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WAR-TORN COUNTRIES, NATURAL RESOURCES, MNERGING POWER INVESTORS AND THE UN DEVELOPMENT SYSTEM

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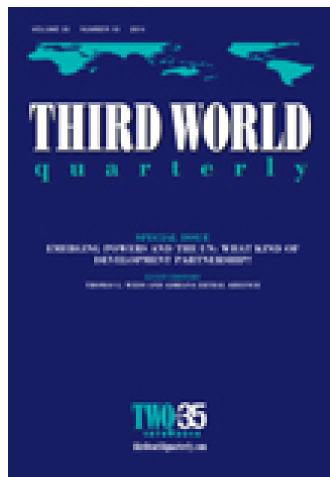

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War-torn countries, natural resources, emerging-power investors and the UN development system

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The unsustainable aid dependency of war-torn countries – most of which are rich in natural resources – makes it imperative to start gradually replacing aid with foreign direct investment (FDI) and exports. This article identifies ways in which stakeholders – governments, the international community, including the UN development system, foreign investors, and local communities – could work together in a 'win-win' situation. Most crucial is avoiding conflict-insensitive policies that fuel discord by putting governments and foreign companies, often from emerging markets, in direct confrontation with local communities. The control of natural resources is often a root cause of conflict, and the latter's exploitation can become a major challenge as wars end. The peculiarities of war-torn countries are discussed along with the specific impediments to attracting FDI into the exploitation of natural resources. An effective and fair legal framework is necessary to ensure that investors do not operate as 'enclaves', creating new conflicts.

Keywords: domestic savings; aid dependency; foreign direct investment; peace building; war-torn countries

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Countries at low levels of development coming out of civil war or other chaos – following peace agreements or military intervention – find it particularly difficult to foster domestic savings or attract foreign direct investment (FDI) in the short run. This is true despite the fact that many of these countries have large endowments of natural resources that are much sought after by investors worldwide. At the same time the so-called peace dividend with which countries often experiment after wars is negligible in countries where military expenditure was largely foreign-financed. In fiscal terms this means that, as the need for military expenditure drops, there is little room for diverting domestic resources to non-military purposes.

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Thus, war-torn countries rely primarily on official aid flows – from both bilateral and multilateral donors, including the United Nations development system (UNDS) – to finance their humanitarian needs as well as their basic operational and development expenditures. Financing is unquestionably a critical ingredient of, and constraint on, economic reconstruction – or the economics of peace – in these countries.

The economics of peace is an intermediate phase between the economics of war and the economics of development. During this phase the main objective should be that the country does not relapse into conflict. Because there cannot be sustained development without peace, the political (or peace) objective should always prevail over the economic (or development) one. For this reason best policies from a purely economic or financial point of view are not always possible or even desirable during this phase. This is what makes economic reconstruction so different from development as usual. Because control of natural resources was often the root cause of the conflict, the exploitation of such resources during this phase is particularly challenging and requires conflict-sensitive policies.[1]

As is well documented in the literature, aid to war-torn countries – which often accounts for a large percentage of these countries' GDP – has been mostly ineffective in helping them to stand on their own feet. In fact, it has often led to serious aid dependency. While 'humanitarian aid' to save lives and provide minimum levels of consumption given largely by foreigners – the UNDS, international NGOs, and bilateral donors – starts in the very early stages of the reconstruction process and has been rather effective, it does not wither soon enough to avoid the price distortions and the work disincentives associated with this type of aid.[2]

At the same time the provision – mostly by the UNDS and bilateral donors – of 'reconstruction aid' is often delayed pending elections, the establishment of institutions and policies, and improved governance, security, and human capacity that would make such aid more effective. In the meantime countries often revert to war. In fact, war-torn countries have shown roughly a 50% chance of relapsing into conflict. Moreover, those that succeed in maintaining the fragile peace often find themselves in an aid trap.[3]

Indeed, reconstruction aid has been largely ineffective in supporting the reactivation of agriculture, legitimate business activities, and other job-creating investment in basic services and infrastructure for the large majority of the population. While domestic and foreign elites often thrive in post-conflict situations, war-torn countries that fail to create a level-playing field for farmers and small entrepreneurs ignore the productive capacity and creativity of a large part of the population. To involve these much-neglected groups – including women – in productive and licit activities is critical to peacebuilding. Unless growth in these countries creates employment and contributes to food security and poverty alleviation, it can become a new source of conflict, often exacerbating existing political, ethnic, regional, and even community divisions.

Because spikes of aid to countries embarking on the transition to peace are often short-lived, war-torn countries have the difficult challenge of replacing aid with FDI and exports as sources of finance and foreign exchange. This task is indeed quite difficult in countries affected by insecurity and where parts of their

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territory may even be outside government control. Such countries often have undeveloped institutional and legal frameworks; weak financial sectors and an unfriendly business climate; weak infrastructure and services; and poor governance, all of which add to the problem.

Moreover, by failing to provide basic services and security, governments are unable to gain political legitimacy in the eyes of the population. At the same time governments have little ownership of domestic policies, which are mostly imposed by donors through conditionality or simply because donors often finance development projects outside the national budget and in projects that may lack governments' blessing. In turn, lacking legitimacy and ownership of domestic policies, national governments find it more difficult to negotiate with foreign investors.

The challenge of economic reconstruction is indeed overwhelming: to create the basis for a just, viable, and sustainable economy in the long run, under the serious constraints of reactivating the economy while maintaining a fragile peace, political stability, and security in the short run. Although short-term jobs are often created, a dynamic and sustainable reactivation of the economy, which is critical to establishing peace, stability, and prosperity has been thoroughly lacking in most war-torn countries.

Investment and job creation may sound like normal development challenges, but in the context of war-torn countries these tasks are fundamentally different, because the latter requires conflict-sensitive policies – even if not optimal from a purely economic or financial viewpoint. The main objective of economic reconstruction in the short run is to address the grievances of crisis-affected groups that have been the root cause of the conflict. It is important to ensure that these groups get an immediate dividend in the form of employment opportunities in the licit economy and better living conditions if peace is to be long lasting.

Looking at the global economy today, two things are clear. First, donor countries have not yet recovered from the aftermath of the 2008–09 global financial crisis and they continue to be affected by fiscal challenges and high unemployment. Together with increased reluctance on the part of taxpayers to fund aid in faraway countries that has led to corruption and waste – as donors' own oversight bodies and the international press have well documented – this situation has affected, and will continue to affect, donors' aid and other support to war-torn countries. Many of the highly aid-dependent countries will find it difficult to sustain such dependency, while those embarking on the transition to peace will find it more difficult to get support.[4]

Second, the rapid growth of emerging markets has led them to a wild search for commodities worldwide, including in high-risk, war-torn countries and, until recently, in marginal and unexploited areas such as the Amazon, populated by indigenous groups that have so far lived in isolation. In both locations investments have been an increasing source of conflict with national and local governments and with displaced or otherwise affected communities.[5]

However, emerging countries whose economies grew rapidly in the 2000s and have become the engine of global growth since the global financial crisis have experienced significantly decelerated rates of growth, which is having an impact on the price of commodities (both as a result of decreased demand and

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high inventories). This situation may reduce companies' appetite to invest in natural resources in war-torn countries or may affect the terms of their investments, making them less attractive and more challenging to host countries.

The process of economic reconstruction – involving national governments and local communities as well as their foreign supporters – has proven to be mostly fragmented, chaotic, and wasteful, and has often-required large expenses in terms of peacekeeping operations or military forces to keep the peace. Hence there is a need for stakeholders to find ways to work together in the design and implementation of a simple, well-thought out, and integrated strategy for the reconstruction of war-torn countries that can result in a 'win-win' situation for all involved.[6]

Many war-torn countries have great potential for the exploitation of natural resources that could help them come out of their aid dependency and set the basis for independence. In most of them, however, FDI in natural resources – both in minerals and agricultural plantations – and government policies to support them have been the source of new conflicts with the displaced communities whose lives and livelihoods are affected. Perhaps Liberia provides the best example of this problem, but there are lessons also from Mozambique, Afghanistan and places such as the Niger Delta, where investors and communities find themselves in a 'no-win' confrontation as a result of conflict-insensitive policies on the part of both the government and investors.

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Old and new issues relating to natural resource exploitation

The control of natural resources has often been the root cause of war – and a serious impediment to peace. Diamonds, for example, were the main source of conflict in Angola, the Democratic Republic of the Congo (DRC), and Sierra Leone; oil was the disputed commodity in Sudan. Indeed, the plunder of natural resources has been a major source of conflict in Africa. Access to natural resources and the concomitant gain in political and economic power is one of the main targets of 'spoilers', who often act violently against peace initiatives. One of the government's challenges in such situations is to ensure that those who benefited from the spoils of war have a stake in the economics of peace so that they will not oppose it.[7]

Other well-documented issues relate to the so-called resource curse, which results because many countries that are rich in national resources mismanage them to such an extent that they derive little economic benefit, not least because of the corruption and instability that their exploitation and trade facilitates. Although corruption in that environment is often rampant, some initiatives have been adopted to control it – and particularly to ensure that corruption does not fund violence.[8]

An area, however, in which research is still incipient relates to the way in which war-torn countries can get out of their aid dependency by effectively promoting FDI in the development, exploitation, and trading of natural resources. This presents a number of challenges. Perhaps the most pressing is the need to establish the right legal and regulatory framework to ensure that natural resources contribute to dynamic, equitable, and sustainable growth rather than to the infamous resource curse. Here the UN development partners can and should provide critical support to war-torn countries.

Donors in war-torn countries normally have an incentive to help these countries develop their natural resources. Such development would not only reduce their need to provide aid but also would increase supply and lower the price of natural resources, something that would normally benefit donors. Moreover, once production and exports increase, their import capacity would also grow, making them a larger market for foreign exports.

A remarkable feature of the past decade is that foreign investors are more diverse than in the past. With the rapid growth of emerging countries, there has been an increasing interest – notably from companies in China, Brazil, India and, to a lesser degree, Indonesia and Malaysia – in exploiting natural resources, even in countries plagued by insecurity, lack of infrastructure, and great uncertainty with respect to legal and regulatory issues. Despite data problems, it is clear that companies from these countries invest abroad under different modalities and with different levels of support from their own governments.[9]

Brazilian companies ventured abroad well before those from China and India. The stock of FDI abroad jumped from $50 billion in 2000 to $230 billion in 2012. Brazilian companies often operate from tax havens, which makes analysis difficult. Brazilian investment abroad is strong not only in mining and energy but also in food production. Although there are no institutionalised policy measures to support global investment by Brazilian firms, the Brazilian Development Bank has a 'Foreign Direct Investment' line of credit to stimulate investment by Brazilian firms abroad, offering preferential interest rates and covering the construction of new installations abroad, equipment purchases, mergers and acquisitions, turnover capital and export support. Brazilian companies have been active investors in Mozambique and Angola, the two largest Portuguese-speaking countries in Africa. The construction company Odebrecht, for example, is among Angola's largest employers, and the steel producer Vale has invested billions in coal mining in Mozambique.

By 2012 China's stock of FDI abroad surpassed $500 billion, as compared to about $5 billion in 1990 and about $30 billion in 2000. While Brazil's stock of $40 billion was eight times larger than China's in 1990, Brazil has now fallen behind. The 2011 Five-Year Plan reaffirmed China's 'going global' policy, and a large part of this is directed to developing countries. Mining, quarrying, and petroleum accounted for about half its new investments, and most of the top green-field investments in 2010 were in energy and raw materials. Some of China's largest global players are involved in war-torn countries, including several oil companies such as China National Petroleum Corporation (CNPC) and China National Offshore Oil Corporation (CNOOC), as well as major construction and railway companies. CNPC, for example, operates in Afghanistan and Sudan, CNOOC operates in Nigeria and Iraq, and the China State Construction Engineering Corporation also operates in Nigeria. China has also been a very active investor in natural resources in Latin America; war-torn countries should learn about this experience, which will help them negotiate with the Chinese.

Since 2000, when restrictions on Indian companies investing abroad were greatly relaxed, their investments have increased rapidly, with the stock of FDI abroad reaching $120 billion in 2012. While manufacturing accounted for the bulk of the investments in the first half of the 2000s, the second half shows a concentration in metals, energy, and natural resource investments. India's Oil

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and Natural Gas Corporation (ONGC) has invested in Iraq. Sudan was among the 10 largest recipients of Indian investment in 2002–09. Indian firms have explored agricultural and resource investments overseas because they face increasing resistance in India to large-scale projects involving displacement and environmental disruption.

FDI from emerging markets – often carried out by state-owned enterprises – raises a number of issues. Are these investors different from the more traditional ones and, if so, which ones are preferable, and why? Can investors from emerging markets bring technologies, know-how, and other expertise more easily adjustable to local conditions and to local inputs? Can these investors' cultural background and corporate practices be better for war-torn countries at low levels of development? Do their background and practices allow them to have better relations with local workers and supply providers? Are these investors more or less likely to create local jobs and adopt more conflict-sensitive policies? How do these investors behave in comparison with those from Western countries that have their own checks and balances at home with regard to their operations worldwide? How do they compare in terms of complying with national legislation and local practices in general, and with respect to transparency and corruption in particular?

It is perhaps too early to answer many of these questions, since much more research is necessary before we can draw definite conclusions. All of them, however, are important in terms of designing an appropriate legal and regulatory framework to ensure maximum impact, and also in terms of finding the appropriate monitoring system to ensure that the negative impacts of FDI in a war-torn country can be minimised.

What is clear, however, is that investments from companies located in emerging markets, particularly in China, will be packaged differently from those from Western countries. The latter's involvement in war-torn countries has been multifaceted: governments in donor countries provide economic aid and technical assistance. Part of the aid goes to building the physical and human infrastructure necessary for natural resource production and trade. At the same time these countries' military forces may be involved in providing security, either separately, or as part of North Atlantic Treaty Organization (NATO) or UN peacekeeping operations. Finally, private investors from these countries – over which the government has no direct control and, in fact, has restrictions in supporting – independently bid for natural resources.

The involvement of emerging market countries in war-torn ones is often quite different. China provides perhaps the most striking contrast to Western countries' involvement. It is neither a major financial supporter nor a contributor of military personnel, although there have been recent increases in resources and police. Furthermore, investors are often state-owned enterprises and, even if 'private-sector' companies are set up for specific purposes (such as building urban and rural roads in Liberia), they are clearly controlled and supported by the government. Some may even receive long-term financing from their government or development banks at preferential terms.

Although China is not a major donor, state-owned companies have flexibility to offer aid as part of their bidding. Moreover, China is willing to provide aid and concessional loans, which are not attached to economic conditionality,

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like that imposed by other donors and creditors, particularly the IMF and World Bank; nor are their aid and loans attached to conditionality with respect to human rights. The case of Angola is illustrative. As C. Alden describes it:

> The state-owned Indian oil company, ONGC 'thought it had secured a deal with Shell to assume the lease for Angola's block 18', but a last-minute decision by Angola's state-run oil company, Sonangol, gave the rights to China's Sinopec. Crucial to the turnaround was the Chinese government's willingness to provide a $2 billion loan to the Angolan government.[10]

This example also illustrates how even other emerging markets' companies find it difficult to compete with Chinese firms, given the different packages that the latter are willing to provide.

A big difference between Western and Chinese companies relates to oversight and accountability. Both Western and Japanese firms have some degree of accountability to their shareholders and boards, are expected to demonstrate a degree of corporate responsibility, and need to make public their labour and environmental practices. They can also be sanctioned by the Foreign Corrupt Practices Act in the USA or by similar legislation elsewhere.[11] US companies in particular often find it difficult to compete with companies from other countries that have more flexibility to bribe local authorities to obtain economic concessions, a rather common practice in war-torn countries.

There is perhaps no better example of how Western and Chinese companies use different packages than the bidding for the Aynak untapped copper mine in Afghanistan in 2007.[12] Western countries and Japan were providing huge amounts of aid and technical assistance to the country, and NATO and US forces were providing security, but the bid from Western companies was significantly lower than that of the Metallurgical Corporation of China's (MCC) $3 billion bid for the mine itself. MCC also committed billions to infrastructure development to bring the copper to the market by rail to Pakistani ports.

The Aynak mine illustrates the difficulty for Western companies of competing with Chinese companies in particular, which count with direct support from their government and put all the aid and investment that they are willing to provide in the same package. It also suggests the danger to war-torn countries of getting less efficient, accountable, and conflict-sensitive investors because they do not compete on a level playing field. Western and Japanese aid, as well as NATO military assistance, continued in Afghanistan, despite the government allocation of the mining rights to a Chinese company. But what will happen after NATO combat troops withdraw? Had US companies been involved in this and other large investments in minerals and hydrocarbons in the country, would that have a different impact on foreign aid in the future?

Erica Downs argues that the Chinese ability to put in the same package investment and infrastructure is consistent with a broader shift in the mining industry away from enclave private sector development and towards leveraging mineral development to benefit the broader economy.[13] Indeed, if one develops a copper mine in landlocked Afghanistan, or coal deposits in Tete Province in Mozambique, or iron ore in Liberia, which are far from the coast, it is necessary to worry about how to bring the product to markets. The issue to be investigated from the Aynak and similar investments, however, is whether linking

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infrastructure to a concrete project is a better and more cost-effective way of building the necessary infrastructure. It may well be. The fragmented approach that the international community – including the UNDS – has followed in these countries is often to build a road here, a bridge there, and an airport elsewhere, without linking infrastructure directly to the specific production and trade needs.

An oft-heard concern relates to Chinese firms' lack of transparency in the way they operate in a country, which extends to the way that they interact with local governments and communities. For example, in an attempt to bring transparency to a process vulnerable to corruption, and amid a bruising political battle over mining legislation in Afghanistan in 2012, the minister of mines, Wahidullah Shahrani, disclosed about 200 contracts for marble, coal, and other mines dating back to 2002. He reported, however, that he had requested the Chinese to make their Aynak contract public, but that the Chinese had legally negotiated a 'non-publication' agreement with the previous minister.[14]

Although more research is necessary before drawing definitive lessons for the effective exploitation of war-torn countries' resources, there is anecdotal evidence about specific conflict-insensitive policies of companies from emerging markets. This is particularly true of Chinese firms that follow the practice of bringing in labour from China rather than employing local workers, of disregarding labour and environmental codes, of using aid to outbid competitor firms in large projects often involving a large bribe to governments, and of being opaque in terms of the nature of their investments and companies. Not surprisingly, these practices often lead to conflict with the local communities. Joshua Kurlantzick, for example, notes:

> Chinese aid through infrastructure development and business projects lacks transparency. In Cambodia local activists accuse both the Cambodian government and Wuzhishan LS, a Chinese state-owned (plantation) firm, of forcing hundreds of villagers (in a northeastern province) off their land, repossessing the property, and then spraying the area, which includes ancestral burial grounds, with dangerous herbicides. Peter Leuprecht, the UN special representative for human rights in Cambodia, said in a statement, 'The government and the company have disregarded the well-being, culture, and livelihoods of the…indigenous people who make up more than half the population of the province'.[15]

Attracting FDI for natural resources in war-torn countries

War-torn countries rich in untapped natural resources face a number of challenges in exploiting them. First, while these countries cannot exploit their own resources because of a lack of technical capacity and financial resources, opening the sectors to global companies may create a dilemma for policymakers similar to the one that countries face with regard to privatisation. Countries may give large incentives to global companies to invest early in the transition from war, with the intention that this will help in the reactivation of the economy. Alternatively they may also wait until reconstruction has progressed and the economy has reactivated, in an effort to obtain a better deal from private investors. In many cases, however, countries will not be able to muddle through until the second alternative becomes feasible, and thus they are forced to part with their resource assets at bargain prices.

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In the DRC, for example, in exchange for investment to upgrade the capacity of the country's diamond production, the government had to agree to future commodity-supply contracts, and at prices well-below market prices and for many years to come. The UN and others have denounced these contracts as unfair. However, only risk-prone investors would put down cash early in the peace transition. This is because of the high probability that the country will relapse into conflict or that future governments may reverse former contracts. To invest under such risky conditions, investors obviously expect a commensurate return.[16] Eventually, however, many governments have had to renegotiate resource contracts with private investors entered into by previous governments, just as countries in the normal process of development in Latin America and elsewhere have also done.

Second, infrastructure linked to richly endowed resources is often at risk of attacks. Thus, the provision of security for such infrastructure is important and often expensive. In 2005 Iraq's oil ministry suffered losses of more than $6 billion from about 200 attacks by armed groups on various oil installations throughout the country.[17]

Third, countries that rely heavily on exports of one or two commodities are vulnerable to Dutch disease – that is, they are likely to have appreciating real exchange rates that distort the price of non-tradable goods and services and undermine export competitiveness. In war-torn countries pressure for a real appreciation of the domestic currency early in the transition also stems from large inflows of aid and other financial resources. In countries such as Afghanistan and Liberia, however, a large part of the aid has been spent abroad (through imports), and Dutch disease has not been a problem. Since real appreciation may become a serious problem to a country's export competitiveness, this could be an issue of policy concern as commodities exports increase.

Fourth, economies that are heavily dependent on production and exports of one or two commodities are also highly vulnerable to changes in international demand and prices. Thus, a 'resource fund' (or stabilisation fund) for these commodities may be the most effective way for the government, which accumulates funds during booms and draws on them during recessions, to attenuate the impact of pro-cyclical fiscal policies. It is best practice to save for a rainy day but, in post-conflict transitions, it pours every day and what is best practice under normal development may be a wasted opportunity during a post-conflict transition.

An issue that requires fuller debate is whether resource-related income should be saved for the benefit of future generations in a fund giving a financial return, or whether it should be invested in human and physical infrastructure to improve the country's future productive capacity and the welfare of the population at the same time. The latter – if effectively and transparently invested – would probably have a higher rate of return than the former. Moreover, investment in infrastructure, by creating productive employment, will probably minimise the high chance that a country in transition to peace will revert to war. This is an area where the UNDS could play a critical role in supporting governments to ensure that resource proceeds are effectively and productively utilised.

Adopting in 2004 a best-practice resource fund modelled after the one created in Norway – a developed country with one of the highest incomes per

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capita and aging populations – did not serve East Timor well. It had a largely illiterate population and collapsing infrastructure, along with one of the fastest population growth rates and lowest per capita incomes in the world. Utilising those funds productively in the country's reconstruction could have served future generations well and at the same time may have avoided the country's relapse into conflict as well as the need for a new peacekeeping operation in 2006.

Adequate legal framework for natural resource exploitation

Perhaps one of the greatest challenges for war-torn countries is establishing the appropriate legal and regulatory framework, often from scratch, to allow them to attract foreign investment for natural resources, including hydrocarbons, mining, and agricultural sectors. Such a framework needs to reaffirm the fact that resources belong to the state for the benefit of all the people in the country. Thus, there is a need to establish a fair revenue-sharing mechanism among regions and provinces based on population and on the amount of resources that each produces. Despite the difficulties, establishing a fair legal framework for the use of natural resources has proved key in improving the prospects for peace and stability in resource-rich countries, though more often in derailing the prospects for them.

Negotiating such laws and having them ratified by parliaments is often extremely difficult politically. The experience of two war-torn countries – very different in terms of their past performances with regard to natural resources – is illustrative of the problems involved. In Iraq, for example, the oil industry was nationalised in the early 1970s. Twenty years later Russian and Chinese companies signed production-sharing agreements with the Iraqi government. In exchange these companies turned about 10% of their profits over to the government. In 2007 the Iraqi cabinet approved an oil bill that was highly unpopular among the Iraqi people. Over 60% of the population believed that oil should be developed and produced by Iraqi state-owned companies rather than by foreign investors.

The law was drafted with support from BearingPoint, a Washington consultancy firm that has major contracts with the US government in Kosovo, Afghanistan, and Iraq. The Iraqi population largely perceived the law as designed 'for the benefit of US oil companies'.[18] Luring contracts for economic reconstruction and investments in the oil sector was not far from the minds of those planning the US occupation. Iraqis reacted negatively to what they saw as an American effort to disempower them by giving contracts to as many as 5,000 foreign contractors, who would take over their oil wealth.[19]

This partly explains why the bill still languishes in parliament. The other major blockage is that the Kurds want to control Kirkuk and the fields around it, which account for about 10% of proven reserves, while the Sunnis live in an oil-poor part of the country, which makes distribution by the Shi'ite government a particularly difficult issue to settle in a way that is agreeable to all.

The Iraqi oil situation illustrates another issue with natural resources in war-torn countries. Indeed, with one of the largest oil reserves in the world, Iraq continues to attract foreign investors and to produce increasing amounts of oil,

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despite the failure to establish the proper legal framework. In the south of the country, where the security situation is calmer, Western oil companies continue to operate under service contracts, and Russia's Lukoil is expected to start soon operating a field considered the world's second-largest untapped oil deposit.[20] It is often the case in resource-rich countries that greed prevails over security and other concerns, particularly when the resources are in areas of relative calm. Although these companies may take advantage of oil opportunities in Iraq, peace and stability in the country will continue to be elusive if there is no framework to allocate revenue equitably.

In Afghanistan extensive geological surveys in the 1950s and 1960s done by Soviet mining experts had identified deposits of copper, iron ore, coal, gold, barite, dolomite, limestone, talc, beryl, lapis lazuli, and emeralds. Natural gas deposits were exploited, and gas was piped to the USSR, which was the main way of servicing Soviet loans, particularly during the Soviet invasion in the 1980s. In 2006 the *Mining Journal* reported additional deposits of lead and zinc, chromite, cobalt, platinum-group metals, uranium, and various gemstones, which have been exploited in the past or could provide opportunities for green-field investments. Based on a 2010 memo from the Pentagon, the *New York Times* reported that the value of Afghanistan's untapped mineral resources could amount to nearly $1 trillion, 'far beyond any previously known reserves and enough to fundamentally alter the Afghan economy and perhaps the Afghan war itself '.[21]

Moreover, Afghanistan also has industrial metals and perhaps one of the world's largest deposits of lithium, used in laptop batteries. Geologists have been exploring the dangerous southern desert in Afghanistan for rare earth elements and suspect that actual quantities may be significantly larger than earlier estimates. These elements are used to manufacture many modern technologies from electric cars to solar panels. Security is a major constraint but, if it were to improve, experts believe that 'Afghanistan could provide an alternative source of rare earth elements for industrial countries concerned with the fact that China currently controls 97% of the world's supply'.[22]

Despite the great potential, little foreign investment has materialised so far, notwithstanding the tremendous publicity over bidding by Chinese and Indian companies for the Aynak copper mines in 2007 and the Hajigak iron-ore deposits in 2011. Investors' greed over two of the world's largest mines prevailed over their security, infrastructure, and other business-climate concerns. But, despite these projects' reported billion-dollar price tags and high expectations about related investments in infrastructure, the investments have shown little progress. While the development of the Aynak mine has been delayed by the discovery of Buddhist treasures that are being rescued by a team of French archaeologists, and despite investors' desire to renegotiate the contract, Hajigak investors are still waiting for the revised mining law that was approved by the cabinet and sent to parliament for approval in 2013.

The lack of an adequate mining and hydrocarbon law, and a series of other impediments typical of war-torn countries, led to a fall in FDI in Afghanistan starting in 2006. A sharply deteriorating security situation, a continued lack of electricity and adequate infrastructure, a shortage of skilled labour, inefficient bureaucratic procedures, and the need to renew companies' licences annually were major factors impeding foreign investment. Land grabs, chronic corruption,

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impunity, the inability to enforce contracts, and the fragmentation and ineffectiveness of aid deterred foreign and domestic investment further. As a result, FDI collapsed to less than 0.5% of GDP annually in 2011–12, from over 4% in 2005. The difficulties in translating interest into investment in natural resources is illustrated by IMF revenue projections from mining amounting to only 2% of GDP by 2025.[23]

In addition to facilitating FDI and ensuring that there is a fair distribution of government revenue from those resources, the legal and regulatory framework for concessions for the exploitation of natural resources should ensure that they do not operate as 'enclaves' and that the country as a whole benefits from the links they create to the domestic economy. In particular, the framework should ensure that there is fair treatment of local communities affected by the concessions.

As an example, concessions in Liberia renegotiated or signed since the 2005 elections differ in the way that they address the corporate responsibilities of foreign investors with regard to workers in the concessions, as well as to indigenous peoples displaced by them. It is important to distinguish between what the concessions contemplate for the displaced and affected groups from what these groups actually get.[24]

Many of the concession contracts include investors' commitment to create clinics, schools, roads, and other infrastructure within the concessions for their workers. They do not, however, require the provision of such services to those groups displaced by the concessions. Some contracts include the creation of financial funds to support displaced populations and may also contain some vague language with regard to compensation for their lost livelihoods. The lack of specificity in this regard has become a source of contention, because companies have often offered to pay for a crop rather than compensating for the sustained loss of livelihoods. Most of the concessions are likely to create environmental problems and are often a threat to the local biodiversity and ecosystems. Although concessionaires are responsible for environmental studies, the real impact is not always monitored and standards are not enforced because of lack of expertise and of the financial means to do it at the local level.

Thus, in addition to the displacement and loss of livelihoods for affected communities, and to the environmental and biodiversity costs associated with many concessions, these often create risks to human security beyond the economic and environmental. This is because of the lack of consultation with local communities about the projects involved and about compensation for the lost livelihoods and other social impacts that affect them dearly. The road can easily lead back to armed conflict.[25]

At the same time, the legal and regulatory framework for natural resource development should include specific requirements for foreign investors detailing that, as a quid pro quo for the preferences granted in terms of land or any tax or tariff exemptions, the government expects foreign investors to pay local workers fair wages and benefits; to establish basic security, human rights and other adequate working conditions; and to achieve minimum levels of investment and/or local employment. The government also expects foreign investments to set up links between their export activities and the local economy by using competitive local inputs and services and increasing other local

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procurement; to contribute to *in situ* training of local workers and transfer of technology and managerial capacity; to train local workers (in the country and abroad) in administrative and managerial jobs so that they can assume more responsible and higher-paid jobs in the concessions; to establish agreements with local technical schools and universities to create specialised courses, internship programmes, and other arrangements to promote transfers of technology and capacity building of the local labour force; and to exercise corporate responsibility in social and environmental areas (ie create local parks, schools, clinics, and other such projects).

International experts will have to be involved in drafting the legal and regulatory framework for the concessions, and the local governments will need to develop capabilities to monitor and enforce it. The latter will be difficult because of the complexity of the contracts and the limited capacity of national and local governments in war-torn countries. Both in drafting the legal framework and its monitoring, the UNDS could play an important and constructive role so that these countries can move away from enclave production. The latter not only limits the impact of FDI on the domestic economy but has also proven to be a source of conflict with the communities.

Conclusion

The problems with economic reconstruction of war-torn countries have been extensively analysed. They often grow fast (albeit from a low base) as a result of large volumes of aid and of the presence of the international community, including foreign troops or large UN peacekeeping operations. This leads to large and unsustainable growth in construction and services. At the same time the rural sector, which provides for the lives and livelihoods of the great majority of people, is neglected. This has clearly been the case in Liberia and Afghanistan.

War-torn countries may also grow fast because of 'enclave-type' production and export of natural resources, including hydrocarbons, mining, and agricultural products. Iraq and Angola are good examples and so is Liberia, where the IMF has estimated that roughly half the rapid growth of recent years is related to this type of activity, mostly in mining, rubber, and palm oil.

Concessions to foreign investors for the exploitation of natural resources, together with ineffective aid policies, have led to 'growth without development', a term coined by Robert Clower in connection with Liberia, where growth benefits mostly foreign investors and domestic elites and increasingly becomes a threat to human security. Enclaves are generally a source of labour exploitation and often displace indigenous communities and endanger their livelihoods, as well as destroying forests and wildlife.[26]

Perhaps Siakor and Knight best articulated the threat to human security in Liberia, when they wrote in a *New York Times* article in 2012 that 'unbeknown to many outside Liberia, Mrs. Johnson Sirleaf's government may now be sowing the seeds of future conflict by handing over huge tracts of land to foreign investors and dispossessing rural Liberians'.[27]

While governments are willing to give large extensions of land to foreign investors, donors – including the UNDS – are willing to finance a large part of the infrastructure that these investors need to exploit natural resources. Yet there

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has been very little interest on the part of donors or investors to finance the infrastructure needs of small farmers and other micro-entrepreneurs, particularly in the communities that have a claim on those resources.

It is thus that the promise of natural resource development for many communities remains just a promise, in part because of overall insecurity in the country that discourages FDI, but in part because of problems with the communities that place the investors and the communities in a 'no-win' confrontation.

The case, for example, of the Niger Delta in Nigeria is illustrative because communities sabotage oil pipelines, capture part of the oil, and put oil workers at risk, raising the cost of production and leading to waste and pollution. In his fascinating book *Untapped: The Scramble for Africa's Oil*, John Ghazvinian describes the details relating to the practice of tapping into a pipeline (oil or natural gas), known as 'illegal bunkering', the problems it creates for all concerned (companies, communities, governments), and how, the more profitable this becomes, the more it attracts the involvement of mafias.[28]

Given the importance of natural resources to the peace, development, and prosperity of many war-torn countries, there is a need for a broad-based debate on how foreign investors can assist in the development and trade of natural resources. At the same time means should be found so that investors can create links to the rest of the economy, including to the communities directly affected by them. It is imperative that governments (at the national and local level), together with foreign investors, donors, and local communities, work in a 'win-win' situation to ensure that the gains from such resources are justly distributed and that aid can be gradually allowed to wither. The UNDS does indeed have a crucially important role to play in supporting governments and local communities in such efforts.

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Notes

1. See del Castillo, *Rebuilding War-torn States*.
2. For a detailed discussion, see ibid; del Castillo, *The Economics of Peace*; and del Castillo, *Guilty Party*.
3. del Castillo, *Rebuilding War-torn States*, 30.
4. For a comparison of aid levels, see del Castillo, "Is the UN System up to the Challenge?"
5. The term 'indigenous communities' is used in a broad sense to include not only indigenous peoples but also other farming communities that live near the natural resources and are dependent on them.
6. For proposals on how the different stakeholders might work together in Afghanistan and Liberia, see del Castillo, *Reconstruction Zones;* Castillo*, Aid and Employment Generation*; and Castillo, *Guilty Party*.
7. See Doyle, "Strategy and Transitional Authority," 82.
8. See Humphreys et al., *Escaping the Resource Curse*.

9. UNCTAD data are used for FDI outflows; information about the different modalities in which these companies operate is from the FDI Investment Profiles of the Columbia Center for International Investment.
10. Alden, "China's New Engagement with Africa," 22.
11. Kurlantzick, "China in Southeast Asia," 207.
12. See Gilpin, *Improving High-value Resource Contracting*.
13. Downs, "China Buys into Afghanistan."
14. See Bowley and Rosenberg, "Mining Contract."
15. Kurlantzick, "China in Southeast Asia," 207.
16. See, for example, the three reports of the United Nations Panel of Experts on the Illegal Exploitation of Natural Resources and Other Forms of Wealth in the DRC.
17. Reported by Agence France-Presse in 2005.
18. Janabi, "Row over Iraqi Oil Law."
19. See Baker and Hamilton, *The Iraq Study Group Report*. See also del Castillo, *Rebuilding War-torn States*, chap. 10.
20. Lawler and Mackey, "Iraq Returns."
21. For detailed information and data sources on Afghanistan in this and the following paragraphs, see del Castillo, *Guilty Party*.
22. Posted by *wadsam*, Afghan Business News Portal, April 25, 2013.
23. See also del Castillo, "Leveling the Afghan Playing Field."
24. Lorenzo Cotula points out that the lack of transparency and of checks and balances in contract negotiations creates a breeding ground for corruption and deals that do not maximise the public interest. Cotula, *Land Grab*.
25. For a thorough analysis of concessions in Liberia, two in the mining sector and two in the agricultural sector, and their impact, see Lanier et al., *Smell-No-Taste*.
26. Clower et al., *Growth without Development*. For a detailed analysis and data sources on Liberia's economy and why Clower's term applies to the post-conflict period, see del Castillo, *Aid and Employment Generation*.
27. Siakor and Knight, "A Nobel Laureate's Problem."
28. Ghazvinian, *Untapped*.

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