

**State Building and the Private Sector in Fragile States**  
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If decreasing the fragility of fragile states was an economic or commercial activity, we likely would see a lower number of states than we have today. We possibly would not even have this meeting! State building is essentially a political process, not an economic one, and this is certainly the perspective of the company managers in fragile states with whom we work.

The question is; in whose interest is it to speak about the role of the corporate sectors in state building activities? Although most companies, naturally, would prefer to work in a stable context, the incentive for companies to be involved in state building activities is very low, difficult to measure, and has a poor short term return on investment. After all, companies are less interested in peace and democracy on a national level and more interested in creating a stable and constructive environment in the area (the footprint area) where they operate. From a company perspective, even fragile states have stable pockets, and the reverse is also true: "stable" states have areas that are too risky from a business perspective.

Because "state-building" is not as straightforward as the terminology would imply, the role of companies in the processes that are involved is also not straightforward. As relatively marginal actors to the multi-faceted processes that underlie state building decisions and actions, corporations need to be both modest, and savvy, in their expectations about their own roles. This is certainly the case when these same companies are sometimes accused of enabling the authorities in fragile states to be less accountable and responsive to the needs of their citizens.

## **Background**

The information for the arguments that I will put forward is gathered through an effort called the Corporate Engagement Project, which is one of the projects of CDA Collaborative Learning Projects. The objective of the Corporate Engagement Project is to ensure that the corporate presence has a positive, rather than a negative, impact on the local communities in countries where social or political tension persist. Over the past seven years, we have collected experience of individual corporations in over twenty varied locations around the world and compared and analyzed these experiences in consultations involving corporate managers and others. This project has identified a number of lessons about how corporations influence, and are being influenced, by the larger political context in which they operate.

## **Five CEP Observations about the Private Sector and State-Building**

Companies, inevitably, interact with governments in countries that are politically weak. It is simply not an option to have no relationship. So the question is not IF companies should have a relationship with a particular Government, but HOW they should engage. This is because companies can interact with governments in a way that decreases state legitimacy and the states willingness to provide services to its citizens or, alternatively, a company's approach can help increase the government's accountability and responsiveness towards its citizens. And, of course, these are a piece of the much larger state building effort. I would like to discuss the following five observations derived from the experiences of the Corporate Engagement Project in this respect.

*1. Expectations that economic actors will positively impact state building, mainly through increased socio-economic welfare and hence political stability, is based more on hopes than on reality*

Companies are often welcomed because the public believes their presence will bring large scale job creation, contribute to local economic development and increase government revenues, which will, in

turn, lead to infrastructural development and social services. All of these are assumed to contribute to increased stability, at least on a local level.

The reality is more complex. Often, the employment opportunities generated by a company are, generally speaking, very limited. There will always be more unemployed youths than any company is able to absorb. Especially when a country emerges from a period of warfare, many youth lack formal education or vocational skills, whereas many corporate jobs require both. When a company needs relatively few non-skilled laborers, this naturally leads to disappointment among those who have high hopes for a better future and have vested these hopes in the company.

### *II. The presence of a company can reinforce intergroup violence*

The presence of a corporate entity also does not necessarily lead to more social and political stability on a local level. The resources that a company brings to a resource-scarce area (in terms of employment, contracts and community projects) become important to people who want access to them. We have often seen how the entry of a corporation into a poor area sets into motion intergroup competition and struggle for access to corporate resources. Such competition and struggle can become violent; it can have significant and lasting negative impacts on that area.

There are various ways by which a company –unintentionally- increased intergroup violence. For example, it can focus its community support only to “host” or “guest” communities with the objective to show benefits to people that are seen as the most apparent “threat” to a company operation. Inevitably, there is a risk that neighboring communities who do not benefit from such support see such an approach as unfair and demand their share. Companies can also hire ex-combatants as security guards, partly in an effort to provide jobs to unemployed youth that otherwise would pose a risk to the corporate presence. However, hiring ex-combatants may create resentment among the local communities who perceive that the company rewards past violent behavior.

There are many more examples where company policies and approaches favor some groups over others. And when the groups that benefit, and those that do not, overlap with existing conflict lines in society, such approaches can easily rekindle old schisms. Of course, that is not helpful when a country tries to become more stable and inclusive.

### *III. “Normal” profit motives can diminish resources needed for state building*

Corporate operations in fragile states are funded by risk capital. That means that companies investing in such countries expect a higher rate of return compared to what they would expect from operations in “stable” countries. One of the ways to achieve higher returns is to lower the costs of doing business, for example by demanding tax exemptions, bringing cheap labor and supplies from their own country, or through other measures that either lower the amount of corporate revenues flowing to the state or decrease benefits to local people such as jobs or local contracts.

At the same time, governments eager to attract foreign investment are in a vulnerable position to accept the companies’ terms. For political reasons, governments trumpet the short-term publicity gains from foreign investment rather than the negative, long-term implications of corporate conditions. When constituencies start to notice unfulfilled promises and perceive they got a “raw deal,” it undermines the legitimacy of the state and can arouse challenges against it.

### *IV. Corporations can buttress authorities who pursue personal interests over state-building goals*

Even if companies are willing to support the government in its efforts to be more responsive to the needs of its constituency, their support needs to be accepted first. Especially when new leaders feel they have made personal sacrifices for the public good, once in a position of power they often find it a challenge to resist using public office for private gains rather than furthering state building efforts, for example through ownership in certain companies. This conflict of interest undermines state credibility. There are cases

where large international companies wanted to contribute to state building efforts but were sidelined by new leaders who were offered deals from corporate competitors. (Sudan example)

In other places, the revenues accruing from the corporate presence allow governments to maintain and even enlarge their power bases. When revenues support a regime that lacks widespread legitimacy, it helps maintain the fragility of the political order with resources that are finite and that, instead, could have been used to increase the ability of governments to serve their constituencies. On the other side, a corporate presence in such countries also allows companies with a better opportunity to have access to decision makers and to develop options that contribute to increased state responsibility and accountability.

#### *V. Companies substitute for weak governments rather than working with and strengthening them.*

In many countries, resource-strapped governments expect companies to provide services that states ought to provide, such as roads, health care, education and even security. When companies see themselves faced with 1) a government unable or unwilling to provide services and 2) local threats and demands for these services, they end up substituting for government.

Not only is this an unsustainable approach, most companies publicize such deeds through ceremonies and signboards that clearly mark the company as the donor of a project. Although this desire to take due credit is understandable, such practices reinforce local notions of government ineffectiveness and, thus, further challenge the state's legitimacy. On the other hand, this allows the government to shirk its responsibilities, thereby weakening the state-population relationship on which effective governance is based.

The result of all these factors is that, although the private sector is initially warmly welcomed, over time, people grow disappointed by the level and slowness by which they observe a difference in their own lives that can be attributed to the corporate presence. Many that expected some kind of a "peace dividend" grow disillusioned as neither the government nor the private sector is providing the better life they had hoped for.

#### **So where does that leave the role for the private sector?**

Do these experiences mean that companies have no role in state building at all? The answer is a qualified and limited no. In fact, there are ways in which companies can contribute to the processes through which governments may become more robust and peaceful. The activities of corporations in situations where governance is weak can either reinforce the weaknesses or, alternatively, can contribute to processes that strengthen it.

The starting point is recognition that companies are not development agencies. They are neither particularly well situated nor even interested in developing the stability of governments per se. For a company to be involved in "state building activities," there needs to be a reason for the business to be involved, either short or long term, directly or indirectly. Company managers need to be able to defend their decisions to support a government to their superiors, as well as to outsiders critical of such an approach. For example, many companies shy away from efforts to support state capacity in certain countries as they fear that some NGOs misinterpret their intentions and, instead, accuse the company of bolstering an undemocratic and illegitimate government. (Myanmar/Burma example)

So what options do companies have on a day to day basis to help develop policies that ensure greater government accountability and responsiveness?

*Provide an incentive to Governments to be more accountable to its citizens*

Some companies make their investment conditional on certain government policies being in place. In discussions with the Colombian government, one oil company stated it wanted to see the government

sign up to the Voluntary Principles on Security and Human Rights. To the company, such an effort would provide them with more confidence that their risk capital would be less at risk.

Another company signed a Production Sharing Agreement with the Government of Sudan that made the startup of company operations conditional on the Peace Agreement being “signed, effective and sustainable.” Again, to the company the business case for this approach was to avoid being pressured by the government to start certain activities the company would feel uneasy with given the political situation in the country. On the other side, it is a good example where companies can send an encouraging signal to a government to further state building activities.

Obviously, companies have most leverage to pose these conditions prior to their investment, when governments are eager to attract foreign investment and the company has not yet made a financial commitment to a country.

#### *Use the comparative expertise to support government activities*

Companies do not only produce, market, service or extract. They also have the expertise and knowledge to plan, program, manage, and organize. In some countries, oil companies have offered the government assistance in their efforts to conduct scenario planning with regard to HIV/AIDS trends or predicting migration patterns. In other places, companies have seconded their own staff to the government to train civil servants in topics such as landownership, cadastral surveys, urban planning and other topics. These are important objectives to the company, the state and local communities but for which the state simply lacked the resources. (Angola, Papua New Guinea)

#### *Strengthen and involve, rather than ignore and substitute for, the government.*

Examples in this regard are:

- Using a tri-partite partnership approach when implementing social investment projects (Colombia, Ghana)
- Support the existing parts of the government that do function but lack the resources to be more effective (EITI office, Human Rights Ombudsman etc.).
- Supporting local civil servants, who are often equally frustrated with their lack of resources, as local communities are (Niger Delta example)
- Use the political leverage of a company to lobby for increased government presences (e.g. House of Justice model - Colombia)

#### *As a company, provide a governance model that serves as a benchmark for civil society in their engagement with the government*

Although this option sounds simplistic, local communities often express the hope that the way a company operates is “different” from their experiences in dealing with authorities. The way a company operates can serve in many ways as a model that civil society groups use in their discussions with government officials. Fair and respectful treatment of workers, intolerance of corruption, objective resolution of grievances, transparent decision making, are all often taken for granted in the business sector, and appreciated by communities, yet rarely reflected in how the government approaches its own “clients”; its constituency.

As civil society groups often have no model they can refer to and that they find acceptable, especially when a country has had a turbulent past, the corporate governance model can be inspirational. In one country, local NGOs and local communities explicitly states over and over that they warmly welcomed companies, but only if “it makes a point of behaving in a different way than our government behaves.” (Mauritania, Bangladesh examples)

#### *Support civil society groups*

Providing transparency to civil society about the revenues that the company helps generate will lead to little change on the ground as long as civil society does not have the capacity, or the ability, to effectively hold a government more accountable in how it spends these revenues. Making revenue figures transparent is the easy part (in most cases), ensuring that this transparency leads to increased accountability is a more challenging task.

This does not mean that the company has to become involved in politics.

- It can use its convening capacity or provide its premises (which can be scarce in some contexts) for civil society groups to have discussions with each other. (Colombia example)
- It can invite or encourage NGOs with a transparency mandate to the area of operation to provide workshops or training. (Ghana)
- It can inquire with the government how it spent the revenues generated by the company.

Then there are a number of options that we need to explore, as the evidence suggests there might be effective ways to increase government accountability and responsiveness.

- I. What are the options for companies to ensure the revenues they help generate are earmarked for activities that we have consistently seen as increasing state legitimacy such as the provision of health care, education etc. We have some examples of companies that made Tax Credit arrangements with governments so that the company provided these services themselves. But if there are ways to include such guarantees into contractual arrangements with a government, this would, of course, be preferable. (Papua New Guinea example)
- II. How appropriate is it, when and in what manner, to engage with state security providers. Some companies are very hesitant, others feel they have no option. We have seen that supplying weapons to such providers is typically a bad idea, whereas we have seen that providing ideas that set rules and a humanitarian framework may actually provide a more constructive, and peaceful working environment. In Papua New Guinea, one mine created an environment with lower than average crime rates and people felt that the police forces (trained by the company) were much more responsive to community requests to provide law and order.
- III. What are the opportunities for collective action? We know that one company is often not powerful enough to address problematic government policies or approaches. But what if a number of companies sat together and developed a strategy to address policies that undermine their own legitimacy and credibility? (Sudan example)

These are some ideas that we have been asked to explore further and I would ask you to help us think through the opportunities that may present themselves.

## **Role for donors**

The above-mentioned examples provide multiple entry points for donors to support private sector initiatives. The issue is that these opportunities are often overlooked.

Colleagues working in the Trade or Foreign Affairs Departments of donor countries periodically ask us: "If my minister asks me for one idea that he or she could put forward at an international policy arena, for example the G-8, what would that idea be?" Then when we reply with some ideas, conditionality comes in: "Well, we need to be able to achieve it within four years because we do not know who the next government will be. It also needs to be visible so that we get some credit. It also cannot be too controversial, otherwise it may backfire politically. And...by the way, we need to be able to explain the idea to the public in one sentence." In other words, donors are looking for a second EITI initiative. However, if there were that many good ideas that can be achieved in the short term and aroused no controversy, they would have been implemented already. Unfortunately, lacking any "big picture" ideas they can put their name on, many donors revert to feeling that there is not much they can do.

In reality, donors can make a substantial difference on the ground if they would take a more context-specific approach. Although we have not yet directed worked with donors over a sustained period of time on this issue, following are some opportunities that we have identified, but that still need to be tested.

- Provide training to companies about best practices and effective stakeholder engagement approaches, including dealing with government officials.
- Use the convening power of Embassies to meet with companies from various sectors of industry to address issues that are interesting both from a business perspective as well as from a state building perspective (the collective action initiative).
- Provide a venue for civil society groups that otherwise cannot meet to discuss issues that are sensitive such as state corruption or state violence
- In particular, include national business leaders in this process. In each country, there are many committed business leaders that are willing to lend their support to a credible effort, and the keyword here is credible, that will bring peace and stability in an area. The issue is that these leaders will stay out of the spotlight if they are not brought into this process, simply because of the personal and reputational risks they take being associated with initiatives that may fail
- Develop programs that make it attractive for the diaspora to return home and to reverse the brain drain so typical for fragile states. This could include incentives for starting new business ventures.
- Offer lessons learned from own experiences. For example, the Canadian Government has many experiences to share and lessons learned to offer with regard to corporate activities in land owned by indigenous peoples, mining laws, direct revenue sharing mechanisms etc. These experiences could be useful to other countries.

These are some ideas that need to be explored further but could be appropriate entry points to work with a broader range of stakeholders on state building efforts.

### **Concluding Words:**

State building is essentially about politics, not economics. Corporate activities can support, or undermine the process of state building but, by themselves not ensure state stability. Still, opportunities exist for donors as well as for the governments of fragile states to become more strategic and creative in using the private sector to help increase the level of accountability and responsiveness of governments towards their citizens. However, they need a compelling “business case.” It is our challenge to develop options that make that case.

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