some of these approaches do not contribute to the economic well-being of communities. After conflict in an effort to establish a means of income (survival) outside of the war economy, there is a pressing need for the population (both former combatants and victims) to have a means by which to provide a livelihood. This illustrates how transitioning societies face pressing economic concerns that may compete with transitional justice considerations for economic, social, and political prioritization.

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<sup>106</sup> Bagwitz et al. (2009)

<sup>107</sup> Bagwitz and Klein 2008; Gunduz and Klein 2008; SaferWorld 2004; Sida 2006

Bagwitz, Daniel; Klein, Brigitte (2008): *Promoting Economic Innovations in Sub-Saharan Africa*. Eschborn, Ger: FIAS. Washington DC: GTZ. [http://www2.gtz.de/wbf/4tDx9kw63gma/Promoting\\_Economic\\_Innovations.pdf](http://www2.gtz.de/wbf/4tDx9kw63gma/Promoting_Economic_Innovations.pdf).

Gunduz, C., & Klein, D. (2008). *Conflict-sensitive approaches to value chain development* (microREPORT #101). Washington, DC: United States Agency for International Development.

Swedish International Development Cooperation Agency. (2006). *Manual for conflict analysis* (Methods Document): SIDA, Division for Peace and Security through Development Cooperation.

International Alert & SaferWorld. (2004). *Conflict-sensitive approaches to development, humanitarian assistance and peacebuilding: a resource pack*. London: International Alert/SaferWorld.

<sup>108</sup> Economic perspectives include the “macroeconomic effects of conflict, and the potential risk for investment; or the impact of a conflict on the livelihoods of individuals and households” (Sweeney 2008: 24).

<sup>109</sup> Fred-Mensah, Ben K (2004): Social Capital Building as Capacity for Postconflict Development: The UNDP in Mozambique and Rwanda. *Global Governance: A Review of Multilateralism and International Organizations*, 10(4):437.

Transitional justice may be deemed a luxury that cannot be afforded by many new democracies; furthermore, “long-term legitimacy and strength of the democratic system in fragile economics... demand that country leaders address more pressing needs”.<sup>110</sup>

This author does acknowledge that transitional justice is important for sustainable peace, as well as addressing the underlying and precipitating factors of conflict, which include social distrust and lack of / unequal economic opportunities. Providing citizens with the ability to earn incomes and productively contribute to society can not only mitigate incentives for violence, but can also improve exchange between former victims and victimizers, demonstrating how economic development and the pursuit of growth can contribute to peace. In understanding that trust is of economic value,<sup>111</sup> post-conflict economic reconstruction programs address not only good governance and institutional reform, but also priorities for building a community of trust. If restorative justice is acknowledged as a mechanism by which to achieve reconciliation, “not so much of punishing perpetrators for wrongs in the past or knowing the truth, but taking steps to address the victims’ situation through the restoration of the physical, psychological, social and economic well-being of the individual,” then the contributions of social capital to both the well-being of the victims and the community address both economic and justice needs of post-conflict society.<sup>112</sup> This tool’s relational factor “functions via its facilitation of inter-human interactions and relationships in the form of cooperation and coordination and enables production actors to manage social and political crisis,” facilitating the transitions to peace in a post-conflict environment.<sup>113</sup> Reconciliation mechanisms, whether “in the form of reparations, restitution and / or broader provision of economic goods (employment, infrastructure, and industries)” hold that “the material and economic well-being of the individual victim and the community is” vital to transitional justice.<sup>114</sup> Accordingly, ex-combatant reintegration program illustrate this concept by “positively impact[ing] conflict resolution processes and ... rebuilding ... social capital” contributing to both peace and restorative justice in addressing material and economic well-being of the community.<sup>115</sup>

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<sup>110</sup> Olsen, Tricia D., Leigh A. Payne and Andrew G. Reiter. 2010. “At What Cost? A Political Economy Approach to Transitional Justice.” *Taiwan Journal of Democracy* 6:1

<sup>111</sup> Fukuyama, Francis (1995) *Trust: The Social Virtues and the Creation of Prosperity*. New York: The Free Press.

<sup>112</sup> Oduro, Franklin (2007): *What do we understand by ‘Reconciliation’? Emerging Definitions of Reconciliation in the Context of Transitional Justice*. A Review of the Literature on Reconciliation. [http://www.iiars.org/dbiniciativas/upload/VARIOS/VS01\\_16\\_03.pdf](http://www.iiars.org/dbiniciativas/upload/VARIOS/VS01_16_03.pdf)

<sup>113</sup> Fred-Mensah, Ben K (2004)

<sup>114</sup> Oduro, Franklin (2007)

<sup>115</sup> Colletta et al. (1996) as cited in Leff 2008: 14. [http://www.accord.org.za/downloads/ajcr/ajcr\\_2008\\_1.pdf](http://www.accord.org.za/downloads/ajcr/ajcr_2008_1.pdf)

Colletta, N., Kostner, M. & Wiederhofer, I. (1996): *Case Studies in War to Peace Transition: the Demobilization and Reintegration of Ex-Combatants in Ethiopia, Namibia, and Uganda*. Washington, DC: World Bank.

Economically, social capital allows for a reduction in transaction costs such as monitoring, negotiating, litigating, and enforcing formal agreements that go along with contracts and formalized business exchanges,<sup>116</sup> while also contributing to poverty alleviation, inequality reduction, and economic growth in complex environments.<sup>117,118</sup> More specifically, the channels through which social capital influences economic development include: (1) lowering the cost and increasing the availability of information sharing via participation in social networks, (2) collective decision making and shared implementation as result of widespread participation and mutual trust, (3) and societal pressure to reduce harmful behavior. These contributions are realized by trusted dissemination of information regarding prices, markets, access to credit, governance regulations, and best practices to increase economic productivity. Furthermore, collective decision making concerning distribution and management of resources (land, water, waste disposal, etc.) is vital for survival of a given community and the building of social capital to engage a diverse subset of the community in decision making, reducing opportunity behavior that could be detrimental.<sup>119</sup>

The question remains – how to build trust in a post-conflict setting while also promoting peace, addressing justice, dis-incentivizing conflict, rebuilding the public sector, and developing the economy? The public sector can best contribute to social capital development by addressing security, governance, and improving the business climate to indirectly increase social capital; for example, “people cannot associate, volunteer, vote, or take care of one another if they fear for their lives when walking down the street. Given a stable and safe environment for public interaction and property rights, it is more likely that trust will arise spontaneously as a result of iterated interactions of rational individuals.”<sup>120</sup> According to Fred-Mensah, “...the major role of institutions in a society is to reduce uncertainty by establish[ing] a stable structure to human interaction” which has major implications for economic growth.<sup>121</sup> Therefore, holistic institutional reform is paramount for building an environment that fosters trust (both among citizens as well as between citizens and their government) so that social capital can be utilized in a developmental capacity to promote peace and economic well-being during reconstruction.

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<sup>116</sup> Fukuyama, Francis (2001)

<sup>117</sup> Krishna, Anirudh; Shrader, Elizabeth (1999): 12.

<sup>118</sup> For further information, the contributions of social capital to both peace and economic development have been documented and measured by the World Bank.

<sup>119</sup> Grootaert, Christian; van Bastelaer, Thierry (2002): *Understanding and Measuring Social Capital: A Multi-Disciplinary Tool for Practitioners*. Washington, DC: World Bank.

<sup>120</sup> Fukuyama, Francis (2001)

<sup>121</sup> Fred-Mensah, Ben K (2004)

Implicit in post-conflict reconstruction is the demand for justice and improved relationships in the aftermath of violence. While transitional justice activities are critical to reconciliation, private sector development contributes to the peacebuilding and conflict-resolution approach to reconciliation that “emphasize[s] building new and peaceful relationships, bridging divides, [and] establishing trust” through a variety of processes.<sup>122</sup> To address the concern that a focus on economic development does not address justice, Oduro explores David Whittaker’s societal-based definition of reconciliation that addresses the need for a “renewed sense of order and [ability] to make improvements in the material welfare of the people (e.g. basic needs of shelter, food and other public amenities)” for individuals to feel secure.<sup>123</sup> Accordingly, societal transformation requires “provision of economic goods for equitable social advancement”.<sup>124</sup> To prevent a relapse in violent conflict, societies must address the political and economic inequalities “which [may be] the products of past oppressions and are the sources of conflict and estrangement [which] need to be reconstructed and transformed to give meaning to reconciliation”.<sup>125</sup>

### **Structural Adjustment and Poverty Reduction Examples**

After 27 years of conflict, warring parties agreed to a ceasefire in 1990, and a peace accord in 1992 ended years of violence in Mozambique. Similar to other developing countries of that time, Mozambique participated in the 1986 Economic Reconstruction Program and 1996 Heavily Indebted Poor Country (HIPC) initiatives of the World Bank and IMF. As previously acknowledged, these structural adjustment programs had numerous negative implications for economic growth and even political and socio-economic stability. First and foremost, they were not implemented with a sensitive understanding of the ongoing conflict and further undermined the role of the Frelimo party in providing governance and macroeconomic stability.

The policies were counterproductive to human development and failed to adequately address the benefits of the agricultural sector. Eased price controls influenced increases in the price of food, leading to reductions in both food and rent subsidies in accordance with social services reduction and initiating of fees for health and education. “At the same time, wage increases were not sufficient for many workers to deal with the price increases, and the burden of

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<sup>122</sup> Oduro (2007): 18

<sup>123</sup> Whittaker, David (1999). *Conflict and Reconciliation in the Contemporary World*. London: Psychology Press.

<sup>124</sup> Oduro (2007): 12

<sup>125</sup> Oduro (2007): 30

adjustment fell disproportionately on the poor,” demonstrating the opposite of pro-poor growth.<sup>126</sup>

Structural adjustment policies failed to be conflict sensitive and address the powerful legacies of the war. Accordingly, the growth that resulted from these policies was misleading and contributed to further inequality, specifically along urban versus rural lines. The government failed to address this until the end of conflict at the initiation of private sector development and pro-poor growth. By this point, the government was enabled to support direct allocation of resources to the most vulnerable populations as a means of poverty alleviation and economic growth in the 1990s.

### **Chapter Three: Private Sector Development Framework**

Economic reconstruction strategies are continuously evolving given the changing nature of post-conflict environments and learning curve of governments, the international financial institutions, donor countries, and other actors. This chapter highlights the post-conflict private sector development (PSD) economic paradigm, defined as the set of activities undertaken to promote growth and reduce poverty by developing a “productive, sustainable, and market-oriented private sector.”<sup>127</sup> This strategic approach addresses “the twin goals of economic growth and peace, in other words, ... strengthen[s] conditions for the growth of a stable, accessible, and competitive private sector and ... contributes to a lasting and durable peace.”<sup>128</sup> In understanding that private sector development is a multifaceted approach, this chapter will acknowledge the competing priorities and importance of conflict-sensitive operations that do not undermine the state or exacerbate inequalities by repeating the mistakes of the past. In conducting an assessment of both the investment climate reform and interventionists strategies of PSD, the following sections argue in favor of a hybrid / integrated approach. Both the investment climate and interventionist approaches to private sector development highlight removing systematic constraints on growth exports and the importance of conflict-sensitive, pro-poor growth. There is significant overlap of the two as illustrated by the Making Markets Work for the Poor (M4P) methodology which is interventionist in approach but transformative of the system and investment climate.<sup>129</sup> Accordingly, an integrated framework of private sector development is

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<sup>126</sup> Dunne, Paul (2006)

<sup>127</sup> Sweeney, Naoise Mac (2008): 13.

<sup>128</sup> Bagwitz et al. (2008)

<sup>129</sup> Sweeney, Naoise Mac (2008): 51.

more sustainable and effectively contributes to post-conflict reconstruction by fostering pro-poor growth and economic development. This is achieved in partnership with all sectors of society while also acknowledging the limited capacities and challenges of these partnerships. The argument for an integrated approach to PSD acknowledges that “private sector development results from an implicit contract between the private sector, the state, and civil society [in which] the priorities for change ... depend on the factors that the main stakeholders believe are undermining the contract or may help to improve it” for the benefit of the populous.<sup>130</sup>

### **Investment Climate: Macroeconomic Stabilization**

Post-conflict economies are plagued with macroeconomic instability including inflation, incorrectly valued currency rates, unemployment, inequality among those who benefit from the war economy, human and economic insecurity, limited availability of skilled labor, constrained mobility, and horizontal inequality. Accordingly, private sector development must operate in the absence of robust financial institutions and macroeconomic stability. The investment climate approach seeks to engage the public sector and addresses the conditions under which economic growth can occur; therefore, it utilizes public and private sector tools to achieve macroeconomic stabilization for growth by addressing legal reforms, business regulations, and infrastructure (i.e. basic inputs, transportation, and communication) projects. The difficulty of this approach is the limited capacity of a government, public sector counterpart; accordingly, development of the private sector should promote both the development of government capacity and macroeconomic stabilization.

The Investment Climate approach is distinct in that its “programming is directed towards improving the economy as a whole, rather than directly helping specific individuals or

Figure 3.1: Infrastructure Programs



<sup>130</sup>OECD (2004): 57.

businesses”; accordingly, it lays the foundation for growth, peace, and stability.<sup>131</sup> For immediate impact, macroeconomic stabilization requires availability of currency for financial institutions, governments, and citizens to facilitate economic activity. A focus on creation of “efficient, accountable, and transparent financial institutions can encourage trust in central government and strengthen the authority of a weak state” coming out of conflict.<sup>132</sup> In the absence of robust financial intuitions, donors are necessary to assist governments with: (1) budgets, (2) controlling spending, (3) keeping track of receipts, (4) reducing borrowing, and (5) budget support as macroeconomic stabilization requires stabilization of currency, reining in inflation, and maintaining steady prices.<sup>133</sup>

Investment climate development activities include public works infrastructure projects (see Figure 3.1<sup>134</sup>) which allow “... jobs to be created quickly, create assets, release commerce from constraints, add to capacity, [and] facilitate access to economic and social services, stimulate economic growth, and of course assist in the demobilization and reintegration of combatants”.<sup>135</sup> Capital for such infrastructure development is often derived from public-private partnerships. Electrical utility is one of the most foundational areas of infrastructure development required to do business in post-conflict, developing countries. Utilizing public-private partnerships to develop this capacity, the public sector can give “the concessions or pu[t] in place tariffs for buying electricity ... while the private sector can provide some of the money, and build and operate the infrastructure. Not only does that offer the benefit of financing, but also, very often, the systems become more effective and better maintained and, therefore, have a longer life”.<sup>136</sup> Access to electricity, and not just individualized owned generators, can significantly impact manufacturing abilities, more equitable distribution of access, as well as simple household activities such as cooking or providing light for children to do their homework.<sup>137</sup> Rebuilding infrastructure after a devastating conflict is a clear priority of any post-conflict society and economic development activities should take advantage of funding spikes which are highest at the beginning of post-conflict phases; “however, there is rarely the capacity

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<sup>131</sup> Sweeney, Naoise Mac (2008): 60.

<sup>132</sup> Sweeney, Naoise Mac (2008): 63.

<sup>133</sup> Sweeney, Naoise Mac (2008): 63.

<sup>134</sup> Sweeney, Naoise Mac (2008): 63.

<sup>135</sup> Dunne, John Paul; Mhone, G (2003): *Africa's Crisis: Recent Analysis of armed conflicts and natural disasters in Africa*. (Working Paper No. 5). Geneva: International Labour Office, Recovery and Reconstruction Department, 7.

<sup>136</sup> Goland, Tony (2012): “Lars H. Thunell on encouraging private-sector investing in emerging markets.” McKinsey Quarterly Interview. [http://www.mckinseyquarterly.com/Lars\\_H\\_Thunell\\_on\\_encouraging\\_private-sector\\_investing\\_in\\_emerging\\_markets\\_2988](http://www.mckinseyquarterly.com/Lars_H_Thunell_on_encouraging_private-sector_investing_in_emerging_markets_2988)

<sup>137</sup> Goland, Tony (2012)

in terms of skilled labor and organizational ability [to] carry out major infrastructure work during this early period when the money is available. By the time capacity has been built up, however, the funding has usually dried up”.<sup>138</sup> These calculations of when to address and prioritize investment climate activities are discussed in Chapter Four’s section on sequencing of the private sector development implementation.

The private sector can grow and function in the absence of robust development but basic business-enabling infrastructure is necessary; this includes water and electricity, basic input supplies, means of transportation, and communication mechanisms. If these inputs are available, infrastructure projects can begin to benefit the community, local private sector, and contracting companies as “procurement strategies can build on [the] existing private-sector and local labour can ... be used for construction work, providing jobs and livelihoods for the post-conflict population. Infrastructure projects should therefore seek to involve local communities and businesses”.<sup>139</sup> While instrumental to economic growth, infrastructure projects are costly, time consuming, and politically sensitive.<sup>140</sup> In a post-conflict environment, the interests of various stakeholders must be weighed to prevent a reigniting of hostilities or negatively impacting a specific demographic. Accordingly, transparency and anti-corruption must be prioritized by both private and public sector actors. Therefore, the implementation of (and choice to undertake) infrastructure projects must assess the trade-off of state control versus private sector efficiency of project management. As with all post-conflict economic activities, the private sector should operate in a manner not to undermine the state.

Governments have five means by which they can address macroeconomic stabilization: monetary policy, fiscal policy, legal reforms, business regulations, and trade policy. Private sector development necessitates policy creation and implementation to lay the foundation for reform. Monetary Policy maintains purchasing power of the state’s currency, controls inflation, determines interest rates, and regulates the banking system. In addition to monetary and fiscal regulation, “in the long-term it is productive capacity ... that improves peoples’ lives” and hence it is important to control the printing and injection of money into the economy.<sup>141</sup> Accordingly, in a post-conflict environment, the focus should be on “rebuilding the central bank; regaining domestic credibility; reestablishing the internal and external banking and payment systems;

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<sup>138</sup> Sweeney, Naoise Mac (2008): 64.

<sup>139</sup> Sweeney, Naoise Mac (2008): 64.

<sup>140</sup> Sweeney, Naoise Mac (2008): 64.

<sup>141</sup> Brauer, Jurgen and Dunne, Paul (2010): 29.

rebuilding systems for bank supervision; restarting the provision of credit; reining in the high inflation; and dealing with the consequen[ces] [of] currency depreciation on foreign-exchange markets”.<sup>142</sup> Such reforms emphasize the integration of monetary and fiscal policy necessary in the aftermath of conflict given the limited nature of governance and regulatory institutions.

In addition to monetary and fiscal policy, as aforementioned, it is widely acknowledged that government and legal systems are often lacking or non-existent in post-conflict settings; accordingly, the development of a favorable investment climate begins with good governance. Legal reforms include addressing the rise of informality in the economy and the importance of property rights. First and foremost, “formalizing the economy aids the transition from war to peace economy, and encourages engagement with the state in a way which bolsters state authority”.<sup>143</sup> As discussed in Chapter One, the rise of informality negatively impacts the government’s ability to generate revenue from taxes for reconstruction efforts; moreover, the rise of informality limits the tax base and can increase the burden on the formal economy, reducing the incentive to invest in productivity enhancing methods and technology. To correct this, it is recommended that governments instill various corrective actions; for example, they can choose to address one sector at a time, separate tax and auditing divisions, address ineffective court prosecution of evaders and increase penalties for evasion, streamline regulatory burdens, reduce red tape, simplify the tax code, shift tax burdens, and address government expenditures.<sup>144</sup> In addition to the aforementioned legal policy enforcements, property rights are often seen as a pre-requisite for private sector development intervention as the “unequal property distributions along factional, ethnic, or other group lines can potentially sow the seeds of future conflict”; accordingly, it is recommended that early legislative action include rewriting property laws among other business-related regulations.<sup>145</sup>

Private sector development can streamline business regulations to address administrative and practical barriers to investment. To this effect, donor countries or corporations can act as guarantors, brokers, or source of information for investors weary of risk management in post-conflict environments. Working with governments to provide a “clear and transparent set of business regulations” will enable donors to “discourage corruption and hopefully break the connection between public office and private business interest” as aforementioned in referencing

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<sup>142</sup> Brauer, Jurgen and Dunne, Paul (2010): 30.

<sup>143</sup> Sweeney, Naoise Mac (2008): 61.

<sup>144</sup> Farrell, Diana (2004)

<sup>145</sup> Sweeney, Naoise Mac (2008): 61.

Peter Ekeh's "Colonialism and the Two Publics in Africa: A Theoretical Statement."<sup>146, 147</sup> This will require private sector actors to hold themselves accountable in operating within legal frameworks and business regulations to prevention corruption and distortion of financial flows. Furthermore, the separation of public office and private business interests will contribute to the accountability and respectability of the public sector and development of good governance in the best interest of the State's citizens.

In addition to legal reforms and business regulations, formalized cross-border trade generates revenue and dis-incentivizes informality which can reduce the power of a separate predatory private sector and incidences of trafficking.<sup>148</sup> Regulated trade stimulates an awareness of international markets and business connections; hence, gaining access to markets corresponds with an adoption of value chains and increases economies of scale for economic growth by encouraging the local private sector to upgrade in commercialization and competitiveness.<sup>149</sup> To build domestic capacity and improve trade policy, donors can facilitate trade across national boundaries and access to foreign markets, assist in brokering trade agreements, and provide guarantees of security and fairness to encourage cooperation and competition.<sup>150</sup> This promotion of security and fairness is paramount in post-conflict settings and relates to the theory that trading partners do not go to war with each other; this concept is similar to the democratic peace theory. Acknowledging that most sub-Saharan conflicts were intrastate wars, the parallel idea is that internal trade and robust market economies dis-incentivize war between neighbors as it promotes interconnectedness and reliance. As it concerns landlocked countries with warring neighbors, border controls and trade tariffs are additional tools of trade policy to be utilized by governments in protecting growth and stability from influential, negative actors.

The investment climate approach, as described here, demonstrates how public agencies best provide indirect support to private sector development with a "stable macro-economic environment, the rule of law, and a set of regulations, policies, and a fiscal regime that are clearly communicated and implemented".<sup>151</sup> This environment encourages individuals to engage in complex economic activities and benefits the poor by changing the investment climate and

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<sup>146</sup> Ekeh, Peter (1975)

<sup>147</sup> Sweeney, Naoise Mac (2008): 61.

<sup>148</sup> Sweeney, Naoise Mac (2008): 64.

<sup>149</sup> Sweeney, Naoise Mac (2008): 64.

<sup>150</sup> Sweeney, Naoise Mac (2008): 64.

<sup>151</sup> Sweeney, Naoise Mac (2008): 50.

cutting some red tape barriers that would keep them in the informal economy. Critics of this approach hold that the emphasis on government tools and regulations may have limited impact and credibility when implemented on the ground; furthermore, “instead of increasing stability through economic growth, structural changes to the macroeconomic system [may] lead to an increase in horizontal inequalities, and the renewal of conflict.”<sup>152</sup> In acknowledging these limitations, it is important to note the preliminary considerations (preconditions) for the investment climate approach to improve macroeconomic stabilization; this includes—but is not limited to—a secure location, counterparts for business, a demand of goods and services, population stability, provision of finances / access to credit, and the development of social capital.

### **Interventionist Approach**

The interventionist approach to private sector development holds that instead of focusing on the investment climate to indirectly increase employment or investment in support of private sector development, that “direct intervention is needed to make a real and tangible difference on the ground”.<sup>153</sup> This direct approach generates more tangible results with clear beneficiaries, produces visible peace dividends, targets specific demographics, and operates despite the presence of weak state structures. Therefore, in post-conflict settings where governance is lacking, interventionist activities may be more easily implemented without the need for a public sector counterpart as they focus on the market itself to stimulate post-conflict private sector development. Tools of the interventionist approach include: (1) promotion of market linkages and value chains to link economic actors and improve relations; (2) promotion of business associations and community groups to rebuild social capital; (3) access to employment and vocational training; (4) microfinance for access to credit, financial services, insurance, and savings; and (5) targeted support including provision of supplies, equipment, and advisory services for relief.<sup>154</sup> This practical approach to private sector development, as illustrated by the Making Markets Work for the Poor (M4P), decreases the risk of a return to conflict by quickly creating visible peace dividends given the fear of a relapse of violence in the first five years after

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<sup>152</sup> Sweeney, Naoise Mac (2008): 51.

<sup>153</sup> Saperstein, Adina and Campbell, Ruth (2008): Accelerating the Transition from Conflict to Sustainable Growth. Microreport #111. Washington, DC: ACDI/VOCA, 1.

<sup>154</sup> Sweeney, Naoise Mac (2008): 51.

the end of conflict.<sup>155</sup> While it produces immediate results, this approach calls into question the sustainability of such programming and the aggregate impact of a targeted approach without good governance.

Market linkages address the need for trust in economic development, indicative of the building of social capital to better facilitate sustainable peace.<sup>156</sup> Informal war economies often engage in ‘above-board’ channels of regional commerce that is mostly illegal as illustrated by resource trafficking. Therefore, in a post-conflict setting it is critical to “foste[r] new, legitimate, market connections offer[ing] local businesses an alternative to those which had previously underpinned the war economy”.<sup>157</sup> This requires two activities: (1) practically linking economic actors to each other<sup>158</sup> and (2) circulating information about markets so actors can adjust to trends.<sup>159</sup> (The importance of clear and effective communication between actors is addressed in Chapter Four.) Value chains promote sectoral linkages for economic growth and improve relationships to build trust and sustain peace. Post-conflict economic development actors and donors can engage all three levels of value chains: micro (individual firms), meso (business associations and regional distribution), and macro (international agreements and foreign markets).<sup>160</sup> At the meso-level, business associations and community groups are vital in promoting government involvement in the private sector in that members can be viewed as a group of constituents able to negotiate and organize themselves in favor of specific conditions for sustainable growth. Moreover, these organizations increase resilience of actors and buffer risks in the market place, which is critical in a post-conflict setting. Inherent in business associations and community groups is the building of social capital and trust to enhance market interactions and relationships. Business associations can focus on specific sectors of high growth and bring together entrepreneurs to encourage formality, innovation, collaboration, and growth. Therefore, private sector development intervention can focus on encouraging the development of these meso-level actors. Of note is that to be conflict-sensitive, it is critical to have broad participation and membership so as to not exacerbate tensions between groups, appear to display

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<sup>155</sup> Sweeney, Naoise Mac (2008): 52.

<sup>156</sup> Sweeney 2008 cited Gündüz, C and Klein, D (2008): *Conflict-Sensitive Approaches to Value Chain Development*. Washington DC: USAID.

<sup>157</sup> Sweeney, Naoise Mac (2008): 53.

<sup>158</sup> To be discussed later in paper

<sup>159</sup> Sweeney, Naoise Mac (2008): 53. References Aaronson et al 2008

<sup>160</sup> Gündüz and Klein (2008); Saperstein and Campbell (2008).

favoritism, or to promote inequality. Specifically, community groups must have a wide base to avoid embedding interest of the private sector in a given community.<sup>161</sup>

In addition, to building social capital with value chains, employment and vocational training are critical in all stages of improvement and building capacity efforts. In post-conflict reconstruction, programming for ex-combatants should be prioritized. In developing countries, there are numerous barriers to employment including health, mobility, and education. Ex-combatants face additional obstacles reintegrating into society; hence, the need for a concerted intervention effort. Given the realities of post-conflict environments, not all jobs created during or in the immediate aftermath of violence will be sustainable. The tradeoffs between sustainability and the immediate need for job creation to promote growth are challenging; it is both practical and efficient to establish labor exchange as well as training in existing livelihood strategies. This includes basic skill training as well as entrepreneurial knowledge about credit, finance, and basic business skills. In the immediate aftermath it is important to acknowledge that there will be a shock to the labor supply given the number of ex-combatants (disproportionately young males) in need of a means of livelihood outside of that provided by fighting. This highlights the significance of reintegration programs and their impact on both peace and growth.

Interventionist activities include targeted support interventions which directly concern the provision of supplies, equipment, advisory services, etc., as well as general knowledge and skills of how they are to be utilized.<sup>162</sup> This allows short-term relief that should be conflict sensitive and provided after conducting a needs assessment (as discussed in previous sections). As previously discussed, access to finance is a critical element of private sector development; accordingly, microfinance institutions and programs have received a wealth of attention. In post-conflict settings this programming addresses the desperate need for access to credit, financial services, insurance, and savings. However, the instability of the population base with high mobility and limited capacity may make microfinance interventions less than ideal and unsustainable.<sup>163</sup> The debates about the effectiveness and sustainability of microfinance programs and whether or not they promote savings and growth are of note, but the analysis of these arguments are beyond the scope of this paper.

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<sup>161</sup> Sweeney, Naoise Mac (2008): 54.

<sup>162</sup> Sweeney, Naoise Mac (2008): 59.

<sup>163</sup> Sweeney, Naoise Mac (2008): 57.

### *Governance and Growth Examples*

The increasing demand and price of minerals and raw materials have significantly impacted growth in Africa and account for 24% of growth in GDP from 2000 - 2008. However, McKinsey Global Institute clarifies that African growth acceleration is not simply a result of a resource boom but that a decline in conflict, improved macroeconomic policy, and a focus on investment climate for business enabled positive growth. These improvements enabled developments in the wholesale and retail trade, transportation, telecommunications, and manufacturing sectors, illustrating the effectiveness of private sector development in the promotion of economic growth.

Contrary to the policies of the 1980s in which government failures were seen as worse than market failures after the dominance of control regimes, promotion of the investment climate approach acknowledges the positive role of the state in providing an environment for economic growth: “research shows that good governance fosters sustained growth in the longer term through domestic and foreign investment, private sector development, improved public sector management and sectoral development”.<sup>164</sup> The first step for many African countries in achieving a climate for economic growth has been to end conflict and establish macroeconomic and political stability. This allows governments to enact macro and microeconomic reforms to decrease inflation, foreign debts, and budget deficits establish a more welcoming environment not only for investment but also for economic exchange among former ‘enemies.’

In sub-Saharan Africa, the 1990s democratization was hoped to represent an end to “decades of economic failure, foreign-aid dependency, official venality and incompetence” that plagued the region with poor governing capacity.<sup>165</sup> Post-conflict Mozambique progressed from being one of the world’s poorest countries in 1987 to the fastest growing economy in sub-Saharan Africa by 1996. Increases in foreign investment and privatization were coupled with a significant decrease in inflation and high economic growth. By 1999, Mozambique’s GNP reached \$2 billion, inflation was at 2%, and economic growth hit 10%. However, interventions in Mozambique mistakenly prioritized high-tech growth that was not sustainable and did not recognize the importance of agricultural development; this reality suggests “that it [is] important to undertake reform and restructuring at the same time and to get to know the nature of the post-

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<sup>164</sup> Kaufmann, Daniel (2011)

<sup>165</sup> Van de Walle, Nicolas (2002): Africa's Range of Regimes. *Journal of Democracy*. 13(2):66-80.

war economy” as this is a prime example of the importance of an integrated investment climate and interventionist approach to economic growth that is conflict-sensitive.<sup>166</sup>

## **Chapter Four: Challenges in Implementation of Private Sector Development**

Post-conflict countries across the sub-Saharan region have seen significant growth spurts in recent years; however, sustainable growth requires institutional development, governance, and adequate policy implementation. In the early 2000s, “the paradigm for private sector development was that the poor relied on [small enterprises] for their livelihoods, these businesses were disadvantaged and that justified subsidizing their access to knowledge and finance” leading to aid dependency and a lack of incentives for adherence to change.<sup>167</sup> Past economic development and poverty alleviation strategies, while focused on facilitating a better livelihood for the poor, are still insufficient for economic reconstruction and promotion of peace in post-conflict countries. While the current private sector development framework, including the investment climate and interventionist approach outlined in Chapter Three, successfully addresses many of the flawed policies of the 1960s – early 2000s, it still falls short of effectively establishing a dynamic private sector and robust institutions where countries are not faced with high aid dependency and distributive issues. These problems have negative implications for the development of public sector capacity and legitimacy, entrepreneur activity, socio-economic stability and robust, sustainable growth of the private sector’s production of goods and services.

### **Aid Dependency and Distributive Issues**

Foreign aid positively contributes to health, education, and infrastructure building; however, in conflict settings “the improvised way in which it is channeled, low absorptive capacity, weak institutions, and procurement policies put special pressure on both governments and donors to use aid effectively and avoid corruption during the transition to peace”.<sup>168</sup> Unfortunately, the volatility of aid flows has created unstable distortions in which growth is related to bubbles of large volumes of aid; under these circumstances, price and wage distortions can discourage investment and work. Further, as it concerns building capacity, large aid flows can “deprive the civil service of needed expertise, since professionals and other skilled people

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<sup>166</sup> Dunne, John Paul (2006)

<sup>167</sup> OCED (2004): 57

<sup>168</sup> del Castillo, Graciana (2011): 7.

often prefer to work as drivers, interpreters, and secretaries with higher-paying multilateral and bilateral agencies and NGOs. This affects not only the government's capacity to provide services and security, but also the current and future productive capacity of the country, since the few skilled people are not using their skills and will lose them over time".<sup>169</sup>

Figure 4.1: ODA as share of GNI

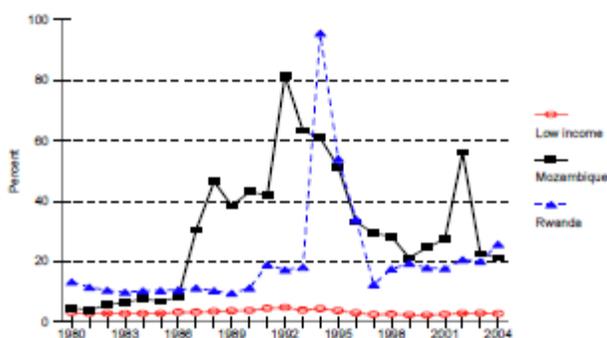


Figure 4: Official development assistance and official aid as share of GNI.  
Source: WDI (2006).

Countries in conflict experience various stages of monetary flow from donors to assist facilitation of economic development: emergency response, humanitarian aid, reconstruction assistance, development aid (whether project specific or government budget assistance), and foreign direct investment. These stages are not mutually exclusive or collectively exhaustive, nor do they follow suite in a linear fashion only. As it concerns the aforementioned paradigms of economic development, the movement away from structural adjustment to private sector development and poverty reduction strategies has been more inclusive of governments as a hybrid of development assistance and foreign direct investment. While this produces tangible results, many critique the policies as 'more of the same,' specifically as it concerns the resulting aid dependency and foreign imposition of policy instruments. For example, Mozambique is still characterized by a heavy dependence on foreign aid, high inequality and poverty levels, and slow development of sectors outside of agriculture. Although regarded as one of the success stories of post-conflict economic development, Mozambique's growth highlights the flawed use of GDP as an indicator of a healthy and stable economic stability. In 2005, although FDI reached US\$107.9m, this was far exceeded by ODA flows of US\$1,286m.<sup>170</sup> Figure 4.1 provides additional information on the amount of ODA as share of GNI, illustrating the spikes during the immediate aftermath of conflict in the early 1990s. Improvements in GDP are not adequate measures of successful economic reconstruction; per capita GDP is a better reflection of inequality, poverty allocation, MDGs achievement, education indicator improvements, etc.

<sup>169</sup> del Castillo (2011): 9.

<sup>170</sup> Bray, John (2007): *The Role of Private Sector Development in Post-Conflict Economic Recovery*. UNDP Report.

The international community has responded well to humanitarian crisis and aid spikes in the immediate aftermath of conflict; however, resulting externalities negatively impact long-term development. Aid can undermine and weaken institutional capacity and accountability leaving countries ‘cash poor but project rich’ and further deterring private investment from high debt recipients. Therefore, when aid is administered it should stimulate growth and not substitute for private sector development. Chapter Two discussed how emergency aid can be detrimental and utilized by warlords to exploit the population during conflict and how it negatively impacts market structures leading to anomalies during the war economy. To increase the short-lived benefits and counter-act unsustainable dependency, scholars suggest that aid is channeled through host governments to support national, integrated reconstruction strategies. In the aftermath of a conflict, aid should target “investment opportunities that use local capabilities, land, and natural resources [to] increase productive capacity. Its economic effect, however, will depend on how productively the aid is invested and the effects it has on the labor market, on the exchange rate, on reactivating production and trade, and on protecting the environment”.<sup>171</sup> Moreover, to be effective, aid must be integrated into other post-conflict reconstruction priorities and activities; this relates to coordination of actors and sequencing of development as “reconstruction aid cannot follow a piecemeal approach”.<sup>172</sup> This paper referenced Mozambique as an example of the negative implications of aid where ODA rose to over 80% of GNI in 1992 and was still at 55% ten years later; alternatively, El Salvador had a peace agreement in 1992 with an ODA at 7% of GNI in 1992, 2.5% in 1997, and 1.4% of GNI in 2001.<sup>173</sup> El Salvador began phasing out humanitarian aid early and gave up benefits under US Government Public Law 480<sup>174</sup>; instead of receiving grains, they reactivated local, basic grain production in 1991 and utilized methods for economic growth and local, private sector development other than ODA and various IFI economic programs.<sup>175</sup>

In understanding that low-income countries are more likely to engage in civil war, significant research has addressed the importance of development and aid in preventing conflict.<sup>176</sup> However, post-conflict aid dependency brings about another set of challenges for transitioning societies (i.e. conditional aid arrangements, unsteady aid flows, imposition of

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<sup>171</sup> del Castillo (2011): 12.

<sup>172</sup> del Castillo (2011): 12.

<sup>173</sup> del Castillo (2011): 14.

<sup>174</sup> Food for peace programs

<sup>175</sup> del Castillo (2011): 14.

<sup>176</sup> Collier (2003)

donor's agendas, corruption, lessen accountability to tax base, lessen government credibility, etc.). These negative externalities highlighted the failure of structural adjustment policies to acknowledge the importance of public sector engagement for growth in a post-conflict setting. The "Mozambique experience suggest[s] that it [is] important to undertake reform and restructuring at the same time and to get to know the nature of the post-war economy".<sup>177</sup> Such measures include building government capacity, data / knowledge and research, infrastructure and communication improvements, participation / reintegration of ex-combatants, emphasis on poverty alleviation and rural development in addition to private sector growth interventions.

In addition to strong aid dependency, distributive issues impact the socio-economic progress of a post-conflict society. In spite of economic growth, Mozambique faces "worsening [of] poverty in rural areas and [possibility] of state capture," in addition to a "predatory elite that robs banks and non-donor resources, smuggles and kills, and maintains a corrupt justice system. A symbiotic relationship has grown up between the Mozambican predatory elite and the donors to maintain the myth of the Mozambican success story".<sup>178</sup> These strong allegations and challenges can be addressed by government channeling of private sector development to curb reliance on foreign aid and harmful capital flows. In addition to promoting growth by addressing inequality and continually providing opportunities for development, Mozambique's private sector can contribute to sustainable peace as well as the state's credibility and capacity for reducing dependency.

There is no easy remedy to address aid dependency, but the quantity of foreign capital flows and the form that it takes (i.e. development assistance or investment capital flows) should be monitored. Some scholars suggest that the timeline in which investment should surpass foreign aid is five years. Given the contextual realities of post-conflict countries, in the immediate aftermath of violence there will be high aid and little private investment. Once infrastructure and institutions are established (resulting from significant investment climate activities), then private investment can surpass aid as the economy 'graduates' from conflict.<sup>179</sup> Slow privatization, corruption, small markets, and a complex / poorly structured regulatory system can slow this transition and should be monitored by external actors. Additionally, the donor procurement often takes place internationally and does not benefit the local economy,

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<sup>177</sup> Dunne (2006): 5

<sup>178</sup> Hanlon 2004: 760 as quoted in Bertelsen, Bjorn Enge (2005): *War, Peace, and Development in Mozambique: A Critical Assessment*. (Presented Workshop Paper). Bergen: Chr. Michelsen Institute, 66.

<sup>179</sup> Bray (2007): 13

giving little incentive for local employment or production. In summary, the most appropriate approach to addressing legitimacy and capacity building in post-conflict countries is by challenging aid through government. This engages the aforementioned issues as well as problems of coordination, fragmentation, corruption, gaps in policy, and duplication of efforts.<sup>180</sup> Although there are fears of government corruption, challenging donor aid through the public sector is ideal because there is (1) more information on and visibility into aid channels within government budgets, (2) less fungibility of aid money pledged to different entities, and (3) greater transparency and accountability controls (of certain entities) to appropriately disburse funds to other groups or individuals.<sup>181</sup>

### **Sequencing of Activities**

The effectiveness of private sector development in promoting both economic growth and sustainable peace is contingent on the manner of its implementation; of the utmost importance is the sequencing of capacity development, risk mitigation strategies, and donor coordination. Capacity development is the “gradual construction of enabling conditions for peaceful development”; this engages local governments, businesses, civil society actors, and the diaspora in establishing networks and inter-institutional working structures committed to common goals.<sup>182</sup> Socio-political sensitivity requires inclusivity in a post-conflict setting, as does sustainable peace in order to react to cultural shift and for change management to take hold for the success of the post-conflict transition.<sup>183</sup> This requires interventions based on existing economic resources, citizens’ basic needs, and the community’s historical comparative advantage; for example, utilization of local resources and inputs should produce products or services tailored to be inclusive of the general community.<sup>184</sup> In a post-conflict setting, this can involve utilizing new business opportunities that emerged during the war economy including “migration of labor, new businesses [even if informal], the break-down of binding traditional market structures, and the opening of new markets, new technologies, and new investments” to assist the masses.<sup>185</sup>

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<sup>180</sup> del Castillo (2011): 11

<sup>181</sup> del Castillo (2011)

<sup>182</sup> Bagwitz et al (2008): 20

<sup>183</sup> Bagwitz et al (2008): 19

<sup>184</sup> Bagwitz et al (2008): 20

<sup>185</sup> Bagwitz et al (2008): 20

Conflict sensitive programming in the private sector development framework must take into account the four different phases of conflict: end of fight; rehabilitation and restoration; reconstruction; development and transformation. The end of violence does not equal economic security as economic reconstruction activities still face significant risk. For example, there are problems of “micro insecurity, with armed inhabitants desensitized to violence, and high rates of robbery, [which can] discourage the acquisition of visible assets. Second, macro insecurity, the considerable risk that war will be resumed ... is particularly important [and] can be reflected in political instability...likely to discourage private investment.... A third type of risk is the fiscal shocks resulting from the war to peace transition”.<sup>186</sup> Therefore, the economy may not be truly open and private sector actors must develop coping strategies to deal with existing commercial mechanisms of rebels, warlords, etc. in the immediate aftermath of conflict.<sup>187</sup> To address this, sustainable private sector development requires a robust civil society and public sector to promote security and incentivize investment. While aid can facilitate infrastructure development and donors can provide guarantees, governments and local actors must improve the investment climate and regulations to encourage sustain capital flow.

The sequencing of activities in all phases of conflict transition and the division of appropriate roles and responsibly for various stakeholders is paramount. During the restoration and rehabilitation phase, conflict-sensitive sequencing of private sector development should consider implementation of Defense, Demobilization, and Reintegration (DDR) strategies with ex-combatants to address grievances, provide economic incentives for peace, and to promote social capital development as discussed in previous chapters. At this time, there is a “need [to] balance demands for greater economic growth with those for greater social justice and human welfare. A series of changes and promises to deal with grievances are likely to have been agreed and to underpin any peace deal. To ignore these and to impose generic policies for economic growth that may have high short run costs may well simply lead to a reigniting of hostilities”.<sup>188</sup> At the same time, transitional justice mechanisms addressing social justice may be costly and their prioritization a risk to economic reconstruction and future growth. Therefore a window of opportunity exist for a “systematic integration of PSD measures as first generation reforms in the immediate post-conflict reconstruction agenda [are] an essential foundation for sustainable

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<sup>186</sup> Dunne (2006): 2

<sup>187</sup> Bray (2007)

<sup>188</sup> Dunne (1996): 4

economic development, ... addressing short-term economic needs and supporting [the] peace building processes wherever feasible”.<sup>189</sup> DCED suggest three approaches concerning conflict sensitivity that go above and beyond the ‘Do No Harm’ principle, (1) working *around* conflict (viewing conflict as an impediment / negative externality to avoid), (2) working *in* conflict (do no harm; minimizing risk), and (3) working *on* conflict (“conscious[ly] attempt[ing] to design policy and programs with a primary focus on conflict prevention, management, or resolution”).<sup>190</sup> The last, active form of working *on* conflict allows implementation of economic programs that create peace-added-value such as conflict-sensitive private sector development.

In 2009, USAID’s research discussed the challenges and best practices regarding implementation of investment climate reform. Although written for the purposes of development professionals from donor countries, many of these lessons are applicable to all parties. Firstly, USAID notes the importance of relationships that can be understood to promote to building of social capital and trust. Managing expectations, improving security, building capacity of local partners, engaging various actors to avoid favoritism or hostility (including possible spoilers, women, diaspora community, etc.), and acknowledging that reform is not prioritized by all are factors for consideration during implementation of any post-conflict agenda. Additionally, while the best design of economic intervention activities utilizes a context-specific approach, there are significant costs and challenges to acquiring accurate and useful data from national accounts, firm-level surveys, household income surveys, expenditure surveys, and qualitative data from private and public sectors of post-conflict countries. If the data is even available, these undertakings often require external funding and their prioritization must be weighed against other vital needs of reconstruction states. In addition to brain drain of skilled workers, post-conflict environments face extensive damage to buildings and institutions, leaving the country with little or no data or data collection capacity.<sup>191</sup> Acknowledging these limitations, it is best to collect data in the immediate aftermath of a conflict to best contribute to post-conflict reconstruction when feasible.

Implementation of private sector development must balance short and long terms goals, acknowledging the trade-offs of interventionists and investment climate strategies. Given the

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<sup>189</sup> Bagwitz et al (2009): 1

<sup>190</sup> Sweeney, Naoise Mac (2008): 23.

<sup>191</sup> Investment Finance Corporation (2009): *A Rough Guide to Investment Climate Reform in Conflict- Affected Countries*. Washington, DC: Investment Climate Department, International Finance Corporation.  
[http://www.ifc.org/ifcext/fias.nsf/AttachmentsByTitle/RoughGuideICReform/\\$FILE/RoughGuideICReform.pdf](http://www.ifc.org/ifcext/fias.nsf/AttachmentsByTitle/RoughGuideICReform/$FILE/RoughGuideICReform.pdf)

post-conflict contextual realities, building parallel governance structures in the immediate aftermath of violence may be necessary; however, in the long run, it may prove problematic to replace indigenous structures or take away from local governance capacity. Accordingly, the preference is for private sector development to utilize existing institutions instead of creating artificial structures when avoidable. Another example of this is the short-term desire to create jobs utilizing the informal economy, but decision makers must consider the sustainability of economic growth given future regulatory reforms. Lastly, the importance of asset building in a post-conflict environment requires “diverting some resources to build outriggers – peace-building investments, recreation of the social contract, and reconstruction of the framework conditions that [underlie] social stability”.<sup>192</sup> This diversion of resources could be utilized for other pro-poor activities; governments and donors must weigh these and other tradeoffs in their desires to achieve both short-term and long-term private sector development goals while building political credibility and the capacity to implement future, sustainable policy reform.

### **Coordination of Actors**

In light of challenges with aid dependency and distributive issues, economic development in post-conflict developing countries requires external assistance. The private sector paradigm supports the emerging trend to seek investment for economic development as opposed to dependency on unpredictable aid cycles for sustainable growth. That being said, while African countries should play the primary role in economic development, realistic imbalances in today’s economy necessitate that the international community address inequalities in trade and eliminate distorting subsidies in industries like agriculture to stimulate growth.<sup>193</sup> For example, the G20 can address trade and infrastructure to assist business-led growth by encouraging an end to protectionist measures, reducing tariffs, and national subsidies.<sup>194</sup> In 1998, Soludo illustrated the need for trade reforms coupled with enhanced capacity to take advantage of opportunities for economic growth. Previous attempts at trade globalization and labor intensive exports had failed to level the playing field because of limited investment in skills and capacity. This provides an opportunity for donors to build the capacity of the population and invest in training of skill laborers.

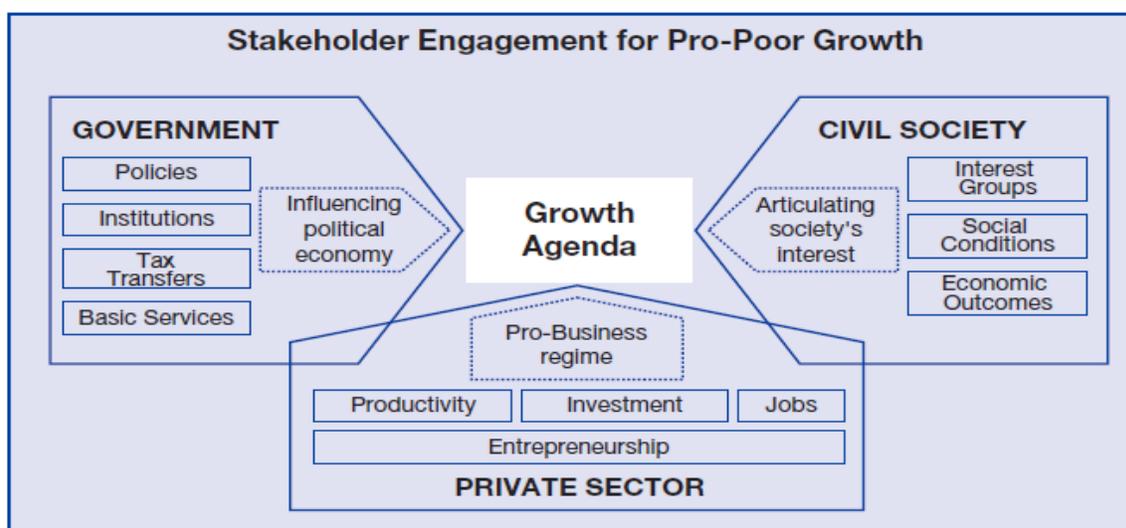
<sup>192</sup> Brauer, Jurgen and Dunne, Paul (2010): 14.

<sup>193</sup> Thiam, Tidjane (2011): The G20 Needs to Facilitate Private Sector-led Growth in Africa. *The Guardian*. <http://www.guardian.co.uk/global-development/poverty-matters/2011/feb/16/g20-private-sector-africa-poverty>

<sup>194</sup> Thiam, Tidjane (2011)

Numerous actors with varying agendas for growth often saturate post-conflict environments. Figure 4.2<sup>195</sup> highlights the importance of the integration of all three sectors of society for pro-poor growth. Additionally, international private sector entities and donors must display flexibility and facilitate coordination among themselves and with local actors to share information concerning deployment of staff, assessments and monitoring of results, and programming to prevent duplication of efforts.<sup>196</sup> These intentional labors will provide mutually beneficial for all involved specifically as it concerns research, policy advice, multi-donor finance mechanisms, and dialogue across the different sectors of local society to produce the best opportunities for growth and sustainable peace. Communication and education / socialization among other actors of activities, challenges, and best practices are vital to success of all concerned.

Figure 4.2



Post-conflict reconstruction requires coordination and cooperation of various actors from the public, private, and civil sectors of society. In analyzing private sector development and economic growth, the “commercial society drives it ... political [government] society provides framework conditions to direct and manage it, and ... civil society checks on the quality of the economy, for instance through insistence on subjecting growth to environment objectives or by demands for equitable growth”.<sup>197</sup> Accordingly, there are best practices for collaboration among

<sup>195</sup> OCED (2004): 51

<sup>196</sup> Sweeney, Naoise Mac (2008): 44-45.

<sup>197</sup> Brauer and Paul (2010): 19

the various actors including the state, local private sector, donor countries, MNCs, local armed groups, diaspora, regional actors, military, civil society organizations, and NGOs. Each actor can utilize different tools for reconstruction; for example, civil society organizations can contribute local knowledge and take ownership of building social capital; the local informal economy can provide jobs to stimulate growth; MNCs can input capital and create jobs with infrastructure projects; ex-combatants can contribute to the labor force; NGOs can train workers; and donor countries can provide conflict-sensitive foreign assistance. It is important to establish communication and coordination mechanisms to prevent duplicate of efforts, exacerbation of tensions, and to account for weakness in any given sector – for example the limited capacity of government in post-conflict settings can be compensated for by a robust civil society and enforcement of community rule of law.

External actors must acknowledge that “the priorities can only be set in the local context by analyzing the extent to which growth is pro-poor ... whether the factors that constitute an enabling environment for private sector development ... are in place, whether the pattern of growth resulting from them offers opportunities for the poor, whether outcomes in important markets are pro-poor, and the extent to which risk aversion and poverty traps exclude the poor. The priorities must also take account of current political settlements and the level of resistance to change”; most of these factors have been described or alluded to throughout this paper.<sup>198</sup> This may require the use of expensive assessments and diagnostic tools to analyze geographic, sector, institutional, and beneficiary terms of growth; the determination to utilize these tools<sup>199</sup> is similar to that of the justice – development economic tradeoffs discussed previously. Regardless of mechanism utilized, it is important to analyze the local context and effectively communicate the realities; how the private sector perceives opportunities, risks, and constraints influences its participation in and manner of development.<sup>200</sup> Continued monitoring and participatory learning, with feedback loops between stakeholders, impact development inputs to shape successful outcomes.<sup>201</sup>

Effective knowledge sharing and donor coordination of actors can assist multi-level interventions in complex environments and addresses short, medium, and long-term needs of post-conflict societies. As it concerns private sector development, the preference for investment

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<sup>198</sup> OCED (2004): 53

<sup>199</sup> Examples include UNCTAD’s investment compass

<sup>200</sup> OCED (2004): 53

<sup>201</sup> OCED (2004): 54

climate over interventionist priorities must be deliberated between various actors for a comprehensive and effective approach. The engagement of government with external actors and the local private sector is paramount in building the governance capacity of post-conflict states; specifically, private-public partnerships are a vital means by which to achieve economic growth and sustainable peace. Private-public partnerships for service provision can meet the needs of the people and facilitate private sector growth while also strengthening government legitimacy. Even in the absence of robust state capacity, it is important to preserve public trust; to this end, private-public partnerships at the very least give the state practice control or symbolic authority over private sector service provision.<sup>202</sup> Donor partnerships with the state can also contribute to its legitimacy and capacity building, ultimately resulting in more sustainable development and prevention of a relapse of conflict; donors can (1) serve as a guarantor by assuming risks and guaranteeing security for loans, (2) protect the interest of the state, (3) reserve regulatory and licensing powers, or (4) establish timelines for private sector provision of services among other functions.<sup>203</sup> Even with this assistance, there remains a challenge to ensure transparency and open communication among actors to prevent duplication of roles and responsibilities; limited cooperation may result from residual hostilities and a lack of trust after conflict.<sup>204</sup> Additionally, post-conflict governments must also be mindful of blurred lines between the public and private sectors, as seen with public officials who control private companies or military leaders who control resource access. These legacies of the conflict economic must be dealt with accordingly and monopolies' over-access to resources must be replaced with free and open competition and access to economic opportunities. External actors can participate in monitoring such progress to ensure that the population benefits from economic growth; these actors must remain mindful not to appear as bias interventionists or as predatory of a country's wealth.

In addition to public-private partnerships, donors can encourage engagement with local NGOs and CSOs to build social trust in post-conflict environments as previously discussed. These actors have a diversified and in-depth understanding of the context and may help prevent the appearance that external actors are 'taking sides' in intervention or development assistance. Depending on the timing of post-conflict reconstruction, these groups may have previously

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<sup>202</sup> Sweeney, Naoise Mac (2008): 31

<sup>203</sup> Sweeney (2008): 31; Bagwitz et al (2008), 130-1

<sup>204</sup> Sweeney, Naoise Mac (2008): 31

“act[ed] as alternative social institutions in the absence of an effective or trustworthy state”.<sup>205</sup> Therefore, government engagement of these entities further promotes government credibility and legitimacy in the eyes of the people. Humanitarian relief groups and external NGOs should also coordinate with these groups and local private sector actors to facilitate integrated relief programming in the aftermath of a conflict or during periods that necessitate emergency response. These efforts can address distributive issues and potential market distortions resulting from a failure to implement conflict-sensitive and context-specific private sector development. The UN World Food Programme’s Purchase for Progress (P4P) program, operational in Mozambique, is an example of such inclusive efforts that engage various stakeholders. This program addresses local procurement of food, cooperative engagement, and stability for investment. Local business associations have direct interest in private sector development; therefore, their coordination with NGOs and CSOs to best meet the needs of citizens helps facilitate pro-poor growth. Often these entities “can be very dynamic and flexible, but may have trouble scaling up or making their businesses sustainable in the long-term” necessitating external assistance; accordingly, early coordinator with other actors may improve opportunities for success.<sup>206</sup>

Multi-national corporations (MNCs) have a critical role to play in post-conflict reconstruction and private sector development. As discussed in Chapter One, the importance of conflict sensitivity is paramount and should exceed the ‘Do No Harm’ principle to actively work *on* conflict assisting with capacity building of local institutions (both private and public) to ensure sustainable peace. MNCs that operate in a conflict environment, and perhaps previously contributed to the war economy, at the very least provide employment opportunities, business linkages, and may also provide information about local knowledge assessment to benefit other actors such as NGOs who have limited resources to conduct similar analysis. Post-conflict environments often provide an unsaturated market with a large labor force, ideal for large MNCs willing to take the risk. That being said, MNCs should be integrated within the wider economy [or else] they will not contribute to broad-based economic growth, and [instead] introduce[e] a parallel economy in an already-destabilized country...add[ing] to fragility. Such an arrangement

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<sup>205</sup> Sweeney, Naoise Mac (2008): 32.

<sup>206</sup> Sweeney, Naoise Mac (2008): 34.

may also attract skilled laborers away from the mainstream economy, and create inequalities which may form the basis for future resentment and conflict”.<sup>207</sup>

By highlighting the failure of previous paradigms to positively build up the public sector, the private sector development paradigm heavily emphasizes the importance of all three sectors of domestic society. Additionally, partnership with international actors and coordination of activities is critical to preventing a relapse in violence by ensuring that underlying causes, especially grievances of specific populations, are addressed. The knowledge transfer between actors and partnership in development activities further builds social capital and forces integration of individuals for economic productivity and sustainable peace.

## Conclusion

This paper highlights the unique needs of post-conflict countries when it comes to the promotion of economies development and sustainable peace. In analyzing various economic development paradigms, the arguments presented here are in favor of the private sector development framework as the leading practices to be implemented. This framework and respective activities acknowledge the uniqueness of a post-war economy:

When wars end, countries confront a multi-pronged transition. Violence must give way to security for inhabitants; lawlessness and political exclusion must give way to the rule of law and participatory government; ethnic, religious, or class / caste polarization must give way to national reconciliation; and ruined war economies must be transformed into functioning market economies that enable ordinary people to support themselves....These multiple tasks make economic reconstruction fundamentally different from ‘development as usual’.<sup>208</sup>

After providing an understanding of the relationship between economics and conflict, Chapter Two outlined how the international financial institutions have pushed ‘development as usual’ agendas of liberalization, competition, open markets, and minimum government tax and expenditures; however, post-conflict development faces “issues concerning urban versus rural development, health, education, and personal security, women, youth, the elderly, and other vulnerable populations”.<sup>209</sup> These approaches failed to help build the sustainability of new governments in post-conflict countries and instance had three major negative impacts on government legitimacy resulting from their implementation: (1) prevention of flexibility in

<sup>207</sup> Sweeney, Naoise Mac (2008): 35.

<sup>208</sup> del Castillo, Graciana (2006): *The Rules of Reconstruction*. Project Syndicate. <http://www.project-syndicate.org/commentary/the-rules-of-reconstruction>

<sup>209</sup> Brauer and Dunne (2010): 7-8

printing money for peace-related programs and emergencies; (2) lack of government control over donor priorities in challenging aid; and (3) challenges in generating tax revenue for service provision to address inequality and other grievances.<sup>210</sup> These examples and those illustrated in Chapter Two highlight the need for post-conflict private sector development to be distinguished from broader economic development activities given that the objectives for the former are two-fold in promotion of both peace and economic growth.

The private sector development framework, described in Chapter Three, shed light onto the importance of reconciling economic development policies with post-conflict challenges including DDR, rehabilitation of services, or development of infrastructure. Rebuilding a post-conflict society demands national ownership, capacity, and ingenuity.<sup>211</sup> Accordingly, domestic policy decisions in post-conflict environments must take into consideration the need to balance long-term goals with the importance of adopting emergency policies, the instability of aid flows, the possibility of corruption and elite exploitation of resource wealth.<sup>212</sup> Accordingly, the engagement of all three sectors of domestic society and external actors are vital to the reconstruction process.

Chapters Three and Four focus on how achievement of sustainable peace requires economic reform that addresses underlying and precipitating factors of conflict which include social distrust and lack of / unequal economic opportunities. Accordingly, distributive issues and aid dependency are unsustainable and can cause a reigniting of hostilities. It is of utmost importance to design incentives in such a way that is within the capacity of a young government. This requires participation of public, private, and civil society actors. For example, this paper has highlighted how providing citizens with the ability to earn incomes and productively contribute to society can mitigate incentives for violence, demonstrating how economic development and the pursuit of growth can contribute to peace even at the community level. As stated previously, in understanding that trust is of economic value,<sup>213</sup> adequate post-conflict economic reconstruction programs must address not only good governance and institutional reform but also the rebuilding of trust.

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<sup>210</sup> del Castillo (2011): 10

<sup>211</sup> del Castillo (2011): 5

<sup>212</sup> Identifying those 'most affected' should also take into consideration equity implications to prevent perceived inequality which can reignite hostilities. Del Castillo (2011) cites the example of UNDP's 1992 arms-for-land program in El Salvador.

<sup>213</sup> Fukuyama (1995)

The analysis of historical economic development paradigms implemented in post-conflict countries and their failures illustrate the need to understanding the role of economic inequality in incentivizing violence and hindering sustained governance and growth. The pro-poor growth and poverty reduction strategies of the late 1990s and early 2000s began to address these concerns; these approaches emphasized the role of institutions in sustaining growth, but still failed to set benchmarks for private sector development or monitor outcomes for the private and civil society sectors.<sup>214</sup> The private sector development framework acknowledges the importance of governance in both growth and sustainable peace. Although written in reference to resource wars, the statements of Le Billion in suggesting that the “likelihood of violent conflict decreases as human capital develops (e.g. through education, trading, and manufacturing skills), the economy diversifies, and governance becomes more representative and accountable” are relevant to development in a broader context.<sup>215</sup> Accordingly, if it is the corruption of the state and inability to secure resources and livelihoods for their citizens that exacerbates conflict, then building the capacity of state institutions should be prioritized to prevent or mitigate conflict. The final chapter of this paper has engaged dialogue about criticism and challenges of the private sector development approach; specifically as it concerns aid dependency, coordination of actors, and challenges in sequencing of actors. While a step in the right direction, this approach must be further refined and will require continued adaptation as public officials, business owners, scholars, development professionals, and others begin to implement these policies in the future post-conflict countries of Iraq, Afghanistan, South Sudan, Libya, etc.

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<sup>214</sup> OCED (2004): 9

<sup>215</sup> Le Billion, Phillipe (2001). The Political Ecology of War: Natural Resources and Armed Conflicts. *Political Geography*, 20:561-584.

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