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Helpdesk Research Report

Private sector engagement in fragile and conflict-affected settings

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Question

Review literature on the role of private sector engagement in supporting efforts to address fragility and conflict and review lessons learned from the approaches to private sector engagement in fragile states by different donors

Contents

1. Overview

This rapid review reviews literature on the role of private sector engagement in supporting efforts to address fragility and conflict. There is broad consensus that creating economic opportunities is critical to addressing fragility and conflict and that economic recovery is a vital aspect of state-building in fragile states. The private sector and private sector development (PSD) are considered to have a crucial role to play in contributing to economic recovery and addressing a number of drivers of fragility.

Whilst PSD is considered to have an important role to play in the field of economic development, there is much debate over what constitutes 'best practice' in PSD and what the term private sector encompasses. The private sector[1] can include local formal, informal and illegal actors, diaspora communities and regional and multinational players (Peschka, 2010). This review adopts DFATs definition of private sector

[1] DFAT use the term 'private sector' to refer to all commercial enterprises (businesses) and includes individual farmers and street traders, small and medium enterprises, large locally-owned firms and multinational corporations.

engagement which is characterised as a tool to achieve better development outcomes in private sector development and human development.

There is also no commonly agreed definition of the terms 'fragile states' and 'fragility'. Most development agencies define fragility as "a fundamental failure of the state to perform functions necessary to meet citizens' basic needs" (Kaplin, 2015; Mcloughlin, 2012: 9; OECD, 2008).

Key findings include:

- Fragile and conflict-affected settings pose challenges for engaging with the private sector. Significant internal and external imbalances are present, including large fiscal and trade deficits and debt arrears.
- Despite these challenges, private sector activity continues, changing shape and direction. Given this resilience, the private sector can be a powerful vehicle for reconstruction and regeneration. The private sector can play a role in several areas including:
  - supporting stabilisation;
  - spurring long-term economic growth;
  - improving transparency;
  - fostering trade;
- The local private sector is considered to have a range of motivations for wanting to address fragility and conflict, and when engaged appropriately, deliver a number of benefits including:
  - the local private sector are more interested in making a difference in peacebuilding and stabilisation efforts than large enterprises as they suffer much more from conflict;
  - they tend to be more labour-intensive than large firms, depend less on imports and maintain more linkages with other local enterprises;
  - they are more likely to have sub-national urban centres as their base, providing a stimulus for regional development.
  - Individually they represent less economic power and are easier to deal with for national and local governments;
  - as the local private sector operates less internationally, they are more likely to invest and expand locally.
- Support from international financial institutions, bilateral donors and other actors can make a significant contribution to the private sector, by ensuring ongoing access to finance, imports, and exports. These efforts work best if they are coupled with reforms to re-establish or strengthen transparency, trust, effectiveness, and legitimacy in the government institutions, which provide the framework within which the private sector operates.
- Research suggests that a balanced strategy combining emergency employment, income generating activities (including private sector development) and the creation of an enabling environment through legal and regulatory reforms, is necessary to support more durable economic growth and to enhance the private sector's impact.

Despite broad consensus that the private sector has a role to play in preventing and resolving conflict and addressing fragility, there is mixed evidence on how best to engage with the private sector and to facilitate PSD. This review draws on literature produced by donors, academics and think tanks.

The literature considered in this review was largely gender-blind.

2. Role of private sector engagement in efforts to address fragility and conflict

There is broad consensus that creating economic opportunities is critical to addressing fragility and conflict and that economic recovery is a vital aspect of state-building (Mcloughlin, 2012). The private sector and private sector development (PSD)[2] are considered to have a role to play in contributing to economic recovery and addressing a number of drivers of fragility and conflict including: unemployment, exclusion and instability (Haider, 2014; Hameed and Mixon, 2013; Mac Sweeney, 2008; WDR, 2011).

According to the World Development Report (2005: 1), private firms (farmers and micro-entrepreneurs, local manufacturing companies and multinational enterprises) are central to the development process, providing over 90% of jobs, creating opportunities for people to apply their talents and improve their situations. They are also the main source of tax revenues, contributing to public funding for health, education and other services (WDR, 2005). They are therefore considered to have a key role to play in both preventing conflict and in supporting efforts to address fragility and conflict. A strong and resilient private sector is most likely to emerge in countries characterised by: an open trade regime; an attractive investment climate; fair, efficient and contestable markets; and where the private sector can access financial services, appropriate skills, technology and connectivity through good infrastructure and IT.

Fragile and conflict-affected settings pose challenges for engaging with the private sector. In fragile states many of the market characteristics, listed above, are absent and significant internal and external imbalances are present; large fiscal and trade deficits and debt arrears. Addressing these macroeconomic imbalances is considered a first priority in economic recovery strategies. DFID (2008) identifies the following market issues associated with fragile states:

- Thin or missing markets often dominated by powerful interests;
- Poor market infrastructure;
- Limited basic services;
- Suspicion of the private sector;
- Rent-seeking and risks of expropriation deter investment;
- Weak government with questionable legitimacy.

Despite these systemic challenges, private sector activity continues in such contexts. Mac Sweeney (2008), notes that the private sector remains resilient to systemic shocks, changing shape and direction. Given this resilience, the private sector is considered by Mac Sweeney (2008), to be a powerful and adaptable vehicle for reconstruction and regeneration (Mac Sweeney, 2008). The literature acknowledges that the predominant form of private sector economic activity and employment, in fragile states, is likely to be informal (i.e. operating outside of formal rules), complicating efforts at private sector engagement (Mcloughlin 2012). De Vries and Specker (2009) identify two types of private sector actors in fragile states:

- large enterprises (often multinationals), which deal in goods (such as telecommunications or beer) or rely on quick gains in high-stake, semi-official goods like mineral resources. Such investors have the resources and the (political) impact to deal with corrupt government influences;

[2] PSD aims to achieve an accessible market system, which encourages broad-based and inclusive economic growth (Mac Sweeney, 2008).

- small local businesses run by families or individuals including the informal sector, roughly defined as the total of unregulated entrepreneurs who operate outside of a judicial framework and pay no taxes. A critical question for policy makers is how to formalise these kinds of enterprises.

Findings of the working group on PSD in fragile, conflict-affected and violent states, hosted by the Center for Strategic and International Studies (CSIS), concluded that economic growth and integration into the international economy is essential to bolstering the stability of fragile and conflict-affected states. The private sector can play a role in several areas including (Hameed and Mixon, 2013: 2):

- providing early stabilisation;
- spurring long-term economic growth;
- improving transparency;
- fostering trade;

Engaging the private sector during conflict

In a WDR background paper, Peschka (2010) notes that the private sector exists in conflict situations and has the potential to both exacerbate or ameliorate conflict. During conflict the private sector continues to operate, however, distortions occur, with a focus on short-term, often illicit, gains, with the private sector characterised by a fusion of actors (such as warlords or military officers who become businessmen). Other distortions result from the destruction of physical infrastructure and the flight of local human and financial capital. Mac Sweeney (2008) comments that the private sector, during conflict or in fragile settings, comes to be defined by informality, lacking regulation or standardised systems of procedure.

Ballentine and Haufler (2009) discussing public policy for conflict-sensitive business, highlight that private sector companies are not neutral during conflict. Companies can have unintended negative effects on conflicts by altering the distribution of economic benefits, upsetting existing cultural and societal relations and/or generating negative externalities, such as environmental pollution (Ballentine and Haufler, 2009: 10). Companies and aid agencies therefore need to be cognisant of these effects when developing policies and strategies.

The impact of conflict, violence, and fragility is seen to have an impact on the formal private sector. Peschka (2010) notes that foreign and local investors are likely to leave the country, taking with them longer-term capital, skills, jobs, and technology and undermining local private sector support institutions. Those private sector actors who stay face difficulty in accessing finance, are often harassed or co-opted by corrupt governments and armed forces, and find it hard to import goods or export products.

Engaging the private sector in peace-building, relief and reconstruction

The World Development Report (WDR, 2011) comments that while short-term recovery from violence can be supported by external assistance or natural resource revenues; the path to longer-term development is dependent on a healthy private sector. The WDR (2011) suggests that the private sector can play a role in supporting the state's peacebuilding efforts, strengthen the state's legitimacy through registering and paying taxes and providing services to the public sector. Through the private sector's provision of essential services, a weak government in a fragile or conflict-affected context can strengthen its social contract and build credibility with its citizens (OECD, 2008).

The WDR (2011) comments that engaging with private sector actors enables a better understanding of how to alleviate bottlenecks to activity which helps restore confidence, signalling to entrepreneurs a more business-friendly environment generating economic revival and encouraging broader reform.

Discussing post-conflict peacebuilding, Mac Sweeney (2008) highlights that local private sector actors are an important stakeholder in any conflict and post-conflict situation. It is suggested that businesses can make strong strategic partners in peacebuilding and stabilisation efforts, participating in peace negotiations to prevent conflict, and engaging indirectly to influence the negotiations. She concludes that donors can engage with local private sector actors through business associations and microfinance initiatives. Specker (2009: 3) identifies four benefits of engaging with the local private sector:

- they are usually more interested in making a difference in peacebuilding than large enterprises as they suffer much more from conflict;
- they tend to be more labour-intensive than large firms, depend less on imports and maintain more linkages with other local enterprises;
- they are more likely to have sub-national urban centres as their base, providing a stimulus for regional development (as large firms tend to be clustered in the capital cities).
- Individually they represent less economic power and are easier to deal with for national and local governments;
- as the local private sector operate less internationally, they are more likely to invest and expand locally. Support for the local private sector can be in the form of financial subsidies, provided that their proposed business activities conform to market trends.

In the aftermath of conflict, the private sector's role can extend beyond providing jobs and generating income. The private sector can lift the burden on government and lend legitimacy to the state by providing essential services (Peschka, 2010; Mcloughlin, 2012). Similarly, the private sector can deliver tangible dividends to the wider population through investments that create jobs but also provide essential services, introduce innovative approaches to development, and generate tax revenues for reconstruction efforts (WDR, 2005). The WDR (2005) notes that to help the private sector meet these challenges, build peace and secure development, it is important to understand more clearly the interrelationships it can have with politics, security, institutions and development.

The private sector can also help address key security issues in fragile and conflict-affected countries through the provision of jobs to unemployed youths and former combatants, either related to national disarmament, demobilisation and resettlement (DDR) initiatives or over the course of a normal business trajectory (Banfield et al, 2006). As Gerson (2001: 103) asserts, "conflict settlement requires the injection of optimism and hope born of employment and economic opportunity. Otherwise, fragile peace arrangements can rarely be sustained. And, over the long term, only the private sector is capable of growing new enterprises, opening investment opportunities, and providing employment and enduring economic security".

Case evidence gathered for the Red Cross from literature on business and peacebuilding demonstrates that business can address drivers of armed violence by building bridges between communities, state and society; providing good offices and information; acting as a pro-peace constituency; strengthening local economies; and limiting access to conflict financing (Wennmann, 2012: 929).

Bray (2009) argues that development actors and government policy-makers need to include private sector actors in their context analyses to ascertain how they may influence the context. Bray (2009) concludes that it is essential that development actors focus on the development of an equitable regulatory environment for the private sector at an early stage of economic recovery to ensure that they are engaged in the peace process and play a role in consolidating peace. Engaging with private sector actors to understand the challenges they face can be particularly helpful here.

3. Lessons learned from donor approaches to private sector engagement

Peschka (2010) comments that private sector engagement and development in fragile and conflict-affected countries requires special policies and instruments to rectify distortions caused by conflict. She posits that a legal private sector is essential to development and peace, providing livelihoods and growth, while paying taxes so governments can provide services to their citizens. PSD has become a central component of efforts to re-establish, engage and support a legal private sector.

Whilst PSD is considered to have an important role to play in the field of post-conflict economic development, there is much debate over what constitutes 'best practice' in PSD. Mac Sweeney (2008) outlines the debate between two dominant PSD schools of thought:

- **The systemic approach** encourages indirect support to the private sector through improving the investment climate. Factors include the macro-economic environment, the rule of law, business regulations and the fiscal regime.
- **The interventionist approach** encourages direct intervention to generate change in the way that markets function. Activities include: promoting market linkages, value chains, business associations and community groups; providing access to employment, vocational training and microfinance; and targeted support.

Proponents of the systemic approach argue that donors should not be involved in 'picking winners', while interventionists argue that a lack of political will often means policy-level changes have little impact on the ground. Despite these differences, there is a high degree of overlap between these two approaches.

Mac Sweeney (2008) suggests that programming should take into account the common characteristics of the conflict and post-conflict situations, as well as the nature of the private sector. However, programming should also be shaped by the specific nature of each individual context. It is agreed that conflict-sensitivity, and the use of conflict assessments[3], are crucial when engaging with the private sector designing PSD interventions (Gündüz et al, 2006). USAID (2012), comment that engaging the private sector and economic associations in conflict management is an important area to consider. Concluding that the private sector and economic associations have a number of unique qualities that have not been sufficiently harnessed for the purposes of conflict management, principally their interest in stability can often bring more pressure to bear on local and national government officials to adopt constructive policies than traditional peacebuilding NGOs, and in areas where other civil society groups are divided along ethnic lines, economic associations are often multi-ethnic.

Mac Sweeney (2008) highlights that the lack of private investment during and after conflict requires reform that promotes the return of capital. The physical rebuilding required in post-conflict countries creates opportunities for local and international investors. Pro-private sector development reforms need to ensure, when possible, opportunities are awarded to the local private sector and that investment reforms allow the local private sector to learn from, grow, and compete with foreign investors.

Peschka (2010) emphasises short-term measures that contribute to peace and to politically important confidence-building in private sector investments, such as:

- creating jobs, with a particular focus on demobilised military and paramilitary forces;
- harnessing immediate business opportunities related to relief and reconstruction (for example, procurement from the local private sector);

[3] See for example; USAID (2012); World Bank (2005) for examples of conflict analysis

- building key skills needed throughout the relief to development continuum;
- facilitating access to finance (e.g. microfinance, remittances);
- building or strengthening government and community institutions and processes.

Long-term economic reform and PSD in post-conflict countries must focus on rebuilding the tax base, employment, and productive legal sectors of the country, this is particularly the case in countries where institutions such as the civil service are absent or constrained (Collier, 2007).

Engaging the private sector in efforts to streamline government can enable a focus on more efficient, effective, and transparent regulations and a smaller, smarter, and directed administration that targets provision of critical services and oversight. Such reforms help overcome the problem of a civil service with limited capacities and results in a stronger business enabling environment (Peschka, 2010).

Longer-term private sector development reforms need to focus on strengthening alternative livelihoods and creating conditions in which informal or illegal markets transform into the legitimate private sector activities. Possible interventions include concentrating more resources on microfinance, rural reforms, and improving land registries and enabling the registration of legitimate businesses (ILO, 2007).

Within this environment, donors need to address a number of key issues if they are to effectively support private sector engagement and development. These include (DFID, 2008: 21):

- Making the best use of an emerging common interest in sustainable development between private companies and development agencies;
- Attracting more private sector participation in both the financing and provision of key development-related services such as infrastructure and some health services;
- Ensuring that the rapidly evolving and integrating global trade and financial systems work for the benefit of people and companies in developing countries;
- Tailoring PSD programmes to the very different contexts and circumstances of partner countries.
- Increasing the PSD performance of international agencies;
- Engaging with new and emerging donors such as China who are making significant trade-related PSD investments in Africa or the vertical funds;
- Improving knowledge management.

When the international community tries to resolve conflict, there often is little direct emphasis on strengthening and diversifying legitimate private sector activity. Support from international financial institutions, bilateral donors and other actors can make a significant contribution at this stage, by ensuring ongoing access to finance, imports, and exports. However, these efforts make sense only if they are coupled with a concerted international effort to re-establish or strengthen transparency, trust, effectiveness, and legitimacy in the government institutions, which provide the overall framework within which the private sector operates.

While DFID and the IFC advocate starting PSD early, the UN places it later in a process of longer-term recovery efforts. However, UNDP (2008) recommends initiating reforms as early as possible, including; prioritising governance and security reforms; empowering local entrepreneurs; and promoting foreign investment.

In the process of promoting regulatory reform, it is important for donors to engage with the local private sector. Not only does this make the reform process more efficient in achieving the desired results, but it also opens up channels of communication between the government and the private sector, and paves the way for a continuing relationship between the two.

Ensuring appropriately designed interventions

Peschka (2010) comments that early support and engagement with the private sector must keep in mind the primacy of local actors, the need for sensitivity, and the importance of having a longer-term and case-by-case view. International organisations and donors should place emphasis on empowering local players to develop a better business-enabling environment. Local businesspeople are considered to be good partners in peacebuilding having a strong interest in ending the conflict, and are often willing to engage in community dialogue and partnerships to champion reforms in the broader community interest.

The UN (2008) advocates three core aspects of approaches to conflict-affected environments, involving:

- being aware of the history of the political and social environment;
- identifying potential points of tension and hostility;
- conducting intervention activities in a way which is sensitive to these.

Reforming the business environment in fragile states

According to Channell (2010) important longer-term reforms must focus on economic recovery and build stability by improving the operating environment for the private sector. Reforms include improved investment laws, clear property rights, land registries, business-friendly taxation, anti-corruption institutions and processes, transparency, and access to finance programmes. It is also important to expand access to services such as electricity and water, judicial reform (particularly of commercial courts and land disputes), small and medium business promotion, rural development, and regional trade.

Business environment reform seeks to reduce the costs and risks that restrict investment and the development of markets in order to increase economic growth, reduce poverty and improve socio-economic welfare (Channell 2010). It addresses the policy, legal, institutional, regulatory and cultural framework within which individuals and firms operate (Channell 2010).

There is a growing body of literature that argues that improvements to an investment climate lead to economic growth. Reform requires identifying and addressing aspects of the business environment that harm commercial activity by reducing trade, compromising property rights, and undermining trust, private sector engagement allows the gathering of such information (Channell 2010).

The 2002 'Bulldozer Initiative' launched by the UN in Bosnia and Herzegovina, with support of the EC, OHR, IMF, USAID, and the World Bank provides one such example. It aimed to address impractical or defunct business regulations, stimulating greater private sector activity. The scheme engaged local business, publicising the project through a travelling roadshow and advertising the scheme through the use of the mass media (Herzberg, 2007).

Market development

According to Gerstle and Meissner (2010: 2), market development is “a sub-field of enterprise and private sector development, in which development programmes seek to help small enterprises participate in, and benefit more from, the existing and potential markets in which they do business”. It represents an interventionist approach, aimed at identifying leverage points within market systems, addressing problems in the way markets function, and the resulting power imbalances (Gerstle and Meissner, 2010). Addressing these issues is considered to have the potential to facilitate reconstruction efforts to reduce poverty, as well as to leverage the private sector to work with households to achieve sustainable livelihoods. As market links are especially likely to suffer during a conflict due to the erosion of trust between groups, improving these links is also considered to benefit peacebuilding and economic development (Mac Sweeney 2008). This may further support the transition from markets dominated by illegal activity, to legitimate market connections (WDR, 2011).

SEEP (2007) comment that market development programmes are based on understanding market trends and the constraints that small enterprises face in engaging in the market more profitably, and identifying what small enterprises need to continue to adapt, and even grow, when the programme concludes and as markets change. Through engagement with private sector actors, they identify four core aspects of successful market development programmes:

- understanding and addressing the role of current key market actors;
- increasing sustainability by promoting commercial relationships;
- working with many lightly rather than few intensively;
- identifying opportunities for leverage and scale.

Mac Sweeney (2008) argues that supporting market development in conflict countries, with clearly targetable beneficiaries can lead to rapid, highly visible, peace dividends. A further benefit is that market development is adaptable to fragile and conflict-affected contexts as it does not rely on government institutions to function effectively. Donors can support market linkages by connecting actors with each other, for example, by circulating information about markets to allow actors to adjust their activities to market trends (Mac Sweeney 2008).

One such intervention is value chain programming which has the objective of enabling poor individuals and households to move out of low-return activities and into higher-return, growing markets by linking poor producers to private sector actors who have access to growing markets and an interest in forming partnerships (Parker 2008). A particular focus of market development initiatives is to add value to products and processes used by various participants within the chain to support the entire group of actors to compete successfully in profitable markets (Parker 2008).

The SEEP Network (2007) documents the experiences and innovations of 13 market development operating in crisis environments. It argues that, where interventions incorporate a clear understanding of the market and its context, they are able to smooth the transition from relief to development, and also to improve the performance of relief programmes.

One such market development initiative is the USAID-funded programme, From Behind the Veil, implemented by the Mennonite Economic Development Associates (MEDA) and the Enterprise and Career Development Institute (ECDI). The programme helps homebound rural women in Pakistan reach lucrative markets through a “woman-to woman” network. The strategy of creating and working with women sales agents was devised to enable isolated women to have in-depth interactions with knowledgeable market traders. Through capacity development of women intermediaries, the program upgrades designs, improves quality, connects producers to quality inputs, and forges market linkages. The activities are geared towards sustainability and the creation of dynamic value chains through (Miehlbradt and McVay, 2006):

- strengthening self-perpetuating networks of sales agents who recruit and train additional agents;
- stimulating support markets, such as those for embroidery patterns and designs;
- building the capacity of sales agents to manage and train producers to meet market demand;
- supporting new lead firms, such as urban-based buying houses that link rural and urban traders.

Sequencing private sector development-related reforms

As noted, the provision of incomes, employment, and access to services are considered central to the prevention of conflict and delivery of peace dividends. The IFC (2009), commenting on investment climate reforms efforts in conflict affected countries, suggest that earlier than conventional prioritisation of private sector development-related reforms can make a difference and deliver multiple dividends. Peschka (2010) suggests that an early donor focus on the following reforms can have particular benefits.

- Reforms of government institutions that regulate the business environment can inculcate transparency, honesty, professionalism, and restore government legitimacy.
- Encouraging investment by eliminating unnecessary regulatory risks generates a wide range of benefits such as additional jobs, provision of a greater range of goods and services, innovation, and reduced prices. It can also encourage businesses to migrate from the informal to the formal sector, improving further compliance with regulations, generating additional tax revenues, and reducing potential for corruption.
- Successful investments in a post-conflict environment increase business confidence, thus generating further investment, creating a self-sustaining cycle of new private sector investment and activity. They also can enhance confidence in regulatory institutions and processes, resulting in greater legitimacy, confidence and trust.

Global and regional models adapted for local realities

Peschka (2010) comments that the donor community has relied heavily on established models. These reflect the priorities of donors and multilaterals and a belief in their universal relevance. She continues that post-conflict governments often have little choice but to adopt these measures and to initiate reforms targeting certain common benchmarks (like the Doing Business scores). One explanation for this reliance is the lack of local capacity and the inability to tailor reforms for local realities. Imposing reforms from outside may be ineffective, or dangerous in situations where peace is fragile and various groups within the country are competing for resources.

The donor community has increasingly focused on developing or adapting solutions to local conditions (see for example GTZ, 2009). This focus involves broader stakeholder consultations and engagement, and acknowledges the challenges of weakened or absent institutions. The GTZ guidelines advocate analysing relevant actors within the local setting (peace and conflict analysis) and evaluating the risks to ministry officials and others who are acting on their behalf in implementing reform programmes.

4. Interventions to enhance the private sector’s impact

Research suggests that a balanced strategy combining emergency employment, income generating activities (including private sector development) and the creation of an enabling environment through legal and regulatory reforms, is necessary to support more durable economic growth and to enhance the private sectors impact (De Vries and Specker, 2009).

Businesses operating in fragile states face numerous obstacles. The World Bank Group’s Enterprise Surveys quantify these constraints to business operations highlighting that the number one environment constraint faced by firms working in conflict areas is lack of access to electricity. The second biggest challenge is obtaining access to finance. Other major issues cited include political instability, informal sector practices, and corruption.

Harnessing immediate business opportunities

Relief and reconstruction efforts entail the arrival of international militaries, bilateral and multilateral development agencies, and NGOs. As basic security is restored, there is a rapid rise in economic activity, in the form of procurement by the various institutions, spending by their international staff and spending by their local staff.

Peschka (2010) suggests that even though local businesses may not initially have the requisite skills to take advantage of these early opportunities, such operations typically last some years. So, there is time to build local capacity to meet the needs of the international presence on the ground. Sectors, such as agribusiness and construction are particularly important following any conflict and could form the basis for concentrated, local development.

For post-conflict countries with low wages and high unemployment and under-employment, comparative studies have demonstrated certain advantages of the employment-intensive approach, such as increased local employment through the building and maintaining of infrastructure, as well as associated skills development. Employment intensive investment also can assist in the process of self-sustaining development, distribution and reinvestment of wealth in local regions (UN, 2009).

Understanding the needs of both the international community and the local private sector provides one means of allowing different actors to be more purposeful in the structuring of their approaches, which can yield not only immediate benefits in the form of income opportunities for the local population but also longer term opportunities in skills development and encourage the launch of new businesses.

Facilitating access to finance

Successful financial sector initiatives in post-conflict countries address shortcomings in basic financial sector regulation and infrastructure including; central bank supervision capacity, reform of banking regulations, restoration of inter-bank payments and clearing mechanisms, introduction of ATMs and other technology etc. Such initiatives involve development partner assistance for governments and central banks (Maimbo and Ratha, 2005).

Stabilisation of money markets is critical for controlling inflationary trends and giving further confidence to investors. Mobile banking or the extension of banking services over mobile phone networks, shows significant promise in further expanding access to low-income borrowers in the challenging settings of fragile states (Maimbo and Ratha, 2005).

5. Risks for private sector development

Conflict, post-conflict and fragile situations present a unique set of challenges to both the private sector and donor community. Problems such as low state capacity and damaged infrastructure are features common to many fragile or crisis environments.

According to the World Bank's Doing Business database, fragile states represent the world's most challenging business environments, often with the most bureaucratic hurdles and the fewest property protections for entrepreneurs. The Doing Business indicators reveal that fragile states, on average, rank below 140 out of 189 economies for ease of doing business. Among the bottom economies in the Doing Business rankings, the majority are fragile states (World Bank, 2016).

Some challenges to private sector activity in fragile settings are well known, e.g. excessive business regulation and poor energy supply. However, unpredictable government behaviour and high transaction costs may (in conjunction with low skills levels) post the most significant challenge.

Poor roads, social divisions, petty corruption, weak contract enforcement, and the insecurity of property make it too costly and risky for producers to reach customers, especially customers in distant cities and countries. This dramatically shrinks market sizes, especially for small-to-medium-sized enterprises and micro businesses that provide most employment in these environments (Kaplan, 2015).

Obstacles

Obstacles to maximising the potential impact of the private sector in fragile and conflict-affected settings relate primarily to a lack of recognition that the private sector has a role and limited understanding of what this role might be (Killick et al. 2005). According to Killick et al. (2005), overcoming these obstacles requires:

- raising awareness of the private sector, among local and international peacebuilding organisations.
- identifying the different roles the private sector can play, depending on the size and nature of the business community.

The 2011 World Development Report echoes this, emphasising the need to focus on developing local capacity – both within the private sector itself and within the government administration that oversees private sector development-related regulations and reforms.

Hameed and Nixon (2013) identify five obstacles relevant to successful engagement with the private sector in private sector development:

- Statist attitudes with citizens reliant on the public rather than private sector to be the main participant in economic activities, while the governments in turn are reluctant to release their hold on lucrative state-owned industries.
- Corruption is widespread and persistent in fragile states. This imposes high transaction costs on the private sector that may be unwilling to tolerate this level of risk.
- Insecure environments encourage donors to tailor programmes for maximum short-term impact which can prove counter-productive. Preventing the emergence of reliable institutions and transparent governance that provide predictability for investors.
- Fragile states experience market-access difficulties due to lack of infrastructure, lack of finance, and counterproductive regulation in potential export markets.
    - Conflict destroys infrastructure, raising the cost of producing and transporting goods in those countries.
    - Securing finance is difficult because fragile countries lack predictable laws and institutions have unreliable banking systems.
    - Low levels of higher education mean that fewer individuals are trained on small business lending procedures, limiting the number of personnel that a private-sector company can interact with.
    - Fragile states are often shut out of trade because of protectionist laws and regulations among their potential trade partners.
- A local economy that lacks diversity, negatively affects the environment for private-sector operations.

Challenges are daunting and challenge rapid reform. Social change and development are slow processes, especially in countries starting at a low level of institutional development. Attempts at sudden and rapid change can create new winners and losers and thereby generate new conflicts or exacerbate existing ones.

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Key websites

- The Donor Committee for Enterprise Development: http://www.enterprise-development.org/

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