



## LESSON PLAN

### **Building Democracy and the Market Economy in Post-Conflict Societies**

*Prerequisite: CIPE Development Institute video presentation by Dr. Muhamet Mustafa*

#### **I. Message**

Post-conflict reconstruction is a crucial period for societies dealing with the damage inflicted by violence. Those societies face complex challenges. But they also have a unique opportunity to build institutions of democratic governance and market economy. Capturing this opportunity is a necessary condition for achieving long-term development. In the short term, reconstruction is a balancing act of providing humanitarian relief without compromising the recipient country's ability to develop a local capacity for sustained growth. International assistance is an important factor in reconstruction, but not without risks. In most cases, aid flows are poorly timed, they do not account well for the absorptive capacity, and they trigger some negative macroeconomic phenomena. The key lesson – and challenge – is to make sure that proper mechanisms exist for transparency, accountability, and grassroots input regarding how this aid is applied. Without that crucial local involvement, aid-sponsored reforms will lack a sense of local ownership and ultimately the ability to succeed.

#### **II. Objectives**

1. Understand the significance and key components of post-conflict reconstruction
2. Identify common challenges to post-conflict recovery
3. Discuss the role of foreign aid (positive and negative) in reconstruction process
4. Understand the importance of building sustainable democratic and market institutions for the long-term success of post-conflict reconstruction

#### **III. Discussion questions**

1. What are specific problems that post-conflict societies face as aid recipients?
2. What is absorptive capacity?
3. Discuss the contents and procedures of CPIA and try to rate your country.
4. Why do local ownership and local inputs matter for reconstruction efforts?
5. Why is the role of civil society and the business community important to building democracy and market economy in post-conflict societies?



#### **IV. Reading list**

##### Required readings:

- Collier, Paul, and Anke Hoeffler, “Aid, Policy, and Growth in Post-Conflict Societies,” World Bank Policy Research Working Paper No. 2902, October 2002, <http://ssrn.com/abstract=636265>.
- World Bank, Country Policy and Institutional Assessment, 2004, <http://siteresources.worldbank.org/IDA/Resources/2004CPIAweb1.pdf>.
- World Bank, 2006 IDA Resource Allocation Index (IRAI) based on the results of CPIA, <http://siteresources.worldbank.org/IDA/Resources/73153-1181752621336/IRA!2006table1.pdf>.
- Shkolnikov, Aleksandr, “The New Post-Conflict Strategy: Building Domestic Capacity for Reform,” Center for International Private Enterprise, 2007, <http://www.cipe.org/publications/fs/pdf/122906.pdf>.
- Mustafa, Muhamet, “Rebuilding Kosovo: Overcoming Challenges to Institutional Reform,” Center for International Private Enterprise, 2007, <http://www.cipe.org/publications/fs/pdf/083107.pdf>.

##### Optional readings:

- Alvarez-Plata, Patricia, and Tilman Brück, “External Debt in Post-Conflict Countries,” German Institute for Economic Research, Discussion Paper 613, <http://www.diw.de/documents/publikationen/73/44626/dp613.pdf>.
- Diamond, Larry, “Building Democracy after Conflict: Lessons from Iraq,” *Journal of Democracy*, January 2005, <http://www.journalofdemocracy.org/articles/gratis/Diamond-16-1.pdf>.
- Fukuyama, Frank, “State Building – Lessons Learned,” *CIPE Feature Service*, April 2005, <http://www.cipe.org/pdf/publications/fs/042505.pdf>.
- Kreimer, Alcira, John Eriksson, Robert Muscat, Margaret Arnold, and Colin Scott, “The World Bank’s Experience with Post-Conflict Reconstruction,” 1998, [http://lnweb18.worldbank.org/oed/oeddoclib.nsf/b57456d58aba40e585256ad400736404/f753e43e728a27b38525681700503796/\\$FILE/PostCon.pdf](http://lnweb18.worldbank.org/oed/oeddoclib.nsf/b57456d58aba40e585256ad400736404/f753e43e728a27b38525681700503796/$FILE/PostCon.pdf).
- Overseas Development Institute, “Scaling up versus Absorptive Capacity: Challenges and Opportunities for Reaching the MDG in Africa,” ODI Briefing Paper, May 2005, [http://www.odi.org.uk/publications/briefing/bp\\_may05\\_absorptive\\_capacity.pdf](http://www.odi.org.uk/publications/briefing/bp_may05_absorptive_capacity.pdf).
- Weiss, Martin A., “World Bank Post-Conflict Aid: Oversight Issues for Congress,” 19 April 2004, Congressional Research Service report, <http://fpc.state.gov/documents/organization/32807.pdf>.
- “World Bank Group Response to Post Conflict Reconstruction in Kosovo: General Framework for an Emergency Assistance Strategy,” July 1999, [http://www.worldbank.org/html/extdr/kosovo/kosovo\\_st.htm](http://www.worldbank.org/html/extdr/kosovo/kosovo_st.htm).



## **V. Lesson plan**

### **Understanding post-conflict reconstruction**

- Post-conflict reconstruction is transition to peace, which includes building democratic and market institutions and typically receives foreign support
  - Almost a quarter of the World Bank's total lending
- The main areas of international assistance
  - Rebuilding physical and institutional infrastructure
  - Budget support for necessary investments
  - Aid to productive sectors of the economy

### **Common challenges to reconstruction assistance**

- Defining the objectives and methods of aid
- Providing proper sequencing and phasing of aid mindful of absorptive capacity
  - Post-conflict aid beyond the 15–45% of GDP saturation point does not produce expected benefits (marginal benefits are inexistent or negative)
- Ensuring adequate transparency and accountability of aid flows

### **Constraints to absorptive capacity**

- Macroeconomic constraints
  - “Dutch disease” – currency appreciation, falling competitiveness
  - Debt sustainability – debt levels rise higher than indicators of economic activity, relations with creditors worsen due to the inability to pay back
  - Inflation and interest rates – swelling money supply fuels inflation and raises interest rates, making investment borrowing more difficult
  - Labor market – high-paying jobs offered by foreign donors to local hires distort the labor market and capture the most qualified workers
- Institutional and policy constraints (capacity, accountability, and responsibility)
- Technical and managerial constraints (insufficient human capital and education)
- Donor behavior constraints (lack of coordination, fragmentation, etc.)

### **The importance of local ownership of aid projects**

- Local ownership
  - Improves local capacity
  - Increases the likelihood of project success
  - Emphasizes grassroots reform initiatives
  - Stimulates institution-building
- Political parties and the business community play an important role in ensuring local ownership of how post-conflict aid is used



## **VI. Sample test questions**

- 1. The long-term goal of post-conflict reconstruction is...**
  - a. Rebuilding physical infrastructure.
  - b. Meeting basic humanitarian needs.
  - c. Building an institutional framework for democratic governance and sustained economic growth.
  
- 2. Some negative effects of foreign aid to post-conflict areas include...**
  - a. “Dutch disease.”
  - b. Debt sustainability problems.
  - c. High inflation and interest rates.
  - d. Distorted labor markets.
  
- 3. Common challenges to reconstruction assistance include all except for...**
  - a. Donor fragmentation.
  - b. Poor coordination among various aid-financed projects.
  - c. Insufficient institutional capacity of the recipient country.
  - d. Too little aid in the initial post-conflict period.
  
- 4. Absorptive capacity is...**
  - a. The ability of a post-conflict country to absorb human losses and damage to physical infrastructure.
  - b. The degree to which a recipient country can use aid efficiently.
  - c. The capacity of donors to absorb the growing demand for aid.
  
- 5. CPIA includes...**
  - a. The aid volume and policy priorities for its use.
  - b. The score about quality of policies and institutions in a country.
  - c. Country position on international relations and policies.
  - d. The World Bank assessment of countries about their absorptive capacity.
  
- 6. Local ownership is important in post-conflict reconstruction because...**
  - a. Foreign donors lack grassroots knowledge to apply assistance effectively.
  - b. Institutions cannot be transplanted wholesale.
  - c. Local ownership helps to build institutional capacity on the ground, which is necessary for sustained development.
  
- 7. Based on experience and evidence, reconstruction process can be sequenced:**
  - a. Within 15 years.
  - b. Within a decade.
  - c. Within three four-year periods.
  - d. During the emergency phase.



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