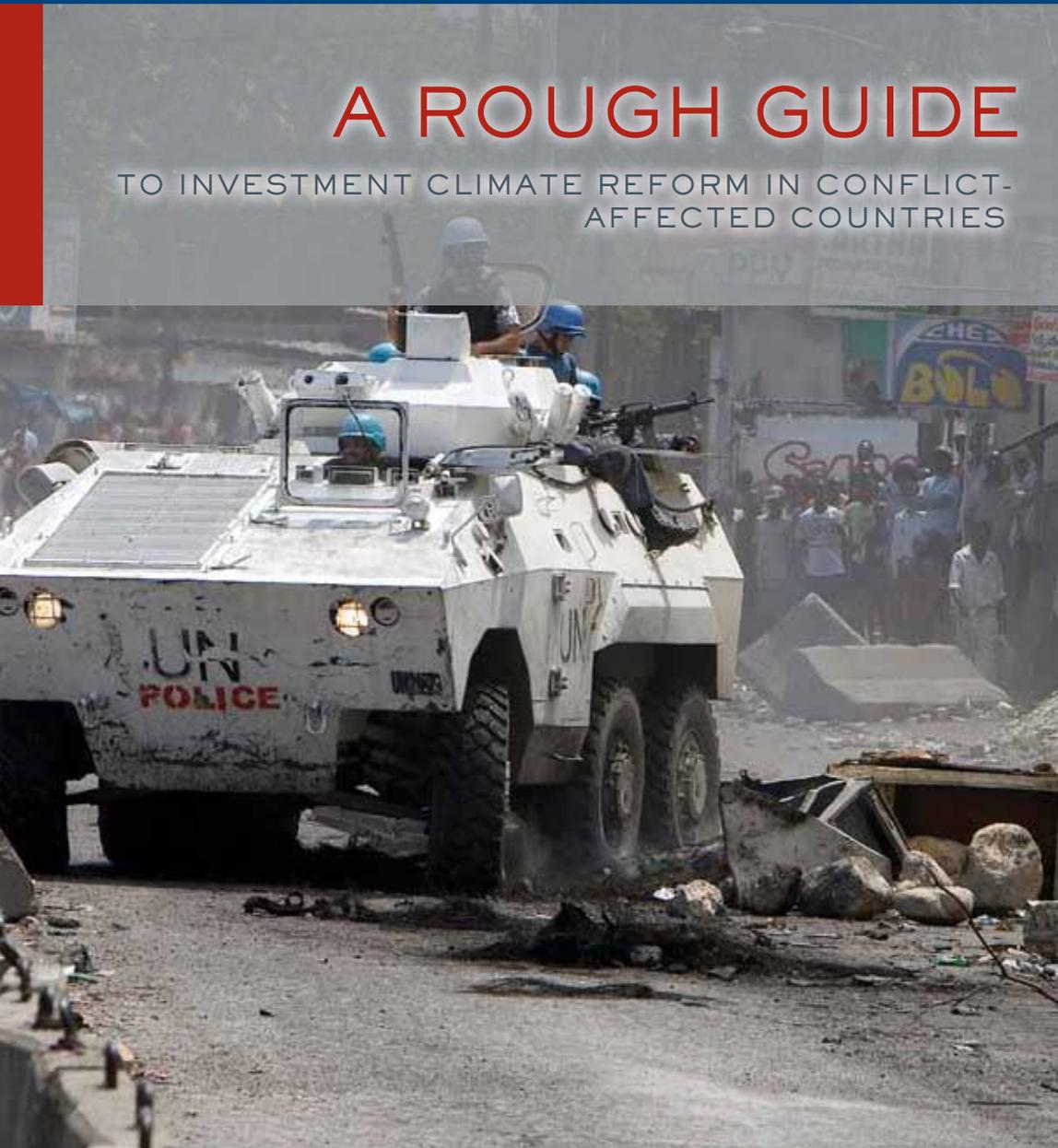


# A ROUGH GUIDE

TO INVESTMENT CLIMATE REFORM IN CONFLICT-AFFECTED COUNTRIES



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# A Rough Guide to Investment Climate Reform in Conflict-Affected Countries



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**Most conflicts have a strong economic**

or commercial dimension and are driven by rational decisions for legal or illegal profit.



## Executive Summary



### What Do Investment Climate Project Teams Face in Conflict-Affected Countries?

- Most conflicts have a strong economic or commercial dimension and are driven by rational decisions for legal or illegal profit
- Conflict has wide-reaching negative impacts on people, infrastructure, institutions, markets, and trust in government—with the scope of such impacts depending on the extent of conflict
- Jobs and investment are critical for peace; investment climate reform increases both
- Investment climate reform is also critical to state-building; reforms to government institutions that regulate the business environment can inculcate transparency, honesty, professionalism, and client service—all key to restoring government legitimacy.



## Guiding principles for catalyzing investment climate reform

- There is no universal blueprint for reform in conflict-affected countries
- Key preconditions for reform include staff safety, humanitarian relief, donor engagement, and openness to reform
- Flexibility and innovation are essential at all stages of reform
- Conflict sensitivity and “do no harm” principles must guide all project decisions

## Investment climate diagnostics

- Technical analysis of the investment climate must be accompanied by analyses of political and economic power and of the causes of conflict.

- Conflict-affected countries do not allow much time for long technical studies—but shorter analysis can still be effective.
- Political and economic analysis is critical for understanding who has what power and interests, and who is connected to whom.
- Good conflict analysis will identify root or historical causes, proximate or recent causes, and triggers of conflict.
- Project teams often do not have to conduct original conflict analysis, and should consult existing analyses.

## Planning for investment climate reform

- Timeframes are longer and costs higher in conflict-affected countries, and projects should build in extra time and budgets accordingly.
- Start early to find the right team members and ensure effective planning and coordination.
- Security preparedness and staff well-being should be among the first considerations when planning a reform project.
- Reputation risks cannot be avoided—only mitigated.

## Implementing investment climate reforms

- Relationships take precedence over implementation arrangements; the latter can change easier than the former.
- Client capacity in conflict-affected countries often need extensive help with reforms, from small to large tasks.
- Managing expectations is important in any project; in conflict-affected countries it can improve the security of project staff.
- Efforts should focus on building a constituency of reform, and avoiding a single champion.
- Including unconventional stakeholders in reform can preempt attempts to spoil change.



- Women are often a silent but powerful stakeholder group for investment climate reform.
- The diaspora can bring ideas, talent, money to support investment and reform; they can also spark resentment from those who stayed in country and endured the conflict. Quick support and rapid follow-up helps build trust in commitment to reform.
- Even the appearance of impartiality can be politically dangerous; a communications strategy can help.
- Mid-level practitioners can be important sources of advice and reform progress; they should not be ignored in favor of top-level government staff.
- Coordination is difficult to achieve in “normal” developing country contexts. It is even more important in conflict-affected countries, and extends past agency-to-agency coordination—it involves strategic location of reform in the wider reconstruction agenda.
- Cultural differences in are to be expected; in conflict-affected countries they include differences between those who have had to survive in very difficult circumstances and international aid workers, and include differences between military and civilian cultures.
- Setbacks and failure are a real possibility, as is the reform work becoming a lower priority as crises emerge and politics shift.





## Monitoring and evaluation of investment climate reform in conflict-affected countries

- The extent of damage to buildings, institutions, and skilled workers may leave a country with little or no data or data collection capacity, making it very difficult to measure impact.
- Given the importance of baselines in assessing project progress, data collection should begin immediately after conflict ends; often many agencies are conducting surveys, and their data could be used or include questions relevant to intended reform.
- The “gold standard” of data collection will elude most project teams; efforts to innovate with methods with indicators may be needed.
- As difficult as it may be, efforts should be made to measure how investment climate reform contributes to peace.



**Given the highly volatile,** fragmented nature of conflict-affected country situations, a lot of information on specific people, decisions, and relationships can only be acquired once you are on the ground.



1

# What to Expect from This Guide



This guide is designed to help project teams engaged in investment climate reform in conflict-affected countries more effectively design, plan, implement, and evaluate reform projects. In this guide *investment climate* refers to government laws, policies, regulations, and procedures that improve institutional governance, bureaucratic efficiency, and industry competitiveness.

Writing a guide on investment climate reform in conflict-affected countries poses challenges. An absence of violence is not the end of conflict, and conflict can be hard to define. Violent conflict can occur in many settings and has innumerable and complex permutations. In this guide *violent conflict* refers to organized armed warfare rather than, for example, criminal gang activity or mob violence (box 1). This somewhat broad definition requires an approach to understanding conflict that is pragmatic, flexible, and tailored to individual countries.

The guide's primary insight is also its framing principle: there are no blueprints for success, and every country needs a unique response. This simple and intuitive idea, echoed through dozens of interviews and IFC notes (called Smart Lessons), has shaped this guide. But the guide also rests on the assumption that lessons from one context can be judiciously adapted and applied to others. The challenge is to provide guidance that is general enough for a breadth of different conflicts, yet specific enough to avoid platitudes that sacrifice its applicability.

### Box 1 Definitions of conflict

There is no agreed definition of armed conflict in international law, but a longstanding definition of it within academia has been developed and used by Uppsala University's Uppsala Conflict Data Program and the International Institute of Peace Research. This definition was developed to support the creation of a database of armed conflicts worldwide since 1946 (with 1989 to the present covered in great detail). It defines armed conflict (war) as a contested incompatibility involving government, territory, or both where the use of armed force between two parties—at least one of which is the government of a state—results in at least a thousand battle-related deaths in one calendar year.

Source: [http://www.pcr.uu.se/research/UCDP/data\\_and\\_publications/definitions\\_all.htm](http://www.pcr.uu.se/research/UCDP/data_and_publications/definitions_all.htm)

What this guide does not do is tell readers what to think. Instead it assumes that beyond certain basic rules of good project management, project teams need a framework to guide their efforts—complemented by suggestions, examples, and reference materials—when developing responses to the challenges identified by the guide. Separate material is being developed for specific areas of investment climate reform that will complement this guide, including a note on developing special economic zones in conflict-affected countries and a capacity assessment tool for investment promotion agencies.

This guide also complements the U.S. Agency for International Development (USAID) *Guide to Economic Growth in Post-Conflict Countries* (Smith 2007). IFC has benefited from a close partnership with USAID in developing this guide. Many of the ideas here were introduced at USAID and IFC workshops, and enhanced by interaction with staff from both agencies.

The guide presents concepts for framing and guiding thinking and offers suggestions, examples, and tools for project use. This information came from nearly 40 interviews with IFC and World Bank staff, a survey of IFC advisory services staff who work in conflict countries, and Smart Lessons written by IFC staff about their learning from project work in conflict-affected countries. This guide also benefits from previous collaboration between the IFC and Deutsche Gesellschaft für Technische Zusammenarbeit (GTZ) on conflict-sensitive private sector development.

The core organizing scheme for the guide is that of a typical project cycle, with six sections. Following this introduction, the guide provides an overview of key issues raised in the literature on investment climate reform in conflict-affected countries and what project teams face. The next section summarizes guiding principles for catalyzing investment climate reform projects in conflict-affected countries. The guide then presents sections on addressing challenges in diagnostics, planning, implementation, and evaluation and learning from such projects. This guide will also be available in extended form online, with links to a document library, an extended literature review, and useful sites with travel tips, security guidance, political analysis, country news, conflict analysis, and

opportunities to exchange advice with fellow practitioners and contribute to our evolving understanding of this work.

## Acknowledgements

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**It takes time** to get the market to sort things out, and the market in post-conflict countries is usually distorted. A lot of actors in the market have distortionary powers that may be related to the number of machine guns that they have stored somewhere.

—Interview with IFC Staff



2

## What do investment climate project teams face in conflict-affected countries?

What are conflict-affected countries, and what causes conflict?

A conflict-affected country has either experienced conflict in the past 10 years, is experiencing conflict, or is at risk of violence.<sup>1</sup> Conflict is extremely destructive to social and economic wealth and makes outbreaks of violence more likely (Collier 2007). Effective engagement in conflict-affected countries is one of the greatest challenges of development, and an improving investment climate is a key reflection of success (Del Castillo 2008; Collier, Hoeffler, and Rohner 2006; Gerson 2000).

Since the Cold War most violent conflicts worldwide—whether referred to as political violence, ethnic violence, or civil, internal, or

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<sup>1</sup> The definition of a conflict-affected country varies among institutions. The World Bank Group uses the definition given in this paragraph.

armed conflict—have been within rather than between states. Conflict can take various forms: interstate wars (such as between the United States and Iraq), civil conflicts and insurgencies at the state level (such as in the Central African Republic; Aceh, Indonesia; and Sri Lanka), or ethnic and community-based conflicts at the sub-state level (such as between Hindus and Christians in India). About 90 percent of the casualties in civil conflicts are women and children (Gantzel 1997).

### Key ideas in this section:

- Most conflicts have a strong economic or commercial dimension and are driven by rational decisions for legal or illegal profit.
- Conflict has wide-reaching negative impacts on people, infrastructure, institutions, markets, and trust in government—with the scope of such impacts depending on the extent of conflict.
- Investment climate reform is crucial to helping countries recover from conflict.
- Jobs and investment are critical for peace; investment climate reform increases both.
- Investment climate reform is also critical to state-building; reforms of government institutions that regulate the business environment can inculcate transparency, honesty, professionalism, and client service—all key to restoring government legitimacy.

Recent literature on contemporary violent conflict and war rejects notions of conflict as being a regressive collapse into chaos driven by mechanistic forces. Research has argued that conflict-affected economies are an “economic system in which production and distribution depend on violence” (Taylor 2004, p. 10). This research found that conflict is self-financing, relying on looting, informal taxation, and resource extraction (including timber, oil, narcotics, and precious minerals), with competing arrangements of power, legitimacy, and livelihood among governments, rebel groups, warlords, and criminal organizations. These actors compete in a shadow economy controlled by violence and marked by corrupt manipulation of state regulation and economic survival at the household level (Ballantine and Sherman 2003; Taylor 2004; Malone and Nitzschke 2005).



Table 1 Features of conflict-affected countries and their impacts on the investment climate

Feature	Impact
Recent violence and possible return to violence	Instability and lack of safety keep away investors and deter local startups
Displaced population	Most workers unemployed and consumers unsettled; both focused on survival, mostly in low-skill jobs
Destroyed infrastructure	Damaged roads, ports, power, and communication networks limit movement of people and goods and hinder production
Land ownership unclear, with overlapping statutory and traditional systems	Businesses unwilling to invest in long-term or high-capital projects
Capital flight, banks destroyed, low savings and high interest rates	Credit and insurance expensive and difficult to obtain
Fragmented markets, widespread informality, dependence on imports, and residual war economy of illegal activity	Informal activity a misallocation of resources and goes untaxed; illegal activity may be a cause of conflict
Key industries or sectors often monopolized by well-connected elite, private or public companies have limited operational skills and little desire to invest	Weak financial basis (debt and/or salary arrears), need for large initial capital investments, mostly large or “cowboy” investors first to enter, long-term resident foreign-owned businesses
Transitional government for up to three years that is fragile, risk adverse, and perhaps uncommitted to reforms	Missing incentives and political will for reform action
Low government capacity to deliver services, provide security, or create enabling business environment; high corruption, often through predatory behavior by the public administration	Government harassment of businesses, low trust in government administration, low investment, low productivity, and high prices for consumers

The same globalizing forces that have allowed easier movement of people, goods, and financing have created a context in which these players can control foreign aid, populations, territories, resources, and illicit trade for profit (Berdal and Malone 2000; Kaldor 1999). Violent conflict often involves human rights abuses against civilians. Violence is frequently carried out by the youngest members of a population, sometimes facilitated by the media (Kellow and Steeves 1999) and an abundant, accessible supply of small arms. In these contexts of conflict, power and legitimacy are based on violent control rather than popular consent (Duffield 2001; Macrae 2002).

Conflict-affected countries will have experienced varying degrees of violence and destruction, loss of capacity, and political instability, and can be unpredictable and prone to crisis (Table 1). Their institutions failed to prevent conflict from turning violent, and they could return to violence unless the causes of conflict are addressed. Loss of life often combines with outward migration, leading to further deterioration in human capital. Capital flight and the destruction of infrastructure (roads, bridges, buildings, communication networks) undermine future economic growth. For example, it has been estimated that GDP falls by more than four percentage points when conflict extends to half of a country's territory (Berdal and Malone 2000; Kaldor 1999). These factors tear at a country's social and institutional fabric, weakening trust and cultural values and providing more challenges for the transition from war to peace (see UNDP 2006).

The current debate on the causes and character of conflict is organized around two broad camps: greed and grievance. Analysts focused on greed contend that wars are primarily caused and sustained by the pursuit of economic wealth. Analysts focused on grievance identify inequality and injustice as the central reason (Ballentine and Nitzchke 2003).

The greed argument has been the focus of much attention in recent years, in no small part because of work by the World Bank's Development Research Group. The group's research found that the most commonly cited causes of conflict—ethnic diversity and economic inequality—do not appear to systematically increase the risk of civil war. Instead the risk of civil war increases in



poor and declining economies that are highly dependent on natural resource exports (Collier 2003).

The grievance argument is the more traditional explanation for war, arguing that people fight to rectify perceived or actual wrongs (Ballentine and Nitzchke 2003). Although not subject to the same quantitative study, this remains a compelling argument with strong evidence. Countries that go to war tend to have a long history of conflict and a popular narrative of injustice (Collier 2003). Few rebel groups fight without an ideological justification that extends beyond simple economic gain, and conflict resolution invariably involves an attempt to address grievance.

But the greed versus grievance debate creates an analytical dichotomy that does not capture the complex reality of conflict. Rather than being driven by a singular force, war is often the result of a complex, unique interaction of factors related to wealth, power, personality, and ideology. Greed and grievance both play a role.

Recognizing this complexity is important because of its policy implications (Ballentine and Nitzchke 2003). Understanding the causes and characteristics of a war is essential to developing policies that mitigate or end it. Incorrectly identifying problems will likely result in prescribing the wrong solutions—and in a fragile post-conflict environment, that can have dire consequences.

## Typology of conflict

Having underscored the complexities and uniqueness of every conflict and country, a basic typology can help sort countries into groups that highlight

important broad features. Uppsala University has a well-known typology that groups conflicts according to numbers of battlefield deaths on a scale of severity ranging from political violence through intermittent armed conflict, intermediate armed conflict, and high armed conflict (<http://www.pcr.uu.se/gpdatabase/search.php>). For the purpose of this guide, conflict will be classified by duration, scope, and intensity of conflict. Duration of conflict refers to how long a conflict has lasted, the scope of a conflict refers to the geographic spread of a conflict, and the intensity of a conflict refers to the number of deaths during a conflict. These broad categories can point project teams toward critical impacts of conflict that can help them form early assumptions about the challenges they might face in a conflict-affected country.

Table 2 describes different countries according to this conflict typology to give a country's conflict a more tangible profile. The Doing Business 2008 score and the World Economic Forum Competitiveness 2007 score is given for each country to suggest the impact of conflict on each country. According to this table, a country's *Doing Business* score does not necessarily improve with the length of time since a conflict ended, and countries with conflict in only a part of the country seem to rank better than countries that suffered violent conflict everywhere.

Loss of human and institutional capacity varies with the intensity and duration of a conflict. In a conflict that lasted a long time, was of high intensity (high numbers of deaths or high armed conflict), and encompassed the entire country, human capital was likely severely depleted by death or displacement, many assets were likely destroyed, and institutions may be gone. Mozambique had such an experience, and 17 years after the end of its conflict it still ranks near the low end of the International Finance Corporation's *Doing Business* scale (Table 2). Sri Lanka's conflict is also of long duration and intensity (high armed conflict) but mostly occurs in one part of the country—resulting in a lower casualty rate and higher *Doing Business* score. Accordingly, approaches to reform in Mozambique and Sri Lanka will differ based on the kind of capacity that can be expected and the functionality of institutions (Box 2).

Table 2 Typology of conflict

Conflict Country	Year Conflict Ended	Length of Conflict	Geographic Scope of Conflict	Number of Deaths from Conflict	Doing Business 2008 Score (out of 178)
Mozambique	1992	17 years	All	1,000,000	134
Rwanda	1994	3 months	All	850,000	150
Bosnia and Herzegovina	1995	5 years	All	125,000	105
Cambodia	1998	23 years	All	2,000,000	150
Timor Leste	1999	24 years	All	200,000	168
Sierra Leone	2002	12 years	All	30,000	160
Angola	2002	27 years	All	800,000	167
Liberia	2003	14 years	All	150,000	167
Sudan	2004	20 years	Part	2,000,000	142
Congo, Dem. Rep.	2005	9 years	All	3,800,000	178
Philippines	2006	16 years	Part	75,000	136
Nepal	2006	11 years	Part	14,000	111
Sri Lanka	Present	26 years	Part	75,000	103
Afghanistan	Present	31 years	All	1,500,000	161

## Investment climate reform in conflict-affected countries

Economic growth plays a crucial role in the transition from war to peace in conflict-affected countries. Research suggests that the risk of reverting to violence for a typical post-conflict society is 40 percent within ten years following a cessation of violence (Collier, Hoeffler, and Rohner 2006). A country with a unitary government, stagnant economic growth, and average spending on peacekeeping has a 75 percent risk of slipping back into war in the 10 years following peace. The same country with four times the average peacekeeping expenditure and 10 percent economic growth has just a 37 percent (Collier 2007). For otherwise peaceful but fragile countries at risk of violent conflict, a country with annual per capita GDP of \$250 has a 15 percent probability of war occurring within five years. This probability falls by half for a country with annual per capita GDP of \$600, and to less than 4 percent for a country with per capita income of \$1,250 (Humphreys 2003). Moreover, in poor or declining economies the risk of violence is increased by heavy dependence on primary commodities (Collier 2007). Thus timely interventions in the fragile periods before violent conflicts begin or soon after they end can be critical.

The private sector is increasingly seen as the engine for catalyzing and sustaining long-term growth. Investment climate reforms were once considered a second- or third-stage intervention, after addressing the needs of refugees or internally displaced people and strengthening macroeconomic conditions. This was largely due to perceptions that the private sector does not need outside support to resume its activities, especially given the urgency of humanitarian needs. But as thinking on conflict has become more holistic, the need to provide early support to the private sector has become widely accepted (Gerson 2000). Further, commercial activity can be implicated in the causes of conflict, and large investors in the extractive or telecommunications industries either enter conflict-affected countries soon after violence ends or were there during it and part of the problem. Thus providing early support for the investment climate is directly relevant both to promoting reconstruction and to addressing causes of conflict.

If poverty contributes to conflict, then at its best the private sector can contribute to peace building by helping to deliver economic diversification and growth,

## Box 2 How does conflict affect human and institutional capacity?

Lebanon and Rwanda have both experienced short conflicts (one month in Lebanon in 2006 and three months in Rwanda in 1994), but the starting capacity and impact of the two countries' conflicts varied. Lebanon had a better-educated population and fewer deaths during its war, while the education level in Rwanda was low and the death toll very high. Rwanda's lower education starting point and higher death toll meant that its short conflict had a greater impact than Lebanon's.

Liberia and Bosnia and Herzegovina have similarly sized populations that experienced many deaths and extensive displacement and physical destruction. Yet their human and institutional capacities differed at the end of their wars. Liberia's skilled population left just before the start of its 14-year war, and stayed away. Fewer of Bosnia's skilled population left during its shorter war, and more people were educated. Bosnia's institutional capacity also remained stronger than Liberia's after their respective wars. The quality of Bosnian institutions and the number of people with institutional memory was greater than in Liberia, where institutions were severely damaged during its conflict. Liberia's institutions were of much lower quality when its conflict began, and its longer, high-intensity, whole-country conflict meant that its reconstruction needs were greater than those of Bosnia.

Source: IFC Interview, 14 March 2008.

investing in new ideas and skills, providing employment opportunities, delivering services, and creating a base for the taxation needed to fund critical services such as health and education (Langford 2005).

Project teams must recognize that without understanding the causes of conflict and without working in a "do no harm" way (see the next section), their projects inadvertently run the risk of reproducing the conditions that originally caused conflict in a country. Investment climate reform projects must at the least avoid contributing to conflict—and, better yet, contribute to peace in conflict-affected countries.

Peace, when it emerges, arrives either by a negotiated settlement or a military victory. Peace by settlement is the most common and is usually fragile, can be

temporary, and often depends on rapid, tangible change. Institutions and entrenched corruption can prove resistant to reform. Key players may cling to the power structures and incentive systems that drove the war even after violence has ended, working actively to block reform.

Peace by military victory is less common but gives enormous space for reform. That was the case in Rwanda in 1994, when the Rwandan Patriotic Front defeated the Hutu government and ended the genocide. In that context, policy decisions did not have to be managed through a complex maze of political parties, legislative members, and informal power holders who could return to the battlefield should subsequent decisions not please them.

Project teams face two main challenges. The first is that the countries most in need of investment climate reform are also those least able to foster it. The second is that even when investment climate reform occurs, it is not always in an appropriate manner. The high costs of security, the breakdown of trust, the destruction of physical infrastructure, the deterioration of governance, and the threat of renewed violence create a reform-resistant environment (Langford 2005). Project teams will need to argue persuasively early on for the inclusion of investment climate reforms in any reconstruction agenda, and implement projects that pay attention to conflict dynamics and political economy, and not just technical aspects.

## Investment climate reform and state-building

Contemporary international post-conflict reconstruction places great emphasis on state-building, where external assistance comes to restore the laws, policies, and institutional functions that matter the most for state functioning. Early interventions to build state institutions are critical to enabling sustainable peace because state institutions are often the main vehicles for dividing resources and both official and unofficial rents among parties to a conflict.

Thus post-conflict reconstruction focuses on strengthening institutions so that they exemplify a culture of compliance with the rule of law and appropriate norms, as well as embody greater inclusion of marginalized members of society. High priority should be given to promoting professionalism among

ministry and agency staff and to using state resources for technical and policy outcomes that support development goals instead of factional or ethnic interests. Without such efforts, corruption in a conflict-affected country can destabilize peace if state resources are perceived to be captured by one faction at the expense of another. Investment climate reform directly supports state-building because it builds institutional functionality and promotes good governance. These in turn legitimize the new post-conflict government and are a force for inclusion—clear benefits of peace.

Reconstruction activities can include public financial management reform of a country's revenue and spending bodies, security sector reform for the military and police, judicial reform to make the court system more effective, and electoral reform to support democratic transitions in the legislative branch. Investment climate reform that builds the capacity of state institutions that regulate the private sector are in line with state-building intentions and directly affect the underlying dynamics of a war economy.

## Investment climate reform and company types

Whether a conflict engulfed a country in a long war with far-reaching devastation (as in Sierra Leone or Somalia), whether a conflict was limited in geographic scope (as in Nepal or Sri Lanka), or whether a conflict was of relatively short duration (as in Bosnia), the investment climate needs of large firms and small or medium-size firms can differ.

In countries where conflict had caused widespread devastation, one way to start rebuilding the private sector is by attracting larger firms that will contribute to the construction of infrastructure or enter an extractive sector. Foreign direct investment can come from the country's diaspora, increasingly as South-South investment but also from Western companies interested in extractive sectors. Conflict-affected countries such as Angola, Iraq, and Sierra Leone offer their extractive sectors and inexpensive workforces as comparative advantages over other countries.

The challenge for such countries lies in converting their extractive industries from wartime exploitation to peaceful uses that leverage additional invest-

ment and private sector growth. This challenge involves attracting foreign and domestic investments into a post-conflict country's extractive resource sectors—sectors that were typically at the center of conflict—and using those investments to catalyze further investments in infrastructure. This challenge also involves developing forward and backward markets to provide inputs for extractive industry operations and process outputs for local and regional markets. Finally, this challenge involves attracting investors who will not engage in unethical practices such as making illicit payments, trading commodities in violation of sanctions, allowing company assets or finances to be used by a fighting force, or hiring a fighting force for protection.<sup>2</sup>

Representatives of large companies working in the extractive sectors who were interviewed for this guide said that administrative barriers usually do not prevent their companies from investing in conflict-affected countries. Still, investment climate reform benefits large foreign firms because it limits the institutional and political space for corruption. From that perspective, investment climate reform stands alongside the Extractive Industry Transparency Initiative, public financial management, and anticorruption and good governance efforts. Of greater relevance is investment climate reform that updates investment codes, improves land access, enables the establishment of special economic zones, or strengthens the investment promotion capacity of institutions leading such efforts.

A second way that a conflict-affected country can try to rebuild its private sector is by building informal businesses and bringing them into the formal sector. Most domestic businesses in such countries are small and informal, and likely operated even during the conflict. Such businesses typically function at a level of survival, constrained in their ability to grow but also employing most workers—especially in urban centers, where displaced populations cluster during fighting.

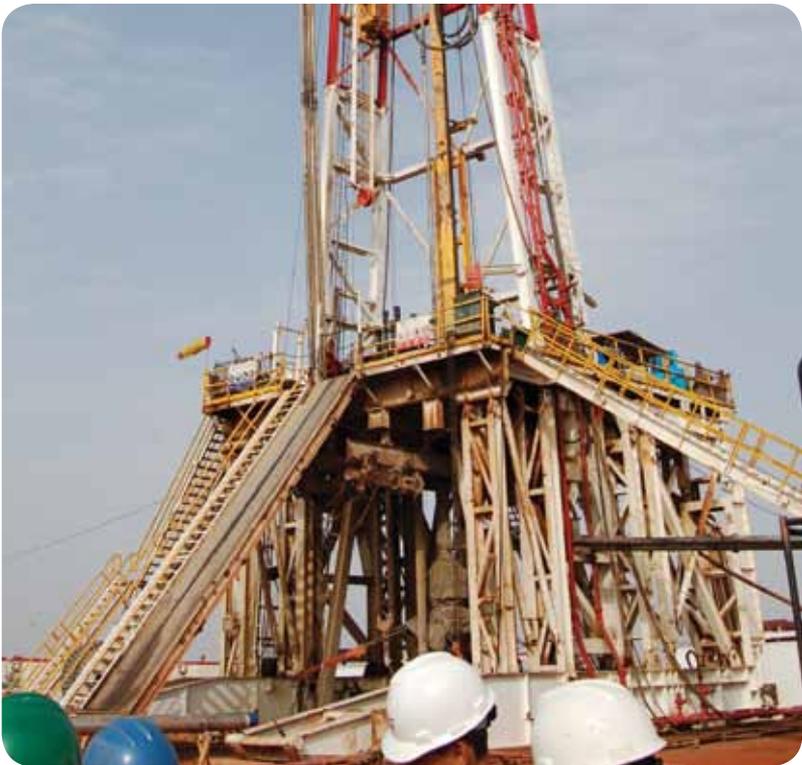
To complement financing and business development services, expanding small businesses such as street-level entrepreneurs required focusing investment

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<sup>2</sup>Two nongovernmental organizations, International Alert and Fafo, have produced a list of liability risks for companies operating in conflict-affected countries. See <http://www.redflags.info>

climate reforms on the administrative barriers that most matter to them: easing business registration, obtaining licenses, importing and exporting, paying taxes, and using movable assets as collateral.

Again, while this guide makes this kind of division of investment climate interventions in conflict-affected countries, all investment climate interventions can benefit all types of companies, regardless of size. This point should be underscored given the preceding observations that investment climate reform should be targeted toward what will create the most employment and attract the most investment in a conflict-affected country. If, for example, informal small and medium-size businesses are the main driver of employment, they should be an operational priority.





**Conflict**, and not technical deficiencies in the private sector, is the problem in conflict-affected countries.

—Interview with IFC Staff



## Guiding Principles for Catalyzing investment climate reform in conflict-affected countries

### A few preconditions

The question of when to initiate investment climate reform in a conflict-affected country is critical. Most project teams consulted for this guide believed in early engagement. Some preconditions for deciding when to go in with new programming or resume existing projects might include:

- Basic safety and security allows the movement of people and goods and resumption of normal business activity.
- Provision of humanitarian relief is well underway.
- There is broad donor interest in engaging in the country.
- Having a government counterpart—ideally, one interested in reform.



Some investment climate reforms can be implemented before basic safety and security exists everywhere in a country. Normal business activity may only be possible in areas where fighting has stopped, and elsewhere as security improves. The project team should not wait until the entire conflict-affected country has become secure.

### **Key ideas in this section:**

- There is no universal blueprint for reform in conflict-affected countries
- Key preconditions for reform include staff safety, humanitarian relief, donor engagement, and openness to reform
- Flexibility and innovation are essential at all stages of reform
- Conflict sensitivity and “do no harm” principles must guide all project decisions

Conflict, and not technical deficiencies in the private sector, is the problem in conflict-affected countries.



Project teams composed mainly of private sector development experts from a development agency often conceptualize their work in technical terms. With investment climate work it is tempting to focus on measuring days, costs, and steps for administrative procedures, or on planning investment promotion campaigns with government and private sector counterparts.

Project teams should bear in mind two main operational issues when working in conflict-affected countries. First, the real problem facing the team is that the country is fragile and failed to prevent conflict from becoming violent on a large scale. However outdated an investment law, however long and complicated it is to pay taxes or import goods, however unequipped an investment promotion intermediary is to attract investors—these are not the main problems. Technical problems are secondary, and resolving them is a means of assisting with post-conflict reconstruction so that a country does not return to violence.

Second, projects add value based on how much a team’s technical interventions make a country less conflict-affected. This means that project teams must go beyond minimal compliance with conflict-related checklists to ask, “What will the country gain by what we bring to the client, the government counterpart, or the business community, that would not otherwise be gained?” This question should inform a project’s diagnostic work, implementation, and expected results.

## Be flexible and innovative

The reform environment in conflict-affected countries requires that project teams be flexible at every stage of the project cycle (IFC Interview 21, 8 April 2008). Situations are often fragile and fluid, with incomplete information and immense country needs. A rigidly planned and implemented approach is unlikely to succeed. Reform in conflict-affected countries does not lend itself to a strictly linear model of operations, where diagnosis ends when implementation begins. Project teams need to be willing and able to respond to emerging information and new opportunities, rethink goals when faced with the reemergence of conflict, and embrace innovative working methods (box 3).

### Box 3 Perseverance and adaptation in Iraq

In 2006 the Iraqi-American Chamber of Commerce and Industry (IACCI) approached IFC seeking accreditation to market Business Edge, IFC's training kit for small and medium-size enterprises. The accreditation process is intensive and interactive, and given that Iraq was still experiencing active fighting and IFC staff could not enter the country, prospects for working together were dim.

Committed to collaboration, IFC and IACCI had to find ways for IACCI staff to participate in Business Edge's course on training trainers, and then for IACCI staff to train its members using Business Edge. Because IFC staff could not enter Iraq to teach the course and videoconferencing was too difficult, IFC unsuccessfully tried to obtain visas for IACCI staff to enter Egypt and Yemen for the training. IFC staff ultimately succeeded in bringing IACCI staff to Jordan, but on the condition that IFC staff confiscate IACCI staff passports during the stay.

The IACCI staff who received the training ended up being highly innovative. One carried two sets of identity papers—one with a Sunni name and one with a Shiite name—and used them based on the neighborhood he intended to visit to train IACCI members. Other IACCI trainers worked in pairs, with one conducting the training and the other keeping watch for possible attacks.

Source: Shohaieb and Nader 2006.



## Prepare for tradeoffs

Implementing reform in conflict-affected countries defies easy prioritization and sequencing. Tradeoffs drive decisionmaking at every phase of the project cycle—often without complete information. Typical tradeoffs often occur between

- “Quick wins” that show rapid results versus interventions that address deeper needs but yield more lasting results only later.
- Incremental versus bold reform.
- Direct implementation by the project team for greater speed and quality versus implementation by government counterparts to build local capacity and legitimacy.

Such tradeoffs shift over time, and as new information emerges and the situation becomes clearer, choices among tradeoffs may become easier to make.

## Effective sequencing varies

The most effective sequencing of project interventions varies by country, with possibilities emerging based on technical needs, political support, and opportunities created by project teams (see the section below on diagnostics). While all aspects of the investment climate may need reform, it may be necessary to start with activities that signal engagement and prepare the political space for reform—such as by establishing a public-private dialogue on a viable sector for reform. Perhaps the greatest danger lies in sequencing activities based on what the project team can offer or because there is project funding, rather than what the country actually needs.

## Conflict sensitivity and “do no harm” principles must guide all decisions

In the mid-1990s humanitarian agencies working in conflict-affected countries began discussing how their emergency relief programs interacted with the populations they were trying to reach, as well as the fighting forces with whom they had to work to access needy populations. Many humanitarian agencies in these situations found that even if their programs reached people in need, the food, blankets, tents, medicine, and water they brought also benefited the

fighting forces—perpetuating conflict. Soldiers at checkpoints would routinely take some of the supplies intended for affected populations or claim to be among the displaced and in need of help. *Hutu Interahamwe* fighters who fled post-genocide Rwanda after their military defeat entered refugee camps near Goma, Democratic Republic of Congo, and received food, medical assistance, and space to regroup in a location that could not be attacked because it was a refugee camp in full view of the international media.

Such experiences in conflict-affected countries led to the emergence of “do no harm” principles. These principles developed into common standards for delivering emergency relief among humanitarian agencies, intended to reduce ways that fighting forces could capture aid to prolong conflict and identify ways that emergency relief could help build peace. The principles were operationalized in techniques that analyzed the context in which emergency relief is delivered, to discover where there were opportunities to deliver aid in a way that minimized exposure to capture and created connections between warring sides to build mutual understanding, trust, and dialogue on common concerns.

An example comes from Tajikistan’s post-conflict recovery. An aid agency began a housing construction project to help communities rebuild their homes after fighting ended. The agency directed its assistance to towns that had suffered the most damage, but these towns were populated by the group that lost the conflict. The group perceived to have won the war perceived the agency as strengthening an opponent they had worked hard to defeat, and the assistance created divisions rather than connections between these two groups (Anderson 1999).

The “do no harm” principles evolved into what is now called “conflict sensitivity”—a concept that has been applied to every type of development assistance, including private sector development. Conflict sensitivity as applied to investment climate reform means understanding the context in which a project operates, recognizing the influence of reform activities on the causes and drivers of conflict, and taking actions to avoid creating conflict and strengthen peace<sup>3</sup>.

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<sup>3</sup> See [www.conflictsensitivity.org](http://www.conflictsensitivity.org); International Alert 2006, and Gaigals and Leonhardt 2001

Examples of conflict sensitivity in the context of investment climate reform are discussed throughout this guide, and include

- Establishing public-private bodies for dialogue that include a wide range of public and private sector representatives from all sides of a conflict.
- Making tax payment and trade processes easily accessible to private sector elements that have faced discrimination.
- Developing special economic zones in ways that respect community land ownership.
- Strengthening an investment promotion agency so it makes the prohibition of government bribery or payment to a fighting force as important as the terms of the deal.

As an operating principle, investment climate project teams should adopt conflict sensitivity throughout the project cycle.



**It's a question** of knowing the country—you need to know who is calling the shots.

—Interview with IFC Staff



## 4

# Investment climate diagnostics in conflict-affected countries

Diagnostic work lies at the heart of efforts to design investment climate reform projects in conflict-affected countries. Such efforts should focus on assessing reform challenges in the country and forming assumptions about the best project response.

Diagnostics depend on effective information gathering and can apply on two levels. One involves project teams continuously testing project assumptions and updating information on a country's political economy (including security). Such efforts will guide monitoring and ensure that projects reflect reality. On the other level, project teams should periodically reflect on what they are learning about which interventions best support investment climate reform in conflict-affected countries, to feed back into future projects. This second point is discussed further in the section below on evaluation.

Three related types of diagnostics need to occur in conflict-affected countries (table 3).

The first is technical analysis of the investment climate, the second is analysis of political and economic power, and the third is analysis of the causes of conflict

Given the complexities of conflict-affected countries, all assumptions about technical challenges and political and economic power, and project responses to them, must be regularly retested. Including local stakeholders in assumption testing and progress assessment is key to building a constituency of reform supporters

### Key ideas in this section:

- Technical analysis of the investment climate must be accompanied by analyses of political and economic power and of the causes of conflict.
- Conflict-affected countries do not allow much time for long technical studies—but shorter analysis can still be effective.
- Political and economic analysis is critical for understanding who has what power and interests, and who is connected to whom.
- Good conflict analysis will identify root or historical causes, proximate or recent causes, and triggers of conflict.
- Project teams often do not have to conduct original conflict analysis, and should consult existing analyses.

Table 3 Three crucial areas of diagnostic work in conflict-affected countries

Investment climate	Political and economic power	Causes of conflict
<ul style="list-style-type: none"> <li>● What are the main government and market failures in the investment climate?</li> <li>● Who or what institutions are best able to promote reform?</li> <li>● What country resources exist on which to build reform efforts?</li> </ul>	<ul style="list-style-type: none"> <li>● Who has what motives and interests related to the project?</li> <li>● What are the relationships between key stakeholders with political and economic power (including parties to the conflict)?</li> <li>● Who has what kind of political and economic power over resources, especially related to other stakeholders and the conflict?</li> </ul>	<ul style="list-style-type: none"> <li>● What are the short- and long-term structures, policies, and events that contributed most to the conflict?</li> <li>● Who needs to be included in the reform process to avoid spoiling it?</li> <li>● How can the technical activities of the project avoid worsening conflict—or, better yet, help foster peace?</li> </ul>

who own change. The project will benefit from having more insider information and insight, while creating a culture of reform and normative, professional behavior among government officials and those in the private sector.

### Technical analysis of the investment climate

Private sector development project teams are usually effective at conducting technical analyses of investment climates. Many analytical tools already exist, and most donors produce such reports regularly. For conflict-affected countries the challenge in conducting such diagnostics involves balancing speed and quality. A rapid response is needed, but so is a credible assessment of the

investment climate challenges facing a conflict-affected country.

One way that FIAS has tried to balance these needs is with “mini diagnostics” that are shorter versions of its standard analytical report, the administrative barriers review (ABR). ABRs examine a wide range of investment climate issues considered most likely to be problematic based on desk research prior to in-country assessments. The reports have helped generate complete pictures of the legal, policy, and administrative changes needed in the investment climates of countries such as Bosnia and Herzegovina, Lebanon, and Sierra Leone, and enabled governments and businesses to manage expectations, stakeholders to set priorities, and donors to coordinate funding. An ABR team then visits a country two or three times for a couple weeks each visit over six to eight months, writing an exhaustive report at the conclusion.

Mini-diagnostics involve teams of the same size with the same goal—examining a wide range of investment climate issues. The difference is that there is only one country visit, and substantial groundwork is conducted in advance to test likely issues that need coverage and to arrange meetings with people best placed to provide information. These reports are much shorter and identify both immediate actions that could be taken and areas needing further inquiry.

The choice between a regular analytical report and an abridged version depends on two factors. The first is the prospect of peace; the second is the intensity of the conflict. If peace emerges in a conflict-affected country (whether high- or low-conflict) through a political deal or peace agreement, there is greater urgency to quickly assess and move to a reform program. Thus a modified rapid assessment tool makes sense in this situation.

If a country is experiencing low-intensity conflict (as in Nepal) or conflict is confined to one part of the country (as in Indonesia or the Philippines), there may be less urgency to seize a moment of peace. In such cases it is reasonable for a project team to use its regular analytical instruments.

The Joint Needs Assessment (JNA) is a common analytical tool for post-conflict needs analysis often conducted by United Nations agencies and the World

Bank Group. For example, IFC was involved in the 2003 JNA for Iraq. Information generated by the diagnostic tools of individual agencies provides vital inputs to JNAs and a framework for identifying investment climate needs within the larger landscape of reconstruction needs.

## Analysis of political and economic power

The term *political and economic power analysis* has many interpretations, but in this guide it means understanding the formal and informal structures and dynamics of the power and wealth of individuals. It seeks to identify the motivations and interests of relevant actors and locate where actors are located—in terms of geography and institutions—relative to other actors and their interests.

Achieving investment climate reform in conflict-affected countries requires acquiring accurate, specific, timely, and actionable information on key actors and the interests and incentives framing their actions and the political cycle (box 4). In insecure and rapidly changing environments, such information is often informal, fragmented, contradictory, and inaccurate.

### **Box 4 The importance of political economy and conflict analysis in Kosovo**

Strong understanding of a country's political economy has practical policy and operational implications. In 2004 the Kosovo Trust Agency began privatizing 300 Kosovar state enterprises. The process was guided by a policy of not prejudicing the eventual final status and equal treatment of Kosovo's ethnic groups. Thus, for example, rather than selling land held by state enterprises, long-term leasing arrangements were developed, bids were allowed to be submitted in both Serbian majority and Albanian majority cities, and all advisory staff were briefed on the official policy of neutrality. By 2007 most of the enterprise sales had been completed. Knowledge of political economy proved critical to this success.

Source: Bach 2008.



Understanding the political and economic situation in a conflict-affected country matters for two reasons. First, there is a need to avoid instigating, exacerbating, or reviving violent conflict and to contribute to peaceful development (World Bank 2002). Second, politics and economics are not static. Key players, as well as the contours of power and wealth, are in constant flux—especially in fragile situations. Thus project teams face three main challenges when analyzing political and economic power:

- Political diagnostics are not always a project team’s strength. Even for some seasoned practitioners, political analysis has been informally learned over a long period and occurs in an ad hoc way in the process of implementing reform. Such analysis largely depends on the skills and interests of individual project teams and is not a formal diagnostic process. As a result some project team members often do not have the skills to conduct detailed analysis of a country’s political economy, and teams do not have a formal means of developing and sharing this knowledge.
- A conflict-affected country’s politics and power arrangements are often opaque, and high-quality, relevant, actionable information is hard to come by. Where such information is publicly available, it is often too broad or outdated to inform project teams in an immediate or practical way.
- Faced with multiple priorities and the need to meet timelines, diagnosis necessarily focuses on understanding the technicalities of the business environment rather than the broader issues of the conflict and political economy.

## Conducting political and economic analysis before the first mission

Knowledge of a country's political and economic situation grows as a project unfolds. Efforts to increase such knowledge should recur throughout project implementation, and not just be a discrete piece of analysis conducted at the

start of a project. A project team should try to gather as much information as possible on a country's political and economic history and current dynamics. Good sources of information include donor reports and academic papers from conferences, country reports and online journals,

### Tip:

Interpreters sit in on critical meetings about conflict-affected countries and have access to all the key players and insight into local culture and politics. By working closely with them, project teams can gain invaluable information on the environments in which they are working.

people from the country in the project team's professional or social network, and people who have lived or worked in the country.

A few websites with publicly available country analysis include:

- <http://www.irinnews.org/> (IRIN news, a service provided by the UN Office for the Coordination of Humanitarian Affairs).
- The BBC, CNN, *The Economist*, and *Christian Science Monitor*.

Websites that provide access to a wide range of regional newspapers include:

- <http://www.wordpress.org>
- <http://www.world-newspapers.com>
- *Far Eastern Economic Review* (<http://www.feer.com>)
- <http://www.lib.berkeley.edu/SSEAL/SouthAsia/newsonline.html>
- <http://www.arab.net>
- <http://www.library.wisc.edu/guides/MidEast/midnet.htm>



- <http://www-sul.stanford.edu/africa/current2.html>
- <http://www.AllAfrica.com>

Some conflict-affected countries have local English-language newspapers containing coverage and analysis of national issues. Though these newspapers are valuable resources, they should be used with the same caution as any other source of information. English-language newspapers can both inform and misinform—especially in contexts where conflicts runs along ethnic fault lines.

### Conducting political and economic analysis during the first mission

Given the highly volatile, fragmented situations in conflict-affected countries, a lot of information on specific people, decisions, and relationships that complements the information described above can be acquired only once project teams are on the ground. Many tools are available from donors or online that can be used to guide political and economic analysis. Such tools are sometimes called *stakeholder analysis*.

Figure 1 A representative “map” of political and economic relationships in a conflict-affected country

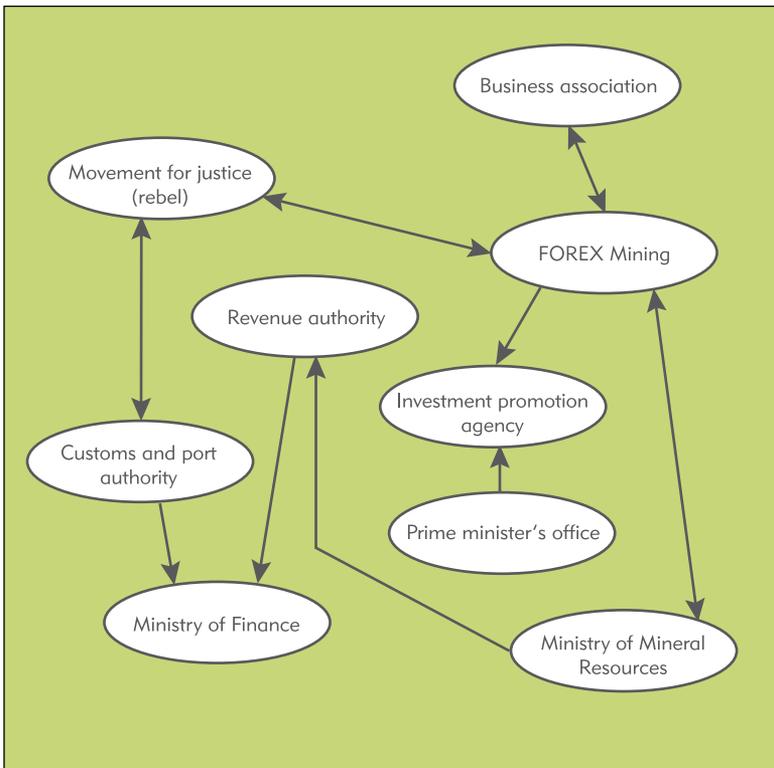


Figure 1 provides a representative “map” of political and economic relationships in a conflict-affected country. To create such a map, take a blank piece of paper and draw circles representing all the institutions—formal and informal—relevant to investment climate reform. For each institution, list the names and titles of key individuals. Try to understand each person’s power, interests, and relationships with other people on the map and with people not involved in investment climate reform but who are politically or economically powerful (box 5).

### **Box 5 Questions for conducting political and economic analysis of individuals in conflict-affected countries**

- What type of power does each person hold? Is it physical (that is, the threat of violence)? Economic (the ability to provide or withhold resources)? Social or religious (a charismatic or spiritual leader)? Technical or organizational (they have skills, access to key players, or hold a key position, such as an adviser)?
- Who are their friends?
- Who are their enemies?
- How are they connected to key political actors (such as the president, prime minister, speaker of the house, rebel or faction leaders, ministers, or senior military leaders)?
- How are they connected to key business actors (such as company owners or heads of business associations).

As more knowledge is gained about the institutions and people with potential influence on investment climate reform, add new circles for them. Draw a line from each name (not institution) in each circle to other names on the map, annotating the lines to explain their relationship. These names and relationships then represent the ecology of the most important people in the project’s reform space and their power and interests. Against this map the technical diagnostics and design of reform goals can be contextualized and the causes of conflict identified (see next section).

## Tip:

When meeting with leaders or those with authority, watch and listen to the person second-in-charge. While the person in authority may be circumspect and even diplomatic in her or his speech, the second-in-charge is sometimes less careful and often reveals the leader's actual attitude or thinking.

So where can this information be found? Most of it will come from informal sources such as conversations. Use the map (explicitly or mentally) when asking questions of people that the project

team meets on the ground. A few tips for obtaining information:

- Trust is everything. It is likely that no one who does not know the project team will share useful information on the team's first visit. Start with people with whom there is a shared professional connection. Staff from a local IFC or World Bank office and from partner organizations working on a specific project can often help answer questions.
- Bilateral or UN agencies often have expatriate or domestic staff members who have worked both in country and for aid agencies. These "insider outsiders" can have a wealth of information on who has what interests, who is connected to whom, and who is influential in what way.
- International military forces can be a great source of information, whether UN or NATO peacekeepers or the U.S. military (for example, in Afghanistan or Iraq). They invest a lot in gathering and analyzing political and economic information.
- Local journalists and members of civil society organizations (particularly from groups focused on political or human rights) can also offer insights. But care is needed when selecting people from the media or civil society groups, because they can sometimes be aligned with political parties. Just as the project team obtains information from them, they likely collect information about the project team.
- Members of the local business community are also good sources of information, but usually include religious and community leaders and policy advocates. Such sources can possess an unusual range of contacts and sometimes a shared personal history with political power holders, yielding valuable details on the actions the power holders during the conflict.

- Foreign-trained government advisers who can bridge the worlds of international development “speak” and local politics can be useful sources of information. Such advisors are often sympathetic to the conceptual approaches and aims of investment climate reform and are willing to help find compromises with the political aims of their government. If possible, use contacts in your organization to informally introduce the project team to new contacts.

### *Checking the backgrounds of project stakeholders*

Background checks of stakeholders are a key part of political and economic analysis in a conflict-affected country and should be conducted whenever a new player is identified as being significant to an investment climate reform project (box 6). In a post-conflict environment, key counterparts—in government

#### **Box 6 What to ask when conducting background checks of stakeholders**

- Where was the person during the war, and what was he or she doing?
- What are the person’s areas of business? Look for company names, owners, and sectors, and when the business occurred.
- What is known about the person’s financial portfolio?
- What are the person’s known sources of income?
- What is the person’s reputation for honesty?
- Is the person in or out of favor with politicians? With which politicians, when, and why?
- Has the person ever been in a political or commercial crisis? What is known about how he or she reacted?
- If the person joined the diaspora, where was he or she living? What did he or she do when living there? When did the person return to the conflict-affected country?

or business—may have been involved in illegal activities during the conflict. These players may then become members of transitional governments or legislatures, possibly as a condition for a peace agreement, and sometimes continue to play roles in democratically elected governments after the transition.

When initiating background checks, Google and Factiva are good starting points. Project teams should also use contacts in the country or region, legal databases, financial institutions that served that stakeholder’s company, and audit reports. In addition, IFC staff can access the Integrity Due Diligence site on the intranet and run searches for issues such as UN travel bans, UN asset freezes, sanctions against companies, and money laundering practices (box 7).

### **Box 7 Background checks for partners and contractors in Kosovo**

While undertaking privatization in Kosovo, IFC staff often had to deal with people who might have been involved in wrongful behavior during the conflict—ranging from smuggling and looting to war crimes. The main question was, who should be allowed to bid for companies and assets? Answering that question involved navigating a minefield of political sensitivities while maintaining a pragmatic approach to privatization.

The team conducted background checks of winning bidders. Privatization rules generally barred people from bidding if they were convicted of a felony after June 1999, when major hostilities ended. The approach was not airtight, and there was still a risk that people with dubious backgrounds slipped through the net. Still, it ultimately proved sufficient for detecting ineligible bidders and avoided the accusation that the project or IFC colluded with power players. Such fairness helps support commitments to peace among the population.

Source: Bach 2008.

Warning signs also include high-profile connections, offshore holdings, and a reputation for bribery. In a conflict-affected country, high-profile connections and offshore holdings—and even bribery—may be a means of survival. And as with potential investors, both domestic and foreign, such players may be happy

to turn over a new leaf and be more ethical now that the conflict is over and there is international support for change.

## Analysis of the causes of conflict

Among the three diagnostic areas, analysis of causes of conflict is the least understood and performed by many project teams. But understanding the causes of conflict is important to designing and implementing projects that avoid aggravating conflict and contribute to peace by addressing its causes. Conflict analysis is useful in identifying, for example, how discriminatory practices for registering a business, obtaining a license, and importing and exporting contributed to conflict.

Conflict analyses for specific countries can be obtained on the Internet or from organizations that produce them. While most project teams only need to be





aware of existing analyses, some teams may need to conduct some conflict analysis on their own to fill gaps.

### Conflict has three types of causes:

- *Structural*—pervasive factors become built into the policies, structures, and fabric of a society and create preconditions for violent conflict.
- *Proximate*—factors contribute to a climate conducive to violent conflict or its escalation, sometimes symptomatic of a deeper problem.
- *Triggers*—single events or their anticipation generate or escalate violent conflict (<http://www.conflictsensitivity.org/node/8>).

As an example, consider the 1994 conflict in Rwanda:

- A structural cause could be what some analysts have said was a colonial (pre-1950s) emphasis on apparent differences between the Hutus and Tutsis and the exclusion of those perceived as Hutus from the colonial administration.

- A proximate cause could be the creation of “Hutu power” newspapers and radio programs, starting in 1990, that said Tutsis were national enemies.
- A trigger was the shooting down of Rwandan President Juvenal Habyarimana’s airplane, widely thought to be the work of Hutu extremists displeased that Habyarimana had agreed to peace negotiations with a Tutsi insurgent group (the Rwandan Patriotic Front) fighting the Hutu-dominated government.

As with political and economic analysis, there are a number of sources for analysis of most conflicts. In addition to the sources suggested above for political and economic analysis, conflict analysis can be found at:

- Academic books, such as *Understanding Civil War: Evidence and Analysis* (Collier and Sambanis 2005).
- <http://www.business-humanrights.org/Home>, a guide to articles, reports, and other websites on business and human rights issues that also covers some conflict topics.
- <http://www.eldis.org/go/topics/resource-guides/corporate-social-responsibility/business-and-conflict>, a repository of articles on topics relevant to business activity and conflict.
- <http://www.crisisgroup.org/home/index.cfm>, which analyzes issues, causes, and politics in current major conflicts.
- <http://www.iiss.org/programmes/conflict>, which provides updates and assessments of many current conflicts.
- <http://www.peri.umass.edu/Modern-Conflicts.404.0.html>, which describes the background and status of most modern conflicts.
- <http://www.globalsecurity.org/index.html>, a pool of security- and conflict-related items from different news sources.
- <http://jir.janes.com/public/jir/resource.shtml>, a site that covers a range of security topics—including organized crime, state stability, country risk, extractive resources, and political scenario analysis.

ANGER MINES  
HATARI BOMB



**Working in conflict-affected** countries involves more everything—more cost, more time, more risk.

—Interview with IFC staff



## 5

# Planning for investment climate reform in conflict-affected countries

Once diagnostic work is complete, planning is the logical next step for investment climate reform efforts in conflict-affected countries—developing specific program interventions and defining their intended results in response to findings about a country’s technical needs, political and economic dynamics, and causes of conflict. Planning should align resources with tasks to produce results consistent with creating employment, attracting investment, and supporting peace.

### Plan for long timeframes

Delivering reform can take longer in conflict-affected countries. In a survey of IFC advisory staff working in such countries, nearly 80 percent said that project timelines need to be longer than in non-conflict countries.

Reform takes longer in conflict-affected countries for many reasons. Weak institutions, physical insecurity, unpredictable political support, transportation and communication breakdowns, and difficulties in finding firms and consultants willing to work in a conflict-affected country can delay or disrupt schedules. On very short notice, parts of a country may become inaccessible, meetings may be canceled and movement restricted, and government counterparts can change.

### Key ideas in this section:

- Timeframes are longer and costs higher in conflict-affected countries, and projects should build in extra time and budgets accordingly.
- Start early to find the right team members and ensure effective planning and coordination.
- Security preparedness and staff well-being should not be left last.
- Reputation risks cannot be avoided—only mitigated.

Perhaps the most common reason for longer timeframes are the myriad unpredictable delays that typify the chaotic and crisis-prone environments of conflict-affected countries. Extra time should be built into projects to allow for the unexpected, manage client and team expectations, and deliver results.

At the same time, there is an inherent tradeoff between the need to have longer timelines and to deliver quick support on the ground. One approach is to scale project interventions based on short-, medium-, and long-term perspectives. Rapid, more easily achieved results could be planned for during the first six months of a project, and increasingly more difficult results planned for the 6–12 month period, and then the 12–18 month period. That way, the project avoids inactivity while testing security conditions and political willingness, and allows success to build on success.

## Budget for higher costs

Working in conflict-affected countries is expensive. In the same survey of IFC advisory staff working in conflict-affected countries, 63 percent of respondents said that project budgets in conflict-affected countries need to be higher than in other countries. In addition, 58 percent believed that supervision should be more intense.

Costs are higher in conflict-affected countries for a variety of reasons. Air flights to such countries may be infrequent and expensive, and transportation, power, and water may not be widely available. Vehicles may be hired on a limited basis, electricity provided by on-site generators, and water delivered to roof top water tanks by water-trucks. Security costs can also be higher because of the need to provide staff offices and living areas with 24-hour armed guards, walled compounds, blast- and shatter-proof windows and doors that are compliant with UN Minimum Operational Security Standards (MOSS). In some cases armored vehicles or armed escorts may be required. In addition, staff and consultant costs often include a hardship premium. One IFC staff member described an impact assessment that, though originally budgeted at \$10,000, ultimately cost \$80,000 when security costs were included.

In addition, low institutional and technical capacity among government counterparts and local workers often requires that project teams spend more time in conflict-affected countries and/or hire technical advisers to work closely with reform counterparts—both governmental and among international partners. Indeed, the complexities and low capacity of conflict-affected countries demand field presence and close supervision. Moreover, in-country project staff signal a serious level of commitment to counterparts, which is crucial for building trust.

## Find the right team members early and move to the ground

One of the biggest challenges for project team leaders in conflict-affected countries is finding the right people for the team and establishing a field presence early on. Most people do not want to work in conflict-affected countries, and finding people with the right skills at the right time can be difficult and time-consuming. There is often also an urgent need to hire national staff in-country. Given that recruitment is likely to be onerous and slow, it is important to identify the right people even at the concept stage of a project.

The first step is identifying needed skills. Two types of skills are required: technical and interpersonal. Technical skills are easily identified, but the interpersonal qualities that people need to operate effectively in conflict-affected countries are less obvious.

Project teams working in conflict-affected countries have consistently identified a number of qualities that they consider essential to effectiveness, including the ability to work and live in an unstable environment, knowledge of and interest in local culture, history, and development, strong diplomatic and communication skills, patience, independence, flexibility, and innovation. Investment climate team leaders should be aware of the need for these qualities and seek to build them into the team either through individuals or across a range of people (Makhlouf and Auier 2008).

Given the cost and difficulty of attracting foreign staff to conflict-affected countries, domestic staff are not only necessary, but they can provide project teams

with enormous insight, understanding, and continuity (box 8). Project success is much harder to achieve without local staff. But in many post-conflict countries with numerous UN agencies and nongovernmental organizations, talented local staff can be hard to find—and competition for local talent can drive up wages. Moreover, wage inflation for local talent can drain government ministries and agencies of badly needed capacity, undermining governmental counterparts. And though domestic staff are usually paid less than foreign staff, rising wages and high turnover can be common during the life of a project. A conflict-affected environment makes it difficult to manage projects remotely. Practical issues like information gathering, coordination, logistics, and issues

### **Box 8 Recruiting local talent in Yemen**

In 2006, IFC began work with the Yemeni government on a Mining Policy Reform Intervention. Within a year the project had produced clear results, including an internationally competitive fiscal regime, draft Mining Law, and rationalized licensing procedures. Recruiting local talent was a major reason for this success. A strong local team made it easier to coordinate and communicate with the client and to retain needed longer-term momentum. The local team also provided invaluable local knowledge and expertise.

Source: Essmat and Tadros 2008.

of reputation and credibility require establishing an in-country project presence. The earlier that a project team can locate someone on the ground, the better. Doing so helps establish credibility and commitment in the eyes of the client and other agencies. It is also the most effective way of understanding the challenges likely to face the project, building and cementing relationships, and familiarizing project staff with the country's culture. In addition, having an ongoing presence secures certain knowledge that can only come with time and experience on the ground, and continuity can matter for project implementation. A sustained presence also helps overcome suspicion that project staff are there only for a short term (IFC Interview. 21, 8 April 2008).



The health and morale of any project team are also critical to a project's success or failure. Working in conflict-affected countries is extremely stressful, and maintaining high morale among project staff is challenging. Project staff in conflict-affected countries often must live with uncertain security and sometimes with no electricity or running water, poor medical services, and limited social lives while being separated from family and friends for long periods. In addition, domestic staff may experience the additional stress of not knowing if family members are alive and/or the challenge of supporting a large extended family network. All these types of stress can lead to long working hours for lack of alternative activities, or to social behaviors that can be hard on staff members' health, create tensions between them, and harm marriages.

When building project teams in conflict-affected countries, consideration for staff should go beyond financial packages. Project planning should prepare staff for the inevitable stresses of danger, isolation, and times of low morale, and such issues should be open to discussion throughout the project. Many international agencies with staff working in a conflict-affected country schedule periodic trips out of the country for rest, and some provide trauma counselors for staff who have experienced violence or a security-based evacuation.

### **Integrate during planning—not just implementation**

Project teams must do more than coordinate with other units in their organizations or with outside agencies during implementation. Coordination must start when a project is at the concept stage, when decisions are being made about staffing, financing, timelines, and results metrics.

Coordination during the planning stage allows for a project team to learn what other agencies are doing or about to implement. It also helps identify ways to leverage existing and planned analytical work, resources, and expertise from within and outside the project team, including outside agencies. When synchronized with other reconstruction efforts, intended and proposed reforms can advocate for a more open policy space that facilitates their implementation.

## Do not ignore security protocols

The potential for violent conflict in conflict-affected countries cannot be treated casually. Project teams must plan for insecurity ahead of establishing a long-term presence in the field. Practical steps that can be taken include:

- **Taking security courses for fieldwork in conflict-affected countries, such as the training offered by the United Nations Department of Safety and Security (UNDSS).** The UNDSS offers online courses on basic security and advanced security in the field (<https://dss.un.org/dssweb/>). The website is accessible to the public, but requires registering to create a user profile. The UNDSS is unfortunately only available to UN or affiliated agencies, and consultants who wish to take the field security course must have an email address from one of these agencies. The courses take a few hours but offer excellent guidance on incidents that project teams might face, such as what to do at armed checkpoints, if a vehicle is hijacked, if a bomb explodes at or near the project office, and so on. Bilateral aid agencies may also offer in-house security training in which project teams may participate.
- **When traveling to a conflict-affected country, ensuring that every member of a project team obtains a security clearance for that country through the UNDSS website.** When the security clearances are issued, notifications are also sent to in-country UN offices, meaning that project team members are visible in the UN security system should they need help or should there be an evacuation. In addition, staff of bilateral aid agencies should register with their diplomatic missions if in-country. It is also wise for team members to register with their home countries' embassy or consulate if present in-country, to increase options should there be a security incident.
- **Visiting the in-country UN security office for a security briefing, so that the project team can be better prepared.** The project team should leave its local contact information (hotel, international telephone number if roaming, or local telephone number) with the security office in case of trouble. The project team should also take as many telephone numbers as possible for security office staff so that the team can find out what is happening if there is an incident. If an evacuation occurs, it will likely be led by a member of the local UN security office making a list of people to be evacuated. By

sitting for a security briefing, project teams can make it more likely that their names will be on such a list.

World Bank Group staff should be aware that few UN staff in the field know that the World Bank Group is part of the UN system, and some may have never heard of the International Finance Corporation. Thus, to ensure their safety should an evacuation or other emergency occur, it is crucial that World Bank Group staff first follow UN protocols on giving travel notifications and attend security briefings when arriving in conflict-affected countries.

### Accept higher levels of risk

Working in conflict-affected countries involves greater risk of failure and of reputation damage. The risk of failure can deter involvement unless such risk is accepted and mitigated where possible. Many of the conditions of conflict-affected countries make failure a possibility. Goals may not be fully achieved by the close of a project due to delays, corruption, or project teams having to leave early for medical or security reasons. Little can be done to prevent such risks.

While these prospects are unpleasant, it can also be said that not engaging in conflict-affected countries is riskier than failing. Addressing conflict is essential to reducing poverty, and the international community must be involved in conflict-affected countries rather than leave them alone. And while risk must be accepted, it can and should be reduced where possible (DAC 2001).

Several actions can mitigate the risks of failure. Staff can conduct or rely on a country risk assessment, which can be part of political and economic analysis (see above) and may be done by a World Bank field office. If there is an in-country UN mission, weekly security situation reports (“sit-reps”) are produced and circulated to UN agencies and nongovernmental organizations. Other risks of failure can be reduced by observing proper procurement, disbursement, and accounting practices. Doing so can be particularly challenging because overly complex and bureaucratic procedures—while reflecting ethical standards—can impair timely project responses.

Risk of damage to reputation is a more slippery concept but an equally real risk. Perhaps the largest source of risk to project teams comes from choice of partners. In conflict-affected countries the options for local partners or reform counterparts may be few. The most able government or private sector counterparts may not always have the greatest integrity, and may have a history of unethical practice or relationships with people who were engaged in unethical conduct during the conflict. Project teams may unwittingly form partnerships with people who are locally known for corruption, ethnic or other political group bias, or for being party to illegal commercial deals. They may also be involved with companies known to have actively participated in a conflict, such as in weapons purchases or in making payments to a fighting faction. Association with such partners, however well intentioned, may result in the project team communicating the wrong message.

While working in Afghanistan, IFC consultants were forced to undertake rigorous due diligence processes to ensure that commercial banking partners were not in violation of anti-money laundering, or financing of terrorism rules, because of the active presence of Al-Qaeda and warlords involved in the opium trade. In Liberia, members of the transitional government and legislature were on UN Security Council travel bans and had their assets frozen. In Iraq, national staff working with the United States government faced their own reputation risks because of their association with controversial foreign interests of the United States. While in all these cases a close working relationship was necessary at times, that relationship had to be cautiously managed to avoid appearing too friendly. By including a large and diverse range of stakeholders in project activities and by constantly communicating intentions, project teams could partly mitigate the generation of rumors and allegations (Interview with IFC consultant March 10<sup>th</sup> 2008; IFC Interview No. 36 March 14).



**Implementation is key.** It is not enough to have good institutions on paper.

—IFC Interview 9, 7 March 2008



## 6

# Implementing investment climate reform in conflict-affected countries

This section focuses on how investment climate promotion teams can respond to some of the main challenges identified by project teams consulted for this guide.

## Working with clients

### Relationships are more important than arrangements

Practitioners interviewed for this guide emphasized the benefits of strong personal relationships with counterparts. In a context of weak institutions and changing leadership, project teams cannot always rely on formal arrangements to ensure that reform occurs. Investing the time and effort to develop relationships with immediate counterparts on a technical level and with higher-level political leaders can help a project weather unexpected institutional changes. Building relationships with informal power holders in the private sector can also help deliver reform if political deadlocks delay a project.

## Key ideas in this section:

- Relationships take precedence over implementation arrangements; the latter can change easier than the former.
- Client capacity in conflict-affected countries often need extensive help with reforms, from small to large tasks.
- Managing expectations is important in any project; in conflict-affected countries it can improve the security of project staff.
- Efforts should focus on building a constituency of reform, and avoiding a single champion.
- Including unconventional stakeholders in reform can preempt attempts to spoil change.
- Women are often a silent but powerful stakeholder group for investment climate reform.
- The diaspora can bring ideas, talent, money to support investment and reform; they can also spark resentment from those who stayed in country and endured the conflict.
- Quick support and rapid follow-up helps build trust in commitment to reform.
- Even the appearance of impartiality can be politically dangerous; a communications strategy can help.
- Mid-level practitioners can be important sources of advice and reform progress; they should not be ignored in favor of top-level government staff.
- Coordination is difficult to achieve in “normal” developing country contexts. It is even more important in conflict-affected countries, and extends past agency to agency coordination—it involves strategic location of reform in the wider reconstruction agenda.
- Cultural differences in are to be expected; in conflict-affected countries they include differences between those who have had to survive in very difficult circumstances and international aid workers, and include differences between military and civilian cultures.
- Setbacks and failure are a real possibility, as is the reform work becoming a lower priority as crises emerge and politics shift.



Informal relationships are also important to changing the minds of stakeholders working on reform. Informal relationships help build clients' trust in project teams' commitment and create space to encourage clients that they can effect change and help them see that change happen. Encouraging belief in change happens as much through informal interactions as it does through formal project work.

### Support clients during implementation

As noted, institutional capacity may be very limited after a conflict. Poor capacity requires project teams to spend more time than usual helping counterparts identify reform priorities that can lead to an actual project amid a likely sea of extensive needs—explaining the reasoning behind proposed reforms and providing practical assistance where needed. Counterparts may need direct help with a range of activities, from drafting legislation to writing policy papers, creating budgets, planning events, preparing presentations, or writing memos.

Project teams should be sensitive to this range of capacity gaps and be willing to step in to provide help where needed. At the same time, project teams should be aware that such help comes at the price of capacity building. Direct support to government counterparts may help move a project along in the short term, but it will not build capacity in the long term.

### Ensure a sense of ownership

One of the most common tradeoffs that project teams encounter is whether to allow client “hand holding” to lead to doing many reform activities directly, or whether to work with clients at their capacity level in order to build capacity. While direct implementation may improve project speed and quality, the danger is that clients will lack a sense of ownership over reform. Thus clients should be involved at every stage of the reform process, and training and education should be provided wherever possible.

An embedded technical advisor who works in-country with the client can also help strike a better balance—but that may be easier said than done. Temporal restrictions, distorted incentives, and low skill levels can mean that there is no time to train people, highly skilled people find work elsewhere, or clients lacking skills cannot meet the demands of reform tasks. In some cases, project teams may have to accept that they will not be the client’s top concern and act accordingly: by extending timelines, setting incremental goals, and investing heavily in local capacity building with an eye on the long term.

### Manage expectations

With the onset of peace and the arrival of numerous international agencies, optimism that change has finally come naturally soars. In addition, expectations of international agencies rise because peace and prosperity are linked to the money these agencies bring. People, and especially former combatants, look for rapid improvements in political and economic conditions—what has been called the “peace dividend.” Local leaders are often under immense pressure to deliver, and progress can be linked to continuing stability and security as ex-fighters and returning displaced populations’ expectations are increasingly expressed.



Investment climate reform efforts are not immune from this sentiment, and clients may end up anticipating far more than can be delivered. The term investment climate reform evokes expectations of foreign investment and employment. When investment does not come in expected volumes or with expected jobs, there can be widespread disappointment and a sense that the government or donors have failed. It can then become harder to motivate individuals or institutions to implement reform.

The most effective way to avoid this problem is be clear from the outset about the likely outcome of proposed reform, the proposed timeframe in which it will occur, and its intended impact on peace building. The adage to “under-promise and over-deliver” is useful to bear in mind. It is also helpful to remember

that as much as international agencies are subject to local expectations, ultimate responsibility for change—and therefore praise or criticism—belongs with government.

## Avoid relying on a single champion

Finding someone with the means and will to champion a proposed reform is essential. A strong champion can play a decisive role in delivering reform where institutions are weak and a country's politics are fragile. At the same time, relying on a single champion presents more constraints than opportunities. For example, reliance on a single person in a conflict-affected country can impede a reform project if that person changes positions, responsibilities, or priorities. Politically, reliance on a single champion whose full interests and background are unknown can increase reputation risk for the project and team. Relying on multiple champions helps manage reform saboteurs, strengthen norms of reform, create trust and accountability, and protect the work from capture by one person. Information gained or given through one champion is dangerous.

Project teams have responded to this challenge by expanding the number of people with a stake in proposed reforms. They acquire a circle of support that can extend across the private and public sectors, creating a constituency for reform. One way to bring together multiple stakeholders is to form technical working groups to focus on specific issues, under a steering committee. These working groups can generate ownership of solutions among sometimes disparate stakeholders, provide a venue for showing the project team's commitment, and bring together conflicting groups in a nonthreatening dialogue that supports peace.

Among key stakeholders, the government is self-evident. But donors also need to be involved as implementation partners, and not just sources of funding. The private sector should also be involved from the outset, for their ideas and support for reform; the domestic private sector is often among the first groups to return to a conflict-affected country. Stakeholders should also include civil society, which can provide powerful reform advocates. Project teams can help link civil society groups to issues and events. Parliamentarians are also critical stakeholders, as they can be useful champions outside the executive branch and

some are influential among their constituents. Ultimately, new laws will have to pass through the legislative branch, making the inclusion of parliamentarians as stakeholders a wise decision.

## Reach out to unconventional stakeholders

Project teams should also reach out to factional leaders and “spoilers” of the peace—typically unconventional stakeholders, and perhaps for good reason. Discussions with rebel or other fighting forces, especially those accused of or known to have committed human rights abuses, can provide them with credibility and leverage. During difficult peace negotiations, their involvement can undermine progress. Rebels and other such factions should not be approached or engaged in technical discussions if doing so would empower them inappropriately or disturb peace negotiations.

Rebel or factional leaders engaged in a peace process and others opposed to peace should be listened to, and project teams should share their views shared in return. In the short term, obtaining their support may reduce barriers to reform and draw them into technical discussions that advance peace negotiations. Members of rebel groups or factions may eventually be included in transitional governments, so having existing openness to discussion can ease that evolution.

International military or peacekeeping forces are another unconventional stakeholder group for most project teams. Such forces may possess excellent background information on politicians and members of the private sector, and are good to know if there is a security incident. They also have valuable resources that may be useful to project efforts. For example, USAID created one of the first industrial parks in Afghanistan using generators provided by the U.S. military.

## Include women

Women are often overlooked in the peace process, and no less so in investment climate reform. Women can suffer disproportionately during conflict; they are targeted for sexual violence and left to maintain basic economic functions such as farming, trading, and sustaining family life while men fight. They are



often the sole caregivers of children while fleeing fighting or living in displaced camps. In some cases, such as during the civil conflicts in El Salvador, Eritrea, and Liberia, new opportunities for women's leadership emerged. Women need careful attention during reintegration, including opportunities to benefit from economic growth that do not return them to unwanted traditional roles that left them vulnerable.

Women can also be an invaluable source of entrepreneurship and economic growth once conflict ends. Women who developed leadership skills and learned how to manage scarce resources for their families in extremely difficult circumstances can possess the business and market acumen and creative determination needed to make their business activities succeed.

### Do not forget the diaspora

The diaspora should also be included in investment climate reform, since many will be interested in returning to their home country after the cessation of violence. They may be among the first investors from abroad because they will require less convincing that things are safe again, unlike foreign investors

who do not know the country. The diaspora can have ideas, talent, investment ideas, and a visceral commitment to making their businesses work that other investors lack. Project teams can encourage diaspora associations to demand accountability and responsibility from their government in exchange for their talent and investment.

But the diaspora is not a silver bullet, and its presence in conflict-affected social and economic space is not neutral. IFC research on diaspora investors in Sierra Leone found that, despite their social networks, they may not understand the local political economy any better than other outside investors. Diaspora investors can also face large opportunity costs as they must choose to move their families back home in post-conflict living conditions—giving up jobs, schooling, health care, homes, and social lives.

Moreover, the diaspora can be aligned with one side or another in a conflict, or with a particular ethnic group. When partial to a side of the conflict, diaspora members can create division and do more harm than good. One way to mitigate this potential harm while tapping the skills and resources of returning diaspora members is to create “criteria of credibility,” whereby diaspora members are identified as viable local partners for foreign investors. Diaspora members may offer opportunities for credible investment partnerships that might initially be missing in a country emerging from conflict. Criteria of credibility could be championed by business associations, linked to membership requirements.

## Public-private dialogue as venues for change

Increasingly at IFC, client engagement is formalized in public-private dialogues. These forums are crucial in post-conflict environments, not only for their benefits to the investment climate but also for building trust and fostering reconciliation. IFC experience and research shows that public-private dialogue are extremely relevant in conflict-affected states, helping to regenerate trust between members of the public and private sectors. IFC is currently implementing public-private dialogues in 13 conflict-affected countries (box 9).

## Box 9 Sustaining peace in Cambodia through public-private dialogue

When fighting in Cambodia ended in 1998, the country had undergone a UN-administered election and was in the midst of transitioning from a communist state while struggling with the Asian financial crisis. The government was focused on instituting a market economy, an effort that enjoyed some initial success. The confluence of these factors led the government to realize that the emerging private sector should be included in the development of the economy if it was going to grow.

The Government Private Sector Forum is structured in two parts, with the main forum held biannually under the chairmanship of the prime minister and making binding cabinet decisions, along with seven working groups that meet regularly on issues such as law, tax and governance, export processing and trade facilitation, and banking and financial services. Each working group is co-chaired by a government minister and private sector representative. The working groups discuss policy-related issues and direct operational impediments facing the private sector (such as road conditions, unofficial fees, and damaged infrastructure).

An important factor that enabled the forum to move forward was the focus on a neutral, shared, apolitical platform that could be used for constructive consultation on issues. If the forum had been perceived as other than a constructive, participatory process, it would not have encouraged business-people to engage in a participatory process for development.

Source: Herzberg and Wright 2006.

By bringing together different groups in conflict-affected countries, public-private dialogue bodies help build a sustainable constituency for investment climate reform and an atmosphere of understanding between the public and private sectors on which reforms make the most sense. In addition, with private sector representation in such a forum—especially from companies working in sectors linked to the conflict or to one of the fighting forces—issues that may initially have been difficult to raise can be discussed on technical terms.

## APPROACH

### Horizontal or vertical approaches to reform?

One common tradeoff with investment climate reform is whether to take a horizontal or vertical approach. A horizontal approach takes the broadest scope, addressing multiple areas in a comprehensive fashion—such as business registration, licensing, inspections, tax simplification, investment code revision, and investment promotion. A vertical approach focuses on a few key sectors, addressing regulatory barriers and investment generation issues that matter the most in making those sectors viable.

A horizontal approach addresses regulatory constraints systemically, benefiting all businesses equally. But this approach can suffer from a lack of strategic focus and may be too much at once for a government with limited capacity or political will. A vertical approach offers more strategic focus and may be an appropriate first step for catalyzing reforms while government and other stakeholders build their skills and commitment to investment climate reform. But by focusing on only a few sectors, a vertical approach tends to bias toward the entry and ease of foreign investors' business activities—at the expense of enabling domestic businesses.

Whether one or both approaches are used over the life of a project, it is important to try to link investment climate reform to domestic investment activity, foreign direct investment, and export market access for local products and services. Doing so helps provide a reality check on the ultimate purpose of investment climate reform and generate support for such reform if it is perceived as contributing to market development.

### Bold or incremental reform?

The choice to undertake either bold or incremental reform confronts project teams throughout the life of their projects. These choices will depend on the amount of government capacity and political will (box 10). Opportunities to switch between incrementalism and boldness can emerge suddenly, such as with changes in leadership or the arrival of new investors in-country. But the

## **Box 10 Boldness in Lebanon and incremental steps in Sierra Leone**

In Lebanon, high-intensity conflict of short duration has recurred since the 1980s. The capacity of Lebanon's human capital has remained high, and entrepreneurialism has remained intact and grown over time. By contrast, Sierra Leone's conflict was intense and lasted for more than 10 years, taking a deep toll on human capital and entrepreneurialism.

While politics in both countries are complex and shifting, Lebanon's government had considerable interest in enacting reforms as a sign of resilience after the country's month-long air bombardment by Israel in 2006. For example, bold reforms were made to the company registration system. In contrast, government workers in Sierra Leone needed considerable ongoing support, and much effort was needed to ease government suspicion of the private sectors in both Lebanon and Sierra Leone because their reforms progressed incrementally rather than boldly.

Source: IFC Staff Interview 24, April 3 2008.

lower government capacity is, the less the government may have a plan for rebuilding; the more limited market activity is and the more widespread damage is, the more important it will be to begin with activities that help resume the basics of market activities. In those circumstances, incremental reform may make more sense.

With higher government capacity and greater political will for change at and below the ministerial level, bold reforms may make more sense. Bold reform requires enough people with sufficient power to have adopted a new mentality about desired reform.

## **Culture counts**

Cultural differences can be a source of miscommunication for project teams. Different values, attitudes, and world views can hinder communication and create misunderstanding. Even if project teams are familiar with a country

and its national culture, they may end up dealing with people whose training and life experiences have resulted in a different way of seeing the world. For example, team members may find themselves engaging with former fighters whose instinct is to control market forces—when one of the core messages of investment climate reform is not to over-regulate. It can be difficult to convince a former guerrilla fighter that less control is best practice.

Cultural differences and misunderstandings can be mitigated by learning about the cultural framework in which clients and stakeholders operate. This can be done formally, by reading books and articles, but is likely better done informally, by talking to people who are from or have worked in the country or region. Project teams should also test their messages with people who know the culture, ensuring that what they want to communicate is what people will hear.

Legal dispute resolution is an example of an area where understanding culture can help. Many countries have both formal and customary legal systems. The formal legal system in conflict-affected countries may be as lacking in capacity and transparent processes as other institutions, and may also have a large backlog of commercial cases. For these reasons, local businesses may avoid settling disputes in formal courts. Customary courts and judicial procedures are usually associated with rural areas and thought to apply to family disputes and other social issues. But they have a huge impact on property issues, including land reform, land titling, construction permits, and secured lending. Returning refugees or displaced communities has enormous implications for land ownership and construction permit processes. Cultural awareness enables a project team to understand alternative dispute resolution approaches available through customary legal systems and to find ways to use these systems to support land swaps or compensation to settle disputes not recognized in the formal judicial system.

## Be impartial, but address inequality

Even after a war has ended, tensions will likely remain between fighting factions. Appearing to favor one group over another, even if unintentionally, may jeopardize a project's success. This is a central principle of “do no harm”



approaches to conflict-affected countries. These approaches first emerged in the humanitarian aid community in the mid-1990s when it was recognized that aid can have negative effects. The internal objectives of aid can be correct, but the structural impact of its delivery can destabilize fragile relationships between groups in conflict (Gaigals 2001; Anderson 1999).

Investment climate reform efforts can inadvertently cause harm by introducing projects that seem to benefit one side of the conflict more than another. For example, a land titling project could aim to support the development of a land cadastre system in communities most devastated by a conflict because, from a technical perspective, those communities have the greatest need for such assistance. But from a conflict-sensitive viewpoint, if those communities were all on a side of the conflict that were perceived to have perpetrated war abuses, that project would cause grievance among nearby communities no matter how strong the technical arguments. By creating destabilizing effects, the project would have done more harm than good. Still, while being sensitive to perceptions goes a long way toward minimizing conflict, project teams must be sure to address inequalities.

## Develop a communications strategy early

A communications strategy has three goals in a conflict-affected country. First, convincing powerful people to support reform. Second, achieving credibility by demonstrating success. And third, listening to people who can advance reform. It is not enough to succeed with reform—it is also necessary to be seen as succeeding. Widespread awareness of effective reform helps build and maintain momentum for further change. The challenge to communicate project team effectiveness without detracting from government authority and achievements.

A communications strategy can take many forms, from informal conversations with religious leaders to targeted media campaigns. The strategy chosen should reflect its purpose, target audience, and resources. For example, in some situations a media campaign is unnecessary or inappropriate, and in others it is not possible because of weak media (Rahman and others 2007).

As in most countries, false perceptions and rumors can abound in conflict-affected countries—but with the difference that some rumors can lead to insecurity in conflict-affected countries. If reforms to the investment promotion agency threaten the powers of political and commercial elites, the potential discovery of corruption and any number of resulting counter-accusations can generate bad feelings.

Successful reforms need to be widely communicated to domestic constituents. Investment climate reform successes should also be communicated to potential foreign investors and to neighboring countries. Information on reform can bolster foreign investor confidence and influence their decision to locate in-country rather than in a neighboring country in an attempt to serve a conflict-affected country from there. Similarly, such information can help investors in neighboring countries enter a conflict-affected country after years of fighting, increasing regional integration. The domestic investment promotion agency, along with members of business associations and political leaders, is important to spreading the message of accomplished reforms. Trade missions, investment road shows, and official visits by government leaders are all good opportunities to advertise post-conflict regulatory change as evidence that a country is recovering. By participating in communications strategies, investment promotion agencies can do more than attract investment; they can also be advocates for reforms that promote better governance. Tips on a communications strategy are in a ‘check-list’ annex to of this Guide.



## Recognize the political cycle

Every political system has a rhythm or cycle. These are often easy to spot in transparent, traditionally democratic countries. Some points in the political cycle are optimal for reform. In the United States, for example, politicians and advocates of change try to time their recommendations early in the life of a new administration, hoping that energy and political will ease their adoption.

Political cycles may not always be as predictable or easy to discern in conflict-affected countries, whether because democratic institutions are new or because of political instability. Still, it is worth trying to identify the best times to attempt reform. In countries holding democratic elections it is worthwhile where possible, to time reforms with the arrival of new leadership. In other cases, optimal timing may result from the appointment of a new minister or from demands for change by a particular constituency. Investors and domestic businesses can be just as sensitive—or even more—to the tone that politicians set through their statements and attitudes toward them than through actual changes in the investment climate.

## Seek advice from people working at intermediate levels

When implementing reform, there is a temptation to focus exclusively on the highest levels of decisionmaking. Often the middle ranks of government institutions play a key role in driving and sustaining reform—while in some cases the intermediate levels contain the most entrenched opponents of reform. Top-level signals and willingness to manage people blocking reforms leadership can be indispensable. But if there are engaged and supportive people at the intermediate levels of an institution, they should not be neglected. Taking the time to identify important players lower down in the ranks of government and cultivating their support can prove extremely fruitful. People working at the middle levels of institutions can often identify the most effective starting point for a proposed reform (IFC interview 9, 7 March 2008).

## Seek quick support and rapid follow-up

When peace comes, it is often fragile. Needs are high, and there is urgency to



complete reforms. One way that successful project teams have responded is by identifying priorities that can be achieved relatively quickly.

Prioritizing quick support involves deciding what is important—that is, likely to have the most impact, ideally both technically and for peace—and what is feasible (Masinde 2007). What this means in practice will vary by situation, and again highlights the need for good understanding of a country’s political and economic situation.

The reform memo that IFC’s Doing Business Rapid Results Unit produces can be useful for identifying quick, actionable technical assistance. Clients may feel some skepticism about the possibility of reform and the likelihood that the project team will follow through with its proposals. One way of dealing with this is to prioritize rapid follow-up involving small actions, making the most out of windows of opportunities that arise and demonstrating the team’s professionalism and commitment.

### Coordinate with other international agencies

The call for better coordination among aid agencies is longstanding but notoriously difficult to practice. Coordination among agencies working in conflict-affected countries is no less crucial (box 11). The main reason is simply to learn what other agencies are doing and ensure that investment climate reform

complements their work. Sharing relevant information with representatives from other agencies is the best way to generate reciprocity from them. But beyond information sharing, coordination is essential to managing the tricky political dynamics of reform and mitigating the corruption that can mark post-conflict economies. In difficult political settings, a united front among donor partners can leverage change around a few issues.

For most project teams, donor coordination should extend to the World Bank, United Nations, regional development banks (such as the Asian Development Bank), bilateral agencies, and even humanitarian agencies.

## Do not be surprised if your work is a low priority

In the difficult conditions imposed by recent conflict, government officials will focus on what they consider immediate priorities, such as security, basic services, and jobs. Investment climate reform may be seen as a low priority.

### **Box 11 Coordination in conflict-affected countries**

International assistance in conflict-affected countries is often coordinated in formal structures, where international partners and government meet in technical working groups to discuss a common reconstruction agenda. In Liberia, donors and the government met in the context of the Liberia Reconstruction Development Committee. In the Democratic Republic of Congo, donors and the government convened the Consolidated Assistance Framework. These coordination structures helped focus donor assistance on post-conflict government development strategies, which are often subsequently articulated in poverty reduction strategies.

One crucial difference between Liberia and the Democratic Republic of Congo is the focus of government leadership on reform. In 2006, Liberia's newly elected government was focused on reform, which enabled a broad reform agenda to be implemented. In the Democratic Republic of Congo the leadership was less focused on reform, and a modest reform agenda remains difficult to implement.

Source: IFC Interview 36, 14 March 2008.

For investment climate reform to be effective, it is not always enough to change the rules. Often attitudes and culture needs to be affected as well. What is intuitive to a practitioner may not be to people living in a community where the private sector's role is marginal. Nonetheless, government, peacekeeping forces, and humanitarian groups must look beyond short-term horizons to long-term growth requirements and not perpetuate the high unemployment that often led to the unrest. The project team will have to communicate that neglect of the investment climate will come at a cost that the government and donors cannot afford.

There are several ways to raise the profile of investment climate work. The most necessary, but most intangible, is to convince the client that investment climate reform can contribute to the transition to peace. The aim should be to establish shared values with key players who would be active in reform. This can be done informally in one-on-one conversations or may occur in a more structured way as part of a workshop or in some cases a broader communications or education strategy. Another approach is to help government officials see links between proposed reforms and the wider reconstruction agenda developed by the government and international partners. In addition, investment climate reform can be linked to specific sectors that the government has prioritized.

## Prepare for setbacks and failure

Poor capacity, inadequate information, fragile institutions, embedded interests, and distorted economies make successful reform harder to achieve than in countries that do not face these conditions. Moments of frustration or disillusionment over the slow pace of reform or change from war to peace are inevitable when working in a conflict-affected country. Project teams should be prepared for the high likelihood of failure. Despite even the best attempts at planning and implementation, project teams should accept that a project may have to be restarted several times.



**We have obvious technical** indicators but these are not enough, more so in conflict-affect countries.

—IFC Staff Interview



7

## Monitoring and evaluation of investment climate reform in conflict-affected countries

**M**onitoring and evaluation can be difficult at the best of times. The nature of conflict-affected countries compounds these difficulties. Unreliable information, poor security, and weak capacity can make evaluation extremely difficult.

The extent of physical damage, death, or displacement of trained government staff from national statistics offices may affect the type and amount of data available in a country. Or rebel forces overrunning a capital city may burn and loot government offices, including the land and company registries. Seaports and airports are also often occupied by fighting forces, given the importance of transport hubs for controlling wartime trade that helps finance fighting. Import and export records may be deliberately destroyed or simply ruined or lost through neglect. Staff trained in the collection, entry, and storage of data, even using simple computer software like Excel, may be unavailable. If a conflict lasted for a long time, the most recent prewar census,

household income expenditure survey, enterprise survey, and investment climate survey data may be out of date or lost.

Project teams consulted for this guide offered recommendations for dealing with these difficult conditions for monitoring and evaluation.

### Start immediately

Given the likely challenges that project teams will face undertaking monitoring and evaluation, the process should begin as soon as possible. This will likely require planning to conduct baseline surveys and establish basic technical

### Key ideas in this section:

- The extent of damage to buildings, institutions, records, and skilled workers may leave a country with little or no data or data collection capacity, making it very difficult to measure impact
- Given the importance of baselines in assessing project progress, data collection should begin immediately after conflict ends; often many agencies are conducting surveys, and their data could be used or include questions relevant to intended reform
- The “gold standard” of data collection will elude most project teams; efforts to innovate with methods with indicators may be needed
- As difficult as it may be, efforts should be made to measure how investment climate reform contributes to peace.

information. Where there are many international agencies in a country following a conflict, it is useful to check if another agency is conducting a related survey whose data could be used, or to check if key project-specific questions could be added to planned surveys. Collaboration with other agencies can also help lower costs and increase survey coverage. The largest constraint to survey work by any agency in a conflict-affected country is the likelihood that transport and communications infrastructure is severely limited.

## Keep it simple

Because data may be scarce and collection of new data difficult, it may be better to select just a few meaningful indicators at the outcome and impact levels, and focus efforts on those. It also may be helpful to focus on a geographically bounded area, such as business climate statistics for the capital city or a survey of businesses in an area adjacent to a port. Tracking too many indicators in a project's monitoring and evaluation design may be unrealistic, and when the project team cannot report on them, may give the appearance that the project is not delivering results.

## Be innovative with techniques

Be prepared to be unorthodox. Some project teams have used photographs or personal stories if data are unavailable or cannot convey the nature of the reform achieved. Perceptions reported by business owners dealing with government regulations when trying to register a business or pay taxes can provide useful information for actual change. In the absence of clear and immediate outcomes, it may be necessary to measure processes instead (IMF Interview 21, 8 April 2008). In conflict-affected countries, monitoring and evaluation techniques will likely develop from a learning by doing approach that adapts and improves on established techniques from countries not recovering from conflict.

## Invest in knowledge transfer

Too often, new project teams are forced to start from scratch because previous knowledge has not been transferred or is presented in an inaccessible way (with poorly organized files, for example). Creating a well-organized, easily accessible

project memory should be a priority from the very start.

## What teams measure influences policy

What the project team chooses to measure can shape perceptions about what is important among stakeholders in government, the private sector, the local media, and other international agencies. For example, if the project team measures foreign investment approvals as an outcome indicator, it will reinforce an assumption that foreign direct investment matters most. But if the team measures turnover in rural markets, it sends a very different signal. The focus of team measurement efforts can shape public opinion, the reconstruction agenda, and even government policy.

## Measure for peace

Despite the challenges of monitoring and evaluation in conflict-affected countries, it is important to try to measure changes in conflict-causing factors. Given that investment climate projects in conflict-affected countries are meant to contribute to peace as much as to technical reform, project teams should have a sense of whether the project is having a positive impact.

Theories of change in peacebuilding efforts, regardless of the type of project, can make causality hard to clarify and attribution to project activities hard to correlate. Relatively few indices measure peace and, where they exist, confront the same issues of poor or no data that all agencies face in post-conflict reconstruction.

Still, perceptions of peace matter in conflict-affected countries and can be used as a proxy for whether the basis for conflict is changing or whether peace is taking hold. The business community, both domestic and international, is increasingly risk adverse and sensitive to political and security threats. As an example, an increase in the number of local businesses operating, even informally selling luxury goods, can be a good sign. It can mean that people are willing to invest or spend their scarce incomes on things not immediately related to survival or sudden flight.



**A thriving domestic private** sector operating in a transparent business environment can attract, provide services for and partner responsible international investment.



## 8

# Check lists and tips



1. A "Go-No Go" Check List for an Investment Climate Reform Project in a Conflict-Affected Country (Mark each box with either a "✓" or an "X")

Has active, sustained violence ceased?

Do people and goods move freely?

Has business activity resumed?

Is the provision of humanitarian relief well underway?

Is there other donor interest in engaging in the country?

Is there a government counterpart interested in reform?

If all boxes were marked with a “✓”, then the basic pre-conditions for working a country have been met. Further secondary conditions may guide decisions to begin an investment climate reform program, such as whether the country aligns with overall strategy, whether there is a business case or fit with products/ services, or whether there are resources to begin a program.

2. Security Protocol Check List (Mark each box with either a “✓” or an “X”)

- Are all project team members certified for taking a field security course?
- Have all project team members registered their travel into their project country with the UNDSS?
- Has the project team received an in-country or regional security briefing from the UN security officer covering their project country?

- Do all project team members have local telephone numbers and does the project team have a Thurya telephone?
- Do all members of the project team have the contact information for the other members (i.e. telephone numbers, hotel name and room, vehicle drivers' contact information)?
- Do all project team members have a point person designated who will remain in contact with the local UN security office to receive or share security-related information?
- Does the project team have an agreed plan of action should there be a need to evacuate the team because of a security incident?

### 3. Communications Strategy Tips<sup>4</sup>

- **Feet on the ground.** Employ a local Communications Officer or consultant who can help to customize, nuance and implement the strategy and can work effectively with the client as well as interface with the key constituencies.
- **Implement a Communications Audit and Stakeholder Mapping.** Identify effective modes and formats of communicating with key constituencies; identify current and potential champions and challengers of reform who can influence, will benefit or be negatively affected by the reform agenda; and identify the five top challenges for each constituency. Typically, constituencies typically include the private sector, professional associations, legislature, judiciary, gender groups, media etc.
- **Find a trigger.** From the results of the stakeholder mapping identify, develop and leverage a trigger that addresses a common challenge for the key constituencies e.g., unemployment, and which demonstrates the urgency, opportunity, benefits and relevance of enacting reforms in addressing this issue. Triggers can also be supported by data from the World Bank Group's annual Doing Business survey and other relevant findings and surveys.

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<sup>4</sup>Source: Nana Yaa Ofori-Atta. (2009). *Reform Communications Checklist*. IFC.



- **Start the story.** Develop core messaging and key audience specific messaging from technical data and the findings of the advisory program that responds to the identified priorities of key constituencies. Help the client to explain what initiatives have already taken place to improve the investment climate. Flyers, posters, a multi-media campaign to ensure the private sector has information on policies, streamlined procedures, new fee regimes, etc. This improves transparency and efficiency and provides stimulus to improve further.
- **Walk with Two Legs.** The country program should be aware of and address perceptions many have about the World Bank Group and the concerns many have about foreign direct investment. Explain the objectives, focus, and expected outcomes of the advisory program as helping to develop the growth of a viable domestic private sector that can create employment, opportunities and provide goods and services. A thriving domestic private sector operating in a transparent business environment can attract, provide services for and partner responsible international investment. Engage the stakeholders regularly. This can include developing profiles of the country program and briefs on the components/work streams to facilitate branding. Training of the media on business/economic and financial news reporting in the context of the country program's priorities, and supporting knowledge management with the legislature, judiciary etc., provide opportunities for effective stakeholder engagement.
- **Answer the 'so what?'** Help the client to explain the next steps on the reform agenda. The messages should be clear and concise and show a direct and explicit link between implementing further investment climate reforms and addressing the priorities of individuals, the private sector and the economy.
- **The reform network and input into public policy.** Build the capacity and network the current and potential champions identified in the audit and mapping in relevant forums and formats, support Public Private Dialogue (PPD) by providing good international practice and analysis of local context supports informed advocacy. A solution oriented dialogue helps the client working with the reform network to identify viable alternatives,

compromises and effectively prioritize the reform agenda. PPD supports the broader goals of good governance and accountability.

- **Set clear targets.** Encourage the client after dialoguing with key constituencies and developing consensus to provide a specific time bound reform agenda—‘21 improvements in 4 months.’ Launching the campaign helps to build awareness and provides momentum for the client and the reform partners to begin and continue working to achieve specific results in a fixed timeframe.
- **‘Then and Now.’** Update the campaign as the improvements are made. A multi media campaign contrasting number of days, fees, number of procedures and the opportunity costs before and after the improvements have been made. This ensures that the private sector and key constituencies know of and benefit from the improved procedures; it provides momentum to deepen the reform agenda.
- **Investment Promotion.** At the end of the specified period (e.g. 21 improvements in four months), implement a ‘Voices and Faces’ multi-media campaign featuring private sector leaders and others to demonstrate that the reforms have happened, and that there are tangible benefits that address some of the prioritized challenges for individuals, the private sector and the economy. This campaign can support investment promotion to local, regional and international investors. It can also be used to set the scene to progress the reform agenda further



**The more limited market activity** is and the more widespread damage is, the more important it will be to begin with activities that help resume the basics of market activities.

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