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Public–Private Partnerships in State-Building and Recovery from Conflict

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RTI employees inspect a wastewater treatment plant that has not worked in 8 years. During the war the tanks were used by Iraqi soldiers to store petroleum products. USAID partner RTI is finding solutions for the ageing, poorly maintained water and wastewater infrastructures. *Source*: www.usaid.gov. Photo: Thomas Hartwell

Summary

- Collaboration between government and business is especially important in states that are recovering from conflict. However, the relationship between the public and private sectors has all too often been undermined by mutual distrust and poor communication.
- While acknowledging the differences between the two sectors, policy-makers should actively seek out partnership opportunities between them.
- Both public- and private-sector agencies need to be sensitive to the ways in which all their actions, even those that appear purely 'technical', can influence the risk of conflict, for better or for worse.
- Specialist companies may contribute in policy areas such as legal, financial and security-sector reform. The most important contribution of the private sector as a whole will be for companies to concentrate on their core commercial activities, create jobs and pay taxes.
- Success demands a focus on local solutions for local problems, and a willingness to select the most appropriate 'tools', whether from government, civil society or business.

Introduction

The 2006 UK Department for International Development (DFID) White Paper *Eliminating World Poverty: Making Governance Work for the Poor* rightly emphasizes the need to build government capacity as an essential step towards ending world poverty. The need for effective governance is all the more pressing in countries that are caught up in – or recovering from – conflict. Successful state-building and post-conflict recovery will require the collaboration of a broad range of different agencies: not just governments and multilateral institutions, but also civil society and business.

This briefing paper focuses on the role of the private sector in partnership with other political, economic and social actors. The private sector's role is critical because it often has access to funds that states lack, as well as sources of expertise that may be hard to locate in government offices. No country can expect to create the economic basis for a lasting recovery from conflict without the active participation of both domestic and international companies. However, although there are many success stories, public–private partnership is often impeded by lingering prejudices on either side, and by a sense of confusion about each other's roles.

The purpose of this paper is therefore to identify the areas where there is broad agreement on the principles of public–private partnership, as well as those where there are continuing controversies, and to point the way forward. It draws on a range of recent research and practical experience as articulated in – among other sources – the December 2005 Chatham House/Control Risks conference on *Partnerships for Stability and Development*: *Improving Collaboration between the Public and Private Sectors.*

A single global agenda

'Stability' and 'development' may at first sight appear to be separate topics but, as Lord Hannay of Chiswick pointed out at the Chatham House conference, they are part of a single agenda: 'You cannot have security and stability without development and you cannot have development without security and stability.' This principle applies both locally and internationally: 'A world plagued with poverty, disease and environmental degradation will be a world short of stability and a breeding ground for the threats which already face us.' International developments since the 9/11 terrorist attacks have underlined the potential links between state failure in Central Asia, the Middle East or Africa and threats to the security of Western interests in Europe and North America.

One key area of broad agreement in this single agenda is the central importance of the state for both stability and development. There may be contention about, for example, the extent of government regulation in the communications sector. There may also be disagreements about the extent to which the state should delegate direct responsibility for managing public utilities such as transport and water. However, few doubt that the state has primary responsibility for defining and administering laws, and for enforcing security. If it is unable to accomplish these vital tasks, both public- and private-sector development will be severely impeded.

At the Chatham House conference, Kanja Ibrahim Sesay of the National Commission for Social Action in Sierra Leone pointed to some of the factors that had contributed to state failure and civil war in his country. They included excessive centralization of decision making; elite monopolization of wealth; a political culture focused on the capture of resources for particular individuals rather than the generation of wealth for all; limited organizational capacity in government; and a climate of mutual suspicion between government and private sector.

The first priority of international policy must be to work with local actors, including business, to increase the effectiveness – and equity – of weak states to prevent them descending into civil war as Sierra Leone did. The second, far more difficult task is to rebuild failed states.

State failures and war economies

Where states break down, the result is not so much a vacuum as the proliferation of local centres of power in 'warlord' domains, each of which is underpinned by its own local and international economic network. In Afghanistan and parts of northern Burma, the main economic basis of these domains has been opium, which ultimately is sold on the streets of Western cities. In parts of Angola and in Sierra Leone, war economies notoriously were based on 'conflict diamonds', many of which found their way into display cases in elite Western showrooms. In such cases the boundary line between political forces and organized crime often becomes increasingly blurred, as does the boundary between local conflict and international collusion.

War economies and criminal networks do not automatically come to an end when fighting stops. In order to negotiate a ceasefire, it is often necessary to make compromises which leave powerful local and regional figures in place, thus impeding the emergence of viable peacetime political and administrative structures.

Examples include Lebanon where – as the events of July 2006 demonstrated all too dramatically – the

Hizbullah movement has been able both to keep its weaponry since the 1975–90 civil war and to run what amounts to a parallel quasi-governmental power structure in the south of the country. In Bosnia the 1995 Dayton Accords ratified a fragmented political structure which, at least for a time, preserved the power of the former communist apparatchiks whose conversion to ethnic nationalism had helped precipitate war in the first place. In Kosovo, ethnic Albanians created parallel networks in the 1990s as a means to circumvent Serbian oppression; in the current century the same networks support organized crime and impede the development of a legitimate political economy.

In all these cases, weak local administrations underpinned by the international community have had the task of rebuilding viable physical and administrative infrastructures in societies that remain fiercely divided. At best, the reconstruction process takes time – not months, but years and possibly decades. The whole process is certain to be intensely political at both the local and the national levels.

A number of questions then arise. What can the private sector do to speed up the process of recovery? What can governments and multilateral institutions do? How can civil society organizations contribute? And how can they best work together?

The need for conflict sensitivity

The first requirement applies to all actors in all sectors: they need to be sensitive to the ways in which all their actions, even those that appear purely 'technical', can either exacerbate the risks of conflict or alleviate it.

In her ground-breaking book *Do No Harm*, Mary B. Anderson (1999) showed how aid agencies could unintentionally contribute to conflict, for example by focusing development initiatives on one half of a divided community. Even if the agency's priority appears justified by a wish to concentrate on the people most in need, it will send the wrong political message. By contrast, projects that focus on common problems – for example cleaning up a shared water supply – may serve as 'connectors', bringing communities together instead of dividing them. Similar principles apply to companies which may, even if unintentionally, exacerbate local social divisions, for example by giving generous compensation to landowners whose land is in the path of a gas pipeline, but nothing at all to their immediate neighbours.

At a broader level, companies risk feeding into 'war economies', for example by purchasing minerals from suppliers who, perhaps via a series of middlemen, are associated with regional warlords. This was the case in the late 1990s and early years of this century with purchases of coltan, a mineral used in the manufacture of mobile phones, which had been sourced in the eastern parts of the Democratic Republic of Congo (DRC). Recent policy-oriented research, for example work on civil wars by Paul Collier et al. (2003), has highlighted the links between distorted economic structures and conflict. The challenge is to create a political and social environment that favours legitimate, transparent economic activity, and therefore reinforces peace-building rather than undermining it. This is a task for both state and private-sector actors.

Creating an enabling environment: the case for public–private partnership

In thinking about post-war reconstruction, there has been a tendency to concentrate on physical infrastructure such as roads, power lines and water supplies. This is appropriate, because all these things are essential. At the same time, the lessons of the recent past point to the importance of the 'software': the need to provide basic security and an equitable legal and administrative framework to create an enabling environment for private-sector development.

The state holds primary responsibility for creating an enabling environment. Governments, not companies, have the political legitimacy to set legal rules, define security frameworks and sign peace treaties. Their legitimacy will be compromised if they appear to be captured by partisan political or commercial interests, whether these come from within the country or outside it. At the same time, alongside international development agencies and civil society organizations, private companies have come to play a supplementary but increasingly important role both as providers of expertise and as implementing agencies.

The case for private-sector involvement in policy reform is first that companies and individual business people know from their own experience what is needed in the economic arena and what is likely to work. Both local and international companies are – in contemporary parlance – stakeholders in economic recovery, and they have expertise to share with the government. Secondly, companies have the resources and skills to serve as implementing agencies for reform programmes, often at short notice. In that respect, they may be able to supplement (though not to replace) government and multilateral agencies.

Security-sector reform

Security-sector reform comes high on the list of priorities for companies as well as governments. In many countries emerging from conflict, poorly paid and badly trained government forces have been a source of insecurity and fear rather than of reassurance.

One example is the DRC where there is a direct link between security-sector reform and the interests of the domestic and international mining sectors. Companies need a secure environment in which to operate. However, in the recent past, mining companies have been accused of colluding with ill-disciplined government forces that have committed human rights abuses. The long-term 'licence to operate' of the companies that are now investing in the country depends in part on their ability to avoid such episodes in future. For this to happen, there need to be well-disciplined, professional armed forces that maintain order without infringing human rights.

In the DRC and other countries recovering from internal conflict, security-sector reform should be a priority area for international assistance. In all cases this assistance must be subject to public oversight, but the actual providers may now come either from government agencies or from specialist private consultancies.

Legal and administrative reform

Legal and administrative reform may seem less urgent, but it is a priority nevertheless. In many cases reforms are necessary because new administrations inherit outdated structures that were designed for socialist political systems that are no longer in place.

International companies were slow to return to post-war Bosnia in the late 1990s despite significant investment in the repair of the country's physical infrastructure: the main deterrents were the socialist-style bureaucratic obstacles and the limited local market, rather than fear of a resurgence of fighting. Local companies complained about the same problems, but Bosnia's legal and administrative reform process only really got under way in the last few years. In the light of subsequent experience, it is clear that it should have begun much earlier.

Algeria is currently going through a similar process of review. In a speech at London's Mansion House during his official visit to the UK in July 2006, Algerian President Abdelaziz Bouteflika reported that his government was investing heavily in national infrastructure as it seeks to recover from years of conflict. However, he hoped that the state's role would be 'only provisional', and would soon be 'overtaken by the forces of a free market'. In order to make that happen, Algeria is reforming its state structures and adapting its laws and regulations to the norms of a market economy.

A related issue is the need to take steps to curb corruption. In the immediate aftermath of an emergency such as a war or, for that matter, a tsunami, aid agencies and companies may be tempted to justify illicit payments to obstructive officials or political bosses as a necessary short cut enabling them to perform vital services. In genuine emergencies everyone has to make their own judgments, but such payments should be resisted because they reinforce corrupt structures, thus making long-term recovery more difficult.

Industry and professional associations are coming to play an increasingly important role in these areas. For example the American Bar Association (ABA) has extensive experience of advising on legal reform in Central and Eastern Europe. Alternative sources of expertise include companies such as Crown Agents with specialist skills in, for example, customs reform.

Financial-sector reform

Financial-sector reform touches on the basic infrastructure of economic activity. Again, this was an issue in Bosnia: until 2001 companies had to cope with socialist-era Payment Bureaux which dominated all public and private financial activity, including payment transactions, savings and tax collection. Their abolition paved the way for a much more efficient private banking sector in which foreign banks have played a key role.

In Afghanistan the challenge has been to create a modern financial sector almost from scratch. The informal *hawala* system based on centuries-old social networks and traditions of trust has provided a much more efficient system for the transfer of funds both locally and internationally than the formal banking network. However, although *hawala* enjoys a high degree of social legitimacy, it needs – at the very least – to be complemented by more formal banking structures if the economy is to recover fully.

One example of public–private partnership in the financial sector comes from Iraq, where a consortium of international banks led by JPMorgan Chase and Co helped set up the Trade Bank of Iraq in 2003. The bank facilitated the import and export of goods and services for an initial period of one year, which was subsequently extended. It had start-up capital of $100 million ($5 million from the then Coalition Provisional Authority and $95 million from the Iraq Development Fund managed by the UN).

Guiding principles

In all these areas of partnership, three principles are paramount. The first is that the ultimate objective of all external actors in reform processes – whether these come from the private or the public sector – should be to reinforce local government capabilities, and not to replace them. The second is transparency and accountability: in matters of public policy, governments call the shots and external parties must be accountable both to them and to the people whom they serve. The third, related area is local ownership: no reform process is likely to survive unless key local actors are involved from the start and lend their full support.

Commercial opportunities, risks and impacts

While specialist companies may be able to contribute to policy reform, the most important contribution of the private sector as a whole will be for companies to concentrate on their core commercial activities, create jobs and pay taxes. However, particularly in the immediate aftermath of conflict, governments need to be realistic in their expectations of the scale and speed of the private-sector response. It may be in the public interest for companies to invest, but the calculations made by individual firms will depend on their own appetite for risk.

Risk assessment goes two ways. Naturally, companies first consider the physical and financial risks to themselves of operating in conflict-affected environments. There are also risks and opportunities for the host country. Specialist risk management consultancies such as Control Risks with both public- and private-sector experience may be able to bridge the gap between the two sides. The extent to which individual companies make a positive or a negative impact – and can secure long-term public and political support in their host countries – will depend on their size, sector and the manner in which they conduct their operations. How far are they sensitive to the risk that their activities may, directly or indirectly, contribute to conflict rather than to peace-building? What are they doing to mitigate such risks?

Local, diaspora, regional and international companies

Local business leaders are of primary importance. They know the terrain, they have the connections, and they have the highest possible motivation for success: they need to survive to provide livelihoods for their families, and to rebuild their countries. The UK-based non-governmental organization (NGO) International Alert has recently published a study highlighting the role of local firms in peace-building, or in reinforcing conflict.

Local business politics can be as fraught and as complicated as any other variety. A report by Sarah Lister and Adam Pain (2004) shows how markets in Afghanistan are not as free as they seem because would-be new entrants are squeezed out by existing operations which enjoy the political support of powerful regional bosses. The extent to which local companies are able to operate successfully will be a key indicator for potential external investors.

After local companies, the firms most likely to invest are those belonging to diaspora entrepreneurs, regional firms (for example Austrian banks in the Balkans, or Turkish hotel owners in the Georgian breakaway republic of Abkhazia), or smaller international firms which see a first-mover advantage in taking higher risks than their established competitors. Large international companies will invest in high-risk countries, but only if they see commensurate returns. Typically this has been because of the large size of reconstruction budgets, as in Iraq, or because of the possibility of securing access to rich natural resources

Oil, gas and mining

Much of the international discussion about the role of the private sector in conflict regions has focused on oil, gas and mining. This makes sense because many of the most attractive new geological opportunities for these industries are in conflict-affected areas. There has also been a long-standing debate on the links between rich natural endowments, war economies and oppressive regimes. Botswana's sound administrative structures have helped turn diamonds into a blessing. Elsewhere in Africa – for example Algeria, Angola, Congo, Nigeria, Sierra Leone and Sudan – rich mineral resources have all too often been associated with the curses of conflict and state failure. The extractive industries are more exposed to political risk than other sectors: they also have a more dramatic impact on their host countries, often bad but potentially good.

Painful experience has been a spur to innovation and reform. Leading Western companies have developed a body of best practice in addressing social impacts and mitigating conflict risks. At the Chatham House conference, Barnaby Briggs of Royal Dutch Shell explained how his company had learnt to look at its operations through a 'conflict lens': do operational decisions reward conflict or constructive behaviour? Do they convey disrespect or respect for stakeholders? Do they contribute to social fragmentation or cohesion?

Much of this experience of working with communities is shared through industry bodies such as the International Petroleum Industry Environmental Conservation Association (IPIECA) and the International Council on Mining and Minerals (ICMM). At a more political level, the UK is leading the Extractive Industries Transparency Initiative (EITI), which involves companies, NGOs and both 'northern' and 'southern' governments, and promotes clear public reporting of oil and gas revenues. Greater transparency should reduce the risk of revenue being diverted to corrupt, private uses, and, in principle, diminish the risk of political conflict.

Telecoms

Telecoms – notably mobile phones – have an entirely different business model. Investments are much smaller, returns are quicker, and the social impacts are much less controversial because it is easy to point to the benefits to local economies. The beneficiaries include small local entrepreneurs who benefit from improved communications to gain better access to markets.

Celtel, founded by Dr Mohammed Ibrahim in 1998, is a notable success story. It has more than 10.5 million customers and provides mobile networks and services to 15 African countries, including conflict-affected regions such as Sierra Leone, the DRC and Sudan. The business opportunities, and social benefits, in countries recovering from conflict are all the more attractive because of the 'pent-up demand' for services that have hitherto been unavailable. Africa's growth potential is enormous: to date only 14% of the continent's inhabitants have access to mobile phones.

At the Chatham House conference, Dr Ibrahim emphasized the importance of the highest standards of corporate governance. The company's board members include former British cabinet minister Lord Prior and a representative of the International Finance Corporation (IFC). This enables it to demonstrate that it is a 'serious' company which will not tolerate any form of corruption.

Construction

The reconstruction of physical infrastructure such as roads, power stations and water utilities is an essential precondition for recovery. For international companies, reconstruction projects in war-affected countries provide a classic case of the need to balance high political and security risks with the potential for high financial returns. In both Afghanistan and Iraq, major construction projects have presented attractive targets for insurgents, leading to a series of casualties.

In many countries the construction sector has run into controversy because of corruption allegations: the temptations are all the greater because of the large scale of major public projects, and the frequent lack of transparency in the procurement process. Bribery allegations in conflict-affected countries are particularly sensitive because they undermine the credibility of the reconstruction process. A second common controversy has been over the extent to which international companies do or do not make use of local sub-contractors – thus creating much-needed local employment – or even over whether the involvement of expensive foreign firms is really necessary in certain projects. The industry provides many examples of the need for public–private collaboration, but also of the hazards that need to be negotiated if partnerships are to retain their credibility.

Banking

The establishment of a good retail banking network is an important part of the recovery process. However, bankers are trained to be risk-averse and are often slower to set up operations than host governments might wish.

Among international banks, Standard Chartered has a reputation for being among the first to set up in post-conflict regions such as Cambodia, Sierra Leone and Afghanistan. This is partly because it is following (or anticipating) its customers, many of whom belong to the diplomatic and development communities. In other cases, regional banks have tended to take the lead. For example, ANZ was the first foreign bank to open a branch in Timor Leste following its split from Indonesia, while South Africa's Stanbic Bank was one of the first to set up in the DRC. In the early stages of post-conflict reconstruction, retail banks tend to be slow to extend their networks outside national capitals, but may do so as the recovery process begins to gather steam.

The role of multilateral institutions: engagement, risk mitigation and standard-setting

Questions about the pace and timing of investment apply to all commercial sectors, not just banks. In the five years after the end of a conflict, countries can typically expect a significant influx of foreign aid but this will begin to tail off as the reconstruction process gathers pace and the attention of the international community turns elsewhere. In order to maintain the momentum of recovery, it is essential to replace aid with commercial investment sooner rather than later. Often this is difficult because countries that have suffered from conflict experience a 'reputation lag' even after the situation has begun to improve.

The World Bank and the regional development banks can help speed up the process in a number of ways. First, the banks' participation in commercial projects in the form of loans or guarantees can help mitigate political risks in conflict-affected areas. For the companies involved, the most important aspect of the banks' involvement is not so much the size of the loan or the guarantee as the political support that they can offer in case of difficulty. One significant recent initiative is the Afghanistan Investment Guarantee Facility which was established in 2004 by the World Bank's Multilateral Investment Guarantee Agency (MIGA) in association with the Asia Development Bank (ADB). The facility puts particular emphasis on the need to support small and medium enterprises (SMEs). However, a recent report by the World Economic Forum (2006) argues that the development banks can and should do much more to develop risk mitigation products that improve developing countries' access to otherwise untapped sources of private finance.

The multilateral banks play a second important role by improving standards among the companies with which they deal. The IFC's revised *Performance Standards on Environmental and Social Sustainability*, which were launched in April 2006, included formal community engagement and security management requirements for all IFC-sponsored projects. The IFC's performance standards have in turn become the benchmark for the 'Equator Principles' on project finance adopted by some 35 leading international banks (*www.equator-principles.org*).

The third area of particular importance is the banks' direct engagement with government, both in the form of loans and in the form of policy advice, all of which can help establish the enabling environment that the private sector needs. In this context, the World Bank's current emphasis on combating corruption in all its forms is especially important.

The UN Global Compact, launched by UN Secretary-General Kofi Annan in 1999, was a significant step forward in the UN's engagement with the private sector. Corporate signatories to the compact declare their commitment to a set of ten basic principles concerning human rights, labour, the environment and transparency. From the compact's inception, participants were concerned with the private sector's role in conflict-affected areas. In 2001 this concern led to the publication of a *Business Guide to Conflict Impact Assessment and Risk Management.* This was followed in 2005 by a guidance document directed at both governments and companies: *Enabling Economies of Peace: Public Policy for Conflict-Sensitive Business*.

Similarly, the United Nations Development Programme (UNDP) has in recent years placed increased emphasis on partnership with the private sector. Its 2004 report *Unleashing Entrepreneurship: Making Business Work for the Poor* highlights the role that small and large companies can play in alleviating poverty and, like the 2006 DFID report, stresses the need for good governance. The UNDP and other UN agencies can play an important role in helping facilitate engagement between the private sector, government agencies and civil society in developing and transition economies.

Outlook: global principles, local solutions

The Chatham House conference on *Partnerships for Stability and Development* highlighted the common interests between the public and private sectors. As Kanja Ibrahim Sesay put it: 'The business sector has a direct interest in promoting good governance in order to build a more stable and predictable enabling environment for the private sector. The public sector, in turn, has a direct interest in promoting enterprises that create jobs, pay taxes and spur development.'

As Sesay went on to say, the relationship between the two sectors has too often been undermined by mutual distrust and poor communication. This observation applies as much to the wider international scene as it does to Sierra Leone. This lack of trust derives in part from deeply entrenched and often divisive institutional cultures. But it is time to get beyond caricatures.

To make progress, both sides need to recognize differences*.* Acknowledging common interests does not mean that the private and public sectors are 'the same'. Companies have to make a profit, and provide value for money, or they fail to survive. Similarly, both sides need to acknowledge diversity. Companies – and, for that matter, government departments – are distinguished as much by their differences in size, sector, national origin and institutional culture as by what they have in common. Different institutions will demand different approaches.

Particularly on the business side, it is essential to continue developing ethical standards. Officials sometimes question whether there is a common ethical basis for engagement between public servants and business people motivated by profit. If companies are to win public trust they need to demonstrate, again and again, that they operate to the highest standards. Similarly, companies and governments have a common interest in combating corruption and refining 'conflict-sensitive' strategies for development. 'Doing no harm' is the minimum requirement.

Looking ahead, three principles should guide policy-makers:

- *Find local solutions for local problems.* There are common principles, but no templates. Local solutions must be grounded in the demands and aspirations of the people whom they are intended to benefit.

- *Select the most appropriate 'tools'.* Private companies have access to specialist resources, and can often respond more rapidly than government agencies. If they are best suited for the task in hand, then use them.

- ***Look for 'win-win' partnership opportunities.*** **Among others, USAID, the US Agency for International Development, is actively seeking opportunities for co-operation between government, business and civil society in development projects. The more examples of such cooperation there are, the more we can learn.**

As much as anything else, both sides need to keep talking. The field of public–private engagement continues to evolve rapidly. We all need to learn from each other's experiences. Neither partnership nor conflict nor state-building will disappear from the international agenda any time soon.

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