The Investment Climate in Post Conflict Situations

Private Sector Development & Peacebuilding

Berlin, September 14 2006

Rob Mills, World Bank Institute
Overview

- Scope of conflict’s impact on the investment climate
  - Policy areas & broader ‘enabling environment’
- Outcome: pervasive informality
- Benefits of investment climate reforms captured too slowly?
- Policy trade-offs & roles for development partners
The impact of conflict on the investment climate is comprehensive...

Security & Stability
- Physical security
- Macroeconomic stability
- Contract enforcement / judicial redress
- Land & property rights

Finance & Infrastructure
- Access to credit & financial services
- Access to utilities (power, water)
- Infrastructure (telecoms, transport)

Workers & Labour Markets
- Supply of skilled labour
- Ease of hire and fire

Regulatory Framework & Taxation
- Red tape (permits, licenses, registration)
- Customs
- Tax policy / rates
- Tax administration

...the policy response has to be equally broad
The broader enabling environment is also affected by conflict...

**Security & Stability**
- Physical security
- Macroeconomic stability
- Contract enforcement / judicial redress
- Land & property rights

**Finance & Infrastructure**
- Access to credit & financial services
- Access to utilities (power, water)
- Infrastructure (telecoms, transport)

**Workers & Labour Markets**
- Supply of skilled labour
- Ease of hire and fire

**Regulatory Framework & Taxation**
- Red tape (permits, licenses, registration)
- Customs
- Tax policy / rates
- Tax administration

**‘Enabling Environment’**
- Institutions
- Governance
- Political Economy
- Capacity
- Social Capital

...these are critical issues, but hard to handle
The post-conflict environment is characterised by informality

**Informal business environment**
- Increased risk & vulnerability for participants
  - Greater reliance on social networks
  - Customer base more localized & less diverse
  - Fewer economies of scale
- New generation of entrepreneurs operating outside formal sector

**Informal regulatory framework**
- Not a ‘benign free-for-all’
  - Existing rules in place, but enforcement predatory or arbitrary
  - New ‘unofficial’ regulatory framework
- Unaccountable
- Prone to rent-seeking
- Potentially highly restrictive
Improving the investment climate can help cement the peace following conflict ...

<table>
<thead>
<tr>
<th>Employment</th>
<th>Delivery of Services</th>
<th>Building Social Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>● Private sector best source of sustainable jobs</td>
<td>● Government capacity limited</td>
<td>● Business transactions bridge divides</td>
</tr>
<tr>
<td>● Job-holders have stake in the peace</td>
<td>● Small-scale delivery possible</td>
<td>– Socio-economic</td>
</tr>
<tr>
<td></td>
<td>● Rapid &amp; responsive</td>
<td>– Rural-urban</td>
</tr>
<tr>
<td></td>
<td></td>
<td>– Borders</td>
</tr>
</tbody>
</table>

Addresses both ‘greed’ and ‘grievance’ factors
... but the investment climate has not been prioritised by development partners

PSD Focus in WBG Financial Operations

Rwanda (1994)

Timor Leste (1999)

Sierra Leone (1999)

Afghanistan (2001)

Haiti (2004)
Investment climate reforms can involve tough trade-offs...

<table>
<thead>
<tr>
<th>Reform...</th>
<th>...or Restore?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Innovative reforms to</td>
<td>Rapidly restore the regulatory framework to boost confidence</td>
</tr>
<tr>
<td>the regulatory framework</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Formal...</th>
<th>...or Informal?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Push firms into formal</td>
<td>Encourage employment through tolerating informality</td>
</tr>
<tr>
<td>sector</td>
<td></td>
</tr>
<tr>
<td>– More competitive</td>
<td></td>
</tr>
<tr>
<td>markets</td>
<td></td>
</tr>
<tr>
<td>– Bigger economies of</td>
<td></td>
</tr>
<tr>
<td>scale</td>
<td></td>
</tr>
<tr>
<td>– Bigger tax take</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Tax Revenues...</th>
<th>...or Incentives?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Levy business taxes for</td>
<td>Minimize the tax burden to encourage firms into the formal sector</td>
</tr>
<tr>
<td>reconstruction and</td>
<td></td>
</tr>
<tr>
<td>public service provision</td>
<td></td>
</tr>
</tbody>
</table>

...but quick wins can boost business confidence
Successful investment climate reform requires a high level of country ownership...

Challenges...

- Wide-ranging reforms
- Vested interests

... & Approaches

- Building capacity
- Improving dialogue & partnership

Different roles for DPs

...but development partners have an important role
Conclusions

● Peace vs. PSD?
● A strong investment climate favours legitimate business activity
  – Enforcement capacity
  – Creates a level playing field for MSMEs
The Investment Climate in Post Conflict Situations

Private Sector Development and Peacebuilding

Berlin, September 14  2006

Rob Mills, World Bank Institute