CHAPTER 4
ECONOMIC FACTORS CAN MAGNIFY FRAGILITY

The evolution of state fragility is not a simple chain of causes and effects or the result of a single factor. It is affected by the interplay and combined outcomes of a range of risks and pressures, cumulative virtuous mechanisms and opportunity windows influencing the functioning and legitimacy of state machinery. Current state institutions derive from historical roots of state formation and their interactions with other conditions, such as geographic characteristics and ethnic and religious population groups.

Their evolution over time, in turn, is linked to exogenous and endogenous economic factors that, by inserting themselves in the institutional setting, can heighten state fragility. That can push state institutions along a downward spiral where their capacities are progressively jeopardised. Or it can strengthen the state by promoting political stability, legitimacy and accountability. Reforms, development policies, external economic shocks and forces – depending on the historical legacy and the commitments of national governments and international institutions – can be a driver of fragility but also a platform to exit fragility.[1]

1. ECONOMIC FACTORS MATTER FOR STATE FRAGILITY – AND FRAGILITY MATTERS FOR THE ECONOMY

The path and level of economic development can affect a country's state fragility, but at the same time result from it.[2] Economic relations differentiate the interests and incentives to cooperate or compete, articulating society in distinct social groups. Moreover, accumulating resources for state-building and for internal social sharing is affected by the pattern of economic development. For instance, many postcolonial states, in an attempt to free themselves from their former colonisers that were buying their products (guaranteeing export markets), implemented inward-looking import-substitution policies, often increasing the role of the state in a highly suboptimal way.

This chapter analyses economic processes that characterise fragile states and are linked to symptoms of state fragility – from weak governance and corruption, to predatory behaviour and conflict. It also explores how these factors can interact to make states more fragile – or create virtuous circles of faster growth and stronger institutions. The aim is to highlight timing and timeconsistency in dealing with the different aspects of fragility. More precisely:

- *Trade openness* interacts with fragility through potential gains from trade that can help countries exit from fragility to resilience, but also through the value of disputed resources, the opportunity costs of contestation and the opportunities for collusion between private agents and public officials.
- *Foreign direct investment (FDI)* can force competition in the local economy by improving efficiency in the allocation of domestic resources and reducing the rents and negative side effects for public governance. In this case, FDI has a positive impact on growth, the extent depending on the sector and on the domestic employment mobilised. Without appropriate incentives and regulation, however, foreign investors can contribute to bad governance and corruption or participate directly or indirectly in the "war economy" and the funding of warlords and civil conflicts.
- *Natural resource wealth* can help state institutions perform their functions, with taxes from resource extraction accounting for most government revenues in fragile states (chapter 2). But fragile states are also likely to fall into vicious circles linking resource management to fading state capabilities – the resource curse. Resource abundance has a positive effect on growth in countries with good institutions, and a negative effect in those with poor institutions.[3] So, because fragile states are characterised by poor institutions, natural resources are more likely to be a curse for them than for other African countries, where natural resources can enhance export-led growth. Intertemporal tradeoffs are very relevant in this situation. Natural resources offer income now, often at the cost of less income in the future. Their efficient management thus requires a long time horizon, not easy for governments that may be illegitimate or risk being overthrown.

1 Fosu 2009.

2 Robinson (2009) argues that Botswana provides an interesting example of the virtual interactions between economic development and state consolidation. In the aftermath of independence in 1996, Botswana had initial conditions similar to those of other Sub-Saharan African countries that followed a less successful and peaceful state formation and economic trajectory. It shared with those countries deep poverty, widespread illiteracy, poor infrastructure, a colonial legacy and multiple ethnic groups. The country was well-endowed with cattle, like Somalia and Sudan, and with diamonds, like Angola and Sierra Leone. According to Robinson, the formation of the modern state – built on "a long process of state and institution formation inherited from the Tswana states" – offers a clue in explaining Botswana's success while at the same time showing the crucial role of state institutions for economic development and the effectiveness of economic policies and paradigms.

3 Mehlum et al. 2006.

- *Drastic changes in access to land and water* has implications for environmental sustainability, food security and power relationships. Closely linked to trade and FDI, these factors can shape social stability, state fragility and economic growth.
- *Food security management* is a core function of government, so fragility has consequences for food security. Perceptions of the state's incapacity or unwillingness to address chronic food insecurity or to protect its citizens from food shocks can undermine the trust in public institutions and thus the legitimacy of government.

2. TRADE OPENNESS CAN INCREASE OR DECREASE STATE FRAGILITY

While state fragility may influence the effectiveness of trade openness on economic outcomes, international trade can produce an impact on fragility. The first effect of trade openness is to change the structure of relative prices of goods and services traded with the rest of the world.

In a context of imperfect governance and law enforcement, trade openness interacts with fragility to produce distributive consequences, fosters economic growth and affects the value of disputed resources, the opportunities for corruption, the opportunity costs of conflict, the choices between productive and predatory activities and the margins for rent-seeking.

In a well-defined institutional setting – where the state ensures security, property rights and contract enforcement – trade openness generally produces global gains. But in weak institutional settings, this is no longer so. And even when there are potential aggregate gains from trade, their distribution may be conflict generating and destabilising, especially when the country's conflict management institutions do not exist or have been dismantled. In addition, the structure of the comparative advantage of the country can affect this dimension. Indeed, the exclusion of some threatening groups from sharing the resources of the state is more likely when the country relies on "point-source" natural resources (fuels, minerals and plantation crops like sugar and cotton) than on manufacturing and diffuse agricultural exports (animals and agricultural produce grown on small family farms, such as rice and wheat).[4] Examples such as the Biafra war in Nigeria in the late 1960s and the civil wars in Angola and in the Democratic Republic of Congo abound. In contrast, when production and benefits are widely distributed across geographical areas, ethnic groups or urban centres, the chances of civil violence seem much reduced.

Openness can also feed back on the vertical relationships between state and society. Trade openness, for example, may interact with the nature of state institutions and the type of redistributive policies chosen by elites. But it may also weaken local economic links between elite groups and other social groups. This, in turn, may produce negative incentives for the elite not to invest in local public goods or to favour inefficient rent-seeking policies.[5]

A number of analyses have investigated the empirical evidence on the links between trade integration and the emergence of domestic conflicts and civil wars. Chauvet et al. (2007) view trade as a motivation of civil wars or as a means to finance rebellion. Indeed, there are forces pushing in opposite directions: some lower the risk of wars, because of the high opportunity costs of conflicts, but some others increase it, because trade provides alternative sources of consumption and income to domestic production, which can be destroyed by the war.

Recent quantitative cross-country studies indicate that open countries are more stable than autarkic ones and less likely to experience civil wars, though important tradeoffs are detected. Martin et al. (2008) find that trade integration may deter wars, if the gains from trade are put at risk during a civil war. But openness may also act as an insurance mechanism and lower the opportunity cost of wars. More precisely, trade openness has contrasting effects on the probability of civil wars: it may deter the most severe ones (those that destroy the largest amount of trade) but may increase the risk of lower scale conflicts.

Focusing on Sub-Saharan Africa, and looking at the effects of trade openness and liberalisation on the outbreak of internal wars in 37 countries for 1980-2000, Bussman et al. (2005) support the view that economic openness has a positive effect on peace and stability, once the restructuring of the economy is over. In the short run, however, trade liberalisation may increase the risk of civil war and conflict during the implementation of the reform measures.

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4 Isham et al. 2005.

5 An example is provided by Segura-Cayuela (2006). When political elites are unwilling to contribute to the provision of public goods and have no state capacity to raise taxes, they generally seek to appropriate resources through price distortions. But the extent of these appropriative policies is limited by the fact that the elites' own business rents may, to some extent, be complementary to what nonelite social groups produce. In such a context, trade openness reduces the opportunity costs of appropriative price policies. Indeed, with trade integration, product prices are likely to be set outside the domestic economy, disconnecting, in a sense, the elites' benefits from the distortions that they impose on the local economy. This, in turn, induces them to manipulate relative domestic prices more intensively to extract rents from nonelites. This reasoning suggests that trade integration may have harmful consequences in countries characterised by low political participation and weak elite responsiveness to the rest of society.

The foregoing discussion suggests policy tradeoffs between the short-term risks of trade reform and long-term gains from openness – and the prevention of severe conflicts and the persistent risks of lower scale tensions. One possible solution to such tradeoffs may be to compensate the immediate losers in order to reduce the short-term risks of political instability and allow enough time for the economy to reach the long-term situation in which enough individuals benefit from the reform.

3. TWO WAY LINKS BETWEEN FOREIGN DIRECT INVESTMENT AND FRAGILITY

While the literature recognises the negative impact of bad domestic governance and corruption on FDI inflows, recent work provides some empirical indications of the reverse effect of FDI on host country governance structures and the ultimate manifestations of state fragility: conflicts and civil wars. Recent research has not provided conclusive empirical evidence on the relationship between FDI and conflicts. Polachek et al. (2005)[6] find that FDI reduces the likelihood of international conflicts, and trade and FDI complement each other in reducing conflicts, while Gissinger and Gleditsch (1999)[7] suggest that in the poorest countries FDI has positive effects on economic welfare, but negative effects on distribution and political unrest. By contrast, Barbieri and Reuveny (2005) find that FDI in the least developed countries reduces the duration of civil wars, but not the likelihood of their onset.[8]

Empirical literature does not provide definitive support to the hypothesis a positive link between FDI and other dimension of state fragility such as corruption. A recent cross-country analysis by Larrain and Tavares (2007) suggests that FDI significantly decreases corruption in the host country, and their results are robust to the inclusion of several determinants of openness in addition to trade intensity and the average tariff, including dependence on natural resources, ethnic fractionalisation and the size of the economy and government expenditure.[9] The relationship between FDI and corruption, however, may depend on the level of development and democracy of the host country. Zhu (2007),[10] for instance, provides empirical support for the view that FDI inflows are likely to reduce corruption in more developed democracies and to increase corruption in less developed nondemocratic countries.

Though not definitive, these results highlight the challenges of FDI policies. First, overcoming state fragility and building strong democratic institutions may be necessary to capture the economic benefits of FDI. Second, while openness to FDI in fragile contexts can reduce the risks of intrastate conflicts, it also needs some form of regulation to promote the quality of investment rather than its quantity. Clearly important for FDI to contribute to the local economy is a legal and accounting framework that encourages transparency and accountability in investors' home countries.

Insights on the nexus between FDI and state fragility can come from a closer look at the main recipients of FDI flows in Sub-Saharan Africa. In only 13 out of 29 Sub-Saharan African fragile countries, the share of FDI inflows on GDP is above the Sub-Saharan African average (itself low, at 3.2%, compared with 4.8% for South East Asia). Most of them are rich in oil and natural resources (Angola, Chad, the Republic of Congo, Equatorial Guinea, Nigeria, São Tomé and Príncipe Sierra Leone and Sudan).[11] So, to understand the impact of FDI on state fragility, it is necessary to first understand the natural resource endowments.

So, while FDI can potentially have a positive impact on growth and poverty reduction, negative externalities prevail when the quality of institutions is low, enhancing the likelihood of conflict and bad management. The resulting vicious circle magnifies the impact of FDI on fragility. To transform this vicious circle into a virtuous one, governments (if legitimate) must commit to a fair distribution of rents by tying their hands. But the low credibility of governments in fragile countries makes a virtuous circle unlikely, unless external agents (such as international organisations) push for and guarantee the commitments.

6 Polachek et al. 2005.
7 Gissinger and Gleditsch 1999.
8 Barbieri and Reuveny 2005.
9 Larrain and Tavares 2007.
10 Zhu 2007.
11 The share of FDI on GDP among these countries ranges from 5% in Angola to 27% in Equatorial Guinea.

4. NATURAL RESOURCE ENDOWMENTS CAN MAKE GOVERNANCE WORSE

Natural resource abundance presents a major opportunity for economic development and state consolidation. A resource-rich state has the funds to build capacity in performing its functions, particularly to finance public expenditure for economic development and poverty reduction. But perverse mechanisms can jeopardise this process: resource dependence can create economic instability, which can turn into political instability. Natural resource abundance may indeed hinder the quality of the governance, a key component of state functioning, and therefore increase the risk of state fragility. But for resource abundance to translate into good overall economic performance and higher standards of living, good governance is perhaps more important than it is in resource-poor economies. This interplay between resource endowment and poor governance can push state fragility along a perverse path.

Natural resources can thus be either a blessing or a curse for resource-rich countries.[12] Empirical studies confirm that point-source resources and resource rents increase corruption and retard economic and institutional development. Because several fragile countries have large endowments of natural resources and low levels of governance, we need to address how abundant natural resources can magnify state fragility (or what can be done to choose the opportunities given by resource endowments and transform the economy into an export-led one).

Developing a natural resource deposit – from prospecting through extraction and revenue management – is connected to the accountability of the government (box 4.1). Resource abundance increases the opportunities to take resources away from an incumbent government (see chapter 2). Rent-seeking can take different forms: from corruption to theft to conflict. Resource rents may indeed lead to the overthrow of the government through insurgency at either a regional or national level. Because changes in commodity prices affect the onset of civil wars, the most recent debate has concentrated on the channels for primary commodities to affect the risk of conflict.[13]

- First, primary commodity exports can finance the escalation and sustainability of rebellion.
- Second, rebellions can be motivated by the desire to capture rents, easier in a lawless context, such as one generated by conflict.
- Third, natural resources may increase the incentives for secession of resource-rich regions.

Resource abundance can also modify the incumbent government's interests and behaviours. Governance can deteriorate in several ways:

- Resource rents can reduce electoral accountability in a democratic system if the government uses some of the money to maintain power through patronage. Vote-buying is a more direct form of divorcing elections from accountability. So, resource rents can undermine the role of elections and make it more desirable for governments to retain power.
- In an autocracy, resource rents can reduce the efficacy of accountability limiting scrutiny, thus reducing the pressure on government to meet citizens' needs.
- Resource rents might alter the likelihood of democracy over autocracy.
- They can also delay fundamental changes to seriously dysfunctional policies.

The fact that resource abundance tends to guarantee rents, especially in fragile states where the rule of law is not fully implemented, can produce an environment in which it is hard to deliver stable economic progress – an environment more vulnerable to social and political unrest. There is ample evidence in the current literature that resource dependence creates economic instability and an inability to develop occupational strategies not strictly related to natural resources.[14]

If the state cannot set the legal framework of exploration and production licences for resource development and extraction, then maldistribution, rent-seeking and inefficiency are likely. Maldistribution comes about because of the spatial distribution of natural resources, rent-seeking because ownership is conferred by physical control of the territory and inefficiency because of the uncertainty about maintaining control. If control is perceived as likely to be temporary, the private incentive is to deplete assets quickly, even if doing so is socially more costly.

12 See the background papers by Collier (2009) and Collier and Venables (2009) for an extensive analysis of this issue.
13 See the background paper by Reynal-Querol (2009).
14 Most literature focuses on the concept of resource dependence and not just availability, which creates a difference of countries that have a more diversified economy and do not depend so strongly on natural resources.

A further consequence is that the absence of property rights, very common in fragile countries, interacts with the lack of information. As with inventions, the incentives to undertaking searches are very low unless discoveries are protected.[15] It is more efficient to wait for others to find natural assets and then take control of them, even if this may involve violence. So, many resources remain undiscovered.

Box 4.1: Codes of conduct and the Natural Resource Charter

International commitments through codes of practice or treaty obligations can be important. Examples are the Extractive Industries Transparency Initiative, the Kimberly process (requiring traded diamonds to be certified as not originating from areas of conflict) and the more recent Natural Resource Charter. The charter is a set of principles for governments and societies on effectively using the opportunities created by natural resources. Its purpose is to assist governments and societies of countries rich in nonrenewable resources to manage those resources in a way that generates economic growth, promotes the welfare of the population and is environmentally sustainable. It also aims to ensure that the opportunities provided by new discoveries and commodity booms are not missed.

What makes the Natural Resource Charter unique is that it is being built through a participatory process guided by academic research.

"The Charter comprises twelve precepts... that encapsulate the choices and suggested strategies that governments might pursue to increase the prospects of sustained economic development from natural resource exploitation:[16]

- The development of natural resources should be designed to secure the maximum benefit for the citizens of the host country.
- Extractive resources are public assets, and decisions about their exploitation should be transparent and subject to informed public oversight.
- Competition is critical for securing value and ensuring integrity.
- Fiscal terms must be robust to changing circumstances and ensure that the country gets full value from its resources.
- National resource companies should be competitive and should not be responsible for regulatory functions or other activities.
- Resource projects may have serious environmental and social effects that must be accounted for and mitigated at all stages of the project cycle.
- Resource revenues should be used primarily to promote sustained inclusive growth through enabling and maintaining high levels of domestic investment.
- Effective use of resource revenues requires building up domestic expenditure gradually and smooth out volatile revenue streams.
- Governments should use resource wealth to increase the efficiency and effectiveness of public spending.
- Governments should invest in a way that enables the private sector to respond to structural changes in the economy.
- The home governments of extractive companies and international capital centres should require and enforce best practices.
- All extractive companies should follow international best practices in contracting, operations and payments".

Several fragile states in Sub-Saharan Africa have adopted the Extractive Industries Transparency Initiative, with the aim of improving governance through the verification and full publication of company payments and government revenues from oil, gas and mining. Oil, gas and mining companies have agreed to support the initiative. Joining is a strong signal of government commitment to transparency.

[15] The problem is analogous to the one analysed in Dixit (1989) for FDI. A recent example is the successful oil explorations in Ghana, which have followed the improvement in property rights.

[16] Taken from: www.naturalresourcecharter.org/index.php/en/the-precepts, accessed on 5 October 2009.

Domestically, it is possible to create commitment mechanisms by entering long-term contracts and building reputation. It may also be possible to design fiscal constitutions under which a share of revenues is put aside for long-term use.

Indeed, Liberia and Niger have approached their aid partners for technical legal assistance on awarding contracts. In Mozambique, analytical work is fostering dialogue on public expenditure management and financial accountability in the context of rising revenues from mineral extraction. Some countries request support in auctioning licences and negotiating contracts with major investors, managing volatile commodity-related revenues and improving the composition and quality of public investments.

5. GOVERNANCE AFFECTS THE RELATIONSHIP BETWEEN LAND AND FRAGILITY

Dramatic changes in land access are usually influenced by government action. The scope is great for land tenure reforms and land policies – land taxation, titling and registration, and regulating land contracts and markets – to reduce poverty, increase agricultural productivity and sustain the environment. But land policies are not neutral, and they can trigger social tensions. African conflicts show that ill-conceived land tenure reforms have been underlying or aggravating factors. Limiting access to land for vast sections of society can result in grievances, frustration, food insecurity and imbalances in political power[17].

In Zimbabwe, land reform begun in 1980 and later the "fast-track resettlement" had heavy impacts on the agriculture, resulting in massive job losses, food insecurity and violent reactions.[18] Land is also an issue in other countries experiencing prolonged crisis such as the Democratic Republic of Congo, Somalia and Sudan.[19] In the Nuba Mountains in Sudan, promulgation of the Unregistered Land Act in 1970, which abolished customary land-use rights and provided a legal basis for land acquisitions by large-scale mechanised agricultural projects, resulted in extensive disenfranchisement of small farmers and nomadic pastoralists: an estimated half of the total area of the plains (the best soils in the region) was taken up by these schemes.[20]

More recently, a new phenomenon with potential important effects on land use and access has emerged in Sub-Saharan Africa. In the aftermath of the food and oil crises and despite the economic and financial crisis, a wave of farmland acquisitions by foreign and domestic investors has picked up and given rise to a hot debate. China, EU, India, the Republic of Korea and the United Arab Emirates governments and private firms seem to be the main investors in Africa's land. But large-scale land deals with other investor countries, such as Egypt, Libya and the United States, have been reported by the international press. Preliminary evidence[21] suggests that FDI in land in Africa tends to be in a small group of countries (Ethiopia, Madagascar, Mozambique, Sudan). But the trend is spreading to other destination areas of the continent. Recent large investments in farmland have been registered in Angola, the Democratic Republic of Congo, Ghana, Liberia, Nigeria and Tanzania.

The consequences for African agriculture and African people can be deep, persistent and not easily reversed. The scale is still largely unknown because of the limited qualitative and quantitative information and neither reliable nor transparent, but available evidence suggest this phenomenon is not marginal. In only five African countries (Ethiopia, Madagascar, Mali, Mozambique and Sudan), 2.5 million hectares of large[22] land deals have been approved since 2004, and pending contracts would push these figures higher.[23] Still incipient, this building wave can be dangerous for the development of a fragile country. It is therefore important to monitor and prevent any possible negative effects of this "special" form of FDI in agriculture on social stability and state fragility (box 4.2).

Perceptions of the great availability and accessibility of farmland and underexploited water in Africa have created interest, but the recent trends in food and oil prices and the protectionist reactions of some major food exporters have been the trigger. Higher demand for food requiring land-demanding production techniques (such as meat and dairy produce), growing demand of energy alternatives to fossil fuel, worsening scarcity of water for productive use and slow growth in farm productivity – and, in some areas, reductions in farm production – all press for farm expansion. Food importers might be less willing to entrust their food security to international markets, and outsourcing food production has become a more feasible national strategy.

17 Vlassenroot et al. 2006.
18 Sachikonye 2003; Pons-Vignon and Solignac Lecomte 2004.
19 Alinovi and Russo 2009.
20 Pantuliano 2008.
21 These evidences are based on Cotula et al. (2009); von Braun and Meinzen-Dick (2009) and GRAIN (2008).
22 Above 1,000 hectares.
23 Cotula et al. 2009.

The link between FDI and foreign policies and national interests has been reinforced by the growing involvement of state-owned enterprises and sovereign wealth funds in international markets. Though most land deals are by private and foreign investors, and in some countries national investors are increasingly interested in farmland acquisitions, the investments are often government-backed, and both host and home governments promote and support large-scale land investments.[24]

Many African countries are now attempting to take advantage of the rising value of land and water. This is why investor commitments on investments, infrastructure or employment are usually required in land deals. The underlying idea is to promote the country's economic development and to reduce poverty by exchanging abundant resources with scarce ones: land for capital, infrastructure, technologies and skills. In many African countries, and especially in fragile ones, the majority of the people live in rural areas. Agricultural development can lead poverty reduction and economic growth, while investments in infrastructure, know-how and technology can have significant positive spillovers.

Box 4.2: Large-scale land acquisitions in Africa – unpacking the land deals

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Land deals are embodied in one contract or several. These need to be examined along with other legal texts defining their broader legal context, including national and international law. Contracts are complex and differ hugely among countries and even projects. More work is needed to identify trends in contractual practice and compare contractual options. But the analysis of a small number of contracts from Africa highlights some key issues.

PARTIES AND OVERALL STRUCTURE

In their basic form, land deals involve at least two parties. On one side is an acquirer, generally a private or government-owned company. But it can also be a foreign government acquiring land directly – for example, under a Special Agricultural Investment Agreement signed in 2002 between Sudan and Syria. On the other side of the deal is a land provider, either a government or, more rarely, a private landowner.

This apparent simplicity hides complexity. Each "deal" may involve multiple contracts and legal instruments – from a framework agreement outlining the key features of the overall deal, where the host government commits itself to make the land available to the investor, to more specific instruments (contractual or otherwise) that actually transfer the land or subsections of it. The extent to which land deals are negotiated or standardised varies across countries and the different stages of negotiation – with instruments to allocate land tending to be more standardised (as for the lease contracts in Mali's Office du Niger).

Each deal typically involves a wide range of parties through the multiple stages of preparing, negotiating, contracting and operationalising the project. First, multiple agencies within the host government are engaged. Even in countries where there is a central point of contact (one-stop shop) for prospective investors, usually an investment promotion agency, this agency alone will not deal with all aspects of the land deal.

Private investors have the advantage of being able to act as a single legal entity with a cohesive set of values. But even here the picture may be more nuanced. Among the possible scenarios, the implementation of deals signed between governments may be driven by private operators, either from inception or as part of subsequent efforts to regain momentum. For example, the Sudan-Syria deal enables Syria to delegate implementation to the private sector, subject to this issue being cleared by the government of Sudan.

LAND RIGHTS TRANSFERRED, SAFEGUARDS FOR LOCAL INTERESTS

Land leases, rather than purchases, predominate in Africa, with durations ranging from short terms to 99 years. Host governments tend to play a key role in allocating land leases, not least because they formally own all or much of the land. So, the extent to which governments take account of local interests in land, water and other natural resources is key.

►►

[24] Cotula et al. 2009.

But host governments may contractually commit themselves to providing land before consulting local land users. In addition, the lack of transparency and checks and balances in contract negotiations encourages corruption and elite captures of benefits. In Mozambique and other countries, national law requires investors to consult local people before land allocations are made. In Ghana, deals with local leaders are common. But even in these cases, shortcomings in implementing legal requirements and in the accountability of local leaders are a recurrent problem.

Security of local land rights is also key. National laws vary, but some recurrent features undermine the position of local people. These include insecure use rights on state-owned land, inaccessible registration procedures, compensation for only the loss of improvements such as crops rather than land, and outdated compensation rates. As a result, local people can lose out, and even investors aiming for good practices suffer from a lack of clear government procedures and guidelines.

THE ECONOMIC EQUILIBRIUM OF LAND DEALS

Land fees and other monetary transfers are generally absent or small, due to the desire to attract investment, the perceived low opportunity costs and the lack of well-established land markets. This alone does not mean the deal is unbalanced: benefits to host countries may include investor commitments on levels of investment and the development of infrastructure such as irrigation systems.

Given the prominence of investment commitments in the economic equilibrium of land deals, enforceability is particularly important. Government land allocations are usually subject to the investor's compliance with investment plans for the first few years of the project, after which the allocation is confirmed. But African governments have rarely used this lever to hold investors to account, with the wording of contracts not specific enough to be enforceable. And one-off assessments at an early stage of implementation do not enable continued monitoring and sanctioning of investment performance over a project's lifespan.

Although the structure of land deals is extremely diverse, a small sample of contracts suggests that much more can be done to tighten key areas affecting economic equilibrium – particularly when these contracts are compared with contractual practice in other sectors like oil and gas. With considerable variation among cases, the contracts tend to lack robust mechanisms to monitor or enforce compliance with investor commitments, guarantee benefits to local people, promote smallholder participation in production activities (say, through contract farming, joint ventures with local landholders or other forms of collaborative production), maximise government revenues and balance food security concerns in both home and host countries.

Agricultural modernisation could help African countries moving up the value chain. Improving agriculture can induce livelihood diversification, generate employment and boost agricultural productivity (through improved seed varieties, know-how and technologies). Land investors and agribusiness could stimulate or directly invest in infrastructure, technologies and interventions for improving access to markets, while land taxes and concessions could provide fiscal revenues.

The risks, however, are worrisome. Changes in access to land and water resources, in resource management and in production techniques can affect environmental sustainability, food security, power relationships and social stability, especially when transactions are dominated by unbalanced negotiations. There is a risk of losing control over land for vast sections of society, with negative effects on food security, social stability and local labour and income opportunities. Land management by foreign investors can generate perverse incentives to use unsustainable production techniques, while land deals and bargaining might create opportunities for corruption and the appropriation of private gains at the expense of national long-term interests.

In some Sub-Saharan African countries, land deals are likely to create friction between the counterparts (box 4.3).[25] Acquisitions tend to be in more profitable areas with irrigation, access to water and infrastructure and areas that are close to markets. And most productive land and water sources targeted for investment are not "unused" resources. Even when classified as "idle", they are likely to be already claimed by preexisting users. This phenomenon has been documented in Ethiopia, Mozambique and Tanzania.[26] It is consistent with the fact that in Africa, resource uses are likely to be underestimated because the large majority of local resource users do not hold formal titles, especially in rural areas. Production techniques that do not require continuous land use are widespread (grazing animals, long-fallow cultivation cycles). Therefore many people rely on common and free access resources for their subsistence.

[25] Cotula et al. 2009: GRAIN 2008.

[26] Sulle 2009; Nhantumbo and Salomao 2009.

International development agencies and the research community are working to provide recommendations and assistance to stakeholders (investors, governments, local populations and civil society) to realise the potential benefits of the renewed interest in agricultural investment. But these efforts are likely to be costly, with uncertain results.

Ensuring the poverty-reducing effects of domestic and foreign investment in Africa's farmland are very challenging, even more so in fragile countries (table 4.1). Such countries have little capacity to negotiate and to reconcile conflicts over resources.

Box 4.3: International investments in Sudan: the "breadbasket" of the Arab region[27]

By Aysen Tanyeri-Abur, Northeastern University, Boston and Nasredin Elamin, Food and Agriculture Organization

Sudan has long been considered the "breadbasket" of the Arab region and a destination for agricultural investment, particularly from Arab countries. With 2.5 million square kilometres, it is the largest country in Africa, and one of the few countries in the region that still has untapped land and water potential. Neighbouring nine African countries and providing sea access for a number of them, it is strategically located. And it has a young population, the result of the rapid population growth in the last 30 years. But the resource wealth of Sudan is overshadowed by widespread food insecurity and poverty (21% of the Sudanese were undernourished in 2003-05; FAO, 2008).

Some recent trends in agricultural investment in Arab countries are influencing the rate and nature of capital flows into Sudan.

- Agriculture and water are emerging as new asset classes for investment because of radical policy changes in Saudi Arabia and worries of Gulf countries after high food prices and export bans of 2007, coupled with lower oil prices.
- Most of the investments are driven by private sector initiatives, although the state has a heavy presence in terms of support and facilitation.
- With one of the highest levels of food insecurity in the Arab region, Sudan is also where most of these investments are destined. More than 50% of the land investment deals in the region are taking place in Sudan.
- Recent investments and mergers may fuel increased investment in the region, as well as a more intraregional trade among Arab countries. And new trade blocs for food and oil such as those between the Association of Southeast Asian Nations and the Gulf Cooperation Council[28] may give way to other trade agreements to facilitate further investments in food and agriculture.

These developments have policy implications. Special attention needs to be given to sustainable investment options and a long-term perspective. In a region short of water and faced with the impossibility of becoming self-sufficient, learning from past policy decisions should be a priority.

Sudan may be relatively rich in land and water resources, but the Nile river basin is expected to be a water-scarce region by 2025.[29] Saudi Arabia has had negative experiences with its own food self-sufficiency policy, with severe resource depletion.[30] Although increased investment in agriculture and food production is crucial for addressing food security concerns in Sudan, unsustainable investments will have negative impacts on both investor and recipient countries and on all stakeholders involved.

The paucity of up-to-date detailed data precludes comprehensive examination of the structure and performance of FDI in Sudanese agriculture.

[27] This box does not reflect the views of the authors respective organizations, and the authors are solely responsible for the content.

[28] Association of Southeast Asian Nations and the Gulf Cooperation Council announced on 30 June 2009 that they are moving towards building a new trade bloc for food and oil, namely rice from ASEAN countries and energy and petrochemicals from the Gulf countries (Reuters 2009).

[29] Revenga et al., 2000

[30] Elhadj, 2008

A few observations on FDI flows to agriculture in Sudan are worth noting:

- FDI in agriculture has been low until recently, averaging less than 1% of total FDI.
- Most FDI in agriculture in Sudan is resource-seeking (box table 1).

Investments in Sudan can be summarised as follows:

Box table 1: Allocations of agricultural land 2000-08

	Total investment (hectares)	Joint venture involvement (hectares)
Foreign investors	713,010	706,640
Saudi Arabia	365,190	48,300
United Arab Emirates	71,820	32,340
Republic of Korea	84,000	500,000
Egypt	5,500	126,000
Others	186,500	
Local	2,363,000	
Total	3,782,650	

Note: Commitments above 1,000 hectares. Not more than 10% of the land deals (foreign investors) are implemented. Processes have been initiated to cancel about 10-15% of the deals with foreign investors.

Source: Author's estimates based on communications with the Ministry of Investment, Sudan

- While the share in total FDI is low, FDI in agriculture has continued to increase in the last decade. Sudan's agricultural FDI grew at an average of 23% from 2000 to 2008, though its share in total FDI remained low, at around 2%.[31] FDI hit 17% of the total in 2009 and is expected to grow to 50% in 2010.[32]
- Intra-Arab FDI constitutes the bulk of FDI in Sudan, at about 93% of all investments, 38% from Saudi Arabia.
- Arab FDI in agriculture in Sudan goes back to the 1970s with the establishment of major projects, through the Arab Authority for Agricultural Investment and Development and other public-private initiatives. The Kenana Sugar Company is one example.[33] Impacts of these investments have been mixed.
- In Sudan, almost all FDI has concentrated in the three most developed regions in the country – Gezira, Khartoum and the River Nile, with 86% of all investment projects – and mostly in primary agriculture.[34] Policies need to address the regional disparities in investment.
- Capital intensity of FDI in Sudan is particularly high for Arab investments. The results also show that although 37% of the total FDI projects and 41% of total FDI capital are in mixed farming, only 25% of total FDI jobs are created by this subsector because of highly capital-intensive production techniques.[35]

The institutional and policy framework is crucial in the continued flow of investment, in providing the right incentives for the allocation of investments and in addressing national food security concerns. Bridging the resource gap in agriculture, Sudan has focused on attracting foreign investment, with less attention given to maximising the positive impacts and domestic links of these investments in terms of improved food security.

The sudden influx of investment in agriculture has prompted new policies. Especially for resource-seeking investments, such as the new land acquisitions, leasing rates and other policies governing land use come into play. Most land in Sudan is leased at annual rates ranging from $2.70 to $35 per hectare, with the lower rates more common. The arrangements for leases depend on the individual cases. Several safeguards have been established by the Sudanese government to ensure that the use of land is in accordance with social and economic concerns. For example, the leases are first established for three years and then extended every seven years up to 99 years. There are also some key requirements from investors, requiring them to establish feeder roads, provide electricity and assign 10-20% of the land invested for local community use (to be negotiated with the locals).[36] ▶▶

[31] Nur, 2009
[32] Reuters, 2008
[33] Kenana Sugar Company was established in Sudan through joint public-private funding by Arab countries in the 1970s. This initiative has greatly increased the productive capacity in the country and expanded sugar production, making Sudan self-sufficient in sugar and even an exporter of sugar. But other social and economic impacts in the region have been mixed.
[34] Nur, 2009
[35] Nur, 2009
[36] Personal communication, Sudan Ministry of Investment.

Sudan, continues to be seen as the breadbasket of the Arab region, with the bulk of the recent investment in land being directed there. However, the question remains: which basic food commodities can profitably be produced in Sudan, particularly in the long run? To meet their food needs, Arab investors' priority is to invest in the production of basic food, particularly wheat. Given the climatic conditions in the country, the capacity for wheat production and productivity in Sudan remains to be investigated. Furthermore, Sudan has huge arable lands, but available water may not be sufficient to cope with future needs of expansion in the magnitude of the recent land leases to foreign investors, without even considering the secondary impacts of these investments on the rural populations and the crowding in urban areas.

Table 4.1: Ensuring the poverty-reducing effects of new investments in farmland

Conditions for sustainable poverty-reducing effects of large-scale land investments	Actions that can help to meet the conditions	Observations
Clear definition and recognition of preexisting resource-use rights.	Land titling of resources; mapping of community resources and informal use of resources. Involvement of local populations indecision-making process.	Most of Africa's people do not hold formal use or property rights of natural resources they have access to. Land titling requires time and resource costly processes. International experience shows that the badly designed land tenure reform and titling programmes can exclude more vulnerable groups and can create destabilising forces. Transparent and informed engagement of local stakeholders is particularly difficult in countries with low levels of education and weak social contracts between citizens and state institutions.
Design of contracts to balance between the priorities, perspectives and incentives of the investors, governments and local populations.	Implementation of transparent and participatory decision-making process. Technical assistance to capacity building for contract design, supervision and management.	See observations above. One of the main obstacles to this condition is the imbalance in bargaining power and negotiating capacity between investors, governments, and local communities and farmers.
Credibility and enforceability of commitments by investors and host governments. Identification and compensation of the rights of people negatively affected.	Baseline assessments of environmental, social and economic conditions. Monitoring of contracts by state institutions or international stakeholders. Actions to ensure transparency and dissemination of information.	Local populations usually lack financial and human resources to meet these conditions. Recipient governments are likely to lack necessary capacity and fiscal resources or willingness to maintain effective structures and impose credible threats of punishment for noncompliance. Problems of asymmetric information can hinder the definition, evaluation and monitoring of compliance.
Creation of better and more labour opportunities.	See actions above on contract enforcement and design. Strengthen involvement of trade unions and labour representatives.	Economic and financial sustainability of the projects might provide new investors with motivations to implicitly or explicitly retract their commitments for implementation of labour standards and labourintensive techniques. Trade unionisation of workers might be against interests of national elite.
Agricultural projects that increase productivity and are environmentally sustainable.	See actions above. Setting up and strengthening institutions (rules, agencies and structures) for environmental regulation and supervision. Technical assistance to new investors and mechanisms to adopt local knowledge of agricultural techniques.	See observations above. In many parts of Africa, land has a low resilience to agricultural intensification. External investors might lack an appropriate knowledge of local ecosystems and sustainable production practices. Contract farming arrangements, joint ventures, and systems of contract growing can improve absorption of local knowledge and benefit sharing among investors and local populations. But these results are likely to be jeopardised by asymmetric economic and power positions of the counterparts.

The EU can support international initiatives for a code of conduct, but it can also help African farmers and populations directly enjoy the benefits of the increased value of African farmland in the current global market by strengthening its actions on long-term programmes for agricultural development and assistance to small-scale farmers. It can leverage its role as a political and economic actor in international negotiations, in diplomatic relations and in global food markets. It can attempt to contain mechanisms that stimulate land demand, such as controls on exports by the main food exporters and energy policies promoting biofuels rather than energy efficiency.

Assessing the contribution of FDI to food security is not an easy task. Not only it is difficult to predict the future development of any investment, it is also a daunting task to address concerns of the various stakeholders (private sector of investor and host countries as well as the governments). Added to this are the different food security concerns and the differences among the countries in terms of resources and incomes. In order to safeguard the concerns of the various parties, it may be useful to develop a framework to highlight the particular aspects of investments, which need to be evaluated so that the negative impacts can be minimized in the future and they can be rendered more sustainable. An important point is also to consider past investments of the same nature and identify lessons learned.

6. HUNGRY POPULATIONS AND FRAGILE INSTITUTIONS

Food insecurity, tightly linked to state fragility, is clearly one of the main threats for African countries.[37] The focus here is on how institutional fragility magnifies the risk of acute food insecurity and on what can be done to achieve the first Millennium Development Goal (halving the proportion of people who suffer from hunger by 2015).

The recent food crisis highlighted the extreme vulnerability of Sub-Saharan African fragile countries' food security to external shocks, mainly because of the low (and stagnant) productivity of African agriculture in the past two decades.

This stagnating productivity went hand in hand with increasing demand, due partly to international factors (increasing demand in China and India) and to population increases, which left most fragile African countries net food importers and substantially increased vulnerability, making a food crisis more likely.[38] An antiagricultural bias induced a move towards urban areas and increased rural-urban inequalities. This stimulated an increase in violence and political insecurity in urban areas, which, in turn, has increased the resources for solving security problems in the cities at the expense of rural funding – a vicious circle. And the high migration to cities, coupled with limited investment in rural areas, has implied less agricultural production, inducing an increase in food imports, further undermining the capacity of agriculture to produce.

A food crisis can increase state fragility along the dimension of legitimacy, as with the food riots induced by the recent spike in the international food prices. But this situation can change if net food buyers become net food sellers (as happened in South and East Asia during the green revolution). Food sellers would raise their incomes and lower the costs of food, pulling people in both fragile and other countries out of poverty, thanks to increased demand.[39] But for the multiplier to start, markets need to work properly. In fragile countries, however, there are many obstacles to market mechanisms, because farmers face limited access to credit and high costs of obtaining information and enforcing contracts. With poor access to formal finance, traders exchange small volumes, trade with areas that are geographically close and increase the likelihood of volatile prices.

Among fragile countries, those in conflict are most at risk of food insecurity. Establishing a causal relationship is not straightforward, but political instability often arises in food-insecure countries. Conflicts and economic collapses are regarded as the cause of more than a third of the food emergencies between 1995 and 2003, while civil strife and refugees or internally displaced persons have been cited as the main reason for more than half the food emergencies in Africa.[40] Conflicts usually reduce agricultural production and income from cash crops and livestock. According to the Food Agriculture Organization, conflicts caused Africa to lose more than $120 billion worth of agricultural production in the last third of the 20th century. Food production declined in 13 of 18 conflict-ridden countries surveyed.[41]

The long-term consequences for agricultural activities can also be severe, while indirect effects and negative externalities can threaten food security in neighbouring countries. There is an interactive, and possibly multiplicative, relationship between the impact of conflict and warfare and agricultural development. Mozambique lost 40% of its assets in agriculture, infrastructure and communication during its 20-year civil war.[42]

37 UNCTAD (2009) estimates that 300 million Africans face chronic hunger.
38 African countries furthermore import major staple commodities, such as wheat and rice (UNCTAD 2009).
39 This trend occurred in China in recent years, until November 2008 when the economic and financial crisis threatened to send "new" urban workers back into rural China.
40 Flores 2004.
41 Stewart et al. 2001.
42 Collier et al. 2003.

Food production problems in countries affected by social disorder or conflict can increase the need for food imports and push up food prices in neighbouring countries. In Uganda, the recent increase in food demand from regional trading partners, such as Kenya and southern Sudan, exerted upward pressure on food prices.[43] And poor postconflict management can hinder a country's agricultural and economic development. The return of agricultural communities to their original landholdings, for example, does not always produce the intended result. In Sierra Leone, measures to permit residents to return to their agricultural land and way of life were prone to elite takeover.[44]

By contrast, food insecurity can encourage fragility. Underinvesting in agriculture heightens the possibility of conflict, as does competition for food or a lack of entitlements to food access.[45] Rebellion and government collapses and conflicts in Ethiopia, Rwanda and Sudan have their origins in food crises caused by natural factors (such as droughts) and the mismanagement of agricultural relief and development aid.[46]

Food security is also closely related to access to water. In fragile countries, water shortages affect human and livestock consumption, and irrigation may become a problem. The use of fertilisers, mainly imported and expensive, is also low.

7. CONCLUSIONS

A country could end up in conflict or peace – or food crisis or no food crisis, or being a food exporter or not, or a mineral exporter or not – depending on the history of relevant variables and the country-specific interaction of the different factors affecting fragility. "History matters," and such persistence makes fragility an even bigger challenge.

The interplay of different economic factors that affect fragility can generate nonlinear effects. FDI and trade, conflicts and food insecurity, and conflicts and natural resources can induce a virtuous circle of attracting more FDI and stimulate growth, but they can also start a vicious circle of weak institutions and corruption.

Persistence is not the only issue. Time also matters: the short horizon of government decision-making is likely to lead to excessive current spending and opportunistic behaviour. Fragile countries, always reacting to emergency situations, have a much shorter time horizon than other countries. A short horizon is exacerbated by the inability to commit, so even a government that is taking a long view may have its decisions influenced by the inability to commit.

These considerations emphasise the importance of time and persistence, because the likelihood that a temporary shock can have a permanent effect on the fragility of a country is very high. They also emphasise how important it is to account for the interactions between different economic factors – and for some time-consistency issues particularly relevant for fragile countries[47].

[43] Benson 2008.
[44] Maconachie 2008.
[45] DFID 2001.
[46] Messer and Cohen 2006; Messer et al. 1998.
[47] For instance, if governments have to attract mineral companies to invest in prospecting or in developing a mine or oil field, the companies face a hold-up. Once the investment is done and regardless of promises, the investors have lost their bargaining power: governments have an incentive to appropriate resource rents. The commitment problem is part of all investments, but more acute in natural resource exploitation and even more so in fragile countries. The capital investment required for resource extraction is typically far higher than for other activities, so more is at stake, and the investment is typically lumpy and cannot be moved. Because the investment is in fragile countries, governments are less accountable.